5 October 2023
ESMA74-2119945925-1689

# Reply form

## on the call for evidence on shortening of the settlement cycle

## Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

- respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by **15 December 2023.**

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

## Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

- Insert your responses to the questions in the Consultation Paper in this reply form.
- Please do not remove tags of the type < ESMA_QUESTION_SETT_0>. Your response to each question has to be framed by the two tags corresponding to the question.
- If you do not wish to respond to a given question, please do not delete it but simply leave the text "TYPE YOUR TEXT HERE" between the tags.
- When you have drafted your responses, save the reply form according to the following convention: ESMA_CP1_SETT _nameofrespondent.

  For example, for a respondent named ABCD, the reply form would be saved with the following name: ESMA_CP1_SETT _ABCD.
- Upload the Word reply form containing your responses to ESMA's website (**pdf documents will not be considered except for annexes**). All contributions should be submitted online at *www.esma.europa.eu* under the heading *'Your input - Consultations'.*

## Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

## Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Data protection'.

## Who should read this paper?

All interested stakeholders are invited to respond to this consultation paper. In particular, ESMA invites market infrastructures (CSDs, CCPs, trading venues), their members and participants, other investment firms, issuers, fund managers, retail and wholesale investors, and their representatives to provide their views to the questions asked in this paper.

# 1 General information about respondent

| | |
|---|---|
| Name of the company / organisation | Associazione Intermediari Mercati Finanziari - ASSOSIM |
| Activity | Associations, professional bodies, industry representatives |
| Are you representing an association? | ☒ |
| Country / Region | Italy |

# 2 Questions

**Q1 : Please describe the impacts on the processes and operations from compressing the intended settlement date to T+1 and to T+0. Please:**

(i) provide as much detail as possible on what issues would emerge in both cases and how they could be addressed with special attention to critical processes (matching, allocation, affirmation and confirmation) and interdependencies. Where relevant please explain if these are general or asset class/instrument/ trade specific.

(ii) Identify processes, operations or types of transaction or financial instrument class that would be severely impacted or no longer doable in a T+1 and in a T+0 environment.

**Please, suggest if there are legislative or regulatory actions that would help address the problems. Where relevant please explain if these are general or asset class/instrument/ trade specific.**

<ESMA_QUESTION_SETT_1>

As a preliminary remark, our members believe that the possibility of compressing the ISD to T+0 is not a viable option at this point in time. In fact, should the compression to T+1 be decided, then this would entail great challenges for the financial industry. A further shortening of the settlement cycle to T+0 would exacerbate the difficulties which our members already foresee with respect to a possible T+1 scenario. Indeed, a T+0 settlement cycle would entail drastic changes to the current pre- and post-trade processes, and it could result in additional risks for the system.

Furthermore, our members are of the opinion that it is premature to comment on the potential impact of a move to T+0 also because the benefits/costs of reducing the cycle to T+1 are not clear and evident at this stage. Therefore, the following analysis and considerations will focus exclusively on the reduction of the settlement cycle to T+1.

Our members expect that in such scenario the main issues would not relate to the settlement process *per se* but to the relevant processes that must take place before settlement occurs. All settlement-related phases (allocation/trade confirmation/matching/settlement confirmation) would be affected by the shortening of the settlement cycle to T+1, albeit at different levels.

In our members' opinion, allocation would be the most critical phase because allocation processes are not standardised across the EU. In addition, issues are envisaged with regard to trade confirmation given that data enrichment tools are not granular enough to have trade confirmations ready for a T+1 settlement.

The aforementioned lack of standardisation prevents intermediaries from automating and speeding up the aforementioned processes, forcing them to manual interventions which, currently and not without difficulty, are carried out within two days after the trading phase. Reducing the settlement cycle by one day would complicate the performance of manual interventions, increase the risk of errors and, consequently, the number of settlement failures. In addition to the above, unlike in the US, the high number of EU CSDs (entailing misaligned procedures, timing, operating models, and cut-offs) further complicates the situation. It is also for this reason that our members believe that the framework outlined above makes a move to T+1 disadvantageous, in terms of settlement efficiency, for the European financial system.

In other words, an implementation of T+1 might be feasible only once settlement efficiency has improved together with a higher level of standardisation and harmonisation so to address operational issues which currently result in late settlement. In order to improve settlement efficiency, our members would suggest promoting a greater use of partial settlement by CSDs.

Finally, our members believe it is essential to set up an expert group with a specific mandate to provide input for the development of an impact assessment/feasibility study on the move to T+1 and a roadmap/detailed implementation plan.

<ESMA_QUESTION_SETT_1>

**Q2 : What would be the consequences of a move to a shorter settlement cycle for (a) hedging practices (i.e. would it lead to increase pre-hedging practices?), (b) transactions with an FX component?**

<ESMA_QUESTION_SETT_2>

With reference to transactions with an FX component our members note that different time zones and cut-off times mean that an FX hedge relating to a particular trading date is generally executed the day after the relevant trading date. Such a circumstance results in a one-day currency/interest rate exposure which would be exacerbated in a T+1 framework (e.g., two days of currency/interest rate exposure). Our members would like to take the opportunity, irrespective of the decision to be taken on T+1, to stress the possibility to strengthen the CLS (Continuous Linked Settlement) netting system in order to reduce the above risks. Last but not least, they would like to emphasise that the impact of shortening the settlement cycle will not only affect the sell-side, but also the buy-side, which would necessarily have to adjust its current operational timeframes.

<ESMA_QUESTION_SETT_2>

**Q3 : Which is your current rate of straight-through processing (STP ), in percentage of the number and of the volume of transactions broken down per type of transaction or per instrument as relevant? In case STP is used only for certain processes/operations, please identify them. Which are the anticipated challenges that you envisage in improving your current rate of STP?**

<ESMA_QUESTION_SETT_3>

Our members consider these figures to be of little significance and misleading in some cases. They deem that an average percentage may be affected by the outliers and may not fully reflect the level of automation of the process. However, with regard to the STP rate, they believe that standardisation, simplification and uniformity of the processes managed by EU CSDs are essential in order to increase this rate.

<ESMA_QUESTION_SETT_3>

**Q4 : Please describe the impacts that, in your views, the shortening of the securities settlement cycle could have beyond post-trade processes, in particular on the functioning of markets (trading) and on the access of retail investors to financial**

**markets. If you identify any negative impact, please identify the piece of legislation affected (MiFID II, MiFIR, Short Selling Regulation…) and elaborate on possible avenues to address it.**

<ESMA_QUESTION_SETT_4>

Our members do not believe that the potential shortening of the settlement cycle would have any impact on retail investors, as they generally benefit from contractual settlement. Instead, our members are of the opinion that there will be a strong impact on short selling practices as a result of the potential increase in settlement fails and the impact of T+1 on securities lending processes. The latter should be based on pre-defined contractual terms and conditions given the time constraints following the T+1 scenario.

Another area of impact is the provision of liquidity. As is well known, market-makers are essential for the provision of liquidity (especially for SMEs). Given capital constraints, in many cases they provide two-way pricing of securities which they do not hold. A shorter settlement cycle could limit the time available to them to find the securities they need. This could result in market-makers increasing bid-ask spreads on less liquid securities, or even removing them from their quote.

A further impact could be represented by additional frictions in the collateral processes due to time constraints which could require trading parties to post excess collateral. This would have a negative impact on capital efficiency. However, it is worth considering that the one-day reduction in exposure should lead to a decrease in margin calls.

<ESMA_QUESTION_SETT_4>

**Q5 : What would be the costs you would have to incur in order to implement the technology and operational changes required to work in a T+1 environment? And in a T+0 environment? Please differentiate between one-off costs and on-going costs, comparing the on-going costs of T+1 and T+0 to those in the current T+2 environment. Where relevant please explain if these are general or asset class/instrument/ trade specific.**

<ESMA_QUESTION_SETT_5>

Our members believe that, at this early stage, it is not possible to quantify the expected implementation costs, until a detailed roadmap/action plan is developed. However, with reference to the costs to be borne by the financial industry, our members would like to highlight the following cost categories: *i)* the pure cost of updating technology, which is affected by the level of IT development of each intermediary; *ii)* the cost of ensuring operational controls in the new and more restricted time windows for the settlement of transactions; *iii)* the project costs associated with the necessary assessments for the implementation of the T+1 settlement cycle.

Again, the standardisation and homogeneity of procedures between market infrastructures would contribute to a smooth the transition to the T+1 settlement cycle (whether confirmed or not) for all types of transactions with consequent cost savings.

<ESMA_QUESTION_SETT_5>

**Q6 : In your view, by how much would settlement fails increase if T+1 would be required in the short, medium and long term? What about T+0? Please provide estimates where possible.**

<ESMA_QUESTION_SETT_6>

A move to T+1 in the short to medium-term is likely to result in a significant increase in settlement fails due to the system's unreadiness resulting from the above-mentioned lack of standardisation and automation.

If the move to T+1 is implemented according to an appropriate and pre-agreed timeframe and supported by initiatives to improve the level of harmonisation, standardisation and automation of post-trade processes, it is possible that settlement fails will not increase in a long-term scenario.

<ESMA_QUESTION_SETT_6>

**Q7 : In your opinion, would the increase in settlement fails/cash penalties remain permanent or would you expect settlement efficiency to come back to higher rates with time? Please elaborate.**

<ESMA_QUESTION_SETT_7>

Please see our members' comments in response to Q6 above.

<ESMA_QUESTION_SETT_7>

**Q8 : Is there any other cost (in particular those resulting from potential impacts to trading identified in the previous section) that ESMA should take into consideration? If yes, please describe the type of cost and provide estimates.**

<ESMA_QUESTION_SETT_8>

TYPE YOUR TEXT HERE

<ESMA_QUESTION_SETT_8>

**Q9 : Do you agree with the mentioned benefits? Are there other benefits that should be accounted for in the assessment of an eventual shortening of the securities settlement cycle?**

<ESMA_QUESTION_SETT_9>

Our members agree with the mentioned benefits provided that the move to T+1 is implemented according to an appropriate and pre-agreed timeframe and is supported by initiatives to improve the level of harmonisation, standardisation and automation of post-trade processes.

Our members would also like to underline the impact of shortening the settlement cycle on the attractiveness of the EU markets. The move of the US system to T+1 will make these markets more attractive to APAC investors. Therefore, when conducting an impact assessment of the move to T+1 this aspect should be carefully considered.

<ESMA_QUESTION_SETT_9>

**Q10 :Please quantify the expected savings from an eventual reduction of collateral requirements derived from T+1 and T+0 (for cleared transactions as well as for non-cleared transactions subject to margin requirements).**

<ESMA_QUESTION_SETT_10>

Although our members are not in a position to quantify the expected savings at this early stage, they would like to note that there could be savings from the reduction of collateral requirements. However, it is worth noting that the majority of collateral posted by intermediaries relates to derivative transactions, which would not fall within the scope of T+1.

<ESMA_QUESTION_SETT_10>

**Q11 : If possible, please provide estimates of the benefits that you would expect from T+1 and from T+0, for example the on-going savings of potentially more automated processes.**

<ESMA_QUESTION_SETT_11>

As mentioned above, our members are not in a position to provide such estimates at this early stage.

<ESMA_QUESTION_SETT_11>

**Q12 : How do you assess the impact that a shorter settlement cycle could have on the liquidity for EU markets (from your perspective and for the market in general)? Please differentiate between T+1 and T+0 where possible.**

<ESMA_QUESTION_SETT_12>

Our members believe that in a T+1 scenario there will be greater constraints in securities financing transactions (SFTs) which could result in a decrease in the volume of securities available for lending. Liquid and efficient securities lending markets are essential for the smooth functioning of capital markets. The envisaged increase in fails could also affect market making activity, resulting in a deterioration in liquidity levels.

<ESMA_QUESTION_SETT_12>

**Q13 : What would be the benefits for retail clients?**

<ESMA_QUESTION_SETT_13>

Our members do not see significant benefits for retail clients.

<ESMA_QUESTION_SETT_13>

**Q14 : How would you weigh the benefits against the costs of moving to a shorter settlement cycle? Please differentiate between a potential move to T+1 and to T+0.**

<ESMA_QUESTION_SETT_14>

Our members believe that the costs will be much higher than the benefits in the short to medium term. Benefits (if any) could only be appreciated in a long-term scenario.

<ESMA_QUESTION_SETT_14>

**Q15 : Please describe the main steps that you would envisage to achieve an eventual shorter securities settlement cycle. In particular, specify: (i) the regulatory and industry milestones; and (ii) the time needed for each milestone and the proposed ultimate deadline.**

<ESMA_QUESTION_SETT_15>

As a preliminary step to a possible process of shortening of the settlement cycle to T+1, our members consider it essential to improve the efficiency of post-trade processes. Furthermore, given the current lack of detail on the initiative, our members hope that - should the move to T+1 be approved - that they will be provided with a detailed, complete and stable medium/long term work plan to allow all stakeholders to start internal analysis and implementation planning.

In terms of regulatory milestones, our members would suggest amending article 5.2 of the CSDR to ensure a fully harmonised adoption of T+1 in all EU countries. Moreover, they would also propose the following amendments to the Settlement Discipline RTS: (i) Article 2 would need to be amended to ensure that the allocation/confirmation process is completed on T+0, (ii) Article 10 would need to be updated to make the partial settlement mandatory.

<ESMA_QUESTION_SETT_15>

**Q16 : Assuming that the EU institutions would decide to shorten the securities settlement cycle in the EU, how long would you need to adapt to the new settlement cycle? And in the case of a move to T+0?**

<ESMA_QUESTION_SETT_16>

As stated above, the elements currently available are not sufficient to carry out an in-depth analysis, and therefore our members are not in a position to indicate a timeframe for the introduction of a T+1 settlement cycle. Once again, they believe that it is necessary to carefully assess all the relevant factors in order to avoid as many critical issues as possible. To this end, our members believe that the following initiatives should be taken by the EU institutions prior to the deployment of action plans by each intermediary: (i) 'mapping' of all regulations that will be affected; (ii) harmonisation of the services provided by market infrastructures to the maximum extent possible (such as, for instance, the Hold & Release functionality, partialisation, cross-border transactions and related cut-off times, etc.)

<ESMA_QUESTION_SETT_16>

**Q17 : Do you think that the CSDR scope of financial instruments is adequate for a shorter settlement cycle? If not, what would be in your views a more adequate scope?**

<ESMA_QUESTION_SETT_17>

Our members consider it adequate.

<ESMA_QUESTION_SETT_17>

**Q18 : Is it feasible to have different settlement cycles across different instruments? Which are the ones that would benefit most? Which least?**

<ESMA_QUESTION_SETT_18>

No, it is essential to converge towards a single settlement cycle because the interdependencies between different instruments are becoming increasingly important. For example, it is inefficient for the settlement cycle of an ETF to differ from the settlement cycle of one or more of its underlyings.

<ESMA_QUESTION_SETT_18>

**Q19 : Which financial instruments/ transaction types are easier to migrate to a shorter settlement period in the EU capital markets? Does the answer differ by asset class? Should it be feasible/advisable to have different migration times for different products/markets/assets? If yes, please elaborate.**

<ESMA_QUESTION_SETT_19>

As mentioned above, our members believe that the migration should affect all instruments at the same time. A phased migration or a migration by classes of instruments would generate misalignments.

<ESMA_QUESTION_SETT_19>

**Q20 : Do you think that the settlement cycle for transactions currently excluded by Article 5 of CSDR should be regulated? If you think that the settlement cycle of some or all of these transactions should be regulated, what would be in your view an appropriate length for their settlement cycle?**

<ESMA_QUESTION_SETT_20>

Our members are aware that the proposal to amend article 7 of the CSDR mandates the EU Commission to adopt delegated acts on penalties taking into account the “transaction type” element. In light of this, they believe it is premature to make any consideration with respect to the subject matter of this question.

<ESMA_QUESTION_SETT_20>

**Q21 : Please describe the impact(s) that the transition to T+1 in other jurisdictions has had or will have on your operations, assuming the EU remains on a T+2 cycle.**

<ESMA_QUESTION_SETT_21>

A move to T+1 in other jurisdictions would entail changes to the operational/IT processes of EU intermediaries operating in such jurisdictions. Our members believe that such a transition would have impacts with reference to: (i) Time zones. The move to T+1 would eliminate the one-day period generally used to deal with any issues affecting the timeliness of settlement. This aspect is emphasized when considering the time zone differences between, for example, the EU and the US/Canada; (ii) Allocations/confirmations. The shortening of the settlement cycle will make it more difficult for intermediaries to meet trade allocation and confirmation deadlines; (iii) FX. The shortening of settlement cycle in other jurisdictions will require a review of the timing and management of FX trades (please see details in our response to Question 2 above); (iv) SFTs (please see details in our responses to Q4 and Q12 above); (v) ETFs. Transactions in exchange-traded funds usually have a higher rate of settlement fails than in other financial instruments. A reduction in the settlement cycle for ETFs is likely to exacerbate this scenario; (vi) Attractiveness of EU markets to APAC investors.

<ESMA_QUESTION_SETT_21>

**Q22 : Can you identify any EU legislative or regulatory action that would reduce the impact of the move to T+1 in third countries for EU market participants? Please specify the content of the regulatory action and justify why it would be necessary. In particular, please clarify whether those regulatory actions would be necessary in the event of a transition of the EU to a shorter settlement cycle, or they would be specific only to address the misaligned cycles.**

<ESMA_QUESTION_SETT_22>

Our members believe that additional action should be taken to: (i) achieve a higher level of STP; (ii) promote and strengthen the harmonised application of European standards; (iii) achieve a higher level of transparency and consistency in the activities of EU CSDs; (iv) standardise asset servicing processes.

<ESMA_QUESTION_SETT_22>

**Q23 : Do you see benefits in the harmonisation of settlement cycles with other non-EU jurisdictions?**

<ESMA_QUESTION_SETT_23>

Assuming that EU settlement and pre-settlement processes reach a higher level of standardisation and automation (as further detailed above), the harmonisation of settlement cycles with other non-EU jurisdictions would likely bring benefits for cross-border settlement and liquidity management.

<ESMA_QUESTION_SETT_23>

**Q24 : Would reducing the settlement cycle bring any other indirect benefits to the Capital Markets Union and the EU's position internationally?**

<ESMA_QUESTION_SETT_24>

A move to T+1 could stimulate further work on harmonisation, standardisation and automation, with consequent benefits for EU markets.

<ESMA_QUESTION_SETT_24>

**Q25 : Do you consider that the adaptation of EU market participants to the shorter settlement cycles in other jurisdictions could facilitate the adoption of T+1 or T+0 in the EU? Please elaborate.**

<ESMA_QUESTION_SETT_25>

Our members believe that the adoption of a shorter settlement cycle in other jurisdictions could provide a useful benchmark not only for the EU financial industry but also for the EU institutions and authorities. However, in case of the adoption of T+1 in the EU, the intermediaries involved would need to put in place ad hoc implementation plans, as the EU system operates differently and with more complexity than the US system.

<ESMA_QUESTION_SETT_25>

**Q26 : Would different settlement cycles in the EU and other non-EU jurisdictions be a viable option?**

<ESMA_QUESTION_SETT_26>

Given that an EU move to T+1 in a few months (e.g., May 2024) is not a viable option, EU stakeholders will have no choice but to manage the move of non-EU jurisdictions to a different settlement cycle. In this respect, it is worth noting that misalignments between settlement cycles have already occurred in the past and have been well-managed. Finally, for the reasons outlined above in relation to APAC investors, having a T+2 settlement cycle could be beneficial for the EU markets.

<ESMA_QUESTION_SETT_26>

**Q27 : Please elaborate about any other issue in relation to the shortening of the securities settlement cycle in the EU or in third-country jurisdictions not previously addressed in the Call for Evidence.**

<ESMA_QUESTION_SETT_27>

As a proposal, our members believe that US multi-listed instruments which are traded/settled in the EU should follow the “place of settlement” criterion. Consequently, the “place of settlement” would determine the length of the settlement cycle. In this respect, a harmonised approach across the EU would be advisable.

<ESMA_QUESTION_SETT_27>