

Response

ECB Consultation on the User Requirements for TARGET2-Securities

“T2S is a technical platform to support CSDs in providing core, borderless and neutral settlement services. The objective is to achieve harmonised and commoditised delivery-versus-payment settlement in central bank money in euros (and possibly other currencies) in substantially all securities in Europe. T2S thereby supports the Lisbon agenda in securities markets.” (T2S User Requirements – Management Summary)

General comments

In general, the EBF believes that, **the URD sets out a good path to follow in the specification stage of the T2S Project.** To ensure that T2S truly delivers on expectations and stated aims, banks urge the ECB to guarantee that T2S becomes the **competition-neutral settlement platform** it is intended to be where there is an evidently level playing field established for custodian banks in particular if CSDs are incentivised to move up the value chain and become Investor CSDs.

We also ask the ECB to guarantee that the following objectives and features will be delivered in the next stage of development:

- experience has proven that banks’ involvement in the key decision making for T2S thus far has been a key factor in getting the Project this far and in a relatively short space of time. Since banks are also the source of transaction volume in T2S, **banks have a very strong claim to participation of at least equal to that of the CSDs in the advisory and technical levels of governance of the next phase of T2S;**
- to secure Europe’s competitive advantage in today’s global financial business, **T2S must be a driver of legal and business practice convergence and harmonisation in the post trading space.** In the first instances this includes market practices, processes and account structures. A standardised recycling period for failing OTC trades is a good example for this harmonisation. **Over time, legal and regulatory issues must also be addressed;**
- in terms of its technical capacity, T2S must be fit for purpose in 2013 and beyond, and therefore must:
 - **provide the possibility of settlement in central bank money other than Euro;**
 - **be able to accommodate a wide scope of instruments;**
- to facilitate a high degree of efficiency in Europe’s post trading space:

- there must be the possibility for **direct connectivity by CSDs' clients and by CCPs to T2S** without unreasonable conditions being placed upon this direct participation;
- there must be **consistency in the business practices associated with the operation of night-time settlement of securities**; and
- notwithstanding the practical character of the compromise solution allowing for flexibility in how settlement instructions could be matched in T2S, the EBF maintains that **matching in T2S only would provide a more compelling economic case in favour of the Project as a whole.**

Furthermore, a number of important considerations from the cash perspective must also be taken into account in the specification of T2S to achieve a high degree of interoperability between T2S and the TARGET2 platforms in particular and the smooth interaction of cash and securities settlement systems in general. These points can be summarised as follows:

- it is considered imperative that **banks retain control over use of their own liquidity**;
- hence, full understanding of the auto collateralisation facility is considered to be essential;
- the statement that **'cash settlements in T2S should take place exclusively in T2S dedicated cash accounts'** is considered highly important;¹
- since T2S is not a payment system, all transfers have to be done via RTGS accounts; and
- the **cost of shared infrastructure should be fairly allocated between the users of the three proposed associated systems** i.e. T2, T2S and CCBM2.

Banks, as clients and in some cases shareholders, of CSDs will be instrumental to the CSDs' decisions as to whether or not they opt to participate on T2S and the EBF, through its members and their member banks stand ready to **encourage CSDs to come to a decision in good time in respect of their participation on T2S in the future.** However, the extent to which assurances can be given over the inclusion of these features will have a bearing upon the extent to which banks seek to influence CSDs participation on T2S in the coming weeks and months.

The EBF's specific comments on the URD follow. Annex I sets out a number of detailed issues that require further consideration to take fully account of the cash perspective. Annex II sets out answers to specific questions asked by the ECB of the market at the January

¹ See section 6.1.1.1. Consequently, the comments relating to cash in this response focus principally on the cash impact beyond T2S dedicated cash accounts with issues related solely to T2S dedicated cash accounts being ignored

2008 T2S Information Session. In the answers to these questions we also set out a number of views from the direct holding markets as work continues in these markets to address these specific set of issues. Annex III is the EBF's general comment on the Economic Impact Assessment. Annex IV reflects our position on the governance of the project in the next stage.

Specific comments

The following section sets out the main issues in respect of the URD for the EBF. The EBF is at the disposal of the ECB to discuss the issues raised here in greater detail and/or where further clarification is necessary.

Chapter 3 – Processing schedule and calendar requirements

The EBF generally agrees with the contents of this chapter but three items in particular require further consideration:

- deadlines for T2S are compatible with the management of treasuries and are parameter driven;
- fail management should be resolved in a harmonised way for all participants; and
- suggestions to change the start of night-time settlement and possibly the maintenance window are necessary.

Due to the long period from specification to implementation there is sufficient room to address these points in due course and after there is clarity about which CSDs will participate on T2S.

Chapter 4 – Roles requirements

We stress that the governance structure is very important for the definitions of roles requirements as well as for the continued maintenance of T2S.

We also highlight that competitive disadvantage can arise between banks if requirements vary from country to country and between different parties. This we feel would undermine the viability of the T2S Project as a whole so we would look for as high a degree of consistency as possible across the markets that have access to T2S. We encourage the ECB to level the playing field across Europe through T2S by developing solutions to support open and liberal market practices in the future.

Chapter 5 - Instruction Lifecycle Management and Matching Requirements

Whilst we are generally content with the outcomes presented in this chapter to drive harmonisation of practices we emphasise the need for ISO Standard compliant reporting and ECSDA Standard compliant matching for the wider matching process.

Chapter 6 – Provision of Liquidity, Collateral Management and Monitoring Liquidity

Whilst the opportunities for misinterpretation should be minimised by developing clear guidance in this area, we strongly support the flexibility afforded to banks in respect of the possibilities to structure accounts.

Chapter 7 – Settlement Processing Requirements

A number of points for banks arise from this chapter:

- the proposed order of settlements and the subsequent impact this will have on settling transactions in oldest intended settlement date order rather than in the order of instruction date as is often the case today creates a possibility for a divergence of outcomes in and between markets. We urge that there is consistency of approach applied across the board.
- the cash and securities reservation process seems quite elaborate. Unused reserved securities and cash balances are released at the end of the day.

Chapter 8 – Settlement Optimisation and Auto-collateralisation Processing Requirements

The EBF raises specific concerns in relation to the following points:

- we lack detail of the prioritisation process to be followed;
- banks argue for a more global optimisation goal aiming at achieving the highest settlement result (such as number of transactions settled or value of transactions settled), which will entail a range of parameters. We are also keen to understand how this proposal will take into account the CNS functionality used by some CCPs, which entails the cancellation of failed transactions and their rebooking for the following value date;
- we have consistently recommended that partial settlement should be optional but that the rules for partial settlement should be harmonised. We also lack clarity on partial settlement for CCPs in the current URD; and
- to improve the efficiency of the proposed T2S system we would urge to make auto-collateralisation a process in which if liquidity were needed it would be provided automatically.

Chapter 9 – Specific Settlement Processing Requirements

The EBF raises a number of specific issues on this chapter:

- The rules for an instruction to be submitted to the CoSD functionality can be part of the individual settlement instruction or can be defined by each CSD in the static data. T2S will automatically submit a valid instruction to the CoSD procedures if the conditions are met. In the case of standing instructions, the CSD will also define in the static data an “administering party” (new concept). Individual settlement instructions contain the administering party. T2S will inform the CSD, the administering party and the relevant T2S parties of the reservation of the securities. Only the administering party (most likely the relevant CSD) will be able to send a

release message (unblock) if the external condition have been fulfilled or a cancellation of the CoSD instructions if conditions can not been fulfilled. CoSD will be recycled until release or cancellation message have been received. The EBF would like to explore further the role of the administering party and the function it will play for conditional securities deliveries.

- The URD still defines “settlement” instructions linked to corporate events and not “bookings”. T2S will offer delivery or receipt FoP instructions, DvD and DvP instructions as well as payment free of delivery (PFoD) instructions, which should allow covering “settlement” for all types of corporate events. T2S will offer the possibility to link corporate event settlement instructions with all or none rule, or to give a high level of priority. The URD has clarified the role of CSD with regards to corporate events when the CSD is an Investor CSD or when the CSD act as Issuer CSD in satisfactory manner. However, the URD has introduced a new concept the “Technical Issuer CSD”. For an investor CSD it is the CSD where its omnibus accounts reflecting the holding of its participants are deposit. This Technical Issuer CSD is in most cases the Issuer CSD but not necessarily even if the Issuer CSD has joined T2S. This concept will allow for relayed links within T2S, which is a position that EBF opposed previously due to the increased complexity this gives rise to. The EBF would therefore propose to discuss the concept of the Technical Issuer CSD in greater detail before any final decisions are made.
- T2S will allow cross CSD settlement (i.e. when the two CSD participating in T2S) to be transparent for users. From a user perspective it will be same process whether settlement will take place between parties having an account in the same CSD or in two different CSDs. The characteristics of cross CSD links will be defined in the static data and T2S will be able to automatically generate all securities and cash instructions as well as the realignment process between the CSDs. Settlement of instructions sent by the relevant parties and these generated automatically by T2S will be settled following the all or none rules. The main concern is whether the Technical Issuer CSD denotes the CSD of the underlying issuer or that of the intermediary CSD. Therefore, this aspect requires clarification. In particular, there remains a need to distinguish whether the Issuer CSD is intended to be part of T2S or not. If the technical issuer CSD denotes the underlying issuer, the concept should only exist if the Issuer CSD does not join T2S. In any event, the EBF remains sceptical towards the introduction of relayed links between CSDs participating in T2S.

Chapter 12 – Interfaces and Connectivity Requirements

The EBF notes the good progress made in this section of the URD and offers its full support to the development of the concept of direct connectivity to T2S to those institutions that so desire it. As we highlighted in our general remarks, the successful implementation of the possibility for direct connectivity is a *conditio sine qua non* for banks to lend their full support to the Project. We therefore are keen to ensure that the rules for direct connectivity set out in Annex 11 will be upheld.

Chapter 15 – Statistical Information and Billing

The extraction of statistical data for authorised parties could become a hurdle if the extraction means gathering big volumes of data out of the “database” during on-line activities. Separate storage for the processing of the statistical requirements should be considered.

Chapter 16 – Static Data Requirements

Whilst we are broadly satisfied with the overall contents of this chapter we query why the data field for “conditional settlement” has been omitted in the final proposals set out in the URD.² We would urge that this be reinserted unless a convincing argument to the contrary can be provided.

Important considerations for the direct holding markets in relation to static data are set out in Annex II to this response.

Chapter 21 – Migration

A number of important considerations arise from this chapter:

- further work is necessary to flesh out migration plans, to ensure progress with the Project. We suggest that the ECB could draw lessons from the completed migration to T2 and apply them as appropriate to T2S. Banks, therefore, look forward to being involved in these discussions; and
- the interval between migrations of one to three months, seems too long (especially if no problems arise) and results in a where long overall migration time span.

We also raise the following additional considerations:

- there is a need to re-evaluate the process to transfer directly connected parties at a later stage. This implies double adaptation costs for them and especially in a case where a party already has a direct connection to T2S (due to the fact that a CSD, where it is a party, has already been migrated to T2S) the two-step process seems inefficient and burdensome;
- the migration plan does not include testing of fall back plans which usually is the case;
- there is a plan according to which testing and simulating is suggested to take place for 5 consecutive settlement days – this seems inadequate; and

² Page 19, line 8.

- the intention is to transfer static data to T2S before the migration week-end. In case of direct holding markets there is a need to update the transfer due to the nature of accounts and the amount of data (that changes substantially on a daily basis).

Annex 2 – Glossary and Standards

It is essential that the glossary is kept up to date with all changes in the URD and in line with the subsequent specification phase.

Annex 4 – Issue Note – the T2S on T2 Concept

There are many advantages to be gained from developing the T2S on T2 concept but this principle should in no way restrict the functionality and/or future development of T2S.

Annex 7 – Issue Note – Cash Accounts

See specific comments in Annex I below.

Annex 9 – Issue Note – Night Time Settlement Options in T2S

If we consider the possibilities that may be used in the context of T2S, there might be negative impacts on the following items if we accept to have different market practices:

- possibility to use one single T2 Cash RTGS account for many countries;
- optimisation of procedures to manage liquidity; and
- single structure and operating mode for liquidity management of related T2S dedicated Cash Accounts.

The EBF therefore makes a strong call for convergence of market practices in these areas to facilitate the efficient use of night time settlement in T2S.

Annex 10 – Issue Note – Cross-CSD Settlement and External CSDs

As a general principle, banks will urge that the highest number possible of CSDs participate on T2S. The greater the number of CSDs participating, the more attractive the economics of the Project will become. In parallel, the fullest participation of CSDs on T2S will help to simplify what appears to be a very complex situation described in Annex 10 should some CSDs choose not to participate on T2S.

Annex 11 – Issue Note – Direct Technical Connectivity

As we have stated throughout this paper and on previous occasions, direct technical connectivity to T2S remains a condition of the EBF's support for T2S as a whole. We therefore are keen to ensure that the rules for direct connectivity set out in Annex 11 will be upheld.

Annex 12 – Issue Note – Corporate Events

As the settlement engine of the CSD's, T2S must be able to process settlement instructions (SIs) like DvP, DvD, FoP etc (as described in the URD). The process which leads to the SIs is in fact outside the scope of T2S. T2S must only set criteria for SIs and must be able to work for prioritisation. The CSDs need the positions (often settled because of the introduction of the record-date), as well as unsettled SIs with regard to transaction management like claims to process Corporate Events (CEs). As to the corporate events, T2S will only have to provide positions and pending transactions, and must be able to process regular settlement features. CE processing savings can only be reached by harmonisation, which is in the scope of the Corporate Actions Joint Working Group (CAJWG) in which the EBF remains active. Overall, we are satisfied with the content of this annex.

Annex 13 – Issue Note – Interactions with Organised Markets and CCPs

We suggest that communication with the CCPs in respect of their interaction with T2S could be improved in the next phase of the Project. The EBF will also pay close attention to relationship between banks, CSDs and T2S as and when Organised Markets and CCPs connect directly to T2S.

Annex 14 – Settlement of direct holdings in T2S

For as long as the T2S fees remain unknown it is impossible to say whether the functionality described in Annex 14 will be cost efficient for direct holding markets.

At this stage it seems that the functionality described in the Annex will be sufficient however this remains to be verified in more detail in the specific user requirements. The settlement features used by the direct holding markets do not affect the settlement procedures applied by indirect holding markets – in other words these participants will not face any extra adaptation burden or extra costs

Overall, T2S should be a key driver of harmonisation of practices at least in the first stage. Direct holding countries must not, however, be overlooked in this drive toward greater harmonisation notwithstanding the added complexity that arises from working through the issues surrounding direct holdings.

Annex 15 – Issue Note – Harmonised Features

Annex 16 – Issue Note - Opportunities for Further Harmonisation

Annex 17 – Issue Note – National Specificities in T2S

The EBF remains strongly supportive of efforts to use T2S as a key driver of harmonisation in Europe's post trading space and we shall keep the issues identified in Annexes 16 and 17 under close review to ensure that the opportunities for further harmonisation are addressed in a risk-based way whilst looking for the number of national specificities imported into T2S to be reduced over time. Banks expect to be fully involved

in future discussions on this important aspect of T2S's future development and we urge that the harmonisation process does not lose momentum in the subsequent specification and implementation phases.

Annex I – Specific comments in respect of the URD from the cash perspective

User requirements

2.5.1 The statement ‘The cash settlement will take place on T2S dedicated cash accounts’ is strongly supported as a means of ring fencing T2S settlement.

3.1.2.3 A description "Start of Day" and it's relevant task exists in the URD document several times. What we could not find, was the description of a further support based on cash forecast information at Start of Day. To support best market practice, and to avoid as well systemic risk, T2S should support the following:

- harmonisation between the deadline for first night time settlement cycle and the provision of a cash forecast;
- based on this cash forecast (where no more settlement instruction will enter in the following settlement window) T2S should support an automated CeBM sweep from a T2 RTGS account into a dedicated T2S cash account;
- Bank treasurers want to use one of the following options, which they want to register in static data;
- a fixed amount - already provided by T2;
- the amount of the cash forecast plus a % rate (security margin);
- the amount of the cash forecast plus a fixed amount (security margin); and
- one of the options in combination with a CAP

3.1.2.5 From a cash perspective, it looks absolutely illogical that the maintenance windows of T2 (cash) and T2S are not synchronised. Bank treasurers want as much as possible synchronised Start of Day, End of Night, and End of Day cut off times. These events are used to either inject CeBM or to take CeBM out of T2S. Bank treasurers fear that mirroring of data will be asynchronous as well, which may create major problems in case one of the 2 systems (T2 & T2S) has a disruption.

3.1.2.6 Please read in conjunction with "Maintenance window" - previous point. In some countries night time settlement is an extremely efficient process, which settles a huge number and value of security transactions. Therefore, bank treasurers want to have an optional automated CeBM re-transfer from the dedicated T2S cash accounts back to the T2 RTGS account. This task should take place directly prior to the maintenance window. The URD explains, that Daytime settlement will start at approx. 05:00 CET. Bank treasurers understand that T2S requires a new CeBM liquidity injection.

- 3.1.2.7 Bank treasurers understand that the mentioned EoD CeBM transfer is the latest automated sweep. We wish to request an optional full liquidity sweep at (shortly after) the deadline for intraday DVP, which is expected for 16:00 CET.
 - 3.1.4 Bank treasurers want to stress the point that after the deadline for DVP, only bilaterally agreed treasury management instructions will be settled. The time after 16:00h should not be used for fails management.
 - 4.5.2 In addition to maintaining standing instructions for the transfer of liquidity, the settlement banks must have the facility to increase, decrease or cancel such standing instructions. Night settlement operations should not have any impact on RTGS accounts.
 - 6.1.1 As an account holder is not allowed to transfer funds to its T2S dedicated cash account from any euro RTGS account, only from the RTGS account linked to the T2S account. The EBF would appreciate to see the possibility for a bank to link a dedicated cash account to any of the banks' RTGS accounts even when held by different NCBs. Please confirm that funds can be transferred immediately to the linked RTGS account.
 - 6.1.2 Clarification is requested on why a T2S dedicated cash account should be used to settle the cash leg of a corporate event which logically is a clean payment. Is this due to the possible connection with other T2S actors? Do participants have any choice in this?
- Reference Id: T2S.06.120: How is the link between the specific instruction and the liquidity reservation controlled?
- 6.1.2/3 Confirmation is requested that a settlement bank has the ability to control all aspects of its T2S dedicated cash account unless it has agreed to a reservation of funds
 - 6.1.3 It is a requirement that such liquidity can be accessed at any time, not just within pre-defined periods
 - 6.1.5 We need to receive information on the cash needs for the current settlement day as well as for the following settlement days to allow proper cash forecasts and this information should be made available on a pull mode (upon participants request) and at the end of day on push mode.
 - 6.1.6. In the general requirements it is stated that the service running the account to be debited will trigger the execution of the liquidity transfer. How does this relate to the description of requirements for pre-defined liquidity transfers and standing order transfers to increase liquidity on the T2S dedicated cash account, since this would appear to require a change in T2 rather than T2S?

Fig. 6.2 In the second grey box add “of the same settlement participant”

6.1.6.1 In case of non-execution as requested (partial or nothing) banks wish to receive immediately an alert in the ICM tool.

6.1.6.2 It is considered important from a treasurer's perspective that the account holder keeps full control of all liquidity, not just outgoing liquidity. For instance, when the CSD is acting on behalf of settlement participant, contractual arrangements are needed. It is mandatory for T2S to know those arrangements and verify them.

6.1.6.3 It is noted that liquidity resulting from intra-day repos will generate an automated transfer to the RTGS account in T2. However, clarification is requested re pledge countries. In such cases, is T2S involved at all?

6.1.6.4 Clarification is requested on why pre-defined orders are not possible between different T2S cash accounts of the same settlement bank (reference ID T2S 06.270).

Partial or pro-rata rule for liquidity transfer orders

In case of insufficient liquidity it is stated that in case of "current orders" no liquidity will be moved at all, and in case of "pre-defined" and "standing orders" that as much as possible will be moved and in the case of multiple orders they will be executed pro-rata. Some members would prefer that only full amounts should be executed on a pre-defined basis. Alerts should be sent in any case current, pre-defined and or standing orders cannot be processed (for whatever reason). As these alerts will be key to liquidity management and control processes, we would like to be consulted on how these alerts will be given to the banks (6.1.6.4 and 6.1.6.5 Reference Id: T2S.06.300 / Reference Id: T2S.06.310/ Reference Id: T2S.06.370 / Reference Id: T2S.06.380).

Predefined and standing liquidity transfer orders

It should be possible to include a start date/time (effective as off) and an expiry date/time in a predefined or standing order (Reference Id: T2S.06.290 and section 6.1.6.5).

To align T2S.06.290 with the section 6.1.6.5 it should only be possible to increase the liquidity on the T2S dedicated cash account. (6.1.6.5.1/2 / Reference Id: T2S.06.400 / Reference Id: T2S.06.420).

Alerts for Floor and Ceiling

It should be avoided that after hitting a floor or ceiling, each next additional booking will again result in an alert being sent.

6.2.1.0 We question, if T2S is the appropriate place to memorize a flag for the existence of a contractual agreement between a CSD and a bank. If a CSD initiates a transfer from a T2 RTGS account, we feel that T2 RTGS needs the same information as well.

6.2.2.0 The same process should be available on an optional basis at 16:00h as well. Bank treasurers have two simple reasons for this request:

- a bank must place excess liquidity in the market, which is still in a dedicated T2S cash account; and
- a payment bank, acting as a provider for a third party, must be able to square the remaining liquidity from a dedicated T2S cash account back to the RTGS account of the third party, because it may have to fulfill its own reserve requirement. See as well, EBF Guidelines on late payments

Fig.6.3 Figure 6-3 shows "only increase of liquidity. Is decrease (transfer from T2S back to T2) allowed or not?

6.2.1 This appears to be in conflict with the requirement in 6.1.6.3 for automatic transfers to the RTGS account in T2.

6.3.1 Does not the role extend to general repos in accordance with section 6.1.6.3?

Auto-collateralisation

As far as auto-collateralisation is concerned, it should be clarified, that auto-collateralisation on stock can also be used to fund the haircuts and purchases of securities which themselves are not eligible for auto-collateralisation with the Eurosystem as it is already the case in some CSDs. As this feature is deemed essential in a liquidity saving settlement process and for the sake of clarity, this aspect should be mentioned in the URD explicitly. Precondition for the use of collateral on stock is the segregation of a bank's propriety and client securities accounts.

6.3.3 The auto-collateralisation limit defined by the NCB should be visible for the participant, in order to incorporate these in their liquidity projections and intra-day liquidity management procedures. (Reference Id: T2S.06.500 / Reference Id: T2S.06.490).

7.1.2.2 We can see the advantage of the loop functionality from a securities perspective. However, on the cash side this could have a negative impact on reconciliation and control as well as making cash forecasting and management of liquidity on the T2S dedicated cash accounts more difficult. Therefore, it is suggested that the looping functionality should be made optional in such a way that the account holder can assign which group of accounts may be used for looping. It should be possible to make several independent groups for looping (Reference ID 07.280).

In each and every case where a direct T2S member settles its security settlement instructions by inviting an additional cash agent, the priority of usage between the existing dedicated T2S cash accounts must be predefined. This should also be part of the static data.

- 7.1.2.4 Confirmation is requested that automatic triggering of auto collateralisation will be subject to the ‘when applicable’ qualification in section 7.1.2.2.
- 7.2.2 There is a need to further explain how this prioritisation can work in case of DVP instructions when the two participants are not inputting the same level of priority.
- 7.2.2.1 Participants should be made aware when reserved priority applies.
- 7.3.2 (Procedure for unused cash and reserved positions at the end of the day). Confirmation is requested that unused liquidity will be transferred back to the relevant RTGS account for use at the account holder’s discretion as stated in 6.1.1. What kind of restriction is meant when referring to the performing of provision-checking?
- 8.1.6 What is meant by term “all or none” and “all or nothing”? Is there any difference? Please explain to avoid confusion.
- 8.2.1 The wording of the contract with the relevant central bank is critical to settlement banks’ obligations and responsibilities and the industry would wish to have the opportunity to comment before such contract(s) is finalised. Also, is it envisaged that where possible such contract will be common to all central banks in the same way as the Harmonised Conditions in the T2 Guideline?
- 8.2.9 The statement that this central bank limit will override the auto collateralisation limit defined by the settlement bank appears to be at slight variance with the statement that neither the settlement bank limit nor the central bank limit must be breached.
- 8.2.10 It is considered important that the settlement bank is advised of any changes in the central bank limit.
- 9.2.1 Again, is liquidity derived from pledge transferred directly across T2 RTGS accounts with no involvement of T2S?
- 10.2.1 Confirmation is requested that a settlement bank can define an auto collateralisation limit of zero by dedicated cash account.
- 12.2.1.2. See comment on 12.3.2 below.
- 12.3.2 There appears to be a contradiction between the statement in 12.2.1.2 that ISO 20022/UNIFI shall be used as standard for T2S communications and the open concept referred to in 12.3.2.1/2. A similar comment would apply to any other shared interfaces.
- 13.5.2.3 The cash forecast offered in the URD, could be improved from the cash perspective. As a minimum requirement, we request information about the potential amount of CeBM which could be generated by auto-collateralisation.

- 14.5 Will the consolidated view include all a bank's RTGS accounts not just the one(s) linked to T2S dedicated cash accounts? Surely, any credit on an RTGS account should be the property of and visible to the settlement bank owning it, not the payment bank (Reference Id T2S 14.840).
- 14.6 CSDs should only be allowed to view cash liquidity in T2S with the agreement of the account holding participant and not on RTGS accounts.
- 16.8.3 We assume that in the definition of auto collateralisation, the account being referred to is the dedicated cash account.
- 20.1.1 Confirmation is requested that the sole reason for the difference between the T2S and T2 calendars is to accommodate non euro currencies.

Annex 4

- 3/4 The shared infrastructure makes transparency in cost allocation essential.

Annex 7

- 1/2 Where a payment bank does not have an RTGS account, do its T2S dedicated cash accounts have to be linked to its settlement bank's RTGS account? If so, does this mean that the settlement bank has to maintain an RTGS account with the same central bank? A clear distinction should exist between the payment bank (holder of T2S DCA) and the settlement bank (holder of T2 RTGS account).
3. If somehow due to the auto-collateralisation the T2S account shows a debit balance, this balance is presumably at the end of day automatically transferred to the T2 RTGS cash account. If so, will at the same time the paper used for auto-collateralisation also be moved to the collateral pool of the bank (in CCBM2)? If not, how will a potential debit balance exceeding the credit line be handled at the T2 platform? If so, what is the follow-up process the next day? Clarification will be appreciated.
- 4.3 How will the settlement process be impacted at the moment a liquidity transfer is processed on the T2S dedicated cash account? Will the settlement process stop and will this also impact other users?
- 4.5 Is the floor only defined as a minimum credit balance on the account, above which liquidity will be moved to the T2 platform? Or can you also define it as a minimum balance below which alerts will be sent to the account holder?

At what moments or frequency will the T2 system check the balance in order to initiate the 'ceiling-triggered' liquidity transfer?

If sufficient funds are transferred to the T2 dedicated cash account, will earlier initiated auto-collateralisation processes be reversed directly? If not, how can auto-collateralisation be reversed? If so, in what order?

Annex 9

Confirmation is requested that finality during overnight settlement will be assured in all relevant jurisdictions notwithstanding that ‘day’ in articles 3 and 4 of the Settlement Finality Directive is assumed to relate to calendar day.

Annex 12

- 2.3 This indicates that the CSD will have the option to settle these pure cash movements either on T2 RTGS accounts or on T2S dedicated cash accounts in line with the service level agreement it has with its participant. Does this mean that such a service level contract is mandatory for participants?

Annex II – Response to supplementary questions from the ECB to the market

- Should optimisation favour number of transactions, overall value or a mix of the two as described in the URD?

A mixed approach to optimisation would be favourable as opposed to an approach focussed on either volume or value. The mixed approach is the optimal way to maximise settlement efficiency whilst not imposing additional complexity and already exists in some markets where a high degree of settlement is achieved.

We feel that an approach focussing on just one of the criteria, volume or value, could be detrimental to various types of operations depending on the business case in question. For example, if the value only approach was favoured, small transactions for retail clients in particular could be blocked resulting in a deterioration of services. For a volume-based approach, high value transactions, such as for fixed income, could probably be settled less readily than for equities trades.

Therefore, since the objective is to maximise overall settlement, optimisation rules, as well as the rules for splitting transactions and all other functions optimising settlement should be based on an approach combining both value and volume.

- Should the liquidity created via the auto collateral function be provided for individual transactions or in lump sums based on a threshold?

It would be preferable to have liquidity provided in lump sums so as to provide the market with a small cushion, reducing the number of auto-collateralisation transactions and thereby increasing settlement efficiency.

- Should collateral on flow be used first, then collateral on stock?

We are neutral about whether to use stock on flow before stock on stock, however if liquidity is to be provided in lump sums then stock must be tried before on flow.

In general the whole process must be completely automatic and the results visible to the settlement bank concerned. If there is a limit placed on the amount of liquidity to be provided in a lump sum with a threshold in excess of that needed to settle the immediate transaction in question, and that limit is imposed by NCBs, there must be no suggestion that one NCB is inclined to be more generous than another.

Importantly, the legal environment must be compatible to provide for the optimal solutions in this area and this is one area where a further harmonisation drive is necessary.

- Whether at CSD level or at T2S level, is there a need to match corporate events settlement instructions?

We believe that there is not a need to match corporate events settlement instructions. Where checks are necessary these should be performed upon validation (such as is the case with matched trades delivered by MTFs).

- For voluntary corporate events, is there a need to send an instruction for each available option or for every securities account position and only match with the option selected by the customer?

This is a decision to be taken in respect of the level of orders to be carried out. Therefore, since each single order is to be sent to T2S the instructing bank could opt for cumulated or single orders and decisions should be based at the outcome of discussions within the CAJWG (Corporate Actions Joint Working Group).

The introduction of T2S will have little bearing on this issue. The MT565 is specifically designed to allow for only one option per instruction, and global market practice as defined by the SMPG states that only one account should be included per instruction. Since this will most probably be re-engineered in ISO 20022, there should be no reason, and very little possibility, for T2S to differ.

- What is perceived to be the major issue in integrating / connecting a corporate event engine with the functions and data of an outsourced T2S settlement engine?

For CSDs to answer. While the CSD is looking to the local market practices, a major issue is one affecting countries where in the same day we can have also a “timing” issue for eligibility criteria.

- Corporate events often involve high costs and a degree of risk, particularly cross border. Do you have suggestions as to how to exploit T2S to reduce costs and risks?

T2S, which is merely a settlement engine, would not help reducing costs and risks for corporate events. The only way to reduce costs and risks in that matter is to harmonise the market practices within Europe.

Questions concerning direct holding markets:

The EBF takes a position on the implications of T2S for direct holding markets since we have consistently emphasised how T2S could act as a driver for harmonisation in general. The objective of T2S is to decrease post-trading costs by providing an efficient settlement platform for CSDs. One of the fundamentals is that CSDs becoming participants in T2S could “outsource” their settlement engines and account databases by replacing legacy systems with T2S. Using centralised and harmonised settlement engine and account databases is expected to bring substantial savings in post-trading activities on both domestic and cross-boarder level. T2S should therefore not disturb the level playing field and should bring equal benefits in costs and efficiency to all joining markets.

- Is there a possibility to put all data in T2S?

The direct holding system per one market-executed trade will require many T2S instructions to accommodate the current “Matching-Allocation-Shift-Transfer-Enrichment Process” [in Greece] all the way to “Final Settlement into the End Investor Accounts”. This will, most likely, result in extra costs, which is expected to be passed on to the custodian banks.

In addition to the numerous end-investor accounts, which must be accommodated for the regular matching or settlement reasons, additional data exists in the current CSD system to support functions of “Registry”, “Extended Notary Function” and “Local Tax” which are independent of any matching or settlement functions. Custodian member banks must supply all data for a new account - end investor always - for all functions to enable settlement at the respective CSD in direct holding markets.

With respect to static data on securities accounts and end-investor information, in direct holding systems each intermediary is required to open a separate securities account for each end-investor (at least for domestic ones) in end-investors own name. Currently there are more than one million securities accounts opened in the Finnish CSD for example. Typically, all the data on account holder or the securities is registered only at CSD level and data content is defined in legislation. Intermediaries do not have this information in their own systems, but use it by queering or pulling information from CSD systems for both settlement and other safekeeping activities.

In the planned T2S model, intermediaries are able to open end-investor accounts. However account information will be limited only to information necessary for settlement. This means that no information on the end-investor will be registered. As certain information on end-investor is by law required to be registered on the securities account, all information on end-investor must be maintained in local CSD-systems.

This would enforce the CSD in a direct holding market to maintain its legacy account database for that information. This means that they would not receive significant cost savings by outsourcing only one part of account databases to T2S. Dividing information between legacy systems and T2S will also endanger the reliable functioning of the systems.

We understand that additional data fields will be reserved for the future needs of T2S and that these additional fields could also be used for specific national needs. However, additional data fields or their functionality has not been described in the URD. Description and definition of additional data fields should be added to URD, following consultation with market participants in the direct holding countries.

Additional data fields would serve to a large extend the additional data need in the direct holding system for end-investor information, such as identification of the end-investor. However from user point of view equally important requirement is that these empty data fields can be used in similar ways as any other fields in T2S, i.e. allow automated administration of the field (ISO 20022), data storage, possibility to make queries on data and change history etc.

When building a system like T2S the cost of additional fields in the static data are not cost issues *per se* and normally space for additional field is reserved anyway for the possible future needs. We also suppose this would not have any negative impact to the running operations or costs of T2S as from T2S point of view the data is redundant as it is not needed for T2S-settlement.

Another identified problem is that CSD and its users should be able to identify the account type as “investor account”. This identifier would enable T2S users to segregate assets of their own from assets of their clients. A specific identifier would be needed also to identify, whether the account holder acts as a nominee (i.e. client of Finish account operator is a custodian) or as an owner to the securities.

- Cost implications for the different procedures?

In addition to the comment above relating to costs and static data, the fact that the direct holding system in which holdings within the end client accounts - kept at CSD level - are by law required and accepted as shareholder proof, is expected to introduce the following cost implications vis-à-vis indirect holding markets. In particular:

- the number of instructions for the settlement process is higher in comparison to those of other markets of comparable size using indirect holding system which has implications for the overall pricing policy of [CSDs operating on] T2S;
- currently the model of settlement used in Greece for example makes efficient use of equities held by investors which are used as collateral for the evaluation of the trading limits of the members of the Athens Stock Exchange, as collateral on hold for increasing settlement efficiency and as a means to reduce the cost of financing for settlement. The eligible collaterals to be used by T2S do not include stocks and therefore, will increase the overall cost of settlement for Participants, and eventually their clients;
- current law and regulation requires one investor account per physical or legal entity to be kept at CSD level. The mapping of those accounts in T2S will increase the actual number of accounts by a factor of 3 at T2S. As we understand that for each Account Operator and for a unique end investor currently at the CSD, a different T2S account needs to be opened and maintained by the CSD at T2S. This will increase the cost of opening and maintaining accounts at T2S and will be transferred to Participants;
- the relatively high number of T2S instructions required to achieve “matching-enrichment-transfers” among HCSD operators for example, for every market executed trade, which is currently done at zero cost to Custodians, will result in additional and substantial Instruction Fees. This will get economically worse in case the matching functions were to take place in T2S;

- the market practice for retail clients (which hold today around 40% of the market capitalisation) of having several Account Operators with different holdings in each of them will prove expensive under the pricing policy of T2S;
- all Corporate Actions that today are handled by the CSD, during night processing, and which appear at the start of day as new balances in the investor accounts will be treated within T2S as Settlement Instructions. Their cost today, in the order of €0.04 per account charged to the issuer, will increase by seven times at least (according to the €0.29 T2S Instruction Cost estimation);
- cost for messages which is today included in the service fee charged by the CSD to us is expected to increase by the related amount of telecommunication cost and message traffic between the CSD and T2S for custodian bank clients in direct holding markets; and
- from official CSD monthly figures, account holdings with a net worth below €3,000 that is about half a million accounts, are not charged by the CSD. Those investors will be required to pay the increased cost due to all of the above reasons. This will in effect distort the business model employed by most local custodians that serve at large extent retail clients and will benefit only large institutional investors.

In effect, the increased local settlement and related cost will off-set any possible reduction in the cross-border settlement cost. Furthermore, if we were to price things accordingly, we expect that it will have a negative impact to the local retail market.

- Possibilities to harmonise the allocation process?

The “allocation-shift-transfer-give up-enrichment-matching” process we believe is idiosyncratic to the direct holding markets which is geared towards the final determination of the “end investor a/c at the CSD level” with the obvious purpose to avoid fails. On the other hand, the omnibus a/c markets deal with tremendously fewer accounts at the CSD level, exploiting internalization within the bank systems, and allow for “different” matching-settlement processes at their CSD level.

We believe the question is not whether the allocation process of the direct holding systems can be harmonised with the T2S instructions but how far the pricing model places the direct holding markets into an economic disadvantage relative to the non-direct holding markets that will employ T2S. Finally, it is also unknown at this moment, how “user friendly” the direct holding simulation at T2S will be and this need to be investigated and resolved too.

Annex III – Comments on the Economic Impact Assessment for T2S

The EBF has long called for a rigorous Economic Impact Assessment (EIA) to allow banks to make a compelling case towards their CSDs for their participation on T2S. However, we leave the detailed comments on the methodology and the scope of the EIA to those institutions that are required to complete the survey.

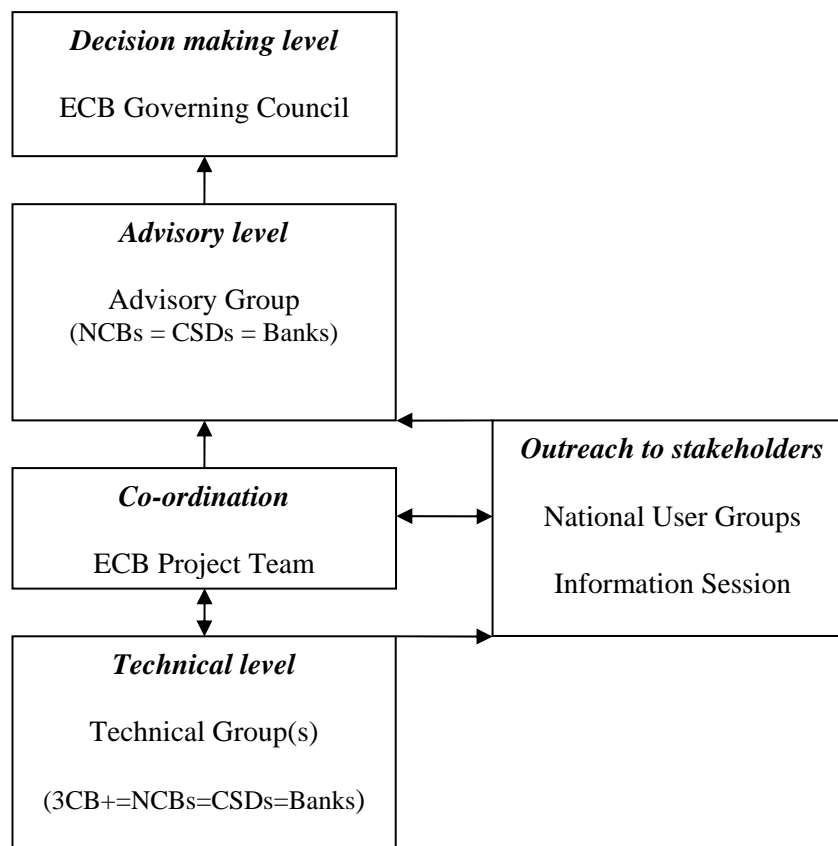
The EBF is generally satisfied with the methodology employed for the Economic Impact Assessment (EIA) for T2S although some questions remain around how practicable it will prove to be to feed with methodology with data to come to a meaningful result. In particular, we consider the projected six year amortisation period to be fair but we suggest that further investment may well be required during or after the initial outlay for fine tuning of the system and/or when additional functionality comes on line. Importantly, we understand the goal of T2S is to have “as close to zero as possible” cost for end-users. We note the figure of €0.29 and would expect that the final figure offered by T2S would not exceed this amount.

Annex IV – Proposals for the governance of T2S in the next stage

The EBF has consistently argued that banks as end-users, or the *de facto* customers for which T2S is to be built, have a strong claim to appropriate representation in the governance throughout the life of the T2S Project. The governance structure deployed for the user requirements phase, where banks have a representation equal to NCBs and CSDs has proven to be an efficient and representative model that has produced sensible and stable outcomes.

In the specification phase decisions advice will have to be submitted and decisions taken, not just in respect of the technical specification of T2S, but also in respect of any subsequent technical modifications to the user requirements. Banks have a strong claim to be represented in the structures governing the debate and the decisions to be taken in relation to these aspects. Therefore, the principles underpinning the model of governance in the current user requirements phase ought to be applied to the governance of the Project in the next specification phase.

Concretely, we propose the following model of governance for the specification phase of T2S:



There are three basic levels to the EBF's proposed governance structure:

- **The decision making level.** This highest level of the ECB's governance architecture has provided stable and sensible outcomes in line with the recommendations of the Advisory Group in respect of T2S to date. We see no need therefore to challenge the current ECB high level governance architecture, which will remain fit for purpose in the next stage.
- **The advisory level.** . Notwithstanding the efficient management of the Advisory Group meetings by the ECB thus far, an issue surrounding the size of the Group remains. Whilst we see scope to streamline the Group by reducing the number of guests in the meeting, the principle of banks having at least equal representation to the CSDs and NCBs must remain.

Solutions will be found among the banking community as to which institutions are to be represented in the future governance structures. However, *a priori* we make the continued case for representation in the governance of those institutions that are either significant, if not leading, players in the European equities business (domiciled within and outside of the Eurozone) and/or associations representative of the sector as a whole to achieve the buy-in of the widest possible number of stakeholders active in the securities business in Europe.

- **The technical level.** This level of governance will be critically important in the specification phase. The "3CB+" which will develop the T2S functionality must be work independently whilst having close links with a Technical Group or Groups. We suggest that the Technical Groups could be reconstituted according to the tasks in hand with suitably skilled professionals drawn from the securities business representing the developers and the owners of the Project (the "3CB+" and the Eurosystem) and the users of T2S (CSDs and banks).

We envisage that the overall co-ordination of the Project would continue to be carried out very effectively by the ECB. One of the main tasks of the Project Team would be to make the link between the technical level and the advisory level whilst also reaching out to the wider community of stakeholders. Stakeholders could submit and exchange views on the progress of the Project with the ECB through the continuation of the National User Groups (where there is sufficient interest) and through the periodic T2S Information Session.