

## INTRODUCTION

Interbolsa – Sociedade Gestora de Sistemas de Liquidação e de Sistemas Centralizados de Valores Mobiliários, S.A. (“Interbolsa”), which is the Portuguese CSD part of Euronext Group, welcomes ESMA’s second consultation to collect additional data from market participants on the operation of buy-in processes, focusing mainly on which entity shall be responsible for operating the buy-in process for OTC transactions that are not centrally cleared.

We also welcome ESMA’s current position, considering that CSDs and trading venues should continue not to be involved in the execution of buy-ins (only transmitting the necessary information).

Moreover, and considering the draft Technical Standards contained in Annex 2 of the Consultation Paper, we believe that the revised standards constitute a considerable improvement compared to the initial draft published in December 2014. We believe they can form the basis of a more workable process for buy-ins under the CSD Regulation.

After analysis of the 3 options proposed in this consultation paper, we consider that option 1, whereby buy-ins are fully managed by the trading counterparties and CSDs and their participants are not required to play an active role, is the suitable course of action.

**Q1: Please provide evidence of how placing the responsibility for the buy-in on the trading party will ensure the buy-in requirements are effectively applied. Please provide quantitative cost-benefit elements to sustain your arguments.**

In our response to the December 2014 consultation paper we defended a solution whereby the trading party is responsible for the buy-in (like option 1). This is because we consider that the trading parties are the only parties that have all the information needed to apply the buy-in rules, namely the reason for the fail, the nature of the transaction and the counterparties. CSDs participants do not have this information.

In relation to the identified weaknesses attributed to option 1, we believe that most of them apply to all 3 options, namely the fact that a strong contractual framework between CSD participants and their clients including the trading counterparties should be set up through the intermediaries chain in order to enforce this option.

On the other hand, we believe that CSD participants and all parties in the chain have incentives to protect themselves via appropriate contractual arrangements if they do not want to be liable towards the other parties for fails caused by their own underlying clients and, also, to be compliant with their own internal compliance rules. We also believe that there is sufficient incentive to ensure proper credit and operational risk management, including where relevant, tightening up/ removing manual processes and collateralizing or pre-funding any perceived exposure.

We consider that the difficulty to implement Option 1 (if any) can arise from the need to set up a harmonised and efficient information and notification flow through the chain of intermediaries from the CSD participants to the trading counterparties. This situation is still inconsistent across the

industry and we believe it is important for all parties to use, as much as possible, electronic matching, confirmations and affirmation systems. CSDs can help in this regard. Currently, CSDs already disclose a lot of information to their participants and this can and should be disclosed to their clients further down the chain of intermediaries to the original counterparties, which are not known to the CSD.

In addition, and considering the fact that information regarding buy-ins should be provided to the regulators, we want to highlight that this obligation may be fulfilled by CSDs if and only if CSDs are timely and consistently informed about the initiation of the buy-in process.

In this context, CSDs should not be liable for information that they cannot check or cross-check insofar as it is transmitted by others (CSDs participants that received the information through the intermediation chain). Only the entity that is first providing the buy-in information that has to be disclosed to regulators should be responsible for its accuracy.

**Q2: Please indicate whether the assumption that the trading party has all the information required to apply the buy in would be correct, in particular in cases where the fail does not originate from the trading party, but would rather be due to a lack of securities held by one of the intermediaries within the chain.**

As referred to above in our response to Q1, we reiterate that the trading parties that entered into the transaction which failed to settle, as the parties at the origin of the transaction, are the only parties in the intermediary chain that will have all the relevant and necessary information to initiate and execute the buy-in, namely the reason for the fail, the nature of the transaction and its counterparties.

**Q3: Should you believe that the collateralisation costs attached to this option are significant, please provide detailed quantitative data to estimate the exact costs and please explain why a participant would need to collateralise its settlement instructions under this option.**

Option 2 would imply that the trading party is responsible for the buy-in but the CSD participant should be responsible for paying the cash compensation in case the trading party does not perform the buy-in.

We believe that in this situation, and in order to cover the risk of default of the trading party that cannot be sufficiently mitigated by the arrangements in place with its clients, the participant might need to collateralize that risk, increasing, as such, the cost to the clients.

With regards to the collateral costs associated with this Option we believe this is best answered by risk managers at trading party or CSD participant.

**Q4: If you believe that option 1 (trading party executes the buy-in) can ensure the applicability of the buy-in provisions are effectively applied, please explain why and what are the disadvantages of the proposed option 2 (trading party executes the buy-in with**

**participant as fall back) compared to option 1, or please evidence the higher costs that option 2 would incur. Please provide details of these costs.**

We consider that the main difference between option 1 and option 2 (and also option 3) is the need for collateralization in Option 2 so that CSD participants can cover the associated settlement risk.

We believe that these collateral requirements will have, for sure, an adverse impact on market efficiency, certainly increasing the cost of settlement.

Furthermore, we believe that the analysis regarding the impact of option 2 and option 3 should seriously consider the impact on the links established or to be established between CSDs (namely because of the T2S project), and more effectively the impact of such options when CSDs will act as investor CSD (acting as a normal CSD participant). We believe that those options will increase the CSD's risk profile and liabilities and will dis-incentive cross-CSD links. The investor CSD (as a participant in another CSD) can be required to enter in the buy-in process (if the participants for which the CSD maintains securities via the link does not deliver securities on time) by paying the cash compensation, if the trading party does not perform the buy-in (option 2) or executes itself the buy-in (under option 3). In this context, the Investor CSD will have to request collateral from its participants (like a CCP), having thus a negative impact on the links established or to be established and on the cost of cross-border transactions.

While the above is relevant to all instruments covered by the consultation, it is particularly important for ETF markets in Europe which are already negatively affected by cross-border settlement fragmentation.

**Q5: Please provide detailed quantitative evidence of the costs associated with the participant being fully responsible for the buy in process and on the methodology used to estimate these costs.**

In Option 3 the CSD participant is responsible for the buy-in process, and also for the cash compensation if and when buy-in is not possible.

In what concerns the costs associated with the participant being fully responsible for the buy-in, we believe that CSDs are not best placed to answer this question.

Nevertheless, we agree with ESMA's analysis that this option the costs of the buy-in process would be significantly increased. This is because participants, being always responsible for the execution of the buy-in, would need to require collateral from their clients in order to protect themselves against the risk of paying the costs of the buy-in. We believe that, in this situation, CSD participants will require full collateralization of settlement instructions.

In light of these considerations, option 3 will make settlement activity in Europe fully collateralized (at least to SD +4), very complex and extremely uncompetitive.