



EUROPEAN CENTRAL BANK

EUROSYSTEM

<b>General Information (Origin of Request)</b> <input checked="" type="checkbox"/> User Requirements (URD) <input checked="" type="checkbox"/> Other User Functional or Technical Documentation (SYS)		
<b>Request raised by:</b> CSDR Task Force	<b>Institute:</b> ECB	<b>Date raised:</b> 23/05/2019
<b>Request title:</b> T2S penalty mechanism: exemption from LMFP on settlement instructions created as a result of partially successful buy-ins		<b>Request ref. no:</b> T2S 0717 URD
<b>Request type:</b> Common	<b>Classification:</b> Regulatory compliance	<b>Urgency:</b> Normal
<b>1. Legal/business importance parameter:</b> Medium		<b>2. Market implementation efforts parameter:</b> Low
<b>3. Operational/Technical risk parameter:</b> Medium		<b>4. Financial impact parameter:</b> Low
<b>Requestor Category:</b> CSDR TF		<b>Status:</b> Implemented

#### Reason for change and expected benefits/business motivation:

The T2S CSDR Task Force was established by the T2S Steering level, in order to identify the necessary changes to the T2S platform resulting from the CSD Regulation (CSDR), with the objective to facilitate T2S CSDs' timely compliance to CSDR.

The core of the work of the T2S CSDR Task Force is reflected in the T2S Penalty Mechanism's user requirements (CR654): it focuses on the daily calculation and reporting of cash penalties for settlement fails, a monthly reporting of the aggregated amounts of cash penalties computed for a given month as well as the operational tools which are necessary for T2S Actors.

Some exemptions from the application of cash penalties are mandated by the CSDR. In the T2S penalty mechanism, these exemptions from cash penalties are performed in two ways:

- Ex ante [prior to the calculation process] on an automated basis by the system, e.g. for Corporate Actions on stock identified by "CORP" ISO transaction type code as these transactions are deemed out of scope of the T2S penalty mechanism;
- Ex post [after the calculation of cash penalties] based on the removal request of already computed cash penalties sent by CSDs.

In the context of discussions around the buy-in process, CSDR TF members have identified a specific scenario whereby:

- (i) A buy-in procedure is triggered, e.g. to deliver 100 securities. The settlement instructions [original transaction] that led to trigger the buy-in are put on [party] hold;
- (ii) The buy-in is initiated by the trading parties but cannot be executed in full, e.g. only 70 securities can successfully be bought in. The resulting instructions for the buy-in for the partial quantity are instructed to T2S. I.e. settlement instructions with 'BYIY' code in the ISO transaction type code (sese.023, Settlement Parameters/Securities Transaction Type/Code) and with ISD equal to the business day when they are entered in T2S. Upon successful settlement of the buy-in for the partial quantity, the settlement instructions [original transaction] that led to trigger the buy-in are cancelled<sup>1</sup>;
- (iii) New settlement instructions with the same ISO transaction type code as the one of the original transaction must be entered by both parties to settle the remaining quantity, i.e. 30 securities.

As per CSDR requirements, Article 16.3 of Commission Delegated Regulation (EU) 2018/1229, where settlement instructions are entered into a securities settlement system as a result of a partially successful buy-in, cash penalties shall only apply as from the day those instructions are entered into the securities settlement system.

The initial assumption from the CSDR TF was that, similarly to the settlement instructions of the buy-in, also the new settlement instructions resulting from the partially successful buy-in can contain the ISD of the business day they are entered in T2S to avoid undue computation of cash penalties.

<sup>1</sup> The cancellation instruction message, sese.020, is populated with the cancellation reason code BYIY that will be added with CR-688

However, following further interactions with market participants, CSDR TF members are of the view that the new settlement instructions should be entered with the same ISD as the one of the original transaction, in order to avoid operational complexities for the processing of corporate actions and to facilitate reconciliation.

As a result, after a partially successful buy-in, when the new settlement instructions for the remaining quantity would be entered in T2S with the ISD of the original transaction, an undue Late Matching Fail Penalty (LMFP) would be computed by T2S for the business days between the ISD of the original transaction and the business day the settlement instructions are entered. Upon reporting of such cash penalties, CSD participants should appeal to their CSD and request an ex post removal of the relevant LMFP. Depending on the volume of cash penalties that would fall under this scenario, this could represent an operational burden.

The CSDR TF has identified a proposal to automate such exemption and the T2S penalty mechanism logic would be updated as follows:

- If both settlement instructions of a transaction contain the buy-in code 'BSSP' in the Settlement Transaction Condition<sup>2</sup> the T2S penalty mechanism shall not compute LMFP for those instructions because they are resulting from a partially successful buy-in i.e. instructed for the remaining quantity to be settled.

It is worth mentioning that the above update does not have any impact on Settlement fail penalties (SEFP). SEFP shall be computed normally for settlement instructions resulting from a partially successful buy-in.

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**Description of requested change:**

## Chapter 22 Computation and Maintenance of Cash Penalties

### 22.4.2 Late Matching Fail Penalty (LMFP)

#### Eligibility of instructions resulting from a partially successful buy-in

Reference ID	T2S.22.172
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T2S shall not compute Late Matching Fail Penalties for a transaction when both matched settlement instructions sent by T2S Actors are populated with the 'BSSP' settlement transaction condition code (sese.023, Settlement Parameters/Settlement Transaction Condition).

Note: This requirement is meant to address the case of a partially successful buy-in where the settlement instructions entered for the remaining quantity to be delivered contain the ISD of the original transaction.

Note: the above process should not be confused with the initiation / creation of a buy-in instruction whereby the sese.023 is populated with the 'BYIY' code in the ISO transaction type code (sese.023, Settlement Parameters/Securities Transaction Type). In that case, T2S shall compute SEFP/LMFP as for any other instruction in scope.

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#### Submitted annexes / related documents:

The following Change Requests are a prerequisite for CR 717

-CR 654: T2S Penalty Mechanism:

<https://www.ecb.europa.eu/paym/target/t2s/governance/pdf/crg/T2S-0654-URD.pdf>

-CR 713: Alignment of T2S Messages with ISO Standards Release 2018 – 2019 and migration to ISO registered versions:

<https://www.ecb.europa.eu/paym/target/t2s/governance/pdf/crg/T2S-0713-SYS.pdf>

[-CR 728: T2S must be able to identify, store, and report settlement information related to settlement instructions created as a result of partially successful buy-in:](#)

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<sup>2</sup> In a first step, the field will be informed as a proprietary code in the sese.023 (SciesStlmTxInstr/StlmParams/StlmTxCond/Prtry/Id), but in the medium term an ISO CR will be raised by 4CB to make it as a standard transaction condition code (SciesStlmTxInstr/StlmParams/StlmTxCond/Cd), as documented in CR728.

**Proposed wording for the Change request:**

**GFS**

3.4.7.3 Description of the functions of the module

(...)

**1- Penalty Eligibility**

**LMFP Penalty Eligibility**

<u>Reference Id</u>	<u>LCMM.PEM.ELI.4.1</u>
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(...)

For each *Penalty Eligibility* instance created, the sub-function determines its Eligible for Penalty attribute as follows:

- | If the underlying *Settlement Instruction* has ISO transaction code "CORP", the Eligible for Penalty is set to "False" and the Reason for Exemption to "ISOT" (i.e. ISO Transaction Code) **{T2S.22.050}**.
- | If the underlying *Settlement Instruction* has Settlement Transaction Condition Code "BSSP", the Settlement Transaction Condition Code of the counterparty Settlement Instruction is checked. If it is "BSSP" too, then the Eligible for Penalty is set to "False" and the Reason for Exemption to "BSSP" **{T2S.22.172}**.
- | Otherwise, the counterparty's *Settlement Instruction* is retrieved through the *Matching Object* and:

(...)

**UDFS:**

**1.6.1.14.4. Penalty Eligibility**

Every business day, T2S analyses the failed Matched Settlement Instructions from the previous business day in order to see if they are eligible for penalties.

(...)

**Eligibility for a Late Matching Fail Penalty (LMFP)**

To determine whether a Settlement Instruction is eligible for a Late Matching Fail Penalty (LMFP) or not, T2S retrieves the Settlement Instructions with Intended Settlement Date equal or earlier than the previous business day and that were matched on the previous business day. I.e.:

- I Matched Settlement Instructions having i) an Intended Settlement Date equal or earlier than the previous business day and ii) a Matching Timestamp between the previous business day Start and End Timestamps.

T2S analyses separately each instruction retrieved, and:

- I Settlement Instructions automatically generated by T2S for realignment purposes are discarded, as they are out of scope of the T2S Penalty Mechanism;
- I Settlement Instructions with ISO Transaction Code "CORP" (related to Corporate Actions on Stock) are exempted, as they are not subject to penalties;
- I Settlement Instructions with Settlement Transaction Condition "BSSP" (resulting from a partially successful buy-in i.e. instructed for the remaining quantity to be settled) and whose counterparty Settlement Instruction also have Settlement Transaction Condition "BSSP", are exempted; i.e. Settlement Instruction won't be exempted if its counterparty Settlement instruction does not have Settlement Transaction Condition "BSSP".

For the rest of Settlement Instructions T2S checks if they were matched late. For this purpose T2S verifies the following conditions:

(...)

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**Outcome/Decisions:**

- \* CRG on 8 October 2019: The CRG requested the preliminary assessment of the updated version of CR-717.
- \* CRG on 27 November 2019: The CRG agreed to recommend CR-717 for authorisation by the T2S Steering Level.
- \* AMI-SeCo on 6 December 2019: The AMI-SeCo concluded to agree to the recommendation of the CRG to propose the CR for CSD/NECSD authorisation.
- \* CRG on 22 January 2020: The CRG took note of the changes made to CR-717 to reflect that a large part of its scope had been integrated in the fast-track CR-728. CRG members agreed to recommend the updates CR-717 for authorisation by the T2S Steering Level.
- \* PMG on 23 January 2020: The PMG recommended the CR for approval by the T2S Steering Level and its inclusion in R5.0.
- \* CSDR on 28 January 2020: The CSDR Task Force was informed of the adjusted CR scope and indicated that from their perspective the target release should be R5.0.
- \* OMG on 30 January 2020: The OMG completed the operational assessment of the CR.
- \* PMG on 31 January 2020: The PMG agreed to launch the detailed assessment in view of R5.0.
- \* CSG on 5 February 2020: The CSG authorised CR-717 for allocation to T2S R5.0.
- \* NECSG on 10 February 2020: The NECSG authorised CR-717 for allocation to T2S R.5.0.

- \* MIB on 13 February 2020: The MIB authorised CR-717 for ranking by the CRG and allocation to a T2S release without discussion.
- \* CRG on 23 April 2020: The CRG took note of the detailed assessment and agreed to recommend the CR717 for Release 5.0 to the PMG.
- \* OMG on 11 May 2020: the OMG did not identify an operational impact for CR-717.
- \* PMG on 28 May 2020: the PMG recommended to the Steering Level the inclusion of the CR in the scope of R5.0.
- \* CSG on 9 June 2020: The CSG approved the inclusion of the CR in the scope of R5.0.
- \* MIB on 15 June 2020: The MIB approved the inclusion of the T2S CR in the scope of R5.0.
- \* CRG on 17 September 2020: the CRG agreed to updates of the wording of the scope defining documents for CR-717.
- \* AMI-SeCo on 16 October 2019: The AMI-SeCo agreed with the recommendation of the CRG.
- \* CSG on 25 October 2019: The CSG authorised the CR for allocation to a T2S release.
- \* NECSG on 28 October 2019: The NECSG authorised the CR for allocation to a T2S release.
- \* MIB on 8 October 2019: The MIB authorised CR-690.
- \* PMG on 23 January 2020: The PMG asked the 4CB to launch the detailed assessment of CR-690 in view of R5.0.
- \* OMG on 11 May 2020: the OMG did not identify an operational impact for CR-690.
- \* PMG on 28 May 2020: the PMG recommended to the Steering Level the inclusion of the CR in the scope of R5.0.
- \* NECSG on 10 June 2020: the CSG approved the allocation of the CR to R5.0.
- \* CSG on 18 June 2020: the CSG approved the allocation of the CR to R5.0.
- \* MIB on 9 July 2020: The MIB approved the inclusion of the CR in R5.0.
- \* CRG on 17 September 2020: the CRG agreed to corrections of the wording of the scope defining documents of CR-690.
- \* OMG on 29 September 2020: The OMG confirmed their earlier operational assessment of CR-717.

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**Preliminary assessment:**

- **Impact:** medium
- **Impacted modules:** LCMM, INTF, SDMG, DMT, SETT msg
- **Findings:**

4CB assumption is that the Penalty LMFP Eligibility Process will only perform the check of the Settlement Transaction Condition, i.e., if both Settlement Instructions of a transaction contain the buy-in code "BSSP" in the Settlement Transaction Condition (*sese.023 -SctiesStlmTxInstr/StlmParams/StlmTxCond/Prtry/Id*), both are exempted from LMFP Penalties.

Element *SctiesStlmTxInstr/StlmParams/StlmTxCond/Prtry/Id* will be unpruned in *sese.023* ISO 20022 message, and limited to BSSP value (i.e. no other values are allowed).

*SctiesStlmTxInstr/StlmParams/StlmTxCond/Prtry/Issr* will be limited to the fixed value "T2S".

In U2A the user will input the value BSSP as a Securities Transaction Condition Code, i.e., no Proprietary field will be enabled. However, BSSP will be reported as Proprietary in the related A2A outbound messages. The same behavior will be implemented for the DMT.

It is also our assumption that the new code "BSSP" is included as a possible value in the messages related to Settlement Instructions originated by T2S, i.e. *sese.024*, and *sese.025*, *sese.028*. If the new code will also be reported in query, responses and/or reports (and flat files) will be analysed during Detailed Assessment. In any case, the "BSSP" will not be allowed as a query criteria.

Flat files and messages related to penalties (i.e. *semt.044*) won't include the Settlement Transaction condition, for possible SEFP that could be imposed on Settlement Instructions with the buy-in code "BSSP" in the Settlement Transaction Condition.

The new BSSP transaction code does not require a dedicated privilege to be used (as is the case for other Securities Transaction Condition Code). Condition / authorisation to be exempted is only based on the fact that the two counterparties include the code BSSP in their instructions.

- **Open issues/ questions to be clarified by the originator:**  
None

EUROSYSTEM ANALYSIS – GENERAL INFORMATION			
T2S Specific Components		Common Components	
<b>LCMM</b>			
	Instructions validation		
	Status management		
	Instruction matching		
	Instructions maintenance		
X	Penalty Mechanism		
<b>Settlement</b>			
	Standardisation and preparation to settlement		
	Night-time Settlement		
	Daytime Recycling and optimisation		
	Daytime Validation, provisioning & booking		
	Auto-collateralisation		
<b>Liquidity Management</b>			
	Outbound Information Management		
	NCB Business Procedures		
	Liquidity Operations		
<b>T2S Interface</b> (as of June 2022 without Static Data Management, Communication for SDMG, Scheduler, Billing)			
	Communication		
	Outbound Processing		
	Inbound Processing		
<b>Static Data Management</b> (until Nov 2021)		<b>Common Reference Data Management</b> (from PROD R6.0 June 2022)	
	Party data management		Party data management
	Securities data management		Securities data management
	Cash account data management		Cash account data management
	Securities account data management		Securities account data management
	Rules and parameters data management		Rules and parameters data management
<b>Statistics and archive</b>		<b>Statistics and archive</b>	
	Statistical information (until June 2022)		Short term statistical information
	Legal archiving (until June 2022)		Legal archiving (from PROD R6.0)
			Data Warehouse (from PROD R6.0)
<b>Information</b> (until June 2022 containing reference data)		<b>CRDM business interface</b> (from PROD R6.0 June 2022)	
	Report management		Report management
	Query management		Query management
			Communication
			Outbound Processing
			Inbound Processing
<b>Operational Services</b>			
	Data Migration (T2S DMT)		Data Migration (CRDM DMT, from PROD R6.0)
	Scheduling (until Nov 2021)		Business Day Management (from PROD R6.0)

		Business Day Management business interface (from PROD R6.0)
	Billing (until June 2022)	Billing (from PROD R6.0)
		Billing business interface (from PROD R6.0)
	Operational Monitoring	Operational and Business Monitoring

Impact on major documentation		
Document	Chapter	Change
Impacted GFS chapter	3.4.7.3 1-Penalty Eligibility	Describe how, when both Settlement Instructions of a transaction contain the buy-in code "BSSP" in the Settlement Transaction Condition, both are exempted from LMFP Penalties.
Impacted UDFS chapter	1.6.1.14.4. Penalty Eligibility	Add that, when both Settlement Instructions of a transaction contain the buy-in code "BSSP" in the Settlement Transaction Condition, both are exempted from LMFP Penalties.
Links with other requests		
Links	Reference	Title
OVERVIEW OF THE IMPACT OF THE REQUEST ON THE T2S SYSTEM AND ON THE PROJECT		
Summary of functional, development, infrastructure and migration impacts		
<p>The Penalty Eligibility process is adjusted in a way that, when both Settlement Instructions of a transaction contain the buy-in code "BSSP" in the Settlement Transaction Condition, both are exempted from LMFP Penalties.</p> <p>The Penalty LMFP Eligibility Process needs to be adjusted so:</p> <ul style="list-style-type: none"> <li>- It will perform the check of the Settlement Transaction Condition of the Settlement Instruction: if it contains the buy-in code "BSSP", then</li> <li>- It will retrieve the Counterparty's Settlement Instruction, and check if it contains the buy-in code "BSSP" in the Settlement Transaction Condition</li> <li>- If both Settlement Instructions contain the buy-in code "BSSP" in the Settlement Transaction Condition, both are exempted from LMFP Penalties.</li> </ul> <p>Penalty testing required to check the exemption is correctly performed. Regression test for the Penalty Eligibility process required.</p> <p><b>Main cost drivers:</b></p> <ul style="list-style-type: none"> <li>- The eligibility process for LMFP has to be adjusted to be able to exempt partial buy in instructions by checking the settlement transaction condition informed in settlement instructions</li> </ul> <p>The changes described in this Change Request do not impact TIPS and the CSLD and ECMS projects.</p>		
Summary of project risk		
n.a.		
Security analysis		
No adverse effect has been identified during security assessment.		



08 April 2020

## Cost assessment on Change Requests

<b>T2S-717-SYS – T2S penalty mechanism: exemption from LMFP on settlement instructions created as a result of partially successful buy-ins</b>			
One-off	Assessment costs*		
	- Preliminary	2,000.00	Euro
	- Detailed	10,000.00	Euro
One-off	Development costs	31,837.72	Euro
Annual	Operational costs		
	- Maintenance costs	3,044.92	Euro
	- Running costs	0.00	Euro

\*The relevant assessment costs will be charged regardless of whether the CR is implemented (Cf. T2S Framework Agreement, Schedule 7, par. 5.2.3).