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](http://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](http://www.esma.europa.eu) under the heading ‘[Data protection](https://www.esma.europa.eu/about-esma/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.

# General information about respondent

|  |  |
| --- | --- |
| Name of the company / organisation | Febelfin |
| Activity | Associations, professional bodies, industry representatives |
| Are you representing an association? |  |
| Country / Region | Belgium |

# Questions

1. : Please describe the impacts on the processes and operations from compressing the intended settlement date to T+1 and to T+0. Please:
2. 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.
3. 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>

The main challenge posed by a shorter settlement cycle relates to post-trade activities being compressed into shorter time frames. While it might be assumed that moving from two days to one day would reduce the available post-trade processing time by 50%, AFME actually estimates market participants will be moving from having 12 hours to 2 hours of post-trade operations time, an 83% reduction. Currently, a significant proportion of settlements take place in “overnight batches”, a window before the start of the business day on intended settlement date. According to ECB statistics for 2021, overnight settlement “accounted for 52.63% of overall volume” within T2S. In order to utilize the overnight window in a T+1 environment, settlement instructions will need to be allocated and matched on trade date, and securities and cash in place ready to exchange (including securities financing and FX transactions). In EU markets in particular, holdings in the same instrument may be spread across multiple CSDs. This creates an additional challenge in efficiently managing inventory and would require securities to be realigned prior to trading.

In light of the above, Febelfin also remarks that the current misalignment of cash/securities settlement deadlines in T2S (16h30 vs. 17h00) would require further harmonization to better accommodate a possible transition to T+1 settlement. Also, members observe a need for stricter client discipline in the sending of instructions and the review of existing market standards/ the development of new market standards and market practices.

We would also like to highlight the risk for realignments in case of multi-listed securities, or for crossborder transactions that usually takes more than one day to be handled.

As to T+0, to our view it is important to distinguish between instantaneous T+0 settlement and delayed T+0 settlement (i.e., settlement with a time gap between trading and settlement, so that the standard post-trade processes can take place, but that settlement still takes place on the same day as trading). Instantaneous T+0 settlement would require pre-funding (extra cost and complexity), and would hamper trading; consider also post-trade process (cut-offs etc.) effectuated out of different time zones.

But delayed T+0 settlement at the end of day may not have these problems, and would allow for settlement netting.

An immediate move to T+0 settlement would require a fundamental transformation of current pre- and post-trade processes including ancillary processes such as FX and funding which could result in the creation of new risks, rather than a reduction. Furthermore, it is feasible that T+0 would have more of a material impact to trading and liquidity which requires close attention and evaluation. For the purpose of the present CfE, we would thus highly recommend to limit the analysis to a T+1 scenario, and not take into account T+0.

<ESMA\_QUESTION\_SETT\_1>

1. : 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>

Time zone differences will impact the possibility of same-day matching processes for investors from outside the EU, vastly reducing the time available to communicate and resolve any breaks or exceptions. This impact would be particularly significant on cross-currency transactions which have an FX component. We would also expect an increase in the number of spot FX transactions.

<ESMA\_QUESTION\_SETT\_2>

1. : 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>

It is unclear what is meant with STP and which processes / market participants it would relate to. We also wish to indicate that STP does not necessarily means ‘fast’ or ‘instantaneous’, as some STP processes (e.g. aspects of sanctions screening) may be considerably time consuming.

<ESMA\_QUESTION\_SETT\_3>

1. : 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>

If not properly prepared for, and unless there is a modification to existing processes, technology and overall behavioral changes, the shortening of the securities settlement cycle could lead to an increase in the number of settlement fails in the market, which will incur cash penalties under Central Securities Depositories Regulation (CSDR) rules, as well as having capital impacts under Basel III requirements.

<ESMA\_QUESTION\_SETT\_4>

1. : 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>

The implementation costs will be contingent on the roadmap, scope, technical changes and timeline that is ultimately agreed, but are generally expected to be accrued in the short-term. Costs will not be borne equally, and we consider that smaller, less sophisticated market participants may generally have to undertake more significant levels of preparation for T+1.

<ESMA\_QUESTION\_SETT\_5>

1. : 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>

This is difficult to assess based on publicly available data. The industry suffers from a lack of high-quality, granular public data on settlement performance. Indeed, there is no universal methodology for calculating settlement rates, leading to differences in figures reported by different sources. Of the data that is publicly available, there is very limited analysis on how settlement fails differ across various types of instrument, and on the average duration of settlement fails. CSDs should be the “golden record” of settlement fails. CSDs subject to the delegated regulation on CSDR settlement discipline measures, are required to submit periodic fail reporting to the relevant National Competent Authority and ESMA which is ultimately publicly disclosed. However, the reporting methodology may create an incomplete or distorted view of settlement fails, and published data is much less granular than that which is provided to regulatory authorities. For example, CSDs are required to count an instruction as a fail for everyday that it is recycled, and instructions that are cancelled after ISD are also counted as fails. There is also limited information available on the underlying causes of settlement fails, which is often not visible to the CSD, especially in the case of an unmatched fail. As a result, it is difficult to make predictions for the future based on incomplete data being available for the current T+2 environment.

<ESMA\_QUESTION\_SETT\_6>

1. : 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>

To our view, an increase in settlement fails/cash penalties – supposedly caused by a rushed migration to T+1 settlement – is to be avoided, as this would imply new risks or damage the existing efficiency and functioning of EU capital markets.

<ESMA\_QUESTION\_SETT\_7>

1. : 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>

Higher operating cost linked to front and back office operational teams doing more shift work.

<ESMA\_QUESTION\_SETT\_8>

1. : 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>

Important benefits, such as reducing systemic risk and improving resilience, are very difficult to quantify and are likely to accrue over a longer time-horizon. It is hoped that there will also be long-term cost savings arising from lower collateral requirements and improved efficiency in post-trade processes however it is unclear at this stage how they will be apportioned to investors.

<ESMA\_QUESTION\_SETT\_9>

1. :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>

See above, answer to Q9.

<ESMA\_QUESTION\_SETT\_10>

1. : 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>

Difficult to estimate, also as certain processes could be taken into consideration for automation regardless of a possible shortening of the settlement cycle.

See also above, answer to Q9.

<ESMA\_QUESTION\_SETT\_11>

1. : 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>

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<ESMA\_QUESTION\_SETT\_12>

1. : What would be the benefits for retail clients?

<ESMA\_QUESTION\_SETT\_13>

See above, answer to Q9.

In general, retail clients have to pre-fund the trades upfront, having cash (in case of a buy) or securities (in case of a sell) in place. Moreover, retail clients have contractual settlement, meaning cash or securities is settled right away on trade date and the financial institutions bears the risk of late settlement.

<ESMA\_QUESTION\_SETT\_13>

1. : 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>

It is difficult to quantify and directly compare costs and benefits. Our shared ambition is for a low-cost, efficient, safe, resilient and integrated post-trade environment which supports a globally competitive EU securities market, with high-levels of automation and standardization. Moving to T+1 does not itself achieve this ambition, but, if implemented correctly, may prove a catalyst towards delivering this objective. The costs of moving to T+1 in itself would probably be more important compared to the rather limited benefits.

<ESMA\_QUESTION\_SETT\_14>

1. : 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>

It is clear that a successful migration to T+1 settlement will require coordinated industry effort and communication between all actors operating and investing in the regions securities markets. It will be crucial to allow an appropriate timeframe for all parties involved to make the necessary technical, operational and regulatory changes which must be based on detailed assessments and allow time for sufficient industry wide testing with clear governance and milestones. A rushed or uncoordinated approach is likely to result in increased risks, costs and inefficiencies in European capital markets.

<ESMA\_QUESTION\_SETT\_15>

1. : 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>

It is of utmost importance that market infrastructures are well prepared, given multiple CSDs in Europe, multiple currencies and a variety of settlement deadlines. If the process for “cross border activity” is efficient and realistic in terms of timing, adaptation to a T+1 settlement cycle should be feasible.

<ESMA\_QUESTION\_SETT\_16>

1. : 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>

To our view it is indeed highly recommended to stick with the CSDR scope of financial instruments, provided that the European shortcomings that make shortening the settlement cycle difficult are first addressed (differences in deadlines, lack of cross-CSD links, ....).

<ESMA\_QUESTION\_SETT\_17>

1. : 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>

It would be (technically and operationally) possible to establish and apply different settlement cycles across different instruments. However, when reducing the settlement cycle, the main goal, prior and upon implementation, should be to maximize uniform processing within the EU area. Creating different settlement cycles across different instruments would imply a contradictory movement which we should avoid.

<ESMA\_QUESTION\_SETT\_18>

1. : 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>

The Belgian financial sector would be more inclined towards a ‘big bang’ migration, i.e., to change the settlement cycle at one go for all products/assets and across all markets.

If a phased approach would be followed for products/assets, we believe it would be worthwhile to focus on the migration of asset classes with high settlement efficiency first (i.e., first debt, then equity). We note however that this would go against the general trend to be observed in other jurisdictions. If a phased approach would be followed in the EU, we advocate for all markets to move at the same time and in the same way.

<ESMA\_QUESTION\_SETT\_19>

1. : 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>

We recommend for transactions currently excluded by Article 5 of CSDR to remain excluded. Also, we are of the view that any shortening of the settlement cycle should not lead to the imposition of additional reporting obligations.

<ESMA\_QUESTION\_SETT\_20>

1. : 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>

Clearly, markets are linked with each other (e.g. multi-listed instruments), so harmonized settlement cycles are advisable in order to avoid mismatches. However, the transition to T+1 in other jurisdictions such as the US also constitutes a time-zone issue, notably for smaller financial institutions, which will not be solved by the EU moving to T+1. The issue is exacerbated for funds comprising assets that are subject to different settlement cycles, and there could be impacts on forex. As the US is yet to transition to T+1, many impacts may remain unknown at present.

<ESMA\_QUESTION\_SETT\_21>

1. : 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>

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<ESMA\_QUESTION\_SETT\_22>

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

<ESMA\_QUESTION\_SETT\_23>

Yes, we especially advocate for the possible alignment on implementation date and modalities with the United Kingdom.

<ESMA\_QUESTION\_SETT\_23>

1. : 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>

Yes, we especially advocate for the possible alignment on implementation date and modalities with the United Kingdom.

<ESMA\_QUESTION\_SETT\_24>

1. : 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>

Yes, as this would decrease the number of needed modifications to adopt a shorter Settlement cycle.

<ESMA\_QUESTION\_SETT\_25>

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

<ESMA\_QUESTION\_SETT\_26>

See above, answer to Q21.

<ESMA\_QUESTION\_SETT\_26>

1. : 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>

Corporate actions processing to be reviewed (currently set up for a T+2 environment) + holistic view needed on possible impacts outside settlement as such.

<ESMA\_QUESTION\_SETT\_27>