Commission Delegated Regulation (EU) 2018/1229 of 25 May 2018 supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council with regard to regulatory technical standards on settlement discipline (Text with EEA relevance)

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(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012[(1)], and in particular Article 6(5) and Article 7(15) thereof,

Whereas:

(1) The provisions in this Regulation are closely linked, since they deal with measures to prevent and address settlement fails and to encourage settlement discipline, by monitoring settlement fails, collecting and distributing cash penalties for settlement fails and by specifying the operational details of the buy-in process. To ensure coherence between those provisions, and to facilitate a comprehensive view of and a compact access to them by persons subject to the obligations, it is appropriate to include them in a single Regulation.

(2) In view of the global nature of financial markets, due regard should be given to the Principles for Financial Market Infrastructures, which have been issued by the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions ('CPSS-IOSCO Principles') in April 2012 and which serve as a global benchmark for regulatory requirements for central securities depositories ('CSDs'). The Recommendations for Securities Settlement Systems, issued by the Committee on Payment and Settlement Systems and the International Organisation of Securities Commissions, covering trade confirmation, settlement cycles, and securities lending, should also be taken into account.

(3) In order to ensure the consistent application of Regulation (EU) No 909/2014 and to specify the technical terms necessary to apply this Regulation, a number of terms should be defined.

(4) Investment firms should ensure that they have all the necessary settlement information in time to allow for an effective and efficient settlement of transactions. In particular,

Changes to legislation: *There are currently no known outstanding effects for the Commission Delegated Regulation (EU) 2018/1229. (See end of Document for details)*

investment firms that do not have the necessary settlement information should communicate with their clients to obtain the information relevant for an efficient settlement, including the standardised data needed for the settlement process.

(5) Straight-through processing ('STP') should be encouraged, since market-wide use of STP is essential both for maintaining high settlement rates as volumes increase and for ensuring timely settlement of cross-border trades. Moreover, both direct and indirect market participants should have the internal automation in place that is necessary to take full advantage of the available STP solutions. In this respect, investment firms should offer their professional clients the possibility of sending confirmations and allocation details electronically, in particular by using international open communication procedures and standards for messaging and reference data. Furthermore, CSDs should facilitate STP and, when processing settlement instructions, should use processes designed to work on an automated basis by default.

(6) CSDs should offer matching possibilities throughout the day to promote early settlement on the intended settlement date.

(7) CSDs should require that participants to their securities settlement systems use a list of mandatory matching fields for the matching of settlement instructions to facilitate settlement and to ensure consistency across securities settlement systems.

(8) CSDs should have sound and efficient system functionalities, policies and procedures that enable them to facilitate and incentivise settlement on the intended settlement date.

(9) CSDs should provide participants with real-time access to information on the status of their settlement instructions in the securities settlement systems they operate to encourage and incentivise timely settlement by those participants.

(10) CSDs should offer real-time gross settlement to participants to their securities settlement systems, or at least several daily settlement possibilities throughout every business day in order to complete final settlement intraday.

(11) The obligation on CSDs to have system functionalities should depend on the settlement efficiency of those CSDs. Certain system functionalities should therefore not be compulsory if the value and the rate of settlement fails in the securities settlement system operated by a CSD do not exceed certain predefined thresholds.

(12) To facilitate the monitoring of settlement fails, CSDs should use a harmonised methodology to report settlement fails to the competent authorities and the relevant authorities. That methodology should cover a common list of items to be reported as well as the frequency of the reports to be delivered. Settlement instructions entered into the securities settlement system operated by CSDs should be monitored each day until they are settled or cancelled.

(13) CSDs should set up working arrangements with the participants that have the highest rates of settlement fails, as well as, if feasible, with relevant central counterparties ('CCPs') and trading venues, in order to identify the main reasons for settlement fails.

(14) CSDs should send monthly reports on settlement fails to their competent authorities and relevant authorities. Competent authorities should also be entitled to request additional

information on settlement fails or more frequent reporting as necessary so that they can perform their tasks. Such additional information or reports should be shared by the requesting competent authorities with the relevant authorities without undue delay.

(15) To promote transparency and facilitate the comparability of settlement fails across the Union, CSDs should use a single template for disclosing settlement fails data to the general public.

(16) To ensure the consistent application of requirements on settlement discipline for CSDs, detailed provisions should be set out concerning the identification of all transactions that remain unsettled after the intended settlement date, the implementation of the buy-in process where applicable, and the application of the penalty mechanisms established by a CSD, including the time of calculation and the collection and distribution of cash penalties.

(17) Rules regarding the processes for the collection and distribution of cash penalties for settlement fails should be applied in coherence with the Commission Delegated Regulation (EU) 2017/389[(2)].

(18) To ensure that cash penalties for settlement fails are applied consistently, CSDs should charge, collect and distribute cash penalties on a regular basis and at least once a month. In addition, to ensure that their risk profile is not affected by the operation of the penalty mechanism, including where penalties are not paid as required by failing participants, CSDs should only be responsible for charging, collecting and distributing those cash penalties. Since a participant may also act as an agent for his clients, CSDs should provide participants with sufficient details regarding the penalty calculation to enable them to recover the cash penalty from their clients.

(19) It is important that the cash penalty levied in the event of a settlement fail does not constitute a source of revenue for CSDs. The cash penalty should therefore be paid into a separate account of the CSD, which should be used exclusively for the collection and distribution of those penalties. The penalties collected should not be used to finance the implementation, maintenance or operation of the penalty mechanism.

(20) In certain cases, a transaction may be part of a chain of transactions, in which case a settlement instruction may depend on another one and the settlement of one instruction may allow for the settlement of several instructions in that chain. The failure of one settlement instruction may thus have knock-on effects, resulting in the failure of subsequent settlement instructions.

(21) To limit the number of cash transfers, CSDs should, therefore, net the amount due to participants against the amount to be paid by those participants and should ensure that the full amount of cash penalties is appropriately distributed within the settlement chain to those participants that suffered from the settlement fail. CSDs should provide participants sufficient information on the calculation of the amounts to be received to enable those participants, where appropriate, to transfer the amounts due to their clients.

(22) The penalty mechanism should apply to all failed transactions, including cleared transactions. Where the failing participant is a CCP, however, the penalty should not be due by that CCP, but by the relevant clearing member that caused the settlement

fail. For that purpose, CSDs should provide CCPs with all the necessary information on the settlement fail and the calculation of the penalty to enable CCPs to charge a penalty to the relevant clearing member and to distribute the collected amount to the clearing member that suffered from the subsequent settlement fail on the same financial instruments.

(23) CSDs using a common settlement infrastructure should work closely together to ensure the appropriate implementation of the penalty mechanism.

(24) In order to support an integrated market for securities settlement, the buy-in process should be harmonised. Given the importance of incentivising timely actions to address settlement fails, it is important to keep all relevant involved parties informed during the buy-in process.

(25) A settlement instruction may fail for all financial instruments included in that instruction, even if some financial instruments are available for delivery in the account of the failing participant. The purpose of a buy-in process is to improve settlement efficiency. In order to minimise the number of buy-ins, a buy-in process should be subject to the mandatory application of partial settlement to the relevant settlement instruction.

(26) Mandatory partial settlement on the last business day of the extension period referred to in Article 7(3) of Regulation (EU) No 909/2014 strikes the right balance between the rights of the buyer to receive the financial instruments bought and the need to minimise the number of financial instruments subject to buy-in. Every bought-in financial instrument should therefore be delivered to the buyer, even if the number of bought-in financial instruments does not allow for the full settlement of the relevant settlement instruction.

(27) Mandatory partial settlement should not apply to settlement instructions that have been put on hold by a participant, because the relevant financial instruments in the respective account may not belong to the client for which the settlement instruction has been entered into the securities settlement system.

(28) To ensure compliance with the obligations set out in Regulation (EU) No 909/2014, all parties in the settlement chain should have contractual arrangements with their relevant counterparties which contain the buy-in process obligations and which are enforceable in all relevant jurisdictions.

(29) In order to improve settlement efficiency, it should always first be verified whether a buy-in process is possible in respect of the relevant transactions and parties thereto.

(30) All entities involved in the buy-in process need to be informed of the status of the buy-in process at key points in time. That information should be exchanged by way of a notification in order for the entities involved to be alerted on the status of the actions to settle the transaction and take further action as need be.

(31) For transactions that are not cleared by a CCP, in order to set up an efficient buy-in process and to avoid that other parties in the settlement chain or participants become liable for obligations contracted by the trading venue members or trading parties, and in

order not to increase the risk profile of CSDs or trading venues, the parties that originally concluded the relevant transaction should be responsible for the execution of the buy-in.

(32) In respect of the settlement of a securities transaction, participants act for their own account or enter settlement instructions into the securities settlement system operated by a CSD upon request by their clients. Those clients may be a CCP and its clearing members, trading venue members or, where the transaction is not executed on a trading venue, trading parties. A buy-in should therefore be effected at the level where the contractual obligations to buy and sell securities have been created.

(33) Given that the buy-in agent should act upon request of a party that does not bear the costs related to the buy-in agent's intervention, the buy-in agent should act according to best execution requirements and protect the interest of the failing clearing member, trading venue member or trading party.

(34) To limit the number of buy-ins and to preserve the liquidity of the market for the relevant financial instruments, the failing clearing member, the failing trading venue member or the failing trading party, as applicable, should be allowed to deliver financial instruments to the CCP, the receiving trading venue members or the receiving trading parties through their participants up to the moment that they are informed that the buy-in agent has been appointed or that an auction has been launched. From that point in time, those parties should only be able to take part in the auction of the financial instruments or to deliver them to the buy-in agent, subject to his prior approval, so as to avoid that the receiving clearing member, the receiving trading venue member or the receiving trading party receives the financial instruments twice. Parties involved in the buy-in process could also limit the number of buy-ins by coordinating their actions amongst themselves, and informing the CSD thereof, where a transaction is part of a chain of transactions and may result in different settlement instructions.

(35) Transactions not cleared by a CCP are generally uncollateralised and therefore each trading venue member or trading party bears the counterparty risk. Moving this risk to other entities such as their participants would force the latter to cover their exposure to counterparty risk with collateral. This could lead to increased costs of securities settlement in a disproportionate manner. The failing clearing member, the failing trading venue member or the failing trading party, as applicable, should therefore bear responsibility for the payment of the buy-in costs, the price difference and the cash compensation in the first place. Where the failing trading venue member or failing trading party do not comply with their obligation to pay those amounts, their participant, as the failing participant, should, however, cover the buy-in costs and the price difference but not the cash compensation.

(36) Delivery obligations of bought-in financial instruments or the payment of cash compensation or of any price difference in the financial instruments subject to buy-in should ultimately be performed through the reception of the relevant financial instruments or cash by the CCP, the receiving trading venue members or the receiving trading parties through their participants.

(37) Where the buy-in fails and in the absence of express communication on whether to extend the buy-in period within the prescribed timeframe, cash compensation should