28 November 2008
final

CESAME REPORT

The work of the Clearing and Settlement Advisory and Monitoring Experts' Group ("CESAME" group)

Solving the industry Giovannini Barriers to post-trading within the EU

28 November 2008

Document

The report is the result of four years of work of the CESAME Group with the support of various post-trading professionals in the European Union. The body of this report has been assembled and partly drafted by the Secretary of the CESAME Group, Doris Kolassa. It does not necessarily represent the Commission's official position.

Brussels, November 2008

Table of Contents

Foreword

David Wright, Deputy Director General DG MARKT, Chairman of the CESAME Group

The creation of an integrated securities market in the EU remains a very important EU policy. If capital and services can flow freely in the EU – the cost of capital will be lower, product choice widened – with competition leading to innovation and long term growth. Of course, investors must be adequately protected and prudential stability is essential. Even if trading arguably, and for a long time, constituted its centrepiece, that does not mean that post-trading arrangements were neglected. On the contrary, they were correctly identified as fundamental operations for a stable and efficiently functioning financial system and as such they have been subject to close scrutiny and detailed policy proposals and developments for the last 8 years or so.

Post-trading arrangements constitute the point of convergence of all aspects of the life of securities. Where securities movements meet cash movements; where the law meets operational arrangements; where the tax collection mechanisms meet dividends and transfers; where issuers, infrastructures, intermediaries and investors create interdependent networks to channel investments and benefits; where insolvencies might threaten the stability of financial systems. Hence the importance, the complexities but also the necessity to have smooth, safe and sound post-trading arrangements in the EU. Without being able to provide this, a true single European securities market will never exist and the entire process of financial market integration will be suboptimal. Diverging, even conflicting, national approaches on these issues create a very difficult problem to solve. As cross-border trading has increased, rationalizing cross-border clearing and settlement problems within the European Union has become more essential and the calls to tackle the barriers all the more insistent.

EU clearing and settlement arrangements have been discussed for a long time. The Lamfalussy[1] report of 1990 concluded that any integration process should be largely in the hands of the private sector. However, it also recognised the public interest in the developments and the need for specific public sector action as well. These findings, coupled with specific policy suggestions, have been further developed by the two Giovannini reports which the Commission took into account when developing its own policy approach.

The Commission was always of the opinion that both sectors, private and public, must at the same time and in a coordinated way go about reforms that affect the very architecture of financial services. The public sector therefore had to play a major role – both in co-ordinating private sector actions and steering regulation of clearing and settlement on a pan-European basis. As acknowledged in the European Commission's Communication of April 2004, it has been essential to ensure that all required actions are taken forward with a clear political and strategic direction backed by Member States. At a practical level, the Commission needed to establish a powerful monitoring and co-ordination mechanism, which would be able to provide an efficient interface between private sector and public sector initiatives, to monitor progress and the consistency of the overall project, reporting critical issues, and ensure transparency of the overall progress to the industry, the public sector and the general public.

---

[1] In 1990, G 10 central banks laid down minimum principles aimed at ensuring the safety of clearing systems. The so-called “Lamfalussy” Report, see http://www.bis.org/publ/cpss04.htm

This crucial task was assigned to the CESAME Group and I would like to thank all its members, guests and the secretariat for the good work. Not all industry-related barriers are dismantled, but real progress has been made and further action is being mapped for the future. In many ways the CESAME Group also set new standards for open discussion and transparency. The willingness of its participants to actively participate in this process has delivered visible success in form of standards and better mutual understanding of processes and terminology which contributes to many other post-trading projects such as the Code of Conduct and TARGET2-Securities. New industry solutions have added to the momentum. This CESAME Group Report is a comprehensive record of the joint efforts and hopefully will serve as a useful introduction for the uninitiated as well as a source of detailed information for the interested expert – and the point of departure for further efforts needed in the future.

Preface

Alberto Giovannini, Principal Policy Advisor to the CESAME Group

In the Spring of 2004 the Commission issued a Communication where it indicated the following intentions (in the order as they appeared in the Communication):

- to set up a consultative and monitoring Group, called CESAME (Clearing & Settlement Advisory and Monitoring Experts) with the mandate to organize the removal of the so-called private sector barriers and advise the Commission on public sector barriers;
- to draw up a Directive on clearing and settlement which addressed questions of (i) rights of access and choice, (ii) a common regulatory framework, and (iii) governance;
- to establish a group to advise on reforms in the taxation area;
- to establish a group to advise on reforms in the legal area.

This framework was coherent with the analysis of two reports I helped to put together, respectively published in 2001 and 2004, which identified the market failures in the European post-trading landscape, represented by a number of barriers to cross-border post-trading services. Such barriers were caused by several technical standards, conventions, regulations and laws which were inconsistent with a single EU securities market. The 2004 report suggested a strategy for removing such barriers, which required the production of new technical standards, conventions, regulations and laws to replace the old, inconsistent ones. According to the arguments presented in the 2004 report, the removal of the barriers to the provision of cross-border post-trading services would have triggered a wave of consolidation in the industry, leading to large, efficient and low cost EU-wide infrastructures.

At the time, we envisaged CESAME to be the centre of this coordinated reform effort, for the simple reason that the presence of so many different actors requires an efficient system for gathering and disseminating information. And that is what CESAME was expected to do. This function is of crucial importance because through appropriate information about the direction of reform, private market participants, suppliers of market infrastructure services, would be able to make long-term plans and investment decisions that are coherent with the actual direction of the marketplace, thereby facilitating and accelerating reform.

The tasks assigned to the EU Commission, to CESAME and its members and to the legal certainty and taxation groups were all tightly consistent with the plan of managing a concerted set of initiatives aimed at the production of new standards, conventions, regulations and laws. This valuable document details the work that centred on CESAME and provides sufficient detail to allow an informed assessment of the success of this articulated reform effort.

Since the method of work is well structured, the progress in the replacement of every standard, convention, regulation and law with new standards, conventions, regulations and laws, as detailed in this Report, is immediately evident. The evidence suggests that, in general, progress has been much slower than originally envisioned (the second Giovannini report published gave aggressive estimates of about 4 years for the completion of the entire project). This big discrepancy between expectations and outcomes is due to a number of factors. First, I think we can now argue that the originally-envisioned time to completion may have been too aggressive, especially regarding the adoption of new standards and conventions. The experience of CESAME has shown that the considerable work leading to the drafting of new

standards and conventions is only a small piece of the whole job: adoption is a voluntary process; it is costly to market participants, and in the absence of strong motivation, slow and uncertain. Second, the big surprise of the way reform has moved forward is an involvement of authorities below what was originally predicted. On the regulatory side, a strong resistance to regulations has led the Commission to drop the directive that it announced in its 2004 Communication, leaving gaps that cannot otherwise be filled (inconsistent regulations can only be replaced by new regulations). As far as the legal certainty work and the taxation work is concerned, the very high-quality preparatory studies that the ad-hoc groups have produced have not yet been followed by the necessary decisive initiatives from Member States. Finally, the absence (so far) of decisive actions by governments may explain the slow pace of private initiatives: government action normally provides an effective catalyst to private sector coordination.

Despite the above-mentioned shortcomings, CESAME has already produced and will produce further important results; the reform path is laid out clearly and is shared by an ever larger number of market participants; the opportunities of a liquid and integrated securities market in Europe are perceived by all, and are waiting to be reaped.

Executive Summary

The barriers to efficient cross-border clearing and settlement in Europe were identified by the two Giovannini reports and reflected in the two Commission Communications on Clearing and Settlement in 2002 and 2004. The Commission's policy regarding post-trading focused on several pillars, such as the liberalisation and integration of existing securities clearing and settlement systems, the application of competition policy, and the adoption of a common regulatory and supervisory framework and of appropriate governance arrangements – squired by industry working groups. One of these, the CESAME group was set up in 2004 to ensure transparency, coherent action and private sector coordination towards the removal of the industry-related barriers highlighted by the Giovannini group, namely barriers 1, 3, 4, 7, 6 and 8. This report presents the progress achieved on these barriers so far.

While Barrier 8, concerning the differences in securities issuances, has been dismantled, more work needs to be done on the other barriers. The work of the industry on barrier 1 (the diversity of IT platforms) is well advanced: the fact-finding phase has been completed; standard-setting and implementation are on track and will be completed by March 2011. Tackling Barrier 3 is more complex and involves the harmonisation of national approaches relating to corporate actions processing and general meetings. The barrier is also intertwined with legal and tax processing aspects. In this area, the fact-finding phase is completed. The work on standard setting shall be completed at the end of 2008 and endorsement is scheduled for 2009. Barriers 4 and 7 both deal with cross-border discrepancies on operating hours and deadlines. The industry was tackling these barriers even before the creation of the CESAME group: hence standards and, to a large extent, implementation are in place, yet the need for further action in this context emerged. These additional actions will be specifically dealt with as an additional barrier alongside the Giovannini's ones. Barrier 6 regarding discrepancies among national standard settlement periods, initially had a low priority and it was felt that it had a global context going beyond Europe. However, the issue recently gained attention within the discussion of TARGET2-Securities and in the context of standardising the processing of corporate actions (Barrier 3) and will be considered by the CESAME2 group established in mid-2008 which will continue the work of the CESAME group.

The CESAME group was also committed to monitor the progress of the dismantling of the public-sector Giovannini barriers, as they are interrelated with industry barriers. The result in this area can be summarised as follows. Only Barrier 14 on conflict of laws on netting has been dismantled for bilateral netting. Barrier 11 (withholding tax relief) and Barrier 12 (restriction on tax collection) was tackled by the FISCO group, which completed the fact-finding and presented solutions which are now under the consideration of the Commission and Member States. The removal of Barrier 5 on practical impediments to remote access to national clearing and settlement systems depends ultimately *inter alia* on the practical implementation of the MiFID and the forthcoming ESCB-CESR recommendations. Barrier 2 (national restrictions on the location of clearing and settlement) has been tackled at legislative level in the MiFID and industry-wise by the Code of Conduct, but the recommendations still need to be put into practice. Barrier 10 (restrictions on primary dealers' activities) has been collapsed into Barrier 2 which is not yet fully dismantled. Some of the various legal barriers have been tackled by the Legal Certainty Group (Barrier 9 on location of securities, Barrier 13 on the absence of an EU legal framework, and certain aspects of Barrier 3 on corporate actions). Now the advice of the Group needs to be put into practice. Barrier 15 (conflicts of law) has stalled and new approaches have to be explored. Finally, discussions have also taken place on the role of the Code of Conduct, on systemic risk management standards for CCPs, and on various CESR and ECB/ESCB initiatives in the post-trading area.

A. Introduction

Promoting integration of the framework for securities trading in Europe needs to be accompanied by parallel measures for post-trading, in particular as regards smooth and cost efficient as well as safe and sound cross-border clearing and settlement of securities transactions. Against this background, the attention of policy makers has gradually shifted from an initial focus on trading to post-trading issues. This development happened in view of the continuous rise of the volumes of cross-border transactions; hence the importance of post-trading arrangements for the smooth functioning of a fully integrated financial market.

This was recognised by the EU legislator who provided the right to access central counterparty, clearing and settlement facilities and to designate a settlement system under Article 34 of the new Markets in Financial Instruments Directive (MiFID)[2]. It was also recognised that such Europe-wide choice had to be supported by approved and effective links between trading and post-trading infrastructures, creating thus a much more integrated post-trading environment in the EU.

However, barriers to safe and efficient cross-border securities post-trading arrangements have been identified. The complexity created by these barriers renders European cross-border post-trading arrangements more cumbersome, less efficient and potentially more risky than necessary. This was identified as a competitive disadvantage vis-à-vis third countries, in particular in comparison to the US financial market.

The "Clearing and Settlement Advisory and Monitoring Experts' Group" (CESAME) has been set up following the Commission Communication on Clearing and Settlement (April 2004) as the industry group tasked with dismantling the industry related so-called Giovannini Barriers to cross-border clearing and settlement (see chapters 1.5 and 1.7). In line with the timeframe set in the Second Giovannini Report, CESAME's mandate expired in June 2008. However, the outstanding work and monitoring will be continued in the CESAME2 Group (see chapter 2.6).

This stocktaking CESAME report describes the activities of the CESAME Group and focuses on the process and stage of dismantling of the six industry-related Giovannini Barriers. It starts with an overview of topics CESAME has dealt with, then examines the Giovannini Barriers, including the measures that have been taken so far, and closes with an outlook on future developments and remaining work to be carried out in order to fully dismantle the barriers. In view of the importance of the public sector barriers, it also includes the relevant developments of these other nine Giovannini Barriers.

1. Historical background

In stark contrast to the widely acknowledged very efficient and safe domestic set-ups of post-trading, the rather poor situation of cross-border post-trading (in terms of safety, effectiveness and pricing) has kept the worldwide securities industry as well as European policy makers busy for a long time[3]. The activities of the European Commission are briefly described below.

---

[2] Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments, OJ L 145, p. 1 of 30 April 2004 (hereinafter "MiFID" – for a consolidated text version see: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:02004L0039-20070921:EN:NOT).

[3] On the European history of post-trading issues see: Peter Norman, Plumbers and Visionaries. Securities Settlement and Europe's Financial Market; 2007

A string of reports of the European Parliament (Andria Report, Kauppi Report[4]), numerous European Council Conclusions[5] on the subject as well as many industry initiatives (e.g. the hub-and-spoke model of Euroclear, the European CCP model of ESF), or the Euroclear Single Platform project, the TARGET2-Securities project and the recently announced Link-up Markets project are proof of the relevance of the topic. Looking at global developments, unsatisfactory levels of efficiency and safety were also the driver for changes in post-trading arrangements in large single economies such as the U.S. (i.e. the creation of DTCC) which furthermore did not have to cope with multiple currencies and had a more homogeneous legal and fiscal environment. Yet even without the cross-border barriers that Europe faces, it took the U.S. a considerable amount of time (roughly 20 years) to reach their aim to consolidate. Indeed some of the inefficiencies in Europe stem from the very diverse historically grown structure of Europe's legal and fiscal systems.

1.1. Economic background

Post trading is cost efficient if it minimises costs for a given quantity of output. Costs related to post trading can be divided in two groups. On one hand there are direct and indirect costs. The former are the costs one has to pay when carrying out a securities transaction (i.e. the costs of clearing and settling the transaction), while the latter are, for example, the costs which arise from back-office facilities that must be maintained. On the other hand, there are the opportunity costs such as the costs related to inefficient use of collateral and trades that are simply foregone because of the complexities involved.

As indicated earlier, the post-trading infrastructures are efficient in the domestic context. However, their interaction at the cross-border level leads to significant inefficiencies. Several studies have attempted to quantify these inefficiencies (see Annex I of Draft working document [insert link]). Five main results emerge from the analysis of these studies:

i. In the EU context, from an investor's point of view, a cross-border equity transaction is, on average[6], twice to six times more expensive than a domestic transaction. The value of the ratio is very high and not in line with the ambitions of a single securities market in the EU. In particular, as concerns the excess costs of a cross-border equity settlement with respect to a domestic equity settlement, available studies seem to converge towards an average value of between €15 and €20 per transaction[7].

---

4 Andria Report, OJ C 38 E of 12 February 2004, p. 265; Kauppi Report, OJ C 157 E of 6 July 2006, p. 485

5 E.g. (ECOFIN) Council Conclusions on Clearing and Settlement of
3 June 2008: http://register.consilium.europa.eu/pdf/en/08/st09/st09720.en08.pdf
9 October 2007: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/96375.pdf
27 February 2007: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/92984.pdf
28 November 2006: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/91899.pdf
25 November 2004: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/82818.pdf

6 In some cases, cross-border transaction costs have been found to exceed domestic ones by several hundred times. Indeed, in the 2004 Annual Report on Competition Policy, Commissioner Kroes found instances where cross-border transactions cost 350 times more than domestic ones. Fortunately, such cases are very limited.

7 The study from which this estimate was taken (AFTI/Eurogroup, 2005) does not include custody costs. A previous study, carried out by the same group in 2002, found excess costs of between €18 and €25 per transaction (again, excluding custody costs). Given that custody costs are higher for cross-border than for domestic holdings of securities, including these would make the excess cost even higher.

ii. From a system point of view, a domestic transaction is up to eight times more expensive in the EU post-trading infrastructures than in the US DTCC[8].

iii. A reasonable range for the aggregate excess cost of post-trading for investors is between €2 billion and €5 billion.[9]

iv. Considering that the estimate for investors' total spending for trading and post-trading is about €28 billion per year in Europe, the integration of the post-trading sector could therefore lead to an average reduction of transaction costs for investors of between 7% and 18%.

v. Additional cost reductions (approximately €700 million) could be achieved through market consolidation.

It is usually argued that the integration of European post-trading activities (defined as the removal of existing Giovannini barriers) should lower cross-border post-trading costs to the level of the domestic ones as access for all users to both domestic and cross-border services would occur under the same conditions.

Such integration could be achieved in different ways. For example, it could occur through mergers and acquisitions or through other strategic measures (like outsourcing, alliances, joint ventures, and reorganisations within financial institutions). It could also be achieved through the harmonisation of practices; or any combination of the two. A reduction in the number of providers and/or the harmonisation of their practices would reduce costs in many different ways. A lower number of systems would mean less investment would be needed to maintain the remaining systems and the links between them. For users of infrastructures, a lower number of systems that operate according to the same rules and standards would mean a substantial reduction in investment in their back offices. There would also be a reduction of costs in operational terms (due to economies of scale and scope there would be a reduction in transaction and custody costs), in terms of "friction" (by reducing the frequency of failed trades in cross-systems transactions) and in liquidity and risk management terms (by facilitating centralised liquidity and collateral management).

The cost reductions in the orders of magnitude described above, could result in significant benefits for the EU economy. The Commission tried to estimate these benefits (see Annex II to the Draft Working document[10]). According to the Commission's calculations the increased liquidity and lowered cost of capital that would result from a 7% to 18% reduction in transaction costs would lead, on average, to an increase in the level of GDP of between €23 billion and €63 billion (in real terms) within a ten-year period.

1.2. Application of Competition Law

Competition issues are often raised in the context of financial markets regulation but while the enforcement of competition law certainly has a role to play, it is not a panacea. Competition between clearing and settlement providers should mean in practice that users have a choice between different providers – and that the providers may also offer their services cross-border.

---

8 The first Giovannini Report found a ratio of 11:1, but the two results can not be compared due to different methodologies used.

9 The figures in points (iii.) to (v.) are taken from the Commission draft working document on post-trading activities of 23 May 2006 and its annexes; http://ec.europa.eu/internal_market/financial-markets/clearing/communication_en.htm

10 http://ec.europa.eu/internal_market/financial-markets/docs/clearing/draft/annex_2_en.pdf

However, if this is not the case, the causes for lack of competition have to be examined. In case of anti-competitive behaviour, there are effective tools of competition law available on national and European level.

Any action of the Commission in respect of competition law issues builds on two legal provisions of European competition law, which prohibit collusion between providers (Article 81 EC Treaty) and abuse by providers of a dominant position (Article 82 EC Treaty), such as by adopting a discriminatory behaviour in objectively similar situations. Ensuring a climate of fair competition between clearing and settlement providers also fosters sufficient pressure for innovation, in coherence with the objectives set out in the Lisbon agenda. Innovation is indeed a basic parameter for competition in the provision of these services.

There may be different reasons (anti-competitive behaviour, fiscal and legal barriers, regulatory constraints) for situations where competition is lacking. Removal of the Giovannini Barriers alone is unlikely to be sufficient to ensure a competitive environment. Even after removal of the barriers, access could be constrained, for instance by different regulatory treatment of entities, which are nominally distinct but effectively perform the same functions (these issues are also covered by the ESCB-CESR recommendations and the work of CESR's Post-Trading Expert Group). Consolidation might also lead towards potential monopoly-like situations in the provision of clearing and settlement services. In a monopoly situation, there is a risk that a single provider would abuse its dominant position to the detriment of its members/participants. In a monopoly situation, the incentive for investing in innovation would depend on two main factors:

- First, the contestability of the market which depends among others on the technology used.

- Second, the existence of appropriate governance mechanisms to ensure that owners and management of systems take into account the need of the users of the systems.

The Commission has already covered the post-trading sector in view of competition. In 2004, the Commission adopted an antitrust decision (which has been appealed; no final judgement has yet been issued)[11] and in May 2006, after an extensive fact finding exercise, the Commission published an *Issues Paper on competition in the EU securities trading and post-trading*[12]. This paper identified different types of behaviour that prevented competition in clearing and settlement from developing to its full potential.

In the clearing area, certain types of behaviour of exchanges or CCPs have been identified as preventing competition. For example, an incumbent exchange in a near-monopoly situation can be tempted to maximize profits at the trading level and to shift rents from clearing to trading, by putting out an exclusive service contract to tender. An incumbent exchange can sometimes impose conditions on the CCP limiting its scope to develop its business freely. CCPs in vertical silos do not appear to be subject to competition either for or in their home market. Finally, due to the lack of industry standards, interoperability between exchanges and CCPs appears underdeveloped and should be encouraged provided that risk issues raised by those links are properly addressed.

In the settlement area, certain types of behaviour of CCPs and CSDs have been identified as preventing competition. As in the clearing area, the absence of industry standards in the settlement area limits interoperability and is a barrier to the development of competition. This

---

[11] The decision found that *Clearstream Banking AG* and its parent company *Clearstream International SA* abused its dominant position by refusing to supply cross-border securities clearing and settlement services and by applying discriminatory prices. This decision has been appealed before the Court of First Instance who has not yet rendered a judgement.

[12] http://ec.europa.eu/comm/competition/antitrust/others/securities_trading.pdf

makes competition between intermediaries more difficult as it tends to favour local settlement agents. Fees for CSD settlement services were also reported as lacking transparency; but part 1 of the Code of Conduct (see section 5.2) has removed this obstacle. Also, some CCPs have concluded contracts according to which the CCP will exclusively provide a direct feed to only one settlement agent. Preventing other settlement agents from having access to the same level of service could limit competition between them.

In both clearing and settlement areas, the *Issues Paper* also points out that the lack of accounting separation and transparency and inadequate analytical reporting create uncertainty about whether competition rules are respected or not. As far as solutions to these issues are concerned, the Paper concludes that one should seek them in a combination of regulatory measures, appropriate actions by the industry and the application of competition rules. At the same time, the role of users and final investors in obtaining a competitive environment is enhanced.

The objective of competition policy is to have more competition which usually leads to a reduction of cost. However, it is important that these cost reductions are not limited to the immediate participants in the post-trading arena, but actually passed on to the end investors. This was highlighted in the Council Conclusions[13] as an item that competition policy should look for.

In recent months, new entrants like Euro-CCP and EMCF (European Multilateral Clearing Facility) have emerged in the post-trading sector. This development was spurred by the launch of multilateral trading facilities (MTFs, e.g. Chi-X, Turquoise) due to the coming into force of MiFID. This forced incumbents to review their offerings and reduce their prices, as would be expected by increased competition.

1.3. Overview of some major global efforts on harmonisation and standard setting in post-trading

Increasing efficiency and reducing risk in the post-trading process has been the focus of many international initiatives. For a long time several groups worked on the core issues and promoted the implementation of measures to reduce risks, increase efficiency, and provide safeguards for investors in post trading. Some of the most important results are mentioned below:

1989 Group of Thirty, "Clearance and Settlement in the World's Securities Markets"

1998 European Monetary Institute, "Standards for the use of EU Securities Settlement Systems in ESCB credit operations"

2000 ISSA Recommendations[14]

2001 CPSS IOSCO Recommendations for Securities Settlement Systems

2003 Group of Thirty, "Global Clearing and Settlement: A Plan of Action"

2004 CPSS IOSCO Recommendations for Central Counterparties

---

[13] Council Conclusions on clearing and settlement of 3 June 2008 http://register.consilium.europa.eu/pdf/en/08/st09/st09720.en08.pdf

[14] http://www.issanet.org/pdf/rec2000.pdf

1.4. The EU initiatives 1970s – 2000: Working Groups, the Kessler Report, the Model Agreement between Central Securities Depositories

As pan-EU financial activity has increased, inefficiencies associated with cross-border clearing and settlement arrangements have become more evident. Improvements are also essential to help European markets compete internationally.

Against the background of lacking a single market for EU post-trading services, the Commission's work in the post-trading field has quite a long tradition: In the European Community, discussions on clearing and settlement of securities started as early as October 1977 when a study on a new system for the settlement of securities transactions within the EC was completed. After several meetings of the ad-hoc working group taking place in the following years, another study on this subject was completed in December 1983[15]. Work continued within the "Working Party on Transactions in Transferable Securities/Working Party on Clearing and Settlement of cross-border securities transactions" and meetings on the "interlinking of clearing systems" (1984-1992), followed by a Conference and the "Study on the clearing and settlement of securities transactions in the Community" (Kessler report, 1988) which lead to the development of a "Model Agreement between Central Securities Depositories" (1994).

1.5. The First Giovannini Report and the 15 Giovannini Barriers

In Spring 2001 the **Commission's Consultation on Clearing and Settlement** [16] was produced which provided input to the ongoing work on the "**First Giovannini Report**" published in late 2001[17]. The expert group under the lead of Alberto Giovannini made clear that difficulties in the post-trading sector existed within three areas:

- technical requirements and market practices,
- taxation, and
- legal certainty

Within these three areas, the First Giovannini Report identified fifteen specific obstacles for an ideal post-trading market, the so called "**Giovannini Barriers**". Six of the barriers are industry related barriers; nine are public sector barriers.

1.6. The European Commission's First Communication on Clearing and Settlement

The European Commission duly followed up the First Giovannini Report in May 2002 with a Communication entitled Clearing and Settlement in the European Union: Main policy issues and future challenges"[18]. The consultation on this first Communication was completed at the end of 2002.

---

15 By M. Hall (London Stock Exchange) and M.G. Duncan (Milan Stock Exchange)

16 http://europa.eu/rapid/pressReleasesAction.do?reference=IP/01/487&format=HTML&aged=1&language=EN&guiLanguage=en

17 Cross Border Clearing and Settlement Arrangements in the European Union, The Giovannini Group, November 2001 ("First Giovannini Report"); http://ec.europa.eu/internal_market/financial-markets/docs/clearing/first_giovannini_report_en.pdf

18 Communication 'Clearing and settlement in the European Union. Main policy issues and future challenges', COM (2002) 257 of 28 May 2002; http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2002:0257:FIN:EN:PDF

1.7. The Second Giovannini Report

The work was not finished for the Giovannini Group. In its second report[19], the Giovannini Group addressed the question of the nature of concrete actions which should be undertaken to eliminate the problems identified in the first report and it gave indications on the period of time needed for completion of the actions. Depending on the complexity of the matter, the timeframes set for removal of the different barriers varied (albeit no decisive starting date was mentioned in this report). Furthermore, as the addressees of the barriers, i.e. the entities called upon for removing them, were not identical (technical and operational issues being assigned to the private sector whereas tax and legal issues needed to be dealt with by the competent national legislators and authorities) procedures and timelines for removal could not be the same.

1.8. The European Commission's Second Communication on Clearing & Settlement

In response to this report, the European Commission issued in April 2004 its Communication "Clearing and Settlement in the European Union – The way forward"[20] describing the roadmap for future action with a view to enhancing the efficiency and safety of post-trading arrangements across Europe. The Commission's policy regarding post-trading is focused on four pillars: (a) the liberalisation and integration of existing securities clearing and settlement systems, (b) the application of competition policy, (c) the adoption of a common regulatory and supervisory framework including questions of definitions, and (d) the adoption of appropriate governance arrangements[21]. In this paper, the European Commission proposed the following measures:

- to draw up a Directive on clearing and settlement[22] which addressed questions of (1) rights of access and choice, (2) a common regulatory framework, and, (3) governance;
- to set up the CESAME Group[23] with respect to issues related to technical requirements and market practices;
- to establish the FISCO Group[24] to advise on further action in the fields of taxation, and

---

19 Second report on EU Clearing and Settlement arrangements, The Giovannini Group, April 2003 ("Second Giovannini Report"); http://ec.europa.eu/internal_market/financial-markets/docs/clearing/second_giovannini_report_en.pdf

20 Clearing and Settlement in the European Union – The way forward, Communication from the Commission to the Council and the European Parliament, COM(2004) 312 final, 28 April 2004 ("Commission second Communication), http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2004:0312:FIN:EN:PDF

21 See p. 10f.

22 In the end, the EU Commission did not adopt a Directive but initiated the creation of an Industry Code of Conduct on Clearing and Settlement; see also Draft Working Document on Post-Trading, 23.05.2006, all information available at http://ec.europa.eu/internal_market/financial-markets/clearing/communication_en.htm#code.

23 "Clearing and Settlement Advisory and Monitoring Experts' Group" ("CESAME"), http://ec.europa.eu/internal_market/financial-markets/clearing/cesame_en.htm.

24 Fiscal Compliance Experts' Group ("FISCO"), http://ec.europa.eu/internal_market/financial-markets/clearing/compliance_en.htm.

– to create the Legal Certainty Group[25] regarding the issue of legal certainty.

The publication of the Second Communication was followed by another public consultation[26] which showed broad support for some issues (e.g. the creation of the working groups CESAME, FISCO and Legal Certainty) but divided views on others (e.g. whether or not the Commission should work on a directive on clearing and settlement).

1.9. Further developments

More details on further developments happening after the creation of the CESAME group, such as the Industry Code of Conduct, the ESCB-CESR Recommendations, the TARGET2-Securities Project are contained in section 5. of this report; the Fiscal Recommendations are described in paragraph 4.1.4.

[25] Legal Certainty Group ("LCG"); http://ec.europa.eu/internal_market/financial-markets/clearing/certainty_en.htm.

[26] See summary of responses: http://ec.europa.eu/internal_market/financial-markets/docs/clearing/2004-consultation/reponses_en.pdf

B. The Giovannini Barriers and the CESAME Group

2. The CESAME Group

In order to achieve the objective[27] stated in the Commission's Communication of April 2004, and to tackle all Giovannini Barriers in parallel, the Commission set up three expert groups. The first one[28], the **Clearing and Settlement Advisory and Monitoring Group ("CESAME")** was an industry group which had a dual role: first to advise and assist the Commission in the integration of EU securities clearing and settlement systems in general; second, to focus on the removal of those Giovannini Barriers for which the private sector has sole or joint responsibility.

The work of the CESAME Group set standards for mutual understanding, open discussion, co-operation and subsequent action of market participants, industry associations and the relevant parts of the public sector. The Group transparent working method was exemplary and contributed tremendously to the success of its work.

2.1. Creation of the CESAME Group; its mandate, Members and Participants

The CESAME Group was set-up in summer 2004 (see press release of 16 July 2004[29] on the first meeting), and was required[30] to:

- support the project and ensure transparency,
- ensure coherent action by
  - being the interface between private and public sector bodies
  - offering informal assistance and
  - liaising with other groups (G30, FISCO, Legal Certainty Group etc.)
- coordinate the action of the private sector in removing certain Giovannini Barriers.

The Members of the CESAME Group[31] were appointed *ad personam* on the basis of their merits, knowledge and capabilities to facilitate the process. However, membership has of course changed to some extent over the years (see participants' lists for each meeting, available on the website). The Group also invited experts from time to time for presentations and discussion of specific topics (see paragraph 5.9. of this report). A key feature of the working method of the Group was that participants where fully transparent on their contact details (in line with data protection requirements) and open to convey outside input of non-members if relevant to the discussion.

---

27 i.e. the creation of efficient and safe EU securities clearing and settlement systems which ensure a level playing field among the different providers of post-trading services,

28 The two other groups, FISCO and Legal Certainty Group – working on fiscal and legal issues – we set up shortly after the CESAME group in 2005, see their respective website: http://ec.europa.eu/internal_market/financial-markets/clearing/compliance_en.htm; http://ec.europa.eu/internal_market/financial-markets/clearing/certainty_en.htm

29 http://europa.eu/rapid/pressReleasesAction.do?reference=IP/04/935&language=en&guiLanguage=en, see Annex 3 for participants

30 Mandate, see Annex 2: http://ec.europa.eu/internal_market/financial-markets/docs/cesame/mandate_en.pdf

31 Detailed participants lists for each meeting are available on the CESAME website

2.2. Meetings of the CESAME Group

The CESAME Group has met usually three times per year. For each of the thirteen meetings[32], the agenda, a list of participants, a report (i.e. the detailed minutes of the meeting, entitled "Synthesis Report") and the operational conclusions were prepared and posted on the CESAME Group's designated website[33]. The large majority of documents distributed at the meetings are also posted on this website.

2.3. Short overview on the Giovannini Barriers, achievements and state of play as per October 2008

The main focus of the Group was the removal of a number of Giovannini Barriers for which it was felt, by the Giovannini Group and the Commission, that the industry was much better placed to obtain results. For memory: the 15 Giovannini Barriers are as follows:

- Barrier 1: The diversity of IT platforms
- Barrier 2: Restrictions on location of clearing and settlement
- Barrier 3: Corporate actions
- Barrier 4: Absence of intra-day settlement finality
- Barrier 5 Impediments to remote access
- Barrier 6: Differences in standard settlement periods
- Barrier 7: Different operating hours/settlement deadlines
- Barrier 8: Differences in securities issuances (dismantled)
- Barrier 9: Restrictions on the location of securities
- Barrier 10: Primary dealer restrictions
- Barrier 11: Restrictions on withholding agents
- Barrier 12: Restriction on tax collection
- Barrier 13: Absence of EU-wide framework of laws
- Barrier 14: Legal treatment of netting
- Barrier 15: Conflict of laws

Out of those 15 Giovannini Barriers, CESAME was asked to tackle six of them (i.e. those identified as industry-related barriers), namely Barrier 1 (The diversity of IT platforms); Barrier 3 (Corporate actions); Barrier 4 (Absence of intra-day settlement finality); Barrier 6 (Differences in standard settlement periods); Barrier 7 (Different operating hours/settlement deadlines); and Barrier 8 (Differences in securities issuances). Early in its work, however, the Group felt the need to revisit the categorisation of these barriers and certain assumptions that were made by the Giovannini Group as to their removal (see paragraph 2.4. below).

2.4. The re-grouping and re-classification of the Giovannini Barriers for CESAME Group's discussion

Through the initial discussion on the importance of the different barriers, it emerged that the industry perceived tackling some barriers as more urgent (or feasible) than others. In regard of timing, notably Barrier 6 on different standard settlement periods was assessed as less important and more difficult to resolve (since previous initiatives to shorten settlement cycles

---

[32] See Annex 4: List of participants

[33] http://ec.europa.eu/internal_market/financial-markets/clearing/cesame_en.htm

were driven on a global basis[34] - which was deemed useful by the industry). However, the group discussed some approaches to alleviate the consequences of this barrier through matching. Certain other barriers were perceived – by industry and public sector – as being strongly connected, therefore, a new grouping of the barriers quickly emerged.

As a result, CESAME combined:

Taking together Barriers 4 and 7: Work on Barriers 4 and 7 by ECSDA had already started quite early and before the CESAME group was established. It resulted in 10 ECSDA-Standards[35] to resolve these two barriers at the same time; therefore both barriers have always been jointly dealt with. The Settlement Finality Directive (SFD) and the recent amendments proposed to the Directive so as to encompass links between CSDs and night processing has also played an important role in removing Barrier 4 (intraday finality).

Collapsing Barrier 10 into Barrier 2: After discussion in the EFC Sub-Committee on Government Bonds (for more details: see chapter 4.5), the public sector stated that Barrier 10 was effectively a sub-issue of Barrier 2 (the 'collapsing' of Barrier 10 into Barrier 2). Also, since Barriers 2 and 9 are both related to 'location', they were always strongly linked.

[34] E.g. the Committee on Payment and Settlement Systems (CPSS) and the Group of 30 recommendations

[35] See First ECSDA response to the second Giovannini Report, April 2004; https://www.ecsda.com/attachments/working_groups/harmonization_(wg5)/first_ecsda_response_to_the_second_giovannini_report.pdf

The table below shows the re-grouped 15 Giovannini Barriers, including an overview on what progress on dismantling them has been achieved (as of October 2008). For the outstanding parts (i.e. work still to be done) please refer to the table at the end, see part "C. Conclusions and outlook" of this report.

Giovannini Barrier[36]	Achievements and state of play
1. **Diversity of IT platforms/interfaces**	SWIFT Common Protocol adopted, implementation (by March 2011) plan in place, gaps identified and work in progress to fill identified gaps
2. ***Restriction on location of C&S*** & 10. ***Primary dealer restrictions***[37]	MiFID rules on choice of settlement location adopted (which should remove restrictions on the secondary markets); Code of conduct signed; implementation of both monitored
9. ***Restrictions on location of securities***	Discussed and proposed solution provided by the Legal Certainty Group
3. **Different rules governing corporate actions**	Market Standards for corporate actions processing and for general meetings drafted; standards for distributions in implementation phase; work to combine them in one set as well as an encompassing schedule for endorsement and implementation is under way
4. **Absence of intra-day settlement finality &** 7. **Different operating hours/settlement deadlines**	10 ECSDA standards adopted and largely implemented by CSDs (Note: as these barriers were dismantled in view of "issuer CSDs", problems remain in view of an "investor CSD" view, see paragraph 5.12.2.)
5. ***Impediments to remote access***	Non-discrimination rule on remote access in MiFID; remote access to central bank credit issue will become irrelevant for TARGETcash participants; issues relating to EU currencies other than the euro have not been discussed in CESAME
6. **Differences in standard settlement periods**	No progress so far; harmonisation of (T+x) standard was not considered a priority; standards for pre-settlement date matching adopted and under implementation; market solutions of same-day-affirmation available
8. **Differences in securities issuances**	Dismantled
11. ***Restrictions on withholding agents***	FISCO 1st Fact Finding Report and solutions suggested by 2nd FISCO Solutions Report; discussed in EU/OECD group; COM Recommendation in preparation
12. ***Restrictions on tax collection***	FISCO 1st Fact Finding Report finished; Solution suggested, i.e. bilateral discussion with Member States concerned
13. ***Absence of EU-wide framework of laws***	Existing Law reviewed by LCG; solutions proposed in second LCG report
14. ***Legal treatment of netting***	Dismantled
15. ***Conflict of laws***	FCD/SFD provide EU-"PRIMA" rule; different rule under Hague Convention debated in Council

2.5. Interdependencies between barriers

The CESAME participants frequently pointed out that fully dismantling certain industry-related barriers would not be possible unless the public sector successfully worked on dismantling their respective barriers. One clear example of this interdependence is Barrier 3: i.e. corporate actions which are intrinsically embedded in the domestic legal (e.g. company

[36] **public barriers in** *light italics***, industry barriers bold and underlined**

[37] "collapsed" into barrier 2 by EFC Sub-Committee on EU Government Bonds

and securities law) and fiscal (withholding tax) framework of each Member State which the market participants have to observe and cannot change themselves. While this is acknowledged by the public sector, the industry is – up to now – still working on listing the obstacles in detail – which is an indispensable prerequisite to ask Member States for change in a targeted way. This situation is expected to improve when the Market Implementation Groups (MIGs) will have reported on their efforts to implement the market standards developed for Barrier 3.

2.6. Timing of the removal - the "Giovannini Indicators"

The removal of the 15 Giovannini Barriers comprises a sequence of actions. The Second Giovannini Report considered that a period of three years from the initiation of the project would be sufficient for the removal of all 15 Giovannini Barriers. This "deadline" implicitly conformed as closely as feasible to the deadline set by the Lisbon European Council for full implementation of the Financial Services Action Plan (FSAP). However, CESAME took its actual commencement of its work in October 2004 as the starting point for the purpose of calculating the target times.

Monitoring the progress on the removal of the Giovannini Barriers is important in this respect. In order to facilitate it, the Commission's Directorate General Internal Market and Services in cooperation with the Directorate General Joint Research Centre has developed a methodology [38], using a combination of qualitative and quantitative indicators. The methodology distinguishes two separate phases: the standard-setting phase and the implementation phase. The first phase refers to the activities connected with the formulation of standards at European level (here the term "standard" has a broad meaning and includes recommendations, standards, legislation etc.) that should help remove the Giovannini Barriers, while the second phase refers to the activities connected with the actual implementation of these standards at national level.

The methodology provides a guide in terms of data collection at national level (to be performed by local Market Implementation Groups and other bodies/entities/organisations) and the compilation of this data for reporting purposes (to be carried out by the Commission). The tables contained throughout this report to indicate the state of play for each barrier are the direct result of application of the methodology to the factual data, some of which was provided by different sources within the industry.

3. The core work of the CESAME group: the six industry-related Giovannini Barriers

The six industry-related Giovannini Barriers were not grouped, although some of them were clearly linked. Therefore, the historical development of the work on these barriers is crucial to the proper understanding of the present grouping of the barriers.

3.1. The six industry Giovannini Barriers

The First Giovannini Report identified six barriers with which the industry should deal, namely

- Barrier 1: The diversity of IT platforms

[38] See: http://ec.europa.eu/internal_market/financial-markets/docs/cesame/ec-docs/indicator_methodology_en.pdf

- Barrier 3: Corporate actions
- Barrier 4: Absence of intra-day settlement finality
- Barrier 6: Differences in standard settlement periods
- Barrier 7: Different operating hours/settlement deadlines
- Barrier 8: Differences in securities issuances (dismantled)

3.2. Barrier 1: Diversity of IT platforms/interfaces

"National differences in the information technology and interfaces used by clearing and settlement providers should be eliminated via an EU wide protocol. SWIFT should ensure the definition of this protocol through the Securities Market Practice Group. Once defined, the protocol should be immediately adopted by the ESCB in respect of its operations. This barrier should be removed within two years from the initiation of this project."

3.2.1. The issue: What is the problem?

Barrier 1 was described in the Giovannini reports as the national differences in information technology (IT) and interfaces used by post-trade clearing and settlement providers. In many cases proprietary systems are deployed which impose substantial back office costs on investors/intermediaries who have to link to these different systems. In particular entities which link to multiple proprietary systems face substantial costs in terms of the investment required to link to and maintain these interfaces. In many cases they are also faced with a greater level of manual processing (which is often connected with a higher risk of errors). Such differences also make straight-through processing more difficult or even unattainable across systems.

What is ISO? What is SWIFT?

The International Organization for Standardization (ISO)[39] is a worldwide federation of national standards bodies (ISO member bodies). It coordinates worldwide standardisation in various business areas including financial markets and services.

SWIFT[40] is a co-operative established by and for the financial industry and a global provider of secure financial messaging services. Its customers can automate and standardise financial transactions, thereby lowering their costs, reducing their operational risk and eliminating inefficiencies from their business operations.

3.2.2. The solution: An industry approach leading to a "Final Protocol Recommendation" linked to ISO standards

The Giovannini reports proposed to develop and implement a standardised protocol for communication, including harmonised connections and messaging protocols based on ISO

[39] http://www.iso.org/iso/home.htm

[40] http://www.swift.com/index.cfm?item_id=43232

standards (ISO 15022 and ISO 20022). Even taking account of the substantial cost implied and the technical challenges, the Giovannini group determined that it could be done within two years (i.e. by early 2007). SWIFT, in their capacity as ISO Registrations Authority[41] and through the Securities Market Practice Group (SMPG)[42], was tasked to define a solution to eliminate Barrier 1. Additionally, ECSDA's Working Group 6 (Communication)[43] was founded to address cross-border Barrier 1 communication issues and contributed to SWIFT's work on solutions to Barrier 1.

After an initial period of research in 2003 and 2004 involving European infrastructures, key institutional participants and a significant number of representative organisations, SWIFT took the process to the next stage by publishing a consultation paper in January 2005. The paper outlined the proposed framework of a common protocol in response to the Giovannini Group report and the mandate of the CESAME group.

Following discussion in the CESAME Group, an Independent Advisory Group (IAG)[44] was created to review the detailed feedback from the industry consultation. This further discussion and feedback helped to define a solution in the form of a standard protocol for communication within the European clearing and settlement industry. The conclusions of the IAG's work between July and September 2005 formed the core of the draft common communication protocol published on 25 October 2005. SWIFT published the final common communication protocol report in March 2006, following comments received on the October 2005 draft.

The ISO 15022 standard and its messages were already central to the communications model of many clearing and settlement systems worldwide – but still not to all entities. While the infrastructures themselves benefited from improved productivity and operational efficiencies, all participants gained from the reduction in risk and costs of domestic and cross-border transactions by the use of ISO standards. Therefore, one of the key recommendations of the protocol was that all securities market infrastructures and participants involved in the European Union clearing and settlement space must support the use of ISO 15022 and/or (the new) ISO 20022 standards. To enable this, the protocol stipulated that by March 2008, a **gap analysis** of the ISO 15022 and ISO 20022 message suite must be completed by SWIFT for all infrastructures in all EU Member States (plus other countries as necessary) to:

---

41 The ISO 15022 and ISO 20022 Registration Authority (RA) is the guardian of the Repository of both standards. The RA's mission is to ensure compliance with the rules and guidelines as defined in the two ISO standards and to publish - on behalf of ISO - the Repositories on respectively http://www.iso15022.org. http://www.iso20022.org.

42 The Securities Market Practice Group (SMPG) started in July 1998 with the mission to create globally-agreed market practices for the securities industry. This would include the harmonisation of non-regulated geographic differences as well as consistent implementation by securities industry participants for processing within and across all markets. Members of the SMPG (broker/dealers, investment managers, custodian banks, central securities depositories and regulators) and the National Market Practice Groups (NMPG) aim at promoting standards in conjunction with defined market practices which should bring the industry closer to its goal of achieving STP. NMPGs analyse and document local practices. SWIFT Standards then collates common elements, specifies additional country requirements and identifies further opportunities for harmonisation of non-regulated differences. After final review and refinement by the SMPG, the documents are published; see http://smpg.webexone.com/default.asp?

43 https://www.ecsda.com/portal/working_groups/communications__wg_6_/

44 Barrier 1 Independent Advisory Group: Following discussion with CESAME, the EU's Giovannini monitoring committee, an independent advisory group under the chairmanship of Stephan Schuster, Co-Chair of the G30 European Monitoring Committee, was created to review the detailed feedback from the industry consultation on the removal of Giovannini Barrier 1. Access all meeting minutes and slides on the Giovannini-dedicated section on swift.com: http://www.swift.com/index.cfm?item_id=43429

a) identify missing functionalities and
b) extend the standards to cover these gaps.

To satisfy this part of the recommendation, and to maintain momentum in the removal of Barrier 1 for the securities market, SWIFT started working with the EU infrastructures to identify the processes and activities that they support in the clearing, settlement and asset servicing market spaces. These activities were mapped against ISO messages to identify the gaps. This consultation with the institutions and market infrastructures showed that infrastructures would be able to deliver most of the basic services with the current ISO message standards, but not all. SWIFT published the preliminary report of this research for comment in December 2006. Institutions were asked to review the report and note whether activities were missing from the inventory, whether they were incorrectly identified or whether the identified ISO message was inappropriate. This further consultation finished on 15 March 2007. SWIFT worked with the SMPG (Securities Market Practice Group) and other industry groups to assess each of the gaps in terms of their market impact. Feedback indicated that, in the majority of cases, clearing and settlement processes are well covered by the ISO standards[45].

The high level Giovannini ISO gap analysis was completed according to the schedule agreed in the original protocol recommendation and communicated to the market in June 2007. The year-long gap analysis process provided an insight into the industry's priorities for enhancing ISO messaging. In particular, it was clear that attention needs to be focused on elimination of high level gaps, and on efforts to increase the rate of adoption of ISO messages in the market worldwide. During this process, SWIFT was strongly encouraged to reach out to institutions and market infrastructures outside Europe, to ensure that the recommendations for removing Barrier 1 become recognised and implemented by all markets around the world. The SMPG (Securities Market Practice Group) also remained committed to helping SWIFT and the community achieve their common goals. Both the existing SMPG market practice guidelines and the SWIFT Giovannini gap analysis are important milestones in the removal of Giovannini Barrier 1. Following this high level analysis, market infrastructures requested SWIFT to undertake a more detailed gap analysis which would acknowledge missing functionalities and provide a timetable for the closure of identified gaps. This further analysis was completed in March 2008.

In June 2007, a draft "File Transfer Rule Book" was published to give best practice guidance for file transfer to complement the Giovannini Protocol Recommendation. This was in response to the growing demands for clear guidance on the implementation of the Giovannini Protocol. To complement the Giovannini Protocol Recommendation published in March 2006, SWIFT had been working with senior industry representatives to develop the File Transfer Rulebook, which specifies generic rules for file construction and best practices for file transfer operations for any and all file transfers, on any network. The objective of the File Transfer Rulebook is to eliminate the requirement for business partners, who need to send file transmissions to each other, to go through expensive and time-consuming design processes before setting up their systems. It does this by specifying header and content structures which can be replicated easily on any technology platform, and which complement the Giovannini

[45] The main gaps in ISO messaging are in clearing; and whilst the vast majority of core settlement and asset servicing processes are covered by existing ISO messages, high-level gaps exist in a few other areas, such as securities reference data and auto-collateralisation.

Protocol by re-using components from the ISO standards domain. The Rulebook[46] open consultation ran until September 2007.

Related issues: From ISO 15022 to ISO 2022 and what is XML?

ISO 15022 set the principles necessary to provide the different communities of users with the tools to design message types to support their specific information flows. These tools consist of a set of syntax and message design rules, a dictionary of data fields and a catalogue for present and future messages built by the industry with the above mentioned fields and rules. To address the evolving needs of the industry as they arise, the Data Field Dictionary and Catalogue of Messages have been kept outside the standard. They are made available by the Registration Authority (which is in this case SWIFT) which maintains them as necessary upon the request of industry participants (i.e. the industry suggests changes and additions).

ISO 20022 – The **UNI**versal **F**inancial **I**ndustry Message scheme (UNIFI) is the updated[47] international standard[48] that defines the ISO platform for the development of financial message standards. Its business modelling approach allows users and developers to represent financial business processes and underlying transactions in a formal but syntax-independent notation. These business transaction models are the "real" business standards and can be converted into physical messages in the desired syntax. UNIFI proposes a standardised XML-based syntax for messages as XML (eXtensible Mark-up Language) is the preferred syntax for e-communication.

The **E<u>x</u>tensible <u>M</u>arkup <u>L</u>anguage** (**XML**) is a general-purpose specification for creating custom markup languages. It is classified as an extensible language because it allows its users to define their own elements. Its primary purpose is to facilitate the sharing of structured data across different information systems, particularly via the Internet, and it is used both to encode documents and to serialize data. It started as a simplified subset of the Standard Generalized Markup Language (SGML), and is designed to be relatively human-legible. XML is recommended by the World Wide Web Consortium. It is a fee-free open standard.

---

[46] The industry representatives who have approved the Rulebook for publication include ISSA, ISITC-IOA and SMPG, as well as Citi, Morgan Stanley, BNPP Securities Services, Euroclear, Clearstream, LCH.Clearnet, UBS, State Street, FBE, Deutsche Bank, Barclays Global Investors, Northern Trust and NCSD. One of the earliest institutions to make use of the rulebook is Standard Bank in South Africa, who have decided to use it to design a new system for the communication of bulk payments for worker remittance processing.

[47] The need for a UNIFI standard arose in the early 2000's with the widespread growth of Internet Protocol (IP) networking, the emergence of XML as the 'de facto' open technical standard for electronic communications and the apparition of a multitude of uncoordinated XML-based standardization initiatives, each having used their own "XML dialect".

[48] The standard was developed within the ISO Technical Committee TC68 (Financial Services). The focus of UNIFI is on international (cross-border) financial communication between financial institutions, their clients and the domestic or international 'market infrastructures' involved in the processing of financial transactions. However, UNIFI can be used for the development of new domestic financial messages as well, thereby streamlining all communications for financial institutions. On top of offering a common and "UNIFIed" way of using XML, the new standard shields investments from future syntax changes by proposing a common business modelling methodology (using UML – Universal Modelling Language) to capture, analyze and syntax-independently describe the business processes of potential users and their information needs.

3.2.3. Stocktaking: What has been achieved so far?

Overview: Timetable of events on Barrier 1 – The development of the Common Protocol

24 December 2004	Consultation paper released http://www.swift.com/index.cfm?item_id=57314
5 January 2005	SWIFT presents protocol framework in response to Giovannini Report http://www.swift.com/index.cfm?item_id=43507
23 March 2005	15 April deadline for feedback on protocol framework http://www.swift.com/index.cfm?item_id=43546
13 July 2005	Industry responds to Giovannini consultation paper
31 August 2005	Independent Advisory Group (IAG) established and working http://www.swift.com/index.cfm?item_id=57398
25 October 2005	Independent Advisory Group completes its task http://www.swift.com/index.cfm?item_id=57938
March 2006	**Final Protocol Recommendations** http://www.swift.com/index.cfm?item_id=58219
27 December 2006	Preliminary Gap Analysis Report http://www.swift.com/index.cfm?item_id=61064
15 June 2007	New File Transfer Rule Book for comment http://www.swift.com/index.cfm?item_id=62254
28 June 2007	High level Gap analysis complete http://www.swift.com/index.cfm?item_id=62392
March 2008	Detailed Gap Analysis Finalised

As the table above shows, the work of the industry is well advanced and on track: concrete actions are planned and timetables are set. The major achievement and key milestone reached in the dismantling of Barrier 1 as regards "standard setting" was the finalization of the final recommendation for the communication protocol designed to eliminate Giovannini Barrier 1 in the European securities Clearing & Settlement market [49] ("Final Protocol Recommendations") which SWIFT released on 3 April 2006 on behalf of the Independent Advisory Group (IAG). Additionally, the vast majority of institutions and infrastructures responding to the draft publication indicated their intent to implement the solution over the specified five year time horizon. The level of support and contribution made by many market participants to the communication protocol ensures that it is an industry designed solution.

In early 2008 SWIFT conducted a survey of European CSDs and CCPs to identify their clients' requirements for Giovannini compliant communications. The survey was designed to provide useful background for the CSDs and CCPs to feed into their plans for implementation of the Barrier 1 protocol. Follow-up discussions with the infrastructures and their industry associations have been held to identify current compliance status and future plans. In March 2008 SWIFT finalized a detailed standards gap analysis to identify missing functionalities. Encouragingly, identified gaps are already in the process of being filled by SWIFT in cooperation with the industry. This process is more advanced for CSD's than for CCP's.

More recently, SWIFT has co-operated with ECSDA on a further survey of the capabilities and plans of CSDs in this area. The table below provides a high level overview of the compliance of CSDs with the Giovannini protocol in respect of the key

[49] http://www.swift.com/index.cfm?item_id=58219

settlement/reconciliation and corporate actions processes based upon feedback from the surveys:

Table: Compliance of CSDs with the Giovannini Protocol for key processes (October 2008)

Country/CSD	Giovannini Barrier 1 Process	ISO15022/20022 Barrier 1 Message Standards Supported: Yes, Partial, No or N/A	Barrier 1 Communications Layer Supported: Yes, Partial, No or N/A	% of Traffic Compliant
Austria OekB	Settlement & Reconciliation	Y	Y	100%
	Corporate Actions	Y	Y	100%
Belgium Euroclear	Settlement & Reconciliation	Y	Y	20%
	Corporate Actions	Y	Y	100%
Bulgaria CDAD	Settlement & Reconciliation	Partial	Y	0%
	Corporate Actions	N		
Cyprus CSD	Settlement & Reconciliation	Partial Impl. late 2008	N	
	Corporate Actions	N	N	
Czech Rep Univyc	Settlement & Reconciliation	N	N	
	Corporate Actions	N	N	
Denmark VP	Settlement & Reconciliation	Partial	Y	
	Corporate Actions	Partial	Y	
Estonia CSD	Settlement & Reconciliation	Partial	N	0%
	Corporate Actions	Y	N	0%
Finland APK	Settlement & Reconciliation	Y	Y	100%
	Corporate Actions	Y	Y	100%
France Euroclear	Settlement & Reconciliation	Y	Y	20%
	Corporate Actions	Y	Y	100%
Germany Clearstream	Settlement & Reconciliation	Y	Y	98% by end 2009
	Corporate Actions	Partial (complete 2009)	Y	98% by end 2009
Greece Hellenic CSD	Settlement & Reconciliation	N	N	
	Corporate Actions	N	N	
Hungary Keler	Settlement & Reconciliation	N (Planning for 2009)	N (Planning for 2009)	
	Corporate Actions	N	N	
ICSD Euroclear	Settlement & Reconciliation	Y	Y	30%
	Corporate Actions	Y	Y	30%
Italy Monte Titoli	Settlement & Reconciliation	Y	Y	100%
	Corporate Actions	Y	Y	100%
Latvia CSD	Settlement & Reconciliation	Y	Y	5%
	Corporate Actions	Y	Y	5%
Lithuania CSD	Settlement & Reconciliation	N	N	
	Corporate Actions	Partial	N	
Luxembourg ICSD Clearstream	Settlement & Reconciliation	Y	Y	100%
	Corporate Actions	Y	Y	100%
Malta CSD	Settlement & Reconciliation	Partial	Implementing	
	Corporate Actions	Partial	Implementing	
Netherlands Euroclear	Settlement & Reconciliation	Y	Y	20%
	Corporate Actions	Y	Y	100%
Poland KDPW	Settlement & Reconciliation	Partial	Y	100% for CSD 0% for clients
	Corporate Actions	Partial	Y	100% for CSD 0% for clients
Portugal Interbolsa	Settlement & Reconciliation	Partial (Settlement only)	N	
	Corporate Actions	N		
Romania CSD	Settlement & Reconciliation	N (Planning for 2009)	N	
	Corporate Actions	N	N	
Slovak Rep CDCP	Settlement & Reconciliation	N	N	
	Corporate Actions	N	N	
Slovenia KDD	Settlement & Reconciliation	N	Y	
	Corporate Actions	N	Y	
Spain Iberclear	Settlement & Reconciliation	Partial	Y	100% of bilateral flows
	Corporate Actions	N	Y	
Sweden VPC	Settlement & Reconciliation	Y	Y	5%
	Corporate Actions	N	Y	
Switzerland ICSD SIS	Settlement & Reconciliation	Y	Y	100%
	Corporate Actions	Y	Y	100%
UK and Ireland Euroclear	Settlement & Reconciliation	Partial	Partial	0%(will be 100% post 2009 CCI)
	Corporate Actions	Partial	Partial	0%(will be 100% post 2009 CCI)

No detailed picture on the compliance of CCPs with the Barrier 1 Communication Protocol could be established, so it is likely that no CCP is currently fully compliant. However, this may well reflect the fact that further message standards' development is required for CCPs.

Overview: Giovannini Indicators – Barrier 1 Solution Definition and associated message standards activities

The Barrier 1 Solution has four main elements: 1. Definition of Protocol, 2. Message Standards Gap Analysis, 3. Standards Availability and 4. Implementation. The table below covers points 1 to 3 and provides an overall indicator of the completeness of these standards related aspects of the protocol.

Table: Giovannini Barrier 1 – Standard setting

Fact-finding sub-phase	***Average progress***	**100%**
	Definition of Protocol	100%
	Completion of gap analysis (standards vs. process)	100%
Standard-setting sub-phase	***Average progress***	**77%**
	Settlement & Reconciliation standards provision	90%
	Corporate actions	85%
	Collateral management	80%
	Cash management	80%
	Clearing	58%
	Other business processes (e.g., proxy, ref. data)	51%
Endorsement sub-phase	***Average progress***	**75%**
	Settlement & Reconciliation standards provision	90%
	Corporate actions	80%
	Collateral management	80%
	Cash management	80%
	Clearing	54%
	Other business processes (e.g., proxy, ref. data)	50%
Overall progress		**91%**

Table: Giovannini Barrier 1 – Implementation

Member State / Institution			**AT**	**BE**	**BG**	**CY**	**CZ**	**DK**	**EE**	**FI**	**FR**	**DE**	**EL**	**HU**	**IE**	**IT**
CSD	***MS***	***S&R***	100%	100%	25%	25%	0%	25%	25%	100%	100%	100%	0%	5%	25%	100%
		CA	100%	100%	0%	0%	0%	25%	100%	100%	100%	25%	0%	0%	25%	100%
	CL		100%	100%	100%	0%	0%	100%	0%	100%	100%	100%	0%	5%	25%	100%
CCP			0%	0%	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	0%	0%	n.a.	0%	n.a.	0%
Overall progress			**67%**	**67%**	**58%**	**8%**	**0%**	**63%**	**28%**	**100%**	**67%**	**57%**	**0%**	**3%**	**25%**	**67%**

Member State / Institution			**LV**	**LT**	**LU**	**MT**	**NL**	**PL**	**PT**	**RO**	**SK**	**SL**	**ES**	**SE**	**UK**	**EU**
CSD	***MS***	***S&R***	100%	0%	100%	25%	100%	25%	50%	5%	0%	0%	25%	100%	25%	**71%**
		CA	100%	25%	100%	25%	100%	25%	0%	0%	0%	0%	0%	0%	25%	**51%**
	CL		100%	0%	100%	5%	100%	100%	0%	0%	0%	100%	100%	100%	25%	**79%**
CCP			n.a.	n.a.	n.a.	n.a.	0%	0%	0%	n.a.	n.a.	n.a.	0%	n.a.	0%	**0%**
Overall progress			**100%**	**5%**	**100%**	**15%**	**67%**	**42%**	**10%**	**2%**	**0%**	**50%**	**38%**	**80%**	**17%**	**49%**

Notes: MS – message standard
CL – communications layer
S&R – settlement and reconciliation
CA – corporate actions
n.a. – not applicable

3.2.4. Future Planning: What still has to be done to dismantle the Barrier

The major activity to deliver the dismantling of Barrier 1 is the full implementation of the Protocol, which is due to be completed by March 2011. This looks challenging but feasible (keeping in mind that it entails major IT changes and extensive testing).

One factor which is relevant to the implementation of the Protocol for removing Barrier 1 is the ongoing discussion within the industry on when to change from ISO 15022 (the standard referred to in the Second Giovannini Report) to the new XML-based ISO 20022 standard. Obviously, this is of major importance for the industry given the high costs involved with such substantial changes to the IT setup of the industry (some of which have only recently incurred the cost of adopting ISO 15022). The CESAME Group acknowledged the importance of the cost factor for the successful introduction of this standard but took into account the fact that normally businesses periodically have to renew and review their IT facilities; the target date of 2011 provides thus ample scope for planning ahead, so that businesses would be able to take into account the new standards when they design and budget for the upgrade or renewal of their facilities. This would minimise the cost effects of the introduction of the new standards. Furthermore, the market has been demanding a high level timetable from SWIFT which indicates when SWIFT will commit to delivering the functionalities which are currently missing from the current ISO 20022 proposals for new messages. The main success of the removal of this barrier will be the actual implementation of the proposed standards across CSDs.

The adoption of ISO 20022 could receive a substantial boost from TARGET2-Securities. Indeed, TARGET2-Securities would use this standard from the start. This would imply the de facto adoption of the standard by those CSDs that would choose to connect to TARGET2-Securities and by those users that would choose to be directly connected to TARGET2-Securities. Even though non-directly connected users would not use ISO 20022, there would be an incentive for its adoption even for them.

An additional issue that needs to be addressed is the reluctance of some intermediaries whose business focuses primarily on their domestic markets to introduce the new standards drawn up, in their view, for cross-border business. To the extent that the introduction of the new standards will not entail 'real' additional cost (but be factored into ongoing IT updates), domestic entities are encouraged to adapt them in order to avoid the running of dual systems by infrastructures. Also, the standards are generic, i.e. will be usable not only for SWIFT clients but for any other providers.

3.3. Barrier 3: Different rules governing corporate actions

"National rules relating to corporate actions, beneficial ownership and custody should be harmonised. The local agent banks acting through the European Credit Sector Associations and together with ECSDA should co-ordinate private-sector proposals. National governments should co-ordinate their response via the relevant EU Council."

3.3.1. The issue: What is the problem?

Corporate actions are events in the life of a public company (usually initiated by the board and approved by the shareholders at their general meeting) which affect the securities (shares

or bonds) issued by the company[50]. Initially, there was some discussion on whether or not general meetings also form a part of corporate actions as described in Barrier 3. However, general meetings are a core part and in fact the source of almost any following corporate actions processing, therefore they had to be part of the solution finding. Consequently, the industry has not only tackled corporate actions in a narrow sense (limited to corporate actions processing), but also covered the main issues related to the preparatory phase of general meetings (e.g. notices to convene the meeting) up to the general meeting itself (e.g. notification of attendance which can include the shareholder's votes); this work is to be seen in the context of the Shareholders Rights Directive (SRD)[51].

The **Giovannini Report** of 2001[52] stated that rules on beneficial ownership, custody and corporate actions should be harmonised at EU level. It highlighted the existence of national differences in operational arrangements but also in legal and tax considerations and regulations; i.e. corporate actions and legal issues (like company law) as well as tax issues (for instance withholding tax on dividends) are closely intertwined and have to be taken into account together. For these reasons, the Giovannini Group considered from the beginning that the tackling of corporate actions processes is one of the most complex issues with many intricate details. In addition, the acting parties – issuers, market infrastructures, intermediaries and investors – see corporate actions processing from different angles (not only for instance when it comes to the costs of processing corporate actions). After the Commission Communication of 2004, the Legal Certainty Group and FISCO were established to deal with, respectively, certain legal and fiscal aspects related to Barrier 3. Against this background, the Legal Certainty Group has also worked on specific legal aspects of corporate actions (see Recommendations 12-14 of the LCG Report).

An example: Harmonising the processing of distributions, e.g. dividend payments

The current market practices as well as rules and regulations in regard of distributions such as dividend payments – the most frequent corporate action event – differ widely from market to market. The absence of a standardised communication process and processing mechanisms has been the cause of significant inefficiencies and considerable costs.

Against this background a set of standards on *i.a.* distributions[53] has been developed that harmonise *inter alia* the information flow from issuers to market participants, the format and contents of such information and how to process the payments. The standards also provide for a sequence of key dates (ex date, record date, payment date) that should warrant in most cases for the distribution (dividend payment) to be directly made to the actual beneficiary, thus

50 Corporate actions can have a direct impact on share-/bondholders, e.g. dividend or coupon payments; others can have an indirect impact, e.g. a stock split could increase liquidity; or almost no impact, e.g. a name change.

51 Directive 2007/36/EC of 11 July 2007 on the exercise of certain rights of shareholders in listed companies, OJ L184 of 14 July 2007, p. 17

52 In detail, the barrier covers a broad range of topics, with an impact beyond pure settlement problems. The differing national practices in the rules governing corporate actions, e.g. how the offering of share options is effected, rights issues etc., information requirements, deadlines for corporate actions and other diverging rules in Member States and markets lead for example to inconsistent treatment of compensation and cash accruals; or the local lodgement of physical documents could inhibit the centralisation of securities settlement and custody. These differences require specialised local knowledge and can be a barrier to efficient cross-border clearing and settlement.

53 Of 25 September 2008 (in consultation until 19 December 2008): http://www.fbe.be/DocShareNoFrame/Docs/2/LADGAMIDLKNEEDNDLCNDCNBL1YC3W4434T3OGO4T476A/EBF/docs/DLS/D1871A_-_CAJWG_Consultation_Paper_25Sep08-2008-01471-01-E.pdf

considerably reducing the number of compensation payments (market claims) (presumably amounting to billions of euros *p.a.*) and reducing thereby annual processing costs in a significant manner (presumably in a multiple of millions of euros).

The implementation of the agreed standards, currently under way, demonstrates in numerous markets the need to adapt market practices to the standards and sometimes also reveals the requirement to change the respective legal and regulatory regimes.

There are a lot of different types of individual corporate actions. ISO Standards 15022/20022 identify around 100 different types whereas some are quite simple, others are much more complex. There are more common corporate actions, e.g. dividend payments and general meetings and very complex ones (e.g. reorganisations). The industry has categorised them into **two broad categories** (this is the result of years-long industry work; the different versions of the so-called "operational conclusions"[54] over time as well as the "overview of industry documents"[55] are testimony to this):

1. Corporate actions *stricto sensu* encompassing
    a) distributions and
    b) reorganisations as well as
    c) transaction management linked with the corporate actions under a) and b)

and

2. General meetings encompassing three processes

    a) Process 1 dealing with the notice to convene the general meeting,
    b) Process 2 dealing with record date and entitlement, and
    c) Process 3 dealing with the notification of attendance including advance voting.

A more detailed description of these categories (as well as background on the record date) can be found in Annex 8.

3.3.2. The solution: Industry's approach

The conclusion was made in the First Giovannini Report (2001) that efforts to improve consistency in the rules governing corporate actions are essential if the integration of EU securities markets is to proceed. As some differences are embodied in law, their removal would not only require industry efforts but a co-ordinated response by national governments.

The Second Giovannini Report (2003) aimed at providing a strategy for removing the problems and Barriers identified in the first Report. The Giovannini Group believed that the **private sector** should take the lead in removing this Barrier and should present a set of agreed proposals on harmonised rules to national governments[56]. Therefore Barrier 3 (corporate actions) was dealt with by **several associations** (see below[57]) which constantly reported

---

54 http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20071022-op-conclusions_en.pdf

55 Under the meeting documents of 18 February 2008 on the CESAME webpage: http://ec.europa.eu/internal_market/financial-markets/clearing/cesame_en.htm

56 See Second Giovanni Report, p. 10, http://ec.europa.eu/economy_finance/publications/publication1950_en.pdf

57 Associations involved are: ECSAs (European Credit Sector Associations: EBF, ESBG, EACB), ECSDA, ESSF (formerly ESF), EuropeanIssuers (formerly EALIC), FESE and EACH

progress to the CESAME Group for discussion, supplemented by input from the Legal Certainty Group. Consistent with the multi-facetted issue, the industry adopted a multi-fold and wide approach.

Table: overview of the different parts of market standards on corporate actions

<table>
<tr><th colspan="8">MARKET STANDARDS ON CORPORATE ACTIONS</th></tr>
<tr><th colspan="5">Corporate Actions strictu senso</th><th colspan="3" rowspan="2">General Meetings</th></tr>
<tr><th colspan="2">Distributions</th><th colspan="3">Reorganisations</th></tr>
<tr><td>Without options</td><td>With options</td><td>Mandatory without options</td><td>Mandatory with options</td><td>Voluntary</td><td rowspan="4"><u>Process 1:</u>
Notice to convene the general meeting</td><td rowspan="4"><u>Process 2:</u>
Record date and entitlement</td><td rowspan="4"><u>Process 3:</u>
Notification of attendance to the general meeting incl. advance voting</td></tr>
<tr><td colspan="5">TRANSACTION MANAGEMENT</td></tr>
<tr><td colspan="5">Market Standards for Transaction Management</td></tr>
<tr><td colspan="2">Market Claims</td><td colspan="2">Transformation</td><td>Buyer Protection Rules</td></tr>
</table>

<u>Corporate actions *stricto sensu*:</u> <u>associations' individual approaches with co-ordination and cooperation following</u>

Individual work of associations (e.g. ECSDA, ECSAs and ESF) started already shortly after the Giovannini Reports. As far as the corporate actions *stricto sensu* are concerned (distributions and reorganisations, see Annex 8 for more details), the relevant associations[58] started with co-ordinating their respective works and shared their respective, finished standards/recommendations. However, to the non-initiated it was rather cumbersome to see through the maze of this work and the need for a single set of universal, harmonised and standardised messages and rules was clearly identified by the CESAME group. Therefore, in 2007 the associations involved decided to establish and work in a joint working group, the "**Corporate Actions Joint Working Group**" (CAJWG)[59]. All relevant stakeholders (like banks, issuers, exchanges, CSDs, CCPs, etc.) are involved via their associations including experts of their members in the standard setting process. The CAJWG has worked out one set of "Market Standards" [60] for all types of corporate actions processing/procedures, *i.e.* distributions and reorganisations as well as for the transaction management linked with these corporate actions.

The developed standards typically cover

- the information flow from the issuer through the chain of market infrastructures and intermediaries (banks, brokers, custodians) to end investors
- key dates
- processing rules

---

58 ECSAs, ECSDA, ESSF (previously ESF), EuropeanIssuers (previously EALIC), EACH and FESE

59 The ESSF chairs the CAJWG and, jointly with the ECSAs, EuropeanIssuers, ECSDA, FESE and EACH, coordinates the work on these corporate actions.

60 which were previously known as 'Common Deliverables', initial version of October 2007: http://www.fbe.be/DocShareNoFrame/Docs/1/LADGAMIDLKNEEDNDLCNDCNBL1DWNW3M9Y4HO4AV9UKBT/EBF/docs/DLS/D0161-Market_Standards_on_Mandatory_Distributions_endorsed_by_all_14-01-2008-2007-01935-01-E.pdf

General meetings: the joint working group on general meetings (JWGGM) developing one set of market standards

As far as general meetings are concerned, the working group was from the start *(i.e.* end 2005) set up as a cross-sector working group, the "**Joint Working Group on General Meetings**" (JWGGM)[61], to develop jointly a single set of standards on general meetings processing.

Implementation and reality-check: the Market Implementation Groups (MIGs)

In addition, the **Market Implementation Groups** (MIGs) were set up at national level in order to facilitate and monitor implementation of the market standards on distributions in the different national markets. It has to be noted that in most markets these MIGs consist mainly of financial intermediaries and CSDs. In a limited number of countries so far, issuers are being involved in the MIGs or joint meetings are set up. These MIGs have recently also been involved in the market consultation of the market standards. Once all standards will be finalised, the MIGs will be involved in their implementation.

3.3.3. Stocktaking: What has been achieved so far?

The process of developing best market practices by the two joint working groups in the form of a single set of "Market Standards" is not yet finalised but is approaching a final stage. As of the end of November 2008, the state of the work in the different areas as is as follows:

Corporate actions *stricto sensu*

Market standards on **distributions** (in cash), the most frequent corporate action event: these Market Standards for Mandatory Distributions[62] had been agreed and endorsed by all associations in January 2008; the implementation work, led by the MIGs is currently being performed. A workshop organised by the ECSAs on 16-17 April 2008 provided for a state of implementation in the various European countries, revealing a high degree of compliance with some remaining gaps, especially in relation to legal dependencies.

Market standards on **distributions with options, reorganisations and transaction management** were finalised by the CAJWG at the end of September 2008 and are currently the subject of a market consultation (until December 2008). The MIGs play a key role in the ongoing consultation and will have a crucial role in the implementation phases.

However, since a single set of market standards was the future aim, also the (already agreed) market standards on distributions were adapted to make them coherent with the other standards and were included into the document (on distributions with options, reorganisations and transaction management) which was distributed for consultation.

---

61 Associations involved are: ECSAs (European Credit Sector Associations: EBF, ESBG, EACB), ECSDA, ESSF (formerly ESF), EuropeanIssuers (formerly EALIC), and FESE

62 Of 25 September 2008 (in consultation until 19 December 2008): http://www.fbe.be/DocShareNoFrame/Docs/2/LADGAMIDLKNEEDNDLCNDCNBL1YC3W4434T3OGO4T476A/EBF/docs/DLS/D1871A_-_CAJWG_Consultation_Paper_25Sep08-2008-01471-01-E.pdf

General Meetings

The initial standard setting phase on operational processes related to **general meetings** was finalised by end April 2008. An initial consultation, limited to standards on Process 1 and a background note (and limited to associations involved), took place in December 2007/January 2008. The complete set of standards for all three processes including an extensive background note was submitted to the market for consultation from end April until the end of June 2008. Feedback was received from European and national associations representing issuers, CSDs, intermediaries and investors as well as from individual organisations of these market participants. During the summer the JWGGM carefully reviewed all feedback that varied from general comments of support, specific comments on the standards and/or the background note, to fundamental opposition in particular to

- the standardised communication, as the default rule, of the information via the CSD and the intermediaries down to the level of the end shareholder; and
- whether this communication could be part of basic custody services and linked thereto the price setting of this communication.

Consequently, the JWGGM had to assess whether there was still a chance of delivering common agreed market standards. The JWGGM decided that it should continue its work on the standards and have a constructive approach, in particular on:

- The fundamental differences: a) communication with the end shareholder: to be accommodated with a realistic opt-out scenario; b) related cost aspect: to be discussed again when discussing a)
- Rewording of the standards: fine tuning of the wording taking into account the market feedback
- Background note: to be revised and redrafted as notes to assist the application of the standards.

The processing of the market feed-back and further revisions by the JWGGM of several mechanisms proposed in the standards as well as the discussions on pending issues in particular the opt-out possibilities from the communication with the end shareholder and cost/pricing issues led to fundamental changes to the standards. As a consequence the JWGGM believed it necessary to plan a further consultation to be finished in the first quarter of 2009.

Table: Overview (Giovannini Indicators) on Barrier 3 achievements

		Fact finding	Standard setting	Endorsement	Average progress
Distributions	***Average progress***	**100%**	**75%**	**0%**	**63%**
	Mandatory[63]	100%	75%	0%	**63%**
	Mandatory with options	100%	75%	0%	**63%**
	Transaction management	100%	75%	0%	**63%**
Reorganisations	***Average progress***	**100%**	**75%**	**0%**	**63%**
	Mandatory with options	100%	75%	0%	**63%**
	Mandatory without options	100%	75%	0%	**63%**
	Voluntary	100%	75%	0%	**63%**
Transaction management		100%	75%	0%	**63%**
General meetings	***Average progress***	**100%**	**75%**	**0%**	**63%**
	Notice to convene GM	100%	75%	0%	**63%**
	Entitlement/shareholder qualification/record date	100%	75%	0%	**63%**
	Notification of attendance to the GM	100%	75%	0%	**63%**
Overall progress		**100%**	**75%**	**0%**	**63%**

The borderline between associations' work on Barrier 3 and the work of the LCG, in particular the LCG Report Part 2 on legal issues regarding Barrier 3 (Recommendations 12-14)

As indicated above, in general the many different issues covered by the term "corporate actions" can be distinguished as either

(i) operational issues – which have to be dealt with by the industry or
(ii) legal issues – which are enshrined in national law that cannot be changed by the industry and thus have to be addressed by the public sector.

The Legal Certainty Group addressed issues pertaining to Barrier 3 in its Recommendations 12, 13 and 14[64]. Whereas Recommendation 12 serves the purpose of delimitation of the scope, Barriers 13 and 14, once transformed into an EU wide legal framework, aim at significantly lowering the effects of holding through intermediated systems cross border on effective corporate actions processing. Notably, Recommendation 14 proposes a harmonised framework of duties of account providers with respect to the processing of corporate actions: relevant information needs to be passed up and down the chain of intermediaries, account providers are held to facilitate the exercise of corporate rights and, lastly, account providers are bound to exercise some specific corporate rights on instruction given by their clients. Further, Recommendation 13 addresses some problems that might occur in relation to corporate actions as soon as holding patterns with a different legal make up have to interconnect cross border: certain jurisdictions might have difficulty in legally recognising that an account holder in a holding chain is not the one who should be entitled to exercise corporate rights. This results for example in situations where account providers are not

63 Standards on mandatory distributions were already adopted by the industry, but subsequently they were adapted to match with the other newly developed standards. This whole set of standards – including the part on mandatory distributions - was then consulted upon which leads to a standard setting rate (according to the methodology for the Giovannini indicators) of 75%, also for mandatory distributions.

64 Recommendations 12-14; http://ec.europa.eu/internal_market/financial-markets/docs/certainty/2ndadvice_final_en.pdf

allowed to cast split votes in a foreign company because the foreign law regards them as ultimate investor. The recommendation set out that, consequently, the law must make possible the interconnection with a holding chain involving holding through one or more account providers using omnibus accounts. Furthermore, the law should recognise that in foreign jurisdictions, holding might occur in the name of an account provider but for the account of other persons (the account provider's clients).

3.3.4. Future Planning: What still has to be done to dismantle the Barrier

The outstanding issue is the final adoption and endorsement of all Market Standards after possible revision based on market feedback, merging them into one single set of Market Standards, undertaking a gap analysis and implementing them.

- **Corporate actions *stricto sensu*:** The consultation on the proposed standards will continue until mid-December 2008. The draft standards might then go through some changes in the first quarter of 2009, depending on the outcome of the consultation.
- **General Meetings:** As regards general meetings, endorsement of all standards was initially planned for autumn 2008 but has been postponed due to re-emerging discussions and subsequent changes to the standards. The standards were finalised at the end of November 2008 and submitted to public consultation in view of smooth endorsement. This means that the standards will presumably be finalised and adopted in the first quarter of 2009. The gap analysis at national level will follow during the next months and implementation should start afterwards. The initial aim was to be fully compliant as soon as operationally possible after the deadline for national implementation of the SRD, namely August 2009.

Table: planned action regarding Market Standards for Corporate Actions

Barrier 3: corporate actions	**Standard setting**	**Implementation**
Distributions, Reorganisations and Transaction Management	*Market consultation ongoing until 19 December 2008; changes of current market standards might occur afterwards*	*Gradually from 2009 (for standards not related to fiscal/legal issues) to 2012*
General meetings	*95% completed; endorsement by associations 1st quarter 2009*	*2010 (subject to the gap analysis and depending on how Member States implement the SRD)*

- **Legal and fiscal issues:** All associations and market participants have insisted numerous times that the processing of corporate actions is firmly rooted in the legal (national company law) and fiscal environment of each Member State. Therefore, Member States have to be aware of the fact that the industry will never be able to dismantle Giovannini Barrier 3 on corporate actions without certain **intervention by Member States** in view of their legal and fiscal set-up (e.g. Barriers 11 and 13, see below).

It is obvious that following the two Giovannini Reports a lot of work has been done by the industry and important goals have been achieved: the knowledge on barrier 3 and its various aspects are much broader; interrelations and overlap to related areas (e.g. company law) are clearer and the conflicting interests of the different stakeholders are more obvious; *i.e.* significant progress was made in the last years. However, after four years of work the industry standards have not been finalised yet. Against this background, high priority should be given

to the finalisation of one single set of standards accompanied by a precise time table for the finalisation and implementation of the standards and followed by detailed annual progress and implementation reports. The industry could also improve transparency on the consultation process and make all relevant information available given on the websites of the involved associations.

3.4. Barriers 4 Absence of intra-day settlement finality and 7 Different operating hours/settlement deadlines

"4. Intra-day settlement finality in all links between settlement systems within the EU should be guaranteed. ECSDA should co-ordinate necessary measures. These measures should be drawn up in close consultation with the ESCB/CESR Joint Working Group.

7. Operating hours and settlement deadlines should be harmonised using TARGET hours as the benchmark. ECSDA should take the lead in this initiative, in close co-ordination with the ESCB."

3.4.1. The issue: What is the problem?

Remaining differences in the opening days, operating hours and deadlines were long cited as harming an efficient cross-border clearing and settlement. The responsibility of fully harmonising opening hours was assigned to the private sector. The European Central Securities Depository Association (ECSDA) took the lead in this project, while co-ordinating actions with central banks, stock exchanges and users of systems.

The Giovannini Group stated in its reports that for assets eligible for use in Euro-system credit operations, the opening hours of the TARGET[65] system should be the guideline across the Euro-zone. It was mentioned that harmonisation across the European Union for opening days, hours and settlement should be achieved with systems that operate with a sufficient number and frequency of batches guaranteeing that securities can be transferred between systems intra-day.

First steps had already been taken as the ECB Users Standards required that all Securities Settlement Systems should have operating days and hours consistent with those of TARGET. However, it was already clear that harmonisation of the closing hours of the systems could not meet the needs of the market without a harmonisation of the time at which the last transaction to be settled on a given day could be entered into the system.

Another aspect was the lack of irrevocable delivery of securities across borders, with the ability to re-use them across the EU. For instance the bond repo markets cited this re-use as a major factor for a continuous growth of financing activities. As settlement systems are required to have intra-day finality for ECB operations, all links between settlement systems should provide intra-day settlement finality within a short period as well. The private sector and central banks were mandated to be involved in setting up intra-day settlement finality as it

---

[65] TARGET was the first RTGS system for the euro, offered by the Eurosystem. It was used for the settlement of central bank operations, large-value euro interbank transfers as well as other euro payments. It provided real-time processing, settlement in central bank money and immediate finality., see http://www.ecb.eu/paym/t2/before/view/html/index.en.html

touches on systemic risks. Real-time or multi-batch systems using the same time table, open on the same days, and operating on compatible or harmonised IT protocols were the aim.

3.4.2. The solution: Industry's approach

Industry work on Barriers 4 and 7 started well before the CESAME Group was created: ECSDA had agreed 10 Standards for implementation until April 2005 for removing Barrier 4 (intraday finality) and Barrier 7 (harmonisation of operating hours and settlement deadlines). However, one has to keep in mind that this exercise was limited to issuer-CSD functions, but it did not tackle the issue from an investor-CSD function[66]. Although there is a high degree of compliance by ECSDA members for some of the standards, others CSDs/ECSDA members who met the targets seemed to have more difficulties in meeting some of the standards. The short time-scale is an indication of the importance all ECSDA members placed on the standards. For ECSDA, it was important to note that the reaching of standards by all securities settlement systems will not, by itself, remove the two Giovannini Barriers. This is due to the fact that other market participants will also have to adapt their practices to match the standards in order to eliminate the two barriers. Where this is the case the report identifies which the market participants who will have to act and how.

3.4.3. Stocktaking: What has been achieved so far?

The market as a whole recognised that ECSDA reached the goal of setting a group of standards for the removal of Barriers 4 and 7 of the Giovannini Report. The standards are implemented by a large number of long-standing/initial ECSDA members, in line with the tasks as drafted by the Giovannini Group. Former CEECSDA members are making a huge effort to meet the same target (see following Tables 1-4). The standards proved to be reliant for the harmonisation of settlement and intraday settlement finality of CSDs but not for cross-border transactions.

[66] This means that although domestic systems open and close more or less at the same time, the conditions for executing transactions at domestic level and at cross-border level are uneven (since they depend on the harmonisation of the cut-off times of the investor CSDs.

Giovannini Barriers 4 and 7: implementation of standards (Giovannini indicators)

Standard	AT	BE	BG	CY	CZ	DK	EE	FI	FR	DE	EL	HU	IE	IT	LV	LT	LU	MT
1	100%	100%	N/A	N/A	0%	50%	N/A	25%	100%	100%	0%	25%	100%	100%	25%	100%	100%	0%
2	100%	100%	100%	N/A	0%	100%	100%	100%	100%	100%	N/A	0%	100%	N/A	100%	100%	100%	0%
3	N/A	100%	N/A	100%	0%	N/A	N/A	N/A	N/A	N/A	N/A	0%	N/A	N/A	N/A	100%	N/A	0%
4	100%	100%	100%	100%	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	0%
5 (start time)	100%	100%	0%	100%	0%	100%	100%	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	0%
5 (finish time)	100%	63%	0%	100%	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	0%
7	100%	100%	100%	100%	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	0%
8	100%	100%	N/A	100%	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	0%
9	100%	63%	0%	N/A	0%	100%	100%	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	0%
9 info	N/A	N/A	N/A	N/A	0%	N/A	100%	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	100%	N/A	0%
10	100%	100%	0%	N/A	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	0%
Overall progress	**100%**	**93%**	**43%**	**100%**	**0%**	**94%**	**100%**	**69%**	**100%**	**100%**	**88%**	**73%**	**100%**	**100%**	**92%**	**100%**	**100%**	**0%**

Standard	NL	PL	PT	RO	SK	SL	ES	SE	UK	MN	NO	SR	CH	EU	EMU	EU-15	EU-12
1	100%	100%	100%	0%	N/A	100%	100%	100%	100%	25%	25%	N/A	100%	94%	96%	96%	56%
2	25%	100%	100%	0%	0%	100%	N/A	100%	100%	N/A	100%	100%	100%	92%	92%	95%	53%
3	N/A	N/A	N/A	0%	N/A	100%	N/A	N/A	N/A	N/A	100%	N/A	N/A	63%	100%	100%	20%
4	100%	100%	100%	0%	100%	100%	100%	100%	100%	100%	100%	100%	100%	99%	100%	100%	72%
5 (start time)	100%	25%	100%	0%	0%	0%	25%	100%	100%	0%	100%	100%	N/A	89%	88%	92%	32%
5 (finish time)	100%	100%	100%	0%	100%	0%	25%	100%	100%	100%	0%	100%	N/A	91%	89%	92%	65%
7	100%	100%	100%	0%	N/A	100%	100%	100%	100%	25%	100%	100%	100%	99%	100%	100%	71%
8	100%	100%	100%	0%	N/A	100%	100%	100%	100%	N/A	100%	N/A	100%	98%	100%	100%	70%
9	100%	25%	100%	0%	100%	100%	25%	100%	100%	N/A	0%	100%	100%	88%	87%	90%	40%
9 info	N/A	25%	N/A	0%	N/A	100%	N/A	N/A	N/A	N/A	N/A	100%	N/A	53%	100%	N/A	25%
10	100%	25%	100%	0%	0%	100%	100%	100%	100%	N/A	0%	100%	100%	97%	100%	100%	35%
Overall progress	**92%**	**70%**	**100%**	**0%**	**50%**	**82%**	**72%**	**100%**	**100%**	**50%**	**63%**	**100%**	**100%**	**94%**	**95%**	**96%**	**52%**

Notes: N/A – not applicable
n.a. – not available
Source: ECSDA

3.4.4. Future Planning: What still has to be done to dismantle the Barriers

Standards achieved, some implementation outstanding:

The standards have been largely adopted and implemented by ECSDA members; so to a large extent, harmonisation of operating hours and cut-off times has been achieved at a domestic level. However, the timely implementation in the ex-CEECSDA countries will have to be monitored. This ECSDA work on the Giovannini Barriers 4 and 7 was focused on harmonising operating hours of the settlement activities of CSDs when they act as "issuer CSDs". This has allowed for harmonisation of operating hours across EU CSDs.

… but further obstacles emerged:

Users of infrastructures have argued that even if all 10 standards on Barriers 4 and 7 are fully implemented throughout the EU, this might still not help users of these infrastructures, in particular when a chain of intermediaries has to be used. This is because infrastructures and intermediaries may apply different operating hours and settlement deadlines to their customers if trades have to be processed through various entities.

Thus, it has become clear that there are operational barriers and obstacles (other than the ones identified by the Giovannini Reports) that impede efficient cross-border settlement and require further action regarding settlement activities that are typically conducted by CSDs as "investors' CSDs". Hence, while harmonisation of operating hours and cut-off times has been achieved at a domestic level, there is still a lack of harmonisation at cross-border level where transactions are intermediated not just by an investor CSD but also often by intermediaries (such as banks) as well, making the chain of transactions complex.

… which will be dealt with as one of the "16th Barriers":

However it is important to note that the industry has delivered what was requested on the dismantling of Barriers 4 and 7 and is nearing full removal of these barriers. Therefore, this achievement should not be diluted by prolonging these barriers by adding additional issues which have not been covered in the Giovannini reports. In order to appropriately cover the missing actions, they have become part of the "16th Giovannini Barrier" (see paragraph 5.10.2 for more details).

TARGET2-Securities could also help remove these two Barriers in those Member States where CSDs would choose to participate in the initiative. This is because TARGET2-Securities would introduce a single schedule (with identical cut-off times for investor and issuer CSDs) for all connected CSDs. While this would not directly solve the issues at custodian level, it could provide an incentive for harmonisation.

3.5. Barrier 6: Differences in standard settlement periods

"Settlement periods for all systems within the EU should be harmonised."

What is a (standard) settlement period?

The settlement period[67] is the time from the trade date to the date when payment is required. The most common settlement period for market trades is one working day (or even same day) for bonds and three working days for equity. This is known as T+3, where T stands for 'Trading Day' and '+3' is the amount of days before settlement is required[68].

While in early days, paper-based clearing and settlement was time-consuming (hence T+7 or T+5 periods or even periods of several weeks/months), due to legal and technical improvements some service providers can nowadays offer settlement in T+0 or even real time settlement to their clients, but non-harmonised settlement cycles create difficulties from the point of view of both the front- and back-offices. On a global level, the aim of the introduction of T+3 was discussed and pushed in a years-long exercise by the G30. The US recently decided not to pursue T+1 settlement and to remain at T+3[69]. On the other hand, India has recently substantially improved and updated (legally and technically) its equity market and has moved to a standard settlement period of T+2.

3.5.1. The issue: What is the problem?

Different settlement periods exist within the European Union but most European markets settle at T+3 as their standard (shorter settlement cycles may be provided as an option). National differences in settlement periods for EU equity markets may result in additional costs to the investor because of a mismatch in funding. Therefore it was questioned in the Second Giovannini Report, whether it is advisable to push for a generalised alignment of the settlement period (i.e. on T+3) or for a general reduction of settlement days. Harmonisation on T+2 would have the benefit of bringing the equity markets into line with the foreign exchange spot market.

One of the consequences of different settlement periods is that operational risks are introduced because the standard settlement period is transferred into a non-standard one. In such cases manual intervention is required which always presents risks. This increases complexity and the incidence of un-matched trades, which can cause dysfunctions in the liquidity function of the banks. Collateral management could also be a problem. Furthermore, as to the trading activity, arbitrage between the same products in different markets across countries is more difficult.

---

67 More specifically, this is the period of time between the settlement date and the transaction date that is allotted to the parties of a transaction to satisfy the transaction's obligations. The buyer must make payment within the settlement period, while the seller must deliver the purchased security within this period.

68 This means that the buyer must transfer cash to the seller, and the seller must transfer ownership of the stock to the buyer within three days after the trade was made.

69 See SEC Concept Release: Securities Transactions Settlement 17 CFR Part 240 [Release no. 33-8398; 34-49405; IC-26384; File no. S7-13-04] RIN 3235-AJ19; http://www.sec.gov/rules/concept/33-8398.htm

Adding to this complex issue is the fact that harmonisation of settlement periods is not only a "stand-alone" requirement in Barrier 6 but also an important element in the standards for the abolishment of Barrier 3 (Corporate Actions). There is even a (corporate actions) market standard that explicitly refers to the harmonisation of settlement periods[70]. The reason is that without the harmonisation of settlement periods, the introduction of a record-date becomes a problem for securities with multiple listings: for such securities, the record-date lies 'one' settlement period after the ex-date, and this means that the same security will have different record-dates (and payment-dates) in T+2 and T+3 markets.

3.5.2. The solution: Industry's approach

The CESAME group has discussed the issue and concluded that harmonisation of settlement periods ((T+x)-standards) was – in comparison to other Giovannini Barriers – not considered a priority. Therefore the Group agreed that this barrier would not be tackled, at least for the time being. It was also mentioned that in the past the harmonisation of settlement periods was preferably discussed on a global level[71].

3.5.3. Stocktaking: What has been achieved so far?

However, two initiatives have been presented and discussed in the context of Barrier 6 that aim at increasing the efficiency of settlement processes and potentially shortening settlement cycles:

Firstly, the standards for pre-settlement date matching worked out by ESSF (formerly ESF) and ECSDA[72] which in the meantime are well advanced and are being implemented at CSD level.

Secondly, another initiative discussed concerns matching processes (based on automation and aimed at straight-through-processing) has been presented by OMGEO: same-day affirmation[73].

What is same-day affirmation (SDA)?

Verifying trade details without delay is essential to identifying discrepancies which can, i.a. lead to errors in recording trades or settlement failures. Same-day affirmation is a way to improve the trade verification process in order to reduce the risk of trades which fail to settle and thus to enhance efficiency, to reduce cost and to improve settlement performance. Trade

---

70 Draft Standards for Corporate Actions Processing, No. 17: "The key dates for Distributions should be the same in all markets; in case of different Settlement Cycles, the Settlement Cycle of the Issuer (I)CSD should prevail."

71 E.g. by the Group of 30 and the Committee on Payments and Settlement Systems (CPSS)

72 See "Proposals to harmonise and standardise pre-settlement date matching processes throughout Europe ", 5 October 2006; http://ec.europa.eu/internal_market/financial-markets/docs/cesame/giovannini/20061023-esf-ecsda-matching_en.pdf

73 See Synthesis reports of 23 October 2006; http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20061023-report_en.pdf ; OMGEO Presentation see http://ec.europa.eu/internal_market/financial-markets/docs/cesame/giovannini/20061023-omgeo_en.pdf

verification precedes the settlement process and is a chain of communication (execution notice, allocation details, confirmation/affirmation[74]) between the parties of a trade which ensure that they are in agreement about the essential trade details (security concerned and amount traded, price, accounts for settlement etc.). SDA means that the entire verification process is completed on the day of the trade itself which helps early detection of any disagreements and leaves more time for the clearing and settlement process.

Furthermore, upon the CESAME meeting of 12 February 2007[75], ICMA gave a presentation[76] on post-trade matching and reporting and the ICMA product TRAX2 which matched[77] and reported transactions.

During the end of the term of the CESAME group mandate, some of its members saw a growing need to return to tackling this barrier as it may have implications with other barriers as well as with other projects, e.g. it might also be related to the TARGET2-Securities project and that there was a link to the "cash leg", too (e.g. to the opening days of TARGET2).

3.5.4. Future Planning: What still has to be done to dismantle the Barrier

The issue will be discussed further and developments monitored against the background of, for instance, the standards for corporate actions processing (which will require a harmonised settlement cycle to achieve full benefits) and also in relation to TARGET2-Securities. There might also be a need to cover this topic on a global scale. Against this background, it is likely that CESAME2 Group will take up the issue.

Regarding other approaches (such as same-day affirmation) which could improve the process in terms of stability and efficiency, the industry has to decide if settlement performance is to be improved by such measures and at which cost (if e.g. a service provider, such as OMGEO[78] is used).

---

74 Most likely, the process needs to be adapted to European practices which are based on a matching concept and not on an affirmation/confirmation concept.

75 http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20070212-report_en.pdf

76 http://ec.europa.eu/internal_market/financial-markets/docs/cesame/giovannini/20070212-icma_en.pdf

77 N.B. There is no universally agreed definition of the term "matching". Many trades actually go through two matching processes: firstly between an investment manager and the broker/dealer immediately after the trade is executed and, secondly immediately prior to settlement within the CSD. This latter process is often referred to as "pre-matching". Mr Costa explained that in the context of his presentation on the TRAX2 system, "matching" refers to the trade confirmation between brokers before settlement.

78 See also the Oxera Report "Building efficiencies in post-trade processing. The Benefits of same-day affirmation", June 2008, commissioned by OMGEO.

3.6. Barrier 8: Differences in securities issuances

"National differences in securities issuance practice should be eliminated."

3.6.1. The issue: What is the problem?

Any securities instrument can only be traded if it is properly 'identified' by its own unique and standardised identifier. This identifier is the ISIN (international securities identification number) which has long been standardised on a worldwide level via the ISO standard 6166. The ISINs are given, maintained and distributed by national numbering agencies (and their international association: ANNA). In the past, national differences in issuance practice arose due to the lack of an efficient same-day distribution mechanism, i.e. an uneven capability to allocate ISIN numbers to securities issues real-time. Therefore, the industry called for a speedy exchange of issuance information and the use of ISIN codes. The International Primary Market Association (IPMA), together with the Association of National Numbering Agencies (ANNA) took the lead.

3.6.2. The solution: speed up the numbering process – first Barrier to be dismantled

This was the first Giovannini Barrier to be dismantled, even before the CESAME group was created. ISINs are now issued and distributed within a few hours by all EU national numbering agencies.

3.6.3. Related issues: licensing fees for ISINs and identifiers for non-securities instruments

The CESAME Group also treated some other issues related to numbering in some of its meetings:

Charging of licensing fees for the use of U.S. ISINs:

A still unsolved issue is that a (non European) numbering agency claims to have a copyright[79] in regard to their national securities number for which it levies licensing fees and requests the signing of licensing fee agreements – also if such ISINs are not directly obtained from this particular numbering agency but via third parties, e.g. data providers (like Reuters, Bloomberg, etc.). More detail on the background is contained in the Report on the CESAME meeting of 16 June 2008[80].

During their discussions[81], CESAME group members concluded

---

[79] N.B. it could not be clarified on what exactly the copyright is claimed (individual number(s), methodology to calculate the number, compilation of ISINs, data collection of ISINs or else)

[80] Point 3.6, page 7: http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20080616-report_en.pdf

[81] The topic was discussed in CESAME meetings on 7 March 2005 (http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20050307report_en.pdf); 10 June 2005 (http://ec.europa.eu/internal_market/financial-

a) that ISINs are similar to a common good for which no charging of fees should occur,
b) that this way of charging was to be considered "double dipping", i.e. a commercial abuse, and at least charging should not occur via separate licensing agreements, but for instance through the data vendors;
c) that the ISO Secretariat should be contacted; and
d) that the matter be referred to the EU-US financial market regulatory dialogue.

Processing of other instruments: Another numbering issue is the development of using other 'instruments' than securities (or cash) for collateralisation purposes, namely credit claims. In order to efficiently process such collateral, there is a need to have harmonisation of procedures of credit claims[82]. However, any standard identifier for such other instruments should be carefully developed in order to avoid any issues on intellectual property rights, such as copyright.

markets/docs/cesame/meetings/20050610-report_en.pdf); 16 June 2008 (http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20080616-report_en.pdf), 22 October 2007 (http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20071022-report_en.pdf);

[82] See e.g. http://www.ecb.int/paym/coll/standards/nonmarketable/html/index.en.html

4. Other topics discussed: Public sector-related Giovannini Barriers

The significant impact that the nine public sector Giovannini Barriers have on the six industry-related Giovannini Barriers was already hinted at in the two Giovannini Reports. CESAME Group members have frequently pointed out that many of the barriers are interrelated and that essential issues, e.g. regarding corporate actions processing, may never be fully dismantled by the industry if the public sector does not address the related legal, regulatory and fiscal problems. In order to follow any progress on the public side, the CESAME Group has therefore in all its meetings also monitored developments on the public Giovannini Barriers. Members were not able to see much progress and thus voiced their disappointment with the slow pace of change – which several Council Conclusions on Clearing and Settlement could not soothe. They have expressed their desire for more involvement and representation of the public sector in the CESAME2 Group, more visible progress, and have contemplated indicating in detail specific national legal and fiscal provisions in the future in order to incite Member States to abolish such rules swiftly.

4.1. Fiscal Barrier 11 (withholding tax)

"Barrier 11: All financial intermediaries established within the EU should be allowed to offer withholding agent services in all of the Member States so as to ensure a level playing field between local and foreign intermediaries. Removing this barrier is the responsibility of national governments and could be co-ordinated via the relevant EU Council. "

4.1.1. The issue: What is the problem?

The majority of Member States restrict withholding responsibilities to entities established within their own jurisdiction. Foreign intermediaries are disadvantaged in their capacity to offer at-source relief from withholding tax while adding an extra cost as they use a local agent.

Therefore, foreign intermediaries should be allowed by national governments to act as withholding agents in all of the EU Member States; such steps should be taken in co-operation with the private sector (which would seem appropriate in light of the G30 proposal to establish an international group on taxation issues).

4.1.2. The solution: Industry's input to the public approach

The mandate of the EU Clearing and Settlement Fiscal Compliance Experts' Working Group (FISCO) was to advise on the best way to remove fiscal compliance barriers related to Giovannini Barriers 11 and 12 on withholding and transaction tax procedures while maintaining the level of transparency and control for Member States. The Group's mandate was strictly limited to the barriers created by the different fiscal compliance procedures; issues related to broader tax policy (e.g. the tax rate and the base on which this rate is imposed) were beyond its scope. Consequently, the solutions identified by the Group will not affect tax revenues in the Member States.

In line with its mandate, the Group issued in April 2006 a Fact-Finding Study[83] describing the inefficiencies identified in current withholding tax procedures. The study also analysed how these procedures hinder the functioning of capital markets and increase the cost of cross-border settlement.

4.1.3. Stocktaking: What has been achieved so far?

FISCO finalised its work in October 2007 by providing its "FISCO Report on Solutions"[84]. At the FISCO Conference in October 2007, the Group presented this report, proposing solutions to the fiscal compliance barriers identified in the Fact-Finding Study. The aim of this report consisted in highlighting the main problems, analysing the advantages and disadvantages of possible ways of action and, whenever possible, indicating solutions. The proposed solutions aim at improved, simplified and modernised fiscal procedures adapted to the way financial markets operate. The report restated that many Member States restrict withholding responsibilities to entities established within their own jurisdiction. As a consequence, foreign intermediaries are disadvantaged in their capacity to offer at source relief from withholding tax by the significant extra cost of using a local agent or local representative in the discharge of their withholding obligations. As a solution the report proposed the introduction of an EU Tax Relief Procedure. The EU Tax Relief Procedure should be built on a model allowing for the appropriate tax relief to be applied at source without excessive documentation requirements and without exposing issuers, intermediaries and investors to unnecessary risks and costs and ensuring the same level of transparency and control for Member States. The report also concluded that the present withholding tax relief procedures do not take sufficient account of the multi-tiered holding environment. A problem is that the present procedures put tax collection responsibilities on an entity that often is not connected to the beneficial owner/final investor and therefore assumes that the market will organize itself to transfer information and paper form documentation on the beneficial owner up to the chain of intermediaries. Consequently, the report considered the present procedures as costly and inefficient.

The Conference highlighted the many concrete problems related to current fiscal compliance barriers and the urgency to solve them. It was stated that the fiscal compliance barriers hinder the functioning of the capital markets, are a burden for the industry and investors alike and increase the costs of cross-border trading. They also lead to a misallocation of resources that could be used in a more efficient way. Consequently, Member States, industry, investors, tax payers and the single market as a whole stand to benefit from the FISCO proposals.

Table – Giovannini Indicators on Barrier 11

Fact finding	Standard setting	Endorsement	Average
100%	30%	0%	**40%**

[83] FISCO (2006). *Fact-finding study on fiscal compliance procedures related to clearing and settlement within the EU*, Brussels, April 2006. http://ec.europa.eu/internal_market/financial-markets/docs/compliance/ff_study_en.pdf

[84] FISCO (2007). *Solutions to fiscal compliance barriers related to post-trading within the EU*, Brussels, October 2007. http://ec.europa.eu/internal_market/financial-markets/docs/compliance/report_en.pdf

4.1.4. Future Planning: What still has to be done to dismantle the Barrier

Regarding withholding tax procedures, the Commission is analysing the advantages and disadvantages of the FISCO proposals and is further discussing with industry. An informal joint "EU/OECD Working Group on Improving Procedures for Tax Relief for Cross-Border Investors" is used as a sounding board for new approaches. In addition, the Commission asks Member States to be proactive in every possible forum.

In line with the November ECOFIN Council Conclusions, the Commission considers a Commission Recommendation to be a possible way forward which could be put forward by early 2009. Such a recommendation could suggest:

- eliminating the need to pass on detailed information on beneficial owners through the custody chain up to the local withholding agents. This could be best achieved by allowing any intermediary in the chain to either assume full withholding responsibilities or to take responsibility for granting withholding tax relief by sending pooled withholding rate information to the upstream intermediary;
- abolishing the requirement of paper-form certification; and
- allowing intermediaries to make use of modern technology to pass on beneficial owner information to the local withholding agent in electronic format.

An analysis ("Economic Business Case") of the cost-benefits coming from an improvement of the current procedures is also being developed. It will show the potential financial effects of the FISCO proposals for intermediaries, investors, national tax authorities and governments. Its preliminary findings show that there are quite sizeable benefits to reap.

4.2. Fiscal Barrier 12 (restrictions on tax collection)

"Barrier 12: Any provisions requiring that taxes on securities transactions be collected via local systems should be removed to ensure a level playing field between domestic and foreign investors. This is clearly a responsibility of national governments and their actions should be co-ordinated via the relevant EU Council."

4.2.1. The issue: What is the problem?

The collection of transaction taxes (still applicable for two Member States, U.K. and Ireland) is integrated into the local settlement system. The foreign investor's choice of provider for securities settlement is reduced as it is necessary to link up with the local settlement system.

4.2.2. The solution: Industry's input to the public approach

To ensure a level playing field between domestic and foreign investors, provisions that taxes on securities transactions be collected via local systems should be removed. This is a responsibility of national governments and consistency in the removal of these restrictions could best be guaranteed by co-ordinated action via the relevant EU Council. Again such steps should be taken in co-operation with the private sector.

In line with its mandate, the Group issued in April 2006 a Fact-Finding Study[85] describing the inefficiencies identified in transaction tax (such as Stamp Duty Tax[86]) procedures. The study also analysed how these procedures hinder the functioning of capital markets and increase the cost of cross-border settlement.

4.2.3. Stocktaking: What has been achieved so far?

FISCO finalised its work in October 2007 by providing its "FISCO Report on Solutions"[87]. The process is described in more detail in paragraph 4.1.3. of this report.

Table: Giovannini Indicators on Barrier 12

Fact finding	Standard setting	Endorsement	Average
100%	30%	0%	**40%**

4.2.4. Future Planning: What still has to be done to dismantle the Barrier

On transaction taxes, the Commission will have further discussions with the two Member States concerned.

4.3. Public Barrier 5 (Impediments to remote access)

"Practical impediments to remote access to national clearing and settlement systems should be removed in order to ensure a level playing field. National governments should draw up a set of conditions upon which access can be guaranteed across the EU. These conditions should be compliant with any requirements set out by ESCB/CESR."

4.3.1. The issue: What is the problem?

Barrier 5 relates to practical impediments to remote access to national post-trading systems, i.e. the possibility for an investment firm to become a member or participant of a system located in another Member State. Such impediments are connected with market/system rules

---

85 FISCO (2006). *Fact-finding study on fiscal compliance procedures related to clearing and settlement within the EU*, Brussels, April 2006. http://ec.europa.eu/internal_market/financial-markets/docs/compliance/ff_study_en.pdf

86 See e.g. in this context Her Majesty's Treasury (HMT) discussion paper for consultation concerning the findings of the joint KPMG/Investment Management Association (IMA) October 2006 report on Schedule 19 of the Finance Act 1999 (Schedule 19), entitled 'Taxation and the Competitiveness of UK funds.' Schedule 19 is the Stamp Duty Reserve Tax (SDRT) legislation that applies to collective investment schemes. The 2006 report argued that Schedule 19 is one factor that is encouraging funds to domicile abroad, emphasising that the tax is too complicated to calculate and its complexity acts as a disincentive to investors. Within the context of this consultation, the European Commission highlighted the work recently presented by the EU Clearing and Settlement Fiscal Compliance Experts' Group (FISCO). The European Commission delivered its reply to the consultation on 25 January 2008. http://www.hm-treasury.gov.uk/media/2/B/consult_stampduty091107_.pdf

87 FISCO (2007). *Solutions to fiscal compliance barriers related to post-trading within the EU*, Brussels, October 2007. http://ec.europa.eu/internal_market/financial-markets/docs/compliance/report_en.pdf

that discriminate access to systems between local and remote members and put the latter at a disadvantage, forcing them to employ third parties or establish a local entity in order to access the relevant system.

As indicated by the First Giovannini Report, the settlement of a transaction involves both a security and a cash leg. Therefore, the problems under this heading relate to:

a) remote access to securities clearing and settlement systems;

b) remote access to payment systems for the cash settlement;

c) access to central bank accounts and

d) access to central bank intra-day liquidity.

Such impediments increase the inefficiency and costs of post-trading services and limit the choice of investors.

4.3.2. The solution: Public approach

Against this background, the Second Giovannini Report indicated that national governments should draw up a set of conditions upon which access to post-trading systems can be guaranteed throughout the EU on the basis of strictly non-discriminatory criteria for local and remote members. These conditions would need to be drawn in co-operation with the ESCB because of the need for access central bank money. According to that report, Barrier 5 should have been removed within a period of three years from the initiation of the project, i.e. three years from the establishment of the CESAME group, i.e. by October 2007.

4.3.3. Stocktaking: What has been achieved so far?

Regarding remote access to clearing and settlement systems, Article 34(1) of MiFID grants to investment firms the right of access to central counterparty, clearing and settlement systems located in another Member State establishing that such access must be based on the same non-discriminatory, transparent and objective criteria as apply to local participants. This right of access, in any case, does not prejudice the right of system operators to refuse it on legitimate commercial grounds. Therefore, the principle for guaranteed remote access to CCPs and CSDs is established at EU level; however no common criteria are established to grant or refuse it. In this sense, ESCB-CESR recommendation 14, if adopted, would guarantee fair and open access to CCPs and CSDs at EU level and the single admissible criteria for denying access would be based on risk alone.

Remote access to payment systems for cash settlement: according to the First Giovannini Report, remote members are required to use a local agent bank or open an account with the local central bank for cash settlement. Under TARGET2, the centralised payment system with a single technical platform was adopted by the Eurosystem. The centralisation of business operations allows users to run one single account to make payments in all the euro area. TARGET2 has been launched on 19 November 2007 and all the central banks of the euro area, the ECB, and the central banks of Denmark, Estonia, Latvia, Lithuania and Poland participate in it from May 2008. Thus, also users from non-euro-Member States participating in the system will be allowed to make cash settlements remotely. Direct remote access to UK

CHAPS[88] is currently restricted to 14 UK based clearing banks. The situation in other EU Member States has not been analysed by CESAME.

The First Giovannini Report also highlights the problem of access to intra-day liquidity (access to central bank money) for remote users, which implies that remote users must use a local bank to finance any funding shortfall. This problem is clearly connected to the monetary policy of central banks, as – due to safety considerations - they cannot finance institutions located in a different jurisdiction than the one of the central bank issuing the currency. This does not mean that nothing can be done about this issue. Indeed, central banks may establish arrangements within themselves that allow remote access to central bank money in a foreign currency[89] (there are practical examples of such solutions, e.g. UK under TARGET, Poland and the Baltic States under TARGET2). In this case it is the domestic central bank that finances the firms in its territory, which participate in a "foreign" payment system, but the arrangement allows remote access to central bank money in a foreign currency, without affecting the monetary policy control of the central banks involved. In the euro area, access to central bank accounts is possible for all non-euro area EU banks, investment firms, CCPS or CSDs. There is also a possibility for non-euro area participants to access intra-day credit in euro, provided that their central bank participates in TARGET2[90]. Similar solutions (including solutions that would allow access to central bank accounts) for other major EU currencies do not seem to have been made available by their respective central banks.

4.3.4. Future Planning: What still has to be done to dismantle the Barrier

According to the findings outlined above, the first problem identified by the Giovannini report related to remote access to central counterparty, clearing and settlement systems should have been solved by MiFID (subject to full implementation, see paragraph at the end of this point). Furthermore, the adoption of the ESCB-CESR recommendations (see paragraph 5.7.) would allow the establishment of a single common criterion to refuse access. The adoption of these recommendations is therefore welcomed in order to fully dismantle this part of the barrier on a practical level.

As for remote access to payment systems, TARGET2 represents a solution for payments in Euro for both Euro and non-Euro Members States. Following MiFiD and the Second Banking Directive remote access to payment systems is today possible for all credit institutions and investment banks meeting the access criteria.

The last problem identified in the First Giovannini Report, access to central bank intra-day liquidity, can be solved through arrangements between central banks that put remote members of different currency areas on a level footing with local members, to the extent that this does not affect the monetary stance, does not undermine the smooth implementation of the monetary policy, by posing unacceptable risk on a central bank. Therefore, the establishment of these arrangements is encouraged to fully dismantle this last aspect of Barrier 5, as long as the concerns above are properly addressed.

---

88 CHAPS is an electronic bank-to-bank same-day value payment made within the UK in either sterling or euro.

89 Although these arrangements may still be subject to quantitative limits.

90 A bank from outside the euro area can also mitigate the problem by using one of its branches of subsidiaries located in the euro area (provided that it has any).

Against this background, all pre-conditions seem to be in place now to effectively dismantle this barrier. However, it has to be monitored if any issues remain open. The Commission is, e.g. currently undertaking an implementation check on MiFID provisions[91].

4.4. Public Barrier 2 (National restrictions on the location of clearing and settlement)

"National restrictions on the location of clearing and settlement [and on the location of securities] should be removed as an essential pre-condition for a market-led integration of EU clearing and settlement arrangements. Removal of these barriers is the responsibility of national governments and could be achieved in the context of adopting the new Investment Services Directive."

4.4.1. The issue: What is the problem?

Barrier 2 relates to national restrictions on the location of clearing and settlement, i.e. restrictions that require investors engaging in cross-border transactions with different trading venues to use multiple post-trading systems. Such restrictions may lead to an inefficient allocation of collateral for the investors, prevent the competition between systems and frequently imply the intervention of a local intermediary[92] to clear and settle cross-border transactions, thus raising the costs of post-trading services. The inefficient allocation of collateral is due to both the need to maintain a series of pools of collateral with all the different systems and to the fact that transactions on the same financial instrument in different trading venues imply the clearing with different systems, each requiring its own margin. Restrictions may typically take the form of market/system rules which provide for the usage of a specific central counterparty and settlement system, thus limiting the choice of investors.

4.4.2. The solution: Public approach

Barriers 2 relates to national restrictions on the location of clearing and settlement both for primary and secondary markets. MiFID and the Code of Conduct contain specific provisions that could serve to dismantle those barriers, however Member States must remove any obstacle to or unfair bias against providers of trading[93], and post-trading services authorised in another Member State.

---

91 See: MiFID Transposition Quality Check, Results of call for evidence from market participants http://ec.europa.eu/internal_market/securities/docs/isd/mifidtr_en.pdf and "MiFID transposition state of play: http://ec.europa.eu/internal_market/securities/isd/mifid_implementation_en.htm

92 Barrier 2 by itself does not imply the intervention of a local intermediary. Barrier 5 on the impediments to remote access does imply it. However, Barrier 2 prevents the possibility of designating other systems than the local one and frequently requires investors to use an intermediary instead of accessing directly all the different national post-trading systems.

93 The work of the Commission's Directorate General Competition regarding trading, clearing and settlement at the time also had an impact on Barriers 2 and 9 as it forced Member States' Debt Management Offices to look at the framework they had established with one trading platform. See: Working document of the Commission services " Competition in EU securities trading and post-trading, Issues Paper" of 26 May 2006; http://ec.europa.eu/comm/competition/sectors/financial_services/securities_trading.pdf

4.4.3. Stocktaking: What has been achieved so far?

As mentioned above, the MiFID contains provisions that are specifically addressed to the post-trading sector:

- Article 34(1), para. 2, grants to CCPs or CSDs the right to be employed in clearing and settlement of transactions in financial instruments undertaken in regulated markets or MTFs located outside the territory of the post-trading infrastructures.
- Article 34(2) grants to members and participants of regulated markets the right to designate the system for the settlement of transactions in financial instruments undertaken on that regulated market, provided that i) the necessary links and arrangements between the designated system and that chosen by the regulated market are in place; ii) the agreement by the competent authority that such a link will guarantee the smooth and orderly function of the market.
- Article 46 grants to regulated markets the right to choose a CCP and/or a CSD of another Member State to clear and/or settle some or all of the trades concluded under their systems. Furthermore, it stipulates that competent authorities may not oppose the use of CCPs or CSDs located in another Member State unless that is necessary for maintaining the orderly functioning of the regulated market. Competent authorities must also take into account the oversight/supervision of CCPs and CSDs exercised by other supervisory authorities. The rights granted to regulated markets under Article 46 are extended to investment firms and market operators operating an MTF through Article 35.

The above-mentioned provisions are applicable since 1 November 2007 and represent an important step forward in dismantling Barrier 2. However, MiFID does not address all of the issues related to Barrier 2:

- It does not grant market participants the right to choose a different CCP from the one designated by the regulated market; in case the latter did not make use of the right granted by Article 46, national CCPs would remain the only viable solution in that particular market.
- While MiFID correctly states that if a market participant wants to designate a settlement system other than the one chosen by the regulated market a link between the two systems must exist, it does not define the necessary conditions for the effective establishment of such links. In absence of such a link, the market participant has no choice but to continue to use the settlement system chosen by the regulated market.

The European Code of Conduct for Clearing and Settlement aims at building on user choices enshrined by MiFID: It offers market participants the freedom to choose their preferred provider of services separately at each layer of the transaction chain (trading, clearing and settlement). The Code's principles and conditions regarding access and interoperability are detailed in the relevant Guideline [94] which take the form of commitments and recommendations by the signing organisations as to how these requirements can be met for cash equities post-trading services. This freedom to choose does not cover the bond markets as the Code applies only to cash equities. While the combined effect of MiFID and the Code

[94] See: Access and Interoperability Guideline of 28 June 2007, http://www.fese.eu/_lib/files/AccessInteroperabilityGuideline.pdf

have established the necessary conditions for removing Barrier 2 for cash equities, the same conclusion may not be reached for bonds (in particular domestic bonds).

Table: Overview on the standard setting on Barrier 2 and 10

Fact finding	Standard setting	Endorsement	Overall progress
100%	60%	60%	**70%**

4.4.4. Future Planning: What still has to be done to dismantle the Barrier

As stated above, the formal conditions for effectively dismantling Barrier 2 for cash equities seem to be in place; it still remains to be seen if this will effectively lead to the removal of all practical impediments. Regarding bonds, further analysis is necessary to determine whether Barrier 2 represents an actual problem and if so, what would be the best way of addressing it (e.g. an extension of the Code to bonds).

Pending full implementation of MiFID in Member States, it is now up to infrastructures and users to make full use of them. Naturally, the Code and the respective Guidelines can only be fully effective if there are no undue legal, fiscal or regulatory barriers to incoming post-trading service providers. Member States must therefore remove any other obstacle to or unfair bias against providers of post-trading services authorised in another Member State. In this area, CESR has already been asked[95] to tackle differences which restrict a common approach in the application of the relevant provisions of the MiFID (i.e. the effective establishment of links which are a necessary precondition for the exercise of the right to choose a clearing/settlement location). CESR and its members should build on this work, so that they adapt their regulatory approaches so as to facilitate the effects envisaged by MiFID in this area, in combination with the conditions of the Code of Conduct. Furthermore, feedback on the implementation of MiFID from the market will most likely provide additional details on impediments which result from the public area[96].

4.5. Public Barrier 10 (National restrictions on the activity of primary dealers and market makers)

"Restrictions on the activity of primary dealers and market makers should be removed. National governments should co-ordinate their actions via the relevant EU Council."

[95] Formal mandate to CESR for technical advice on identifying regulatory arrangements for post-trading infrastructures and advising on possible solutions in terms of bridging any potential differences in these arrangements of 28.07.2008 http://ec.europa.eu/internal_market/financial-markets/docs/clearing/2008_07_28_cesr_mandate.pdf

[96] See: MiFID Transposition Quality Check, Results of call for evidence from market participants http://ec.europa.eu/internal_market/securities/docs/isd/mifidtr_en.pdf

4.5.1. The issue: What is the problem?

Barrier 10 relates to the activity of primary dealers and market-makers which often requires the setting-up of local securities operations and the settlement of primary-market transactions in the local settlement system. This barrier represents a specific case of Barrier 2 for the primary market. In the context of this barrier other problems faced by primary dealers or market makers, such as admissibility criteria, have been raised. However, these problems do not concern post-trading activities and are therefore outside the scope of the present report.

4.5.2. The solution: Public approach and the industry's input

Since Barrier 10 has been 'collapsed' into Barrier 2 (see below, chapter 4.5.3), the solutions mentioned in paragraph 4.3.2 are valid also for Barrier 10, however it is worth mentioning that the Code of Conduct on clearing and settlement applies only to equities; therefore not granting primary dealers in bonds the same rights that the Code grants to investors in equities.

4.5.3. Stocktaking: What has been achieved so far?

The Economic and Financial Committee Sub-Committee of national debt managers, the so-called Thomson Group, concluded in its report[97] that "*any restrictions on clearing and settlement activities in the primary or secondary market cannot be removed in isolation, but only in the broader context also considering restrictions related to rules and regulations in securities markets"*. Therefore Barrier 10 should not be considered in isolation, but in the context of dismantling Barrier 2 and the removal of the latter would also imply that primary dealers and market makers would be allowed to centralise their cross-border settlements in fewer systems.

As mentioned above, the Code of Conduct for clearing and settlement applies only to equities, and thus cannot grant primary dealers in bonds any rights or alleviate Barrier 10.

4.5.4. Future Planning: What still has to be done to dismantle the Barrier

Possibly, the Thomson Group might undertake an updated study; the Commission will carry out an implementation check of MiFID where the relevant provisions to this barrier will be one of the main items. However, as Barrier 10 has been 'collapsed' into Barrier 2, no further work will be undertaken which relates solely to this barrier; instead, the issues will be addressed and solved within the scope of Barrier 2. Also, TARGET2-Securities would go a long way towards eliminating this barrier for what concerns the choice of the location of settlement. Indeed, by providing a single settlement location it would greatly reduce the cost of establishing links between CSDs, a necessary condition for allowing choice of location of settlement.

---

97 Economic and Financial Committee (2006). "Restrictions on the location of clearing and settlement in the EU government bond markets", Brussels, 29 May 2006. http://ec.europa.eu/internal_market/financial-markets/docs/cesame/ec-docs/20060612-barrier-10_en.pdf

4.6. Legal Barrier 9 (location of securities)

"National restrictions [on the location of clearing and settlement and] on the location of securities should be removed as an essential pre-condition for a market-led integration of EU clearing and settlement arrangements. Removal of these barriers is the responsibility of national governments and could be achieved in the context of adopting the new Investment Services Directive."

4.6.1. The issue: What is the problem?

The Giovannini Group identified, under the label of Barrier 9, restrictions regarding the location of securities as limitations to the choice of investors and issuers and as contrary to the principles underlying the internal market for financial services. These national restrictions reflected the evolution of historically efficient national structures but are difficult to justify in the context of an integrated EU financial system[98].

Such restrictions came in the form of either market rules or national law. Two types of restrictions could be found: on one hand, requirements that issues in securities listed in regulated markets were deposited exclusively in the local settlement systems; and, on the other hand, listing on a regulated market required registration with a local registrar for purposes of holding of the issue.

The Second Giovannini Report furthermore indicated that restriction of the location of securities entailed equally impediments to the free choice of the location of clearing and settlement of securities, as the logic in restricting the location of clearing and settlement derived from restrictions on the location of securities[99]. It made clear that the removal of this barrier was a pre-condition for market led integration of the EU clearing and settlement environment. Responsibility for removing these restrictions lies primarily with national governments, even if the source of the restriction is in some cases to be found in stock exchange rules.

4.6.2. The solution: Industry's input to the public approach

The EU Commission confirmed in its 2004 Communication its intention to consider this issue further, taking into account the differences between the various types of securities, as well as the company law implications of such requirements, and to include it in the mandate of the LCG[100].

The Legal Certainty Group, in its Recommendation 15, refined the description of the task given by the Giovannini Report and illustrated the different forms that restrictions on the location of securities can have: the importability is restricted where foreign securities issues are not admitted to a local holding system; the exportability is restricted where securities issues are bound to the national holding system and are not allowed to be held abroad. In its Recommendation, the Legal Certainty Group developed an approach based on the distinction between the worlds of "creation" and "holding and settlement" of securities. Whereas all steps

---

98 First Giovannini Report, pp. 49 *et seq*.; Commission 2004 Communication, p. 25.

99 Second Giovannini Report, p. 18 *et seq*.

100 Clearing and Settlement in the Euroean Union – The way forward, Communication from the Commission to the Council and the European Parliament, 28.4.2004, COM(2004) 312, p. 25

of creation must remain tied to the law governing the issuer, any other steps, including the making of the initial book-entry in a settlement system, should be able to be made under the law of a different jurisdiction.

4.6.3. Stocktaking: What has been achieved so far?

The Legal Certainty Group undertook a fact finding study confirming that the restrictions on the location of securities persist to date. Consequently, the issue was addressed in the Group's Second Advice on Solutions to Legal Barriers related to Post-Trading within the EU, published in August 2008 (see Recommendation 15).

Table: Overview on the standard setting phase on barrier 9

Fact finding	Standard setting	Endorsement	Average
100%	40%	0%	**35%**

4.6.4. Future Planning: What still has to be done to dismantle the Barrier

The Advice of the Legal Certainty Group is an informal paper addressed to the EU Commission Services. In general, the Commission welcomed the recommendations of the Legal Certainty Group which provide a sound basis for making the EU post-trading market more cost-efficient and safer from a legal point of view and the Commission will consider the merits of proposing legislation in this area. Given that the Legal Certainty Group proposed to draw up Community legislation on Barrier 9, the EU Commission will have to consider the Advice in detail and subsequently will have to take a decision regarding any specific initiative to make a formal legislative proposal. Given the technical complexity of the matter, the preparation and possible adoption of any future legislation will take a certain time and any proposal may be ready, at the earliest, in the course of the year 2010.

4.7. Legal Barrier 13 (absence of EU legal framework)

"Barrier 13 is the absence of an EU-wide framework for the treatment of ownership of securities. In modern securities markets, securities are held for others by intermediaries, for which purpose they maintain accounts. These accounts are treated commercially and economically as being the focus of ownership. However, legally their status differs across the EU. There is a lack of clarity about who has what rights and of what kind when securities are held for investors by means of an intermediary's accounting records ("book-entries")."

4.7.1. The issue: What is the problem?

The issue described in the Second Giovannini Report is still unresolved: there are no common rules regarding the substantive law question. The Giovannini Report had qualified this situation as the most important source of legal risk in cross border transactions, together with the absence of a harmonised conflict-of-laws rule. The reasoning underlying Barrier 13

reflects certain needs of the financial market for legally sound securities holding and transactions:

- Book-entry securities and collateral interests over book-entry securities need to be legally protected against the insolvency of the intermediary, of the transferor or of the collateral provider);

- The law should reflect the predominant rule of account entries and consequently admit that book entry securities are acquired, disposed of and encumbered by means of making book entries or otherwise referring to securities accounts (and not, for example, by shift in "possession");

- There need to be clear and simple rules for acquisition, disposal and the creation of collateral interests in book-entry securities, limiting formalities to a minimum without neglecting investor protection;

- There need to be clear rules setting conditions for invalidity and reversibility of credits;

- The integrity of the issue needs to be guaranteed, i.e. there need to be measures against an inflation of the number of securities by over-crediting clients' accounts.

Some of the relevant problems are dealt with in the Financial Collateral Directive (FCD) and in the Settlement Finality Directive (SFD); however, the scope of these two directives is very limited and does not comprehensively address all aspects of Barrier 13.

4.7.2. The solution

The Commission has mandated the Legal Certainty Group to develop a comprehensive proposal on how the above described situation of legal patchwork throughout the EU could be eliminated. The Legal Certainty Group proposed in its Recommendation 1-11 harmonisation without encroaching to deeply upon national corporate and insolvency law. It followed a rather functional and neutral approach. Under this approach, reference to traditional legal concepts was avoided and a rather descriptive language was used in order to allow national legislators to implement the future rules in harmony with fundamental concepts of the Member States' law. Consequently, under this proposal national rules would still govern the holding, acquisition and disposition of book-entry securities; however, there had to be harmonised rules on certain core aspects.

In 11 Recommendations, the Legal Certainty Group delivered the blueprint for future legislative action on an EU level. The Recommendations addressed issues such as: the nature of book-entry securities, methods for acquisition and disposition of book-entry securities, rules on validity and reversal of acquisitions and dispositions; rules on the protection of acquirers and priority of interests over conflicting rights; rules on the integrity of the issue; rules regarding obligations and liabilities of the intermediary; rules on instructions, rules on attachments of book-entry securities, etc.

4.7.3. Stocktaking: What has been achieved so far?

The Legal Certainty Group undertook a fact finding study confirming that the legal differences actually exist and hamper smooth cross border holding and disposition of book-

entry securities. It has delivered a blueprint for a solution to the barrier which is the first part of standard setting and can serve as a basis for future legislative action.

Table: Overview on the standard setting phase of Barrier 13

Fact finding	Standard setting	Endorsement	Average
100%	40%	0%	**35%**

4.7.4. Future Planning: What still has to be done to dismantle the Barrier

As the dismantling of Barrier 13 requires harmonisation of national legislation in the field of securities holding and settlement and related legal areas, it seems that the necessary framework can only be established by a harmonising EU legislative initiative. The Commission will discuss the Legal Certainty Group's Advice, assess the necessary further steps and set up a timeframe for any subsequent action, in particular consider the merits of proposing legislation in this area.

4.8. Legal Barrier 14 (Netting) – dismantled

"The EU Collateral Directive will remove much of the legal uncertainty relating to netting [and the uneven application of conflict of laws]. Member States should ensure the full implementation of this Directive by the scheduled date of 27 December 2003."

4.8.1. The issue: What is the problem?

The First Giovannini Report set out that netting was generally recognised in one form or the other in most EU countries[101]. However, its availability was often limited to specific products, types of counterparty or forms of contractual documentation. This led to the need for a detailed analysis of each transaction before it could be safely assumed that netting would be possible. There was agreement that any legal uncertainty in this area needed to be removed.

4.8.2. The solution: Public sector approach

By the time of the preparation of the Second Giovannini Report, the Financial Collateral Arrangements Directive (FCD) had already been adopted. The Second Giovannini report stated that by the implementation of this Directive, Barrier 14 would be removed for most purposes, as the Directive expressly recognised close-out netting[102]. This view was also confirmed by the EU Commission[103]. Furthermore, the Commission adopted on 24 April 2008

---

101 First Giovannini Report, p. 57

102 Second Giovannini Report, p. 12

103 Commission 2004 Communication, p. 23; see also Evaluation Report COM (2006) 833 of 20 December 2006; http://ec.europa.eu/internal_market/financial-markets/docs/collateral/fcd_report_en.pdf

a proposal to amend, inter alia, the Financial Collateral Arrangements Directive in order to bring the directive in line with market and regulatory developments in the post-trading area[104].

4.8.3. Stocktaking: What has been achieved so far?

Therefore, Barrier 14 has in fact been dismantled for bilateral netting (i.e. close-out netting).

4.8.4. Future Planning: What issues remain on netting?

Possible new related issues (e.g. tri-party netting) will have to be monitored and discussed in due course, see section 5.10.1.

4.9. Legal Barrier 15 (conflict of laws)

"The EU Collateral Directive will remove much of the legal uncertainty relating to […] the uneven application of conflict of laws. […], there remains a need for a legal framework across the EU under which, whenever securities are held using an intermediary, it is the accounts of that intermediary that establish ownership of those securities."

4.9.1. The issue: What is the problem?

This barrier concerns the question of which law applies for intermediated securities in case two or more jurisdictions are involved. This "conflict of laws"–issue is an issue for all kinds of securities. For a limited scope of securities, the Settlement Finality Directive (and later the Financial Collateral Directive and the Winding-up of Credit Institutions Directive) tried to solve the problem by introducing the rule that the applicable law is determined by where the account is "held" or "maintained". This is the so-called “Place of the Relevant Intermediary Approach” or "PRIMA-rule". Although this rule has helped European market participants to determine the applicable law, there was some criticism that as in the digital environment accounts evidently do not have a physical location, that rule might still leave some uncertainties. Furthermore, the relevant provisions are limited in scope (regarding the instruments covered by the PRIMA rule) and most notably provide no global solution.

4.9.2. The solution: Public sector approach

In theory, different solutions can be envisaged to tackle the issue. One attempt to overcome these problems was the Hague Securities Convention [105] concluded in 2002, but this Convention is not yet in force (only the USA and Switzerland have signed so far; no ratification). The Convention contains a different conflict of laws-rule that allows a large degree of freedom to the parties to choose the applicable law. However, this solution is highly

---

[104] See http://ec.europa.eu/internal_market/financial-markets/docs/proposal/sfd_fcd_proposal_en.pdf

[105] Convention on the law applicable to certain rights in respect of securities held with an account provider, of 5 July 2006 (adopted in December 2002, but the Convention officially indicates the date of the first signature), http://hcch.e-vision.nl/index_en.php?act=conventions.text&cid=72

contested by a number of Member States and some parts of the industry; the European Parliament voted against it[106], and the ECB and other stakeholders are not convinced that the approach taken by the Hague Convention is the right one.

4.9.3. Stocktaking: What has been achieved so far?

Given that the Hague Securities Convention did not gather enough favour and momentum, the Commission is looking for other solutions. Strictly speaking, the Financial Collateral Arrangements Directive (FCD, see paragraph 4.8.2) solves the issue of Barrier 15, but it is a solution which is limited in scope and geographically.

4.9.4. Future Planning: What still has to be done to dismantle the Barrier

The Commission, together with the ECB, is exploring other (including more technical[107]) ways to enhance legal certainty both at the European and at the global level, bearing in mind that solving the issues is important for EU markets. Member States and industry should also contribute to the discussion in order to identify appropriate solutions.

---

106 http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P6-TA-2006-0608+0+DOC+XML+V0//EN&language=RO.

107 For instance the idea of diagnostic numbers (called DENISA), see report of the CESAME meeting on 12 June 2006, page 9 (http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20060612-report_en.pdf)

5. Other topics discussed: General issues related to post-trading

The mandate of the CESAME Group was rather wide and members willingly took up the opportunity not only to identify, discuss and explore their core focus of the industry-related Giovannini Barriers, but also to go further. They took an active interest in looking into the state of play of all public Giovannini Barriers (which have a wide impact on almost any industry solution; see the issues described in section 4. above) and they actively discussed other topics relevant to post-trading with many guests. These other issues were vital to the work and some of them have a significant impact on the industry – or might have in the future.

5.1. CESAME sub-group on definitions

At its meeting on 25 October 2004 the CESAME group expressed its will to assist the Commission in its efforts to develop functional definitions in the area of post-trading. CESAME agreed that it would be beneficial to the overall current debate on post-trading to establish a set of definitions that may be used commonly and which capture the functions, rather than the institutions, involved in post-trading activities. The Commission acted on this offer and duly convened a "Definitions' Sub-Group" with a view to assisting the Commission in the development of functional definitions for use in future discussions. The sub-group has had three meetings and has also worked intensely via e-mails and bilateral meetings.

The result of the work of the Sub-Group was a note[108] that contains a number of definitions. The note focused on securities, as the sub-group had already agreed that more work was needed to adapt the definitions proposed in the note on derivatives. The functional definitions set out in the note were only designed to help marshal the future debate. In essence, the definitions in the note did not address the issue of whether institutional differences in any legal instruments are, or may be, important or not.

In order to achieve, to the maximum extent possible, a consensus on a restricted set of definitions, the work has been conducted on a purely functional basis. This implies that that the definitions described were intended, as much as possible, to describe technical processes. It is important to mention that the experts, members of the sub-group, with a banking background, disagreed with the broad approach taken with respect to the proposed definitions, in particular as regards the definition of settlement. They have recommended that the Commission adopt a consistent approach – i.e. a risk-based functional approach – across all definitions, and not only with respect to the distinction between "counterparty clearing" and "central counterparty clearing".

Finally, the work has been conducted on the basis that terms with strong legal connotations ('netting' or 'execution', for example) should be avoided. The aim has been to capture functions, and not to specify the legal basis or effect of those functions. In practical terms, the definitions developed by the sub-group were used, to a certain extent, in the development of the Code of Conduct; principally in connection with the latter's third part, *i.e.* concerning accounting separation.

The note of the Sub-Group later proved very useful as a basis for further discussions among the industry, e.g. in regard to the Code of Conduct which also includes some definitions. A

[108] http://ec.europa.eu/internal_market/financial-markets/docs/cesame/ec-docs/20051027_definitions1_en.pdf

non-exhaustive overview on available glossaries in the area of clearing and settlement can be found in Annex 7.

5.2. The European Code of Conduct for Clearing and Settlement

The European Code of Conduct for Clearing and Settlement[109] (the "Code" or the "Code of Conduct") was presented by the industry to Commissioner McCreevy in November 2006. The aim of the Code is to make user choices enshrined by MiFID not a theoretical possibility but an effective option. It is the common objective of the organisations signing the Code to establish a strong European capital market and to allow investors the choice to trade any European security – whether it is a domestic or a foreign security – within a consistent, coherent and efficient European framework. The ultimate aim is to offer market participants the freedom to choose their preferred provider of services separately at each layer of the transaction chain (trading, clearing and settlement). The Code accordingly contains three sets of commitments:

(i) price transparency, in order to enable customers to understand the services they will be provided with, and to understand the prices they will have to pay for these services, including discount schemes; to facilitate the comparison of prices and services, and to enable customers to reconcile ex-post billing of their business flow against the published prices and the services provided;

(ii) access and interoperability, in order to make it easier for infrastructures to set up links with infrastructures in other countries, and;

(iii) service unbundling, in order to give customers flexibility when choosing which services to purchase, and accounting separation, providing relevant information on the services provided. These measures are designed:

- to make transparent the relation between revenues and costs of different services in order to facilitate competition,
- to make transparent potential cross-subsidies between the different services as described in paragraph 40, and
- to provide users with choice regarding the services available for purchase.

The Code holds the potential to address two Giovannini Barriers: first, Barrier 2 on restrictions on the location of clearing and settlement and second, Barrier 5 on impediments to remote access.

Already MiFID addresses restrictions on the location of clearing and settlement. Article 34 of MiFID grants remote access for investment firms to foreign CCPs/CSDs. It also allows market participants to designate settlement location for trades (but not CCP) provided links are in place and competent authorities agree. Article 46 of MiFID furthermore allows regulated markets to choose a particular CCP/CSD to clear and settle transactions. However, MiFID does not explicitly provide market participants with the right to choose a CCP and does not cover relations among post-trading infrastructure. Thus, the post-trading provisions contained in MiFID are not by themselves sufficient to fully eliminate this barrier. However, they represent an important step forward which should be further elaborated. Building on MiFID, the Code's guidelines on access and interoperability set out the conditions, rules and

[109] See e.g. http://www.fese.be/en/?inc=cat&id=19

procedures that infrastructures have committed to respect when they seek to establish links between themselves. This therefore holds the potential to complement MiFID and to contribute towards eliminating Giovannini Barriers 2 and 5, though the Code does not have the same legally binding effects as MiFID.

The Code – and the accompanying Access and Interoperability Guideline[110] – lays out four different link scenarios: (i) standard unilateral access, (ii) customised access, (iii) transaction feed access, and (iv) interoperability. Under the Code and the Guideline, an infrastructure has an absolute right to gain standard unilateral access to another infrastructure. The rights under the three other link scenarios are conditional upon e.g. commercial agreement, technical and operational readiness, no impact on risk, etc.

The Code and the Guideline do not only lay down the conditions under which a link is to be accepted. They also delineate the process that infrastructures should follow when negotiating the links. Moreover, the Code and the Guideline also introduce a mediation mechanism, should the parties involved in a link request fail to agree. By laying down the conditions for setting up links and the process to follow when negotiating links and by introducing a mediation mechanism, the Code and the Guideline have taken significant steps towards potentially eliminating Barrier 2 on the restrictions on location of clearing and settlement and Barrier 5 on impediments to remote access. However, while the Code has achieved a lot in a short period of time, notably as regards price transparency, improvements can be made on price comparability, and its effectiveness remains to be proven as regards its more difficult parts, namely access and interoperability.

Initial results are encouraging; following agreement on the Guideline in Summer 2007, infrastructures quickly tried to exploit the increased opportunity to set up links with other markets. So far, these link requests have occurred primarily in the clearing space and for some of the most significant European markets (LSE, Deutsche Börse, Euronext, Borsa Italiana).[111] Nevertheless, while link discussions have so far been held in a constructive spirit they inevitably run into difficult issues. Some of these were foreseen by the Code and the Guideline and should accordingly be resolved in line with the rules and procedures foreseen by these two instruments. Other issues go beyond the Code and the Guideline and will accordingly need to be addressed in a complementary manner. The Commission is doing its part to address some of the public policy issues that have arisen in this context, e.g. working with the industry, CESR and national regulators to address the potential impact of differing national regulatory arrangements on the effective possibility of cross-border service provision.

The Code of Conduct has given rise to numerous link requests. When bringing these forward, requesting organisations have often run into differences in regulatory arrangements. For example, while central counterparty clearing houses are required to be a credit institution in certain Member States (e.g. France, Germany), this is not the case in others (e.g. United Kingdom, Italy). Such differences make it more difficult to realise links. CESR's Post-Trading Expert Group (PTEG, see section 5.4.) has started to map these differences. The Commission has issued a formal mandate[112] requesting CESR to conclude the mapping exercise and to

---

110 http://www.fese.eu/_lib/files/AccessInteroperabilityGuideline.pdf

111 For illustration, the most common link request so far is from a CCP, who wants to receive (i) transaction feed access from the trading venue, (ii) interoperability with the incumbent CCP, and (iii) standard or customised access with the local CSD. The number referred to in the text above treats these three separate requests as related, as they emanate from the same requesting organisation. Accordingly, behind the 20 sets of requests referred to above hides a significantly higher number of separate requests.

112 See the formal mandate to CESR of 28 July 2008 for technical advice on identifying regulatory arrangements for post-trading infrastructures and advising on possible solutions in terms of bridging any

provide advice on how potential differences can be bridged. CESR will conclude the exercise by early 2009.

Implementation of the Code is reviewed by the Monitoring Group of the Code of Conduct (MOG)[113] composed of representatives of the European Commission, CESR and the ECB. It meets every quarter and takes stock of how price transparency, access and interoperability and service unbundling and accounting separation are being implemented by market infrastructures. To that end, it invites providers of infrastructures and users to attend their meetings in order to provide their views and assessments. The MOG publishes a summary after each meeting, which is made public. The MOG will also prepare annual reports taking stock of its work.

In addition to the monitoring exercised by the MOG, the Code foresees that external auditors will monitor how infrastructures implement the service unbundling and accounting separation part of the Code. Specific Terms of Reference govern this procedure and were finalised in July 2008. In short, each infrastructure will every year prepare a Self-assessment Report outlining how it complies with this part of the Code. Auditors will prepare an Assurance Report in which they will assess the content and the format of the Self-assessment Report. The Assurance and the Self-assessment Report, together with the confidential accounting separation data will be sent to national regulators who will confirm the receipt of this information. In addition, each infrastructure will prepare a public statement on compliance with the stipulations of the Code of Conduct on service unbundling and accounting separation. This public statement will be accompanied by an Auditor's Report.

In conclusion, it should be remembered that in order to fully exploit the Code's potential benefits, parallel action is needed in other areas. Notably, the functioning of the Code is dependent on actions by Member States, as link requests have frequently run into barriers of either a regulatory or supervisory nature. Accordingly, action by Member States to dismantle such barriers would be necessary for the proper functioning of the Code.

In response to a Council request, the Commission reported to the EFC (in November 2008) and to ECOFIN (in December 2008) about the different aspects of the Code of Conduct and its functioning.

5.3. Systemic risk management industry standards for CCPs

Systemic risk arises in the context of clearing and settlement arrangements when the failure of one system or participant in a system to meet its required obligations threatens the capacity of other participants or financial institutions to meet their obligations. This could cause significant liquidity or credit problems and might threaten the stability of the financial system as a whole.

In view of the Code of Conduct's (see section 5.2) part on access and interoperability, Central Counterparties (CCPs) have been faced with a new aspect: systemic risk that may arise when CCPs become interoperable, and how to deal with it. Therefore, the CCPs' association, EACH, conducted work on links between CCPs, in particular on the development of inter-CCP risk management standards.

---

potential differences in these arrangements: http://ec.europa.eu/internal_market/financial-markets/docs/clearing/2008_07_28_cesr_mandate.pdf

[113] See website of the MOG for further links and documents: http://ec.europa.eu/internal_market/financial-markets/clearing/mog_en.htm

EACH has established seven standards[114] to be adopted in order to prevent competition between CCPs leading to a decline in risk management standards. This work was undertaken in order to define principles to support the requirement for CCPs that establish interoperable relationships to arrange an adequate collateralisation scheme to cover inter-CCP exposures and to define a risk management model which ensures the fair and non-discriminatory treatment of both requesting and receiving CCPs (as requested by the Guideline). The defined standards require compliance with the CPSS-IOSCO recommendation on CCPs as regards the issue of links between CCPs (Recommendation 11) and took into account the work conducted to date by central banks and regulators on the ESCB-CESR recommendations. However, as each CCP has its own risk framework, and there are several different risk management models currently in place for existing links between CCPs, there is no definition of a single risk management model for inter-CCP links (i.e. the question of how to collateralise inter-CCP positions), in particular since regulators will have to be satisfied with the recommended model.

The recurring items in this discussion[115] are concerns regarding the implications that interoperability could have as regards the soundness of CCPs (interoperability must not lead to a race to the bottom in terms of risk management practices). As CCPs should not compete on the basis of risk, the industry concluded that the Code was to be complemented by other standards as regards risk management aspects, such as those being developed by EACH and the ESCB-CESR Recommendations. Users often point out that transparency regarding the risk management arrangements adopted by CCPs is extremely important in order to allow users to assess their own exposure to CCPs and to assess the net value of the risk mitigation effect of using a CCP.

5.4. CESR's Post-Trading Expert Group (PTEG)

In anticipation of regulatory and market developments and in the context of the various initiatives developed by the public and private sector in the area of post trading, members of CESR decided in 2007 to establish a group of CESR experts, the **Post-Trading Expert Group** (PTEG), to focus on post-trading activities in the EU, relevant to CESR and its members. CESR decided to create this platform to follow all initiatives in the area of post-trading more closely, establish a place to share supervisory experiences and, where appropriate, to respond to these initiatives.

In view of the responsibilities of national securities regulators for post-trading activities in the respective Member States (such as the expected effects of MiFID, the Code of Conduct and TARGET2-Securities), the PTEG now focuses on a number of regulatory initiatives going on in the area of post-trading, with the objective of enhancing a level playing-field and the safety and soundness of post-trading activities within the EU. The political support for these regulatory initiatives was reflected in the conclusions of the EU Council on Clearing and Settlement of 9 October 2007[116] and explicit political support and guidance was given by the

---

[114] See http://www.eachorg.eu/digitalAssets/49/49417_EACH_Inter_CCP_Risk_Management_Standards_July_2008.pdf

[115] E.g. when LCH.Clearnet presented their views on CCP clearing to the CESAME group; see page 4 of the Report on the meeting of 20 February 2006: http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20060220-report_en.pdf

[116] http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/96375.pdf

EU Council for the work on CESR/ESCB transformation of the Standards for Securities Clearing and Settlement into Recommendations in the Council Conclusions of 3 June 2008[117].

The first area of work for the PTEG is the Code of Conduct for Clearing and Settlement, in particular with regard to the envisaged role of regulators in acting as recipient of information under the third phase of the Code. The Code of Conduct is developed and signed by the providers of infrastructures for Trading, Clearing and Settlement, i.e. Stock Exchanges, Central Counterparties (CCPs) and (International) Central Securities Depositories ((I)CSDs) within and outside the EU-area. CESR is a member of the Monitoring Group, the group established by the European Commission with the mandate to review the compliance with the Code by the signatories (see section 5.2.).

The second area of work covered by the PTEG is the ESCB-project TARGET2-Securities (T2S). This long-term project (see section 5.5.) aims to create a single and central platform for the cross-border and domestic settlement of securities against central bank money in euro (and Danish crowns and possibly other currencies), run by the Eurosystem. CESR is an observer in the T2S Advisory Group, an advisory body to the Governing Council of the ECB in the structure for the T2S-project, and remains in dialogue with the ECB on this project in various other ways. An important area, where CESR is also fully involved, concerns the work on the contractual arrangements between T2S and CSDs which will be the basis for the provision of certain services to CSDs. Given the regulatory implications of this service provision, national regulators will need to approve those arrangements. Therefore, CESR's role in coming to a harmonised approach among regulators in that respect is a major task in which coordination between all stakeholders is required.

Thirdly, with regard to their role in the draft ESCB-CESR Recommendations for Securities Clearing and Settlement, the PTEG prepares the views of securities regulators (see section 5.7.).

The PTEG's projects relating to the implementation of the Code of Conduct merit particular mention in this report. First, PTEG launched a stock-taking exercise on the various national regulatory conditions which are imposed on post-trading infrastructures seeking cross-border access and interoperability. This is an on-going exercise which has resulted in a better understanding of requirements and the fact that some CESR members are currently in the process of reviewing their internal requirements in this respect. Second, PTEG discussed and agreed the degree of supervisory engagement with regard to the third phase of the Code, as requested by the Code's signatories.

Both exercises revealed however a number of weaknesses in the whole process. Firstly, a number of supervisors deplored the fact that the Code of Conduct was agreed by supervised entities without the involvement of their supervisors, even though the Code itself acknowledges their importance and the relevance of the national legal and regulatory environment. Due to the self-regulatory nature, regulators are not in a position to enforce the Code. Secondly, in addition to CESR members, other national authorities are also involved in the supervision and the oversight of the signatories of the Code. These authorities do not participate in PTEG. Thirdly, certain signatories of the Code are established in non-EU countries and their supervisors are also not CESR members.

The work of the PTEG is also of particular relevance in view of the former proposal for a revised Investment Services Directive (ISD), which is now the adopted and implemented MiFID. Articles 34, 35, and 46 of MiFID enshrining the basic right of users to make a free

[117] http://register.consilium.europa.eu/pdf/en/08/st09/st09720.en08.pdf

choice of the settlement location was thus a welcomed further step in allowing market-led integration of the EU settlement environment. National regulators are typically concerned about the implications of external access for the smooth functioning of domestic markets and/or about the applicable supervisory regime for external participants. If a level playing field is to be assured among EU clearing and settlement providers, central counterparties and central securities depositories should have a right on the basis of MiFID, subject to non-discriminatory, transparent and objective criteria and without prejudice to the right of refusal of access by operators of clearing and settlement systems, to become members of these other clearing and settlement systems. In this view, the ESCB-CESR recommendations (see section 5.7.) could be a common set of recommendations to ensure the efficiency and soundness of EU clearing and settlement systems.

5.5. Eurosystem's initiatives in the post-trading area: TARGET2-Securities and the Giovannini Barriers

TARGET2-Securities (T2S) is the Eurosystem's initiative to provide borderless settlement services on a voluntary basis to CSDs. It is designed to be a technical platform for CSDs for the real-time delivery-versus-payment (DvP) settlement of securities against central bank money in euro (as well as in Danish crowns, and possibly in further currencies), concentrating securities and cash settlements within a single IT infrastructure. T2S will not replace CSDs or the contractual relationships between CSDs and their users. The project implies that CSDs' securities accounts are technically maintained and operated on the T2S platform, while they are legally maintained under the responsibility of the CSDs, with the accounts being opened and maintained in the books of the respective CSD. T2S would as such not be considered a system under the settlement finality directive, but a common technical platform, therefore finality of transfer orders will be achieved according to the rules of the participating CSDs.

T2S would thus allow CSDs to use the services of a common integrated platform, which would result in greater efficiency and large economies of scale and finally benefits for investors. It is important to signal that the use of an integrated technical platform would allow applying the same settlement fees both for cross-border and domestic transactions.

As previously mentioned, Giovannini Barriers 2 and 10 (which relate to restrictions that require the use of multiple systems) could be dismantled by the effective establishment of links between systems. T2S would facilitate and support the establishment of links between CSDs and would increase the efficiency and the predictability of the completion of the legal transfer, due to the transfer order finality on both sides of a cross-system transaction and the standardised simultaneous settlement in T2S on the accounts of both CSDs involved, resulting in the legal exchange of cash and securities. This would also result in reducing the overall costs of such links.

T2S would also eliminate Barrier 4 (absence of intra-day settlement finality) and Barrier 7 (national differences in operating hours/settlement deadlines) as within a single platform there could no longer be different operating days/hours and problems of intra-day finality. T2S would also directly facilitate the removal of Barrier 1 (national differences in information technology and interfaces) as it would use the Giovannini protocol (based on ISO standards) for messaging. It is however important to stress that T2S would not be operational before 2013, therefore the work undertaken by the private sector in dismantling the above-mentioned barriers will most likely not be delivered before 2013.

Moreover, in principle, there would be no direct contribution of T2S to the removal of Barrier 3 (differences in national rules relating to corporate actions, beneficial ownership and

custody). However, there is a possibility that the harmonisation of the settlement process itself could increase the pressure on CSDs, issuers and intermediaries to accelerate the work on convergence and harmonisation of rules on corporate actions. Similarly, T2S would on one hand not have a direct impact on Barrier 9 (national restrictions on the location of securities) as its elimination would require changes in national laws; on the other hand, the platform would finally allow for seamless cross-system DvP (delivery versus payment) settlement in central bank money.

5.6. Eurosystem's initiatives in the post-trading area: CCBM and the Giovannini Barriers

In March 2007 the Eurosystem decided to develop a single IT platform for the management of eligible collateral used for domestic and cross-border credit operations. The objective of the project called Collateral Central Bank Management (hereinafter CCBM2) is to increase the efficiency of the Eurosystem's internal systems for collateral management, optimising the cost of mobilising collateral, establishing efficient methods for delivering and accepting securities and non-marketable assets (notably credit claims) both at domestic and cross-border levels and providing a harmonised level of service based on Giovannini communication protocol developed by SWIFT. Such a standardised solution would facilitate the interaction of counterparties acting as collateral providers with the Eurosystem, in particular for those active cross-borders.

CCBM2 would thus guarantee collateral providers a single harmonised procedure for domestic and cross-border use of collateral, improving the efficiency the speediness and reducing the cost of the process and thus facilitating the cross-border use of collateral.

According to the principles established by the Eurosystem, CCBM2 will be fully compatible and interfaced with TARGET2-Cash and TARGET2-Securities (T2S), will cover different collateralisation techniques (such as pledge and repo), will handle all eligible collateral (both securities and non-marketable assets), will process instructions in real time on a straight-through-processing and will be able to take collateral through all eligible Securities Settlement Systems (SSSs) and related eligible links between them, as well as the central bank procedures for handling of credit claims.

Against this background, CCBM2 would actually facilitate the provision of collateral and guarantee compatibility with TARGET2 and T2S and thus contribute to the improvement of the efficiency of post-trading services in the Euro-area. CCBM2 would not be directly addressing the removal of specific Giovannini Barriers (apart from Barrier 1, since it will imply that all the Eurosystem central banks will adopt the Giovannini IT communication protocol, and the barrier on the location of collateral/settlement, since it will promote the removal of the "repatriation requirement" in the conduct of Eurosystem monetary policy operations). Thus, CCBM2 may promote the adoption of specific standards facilitating the process for dismantling some barriers. As with T2S, CCBM2 will be based on the Giovannini communication protocol and would therefore contribute to the removal of Barrier 1. As for the restrictions on the location of clearing and settlement (Barrier 2/10), these barriers do not pose particular problems on the cross-border provision of collateral and therefore CCBM2 would not have a direct contribution on the removal of them, however a greater efficiency in the collateral management would definitely contribute to the improvement of clearing cross-border transactions.

5.7. ESCB-CESR initiative in the post-trading area: from draft standards to recommendations

The international community has increasingly focused on the soundness, safety and resilience of the post-trading infrastructure when assessing the strength and vulnerabilities of the financial markets in various countries. In an effort to provide an adequate response to these issues, the European System of Central Banks (ESCB) and the Committee of European Securities Regulators (CESR) set up a joint group in order to adopt common recommendations standards on Securities Clearing and Settlement Systems in the EU. These standards would be the adaptation into the EU of the corresponding recommendations adopted in 2001 and 2004 by CPSS and IOSCO.

It was considered that adoption of common standards, which would be incorporated into the rulebooks of the various EU supervisors, regulators and overseers and be applied by the supervised entities, would provide a minimum level of harmonisation of EU supervisory practices and approaches. Coupled with a common assessment methodology and taking into account the intensified dialogue among regulators, these standards could also enhance and accelerate regulatory convergence.

However, the ESCB-CESR work stumbled upon a number of difficulties which have prevented the conclusion of the work so far. These difficulties are the result of the fact that most of the business and legal conditions relevant for the securities clearing and settlement industry derive from national regulations which are not harmonised. In essence, the underlying difficulty of the whole exercise is whether (a) the supervisors and the overseers may be allowed to make explicit or implicit policy choices affecting business practices in this area, and (b) whether all authorities share a common view as to the way forward.

In practice, the three main issues that prevented the adoption of the standards were (a) their legal basis, (b) the way to deal with systemically important custodian banks which provide settlement services and (c) how to deal with CSDs which have a banking licence, especially as regards the risk mitigation techniques they use. In 2008, a compromise solution was reached between the national Ministries that could unblock the whole process. On the basis of the conclusions of the EU Council of 3 June 2008[118], both CESR and the ESCB were requested to complete the work, taking into account the guidance given by the Council.[119] The ex-draft standards will become non-binding "recommendations"; they will be addressed to public authorities and not to supervised entities; custodian banks will be left out of their scope (but CEBS is invited by the Council to further review, in cooperation with CESR, the coverage of risks borne by custodians, taking into account that some CSDs/ICSDs/CCPs are also subject to the Capital Requirements Directive so as to ensure a level playing-field while avoiding inconsistencies in the treatment of custodians and double regulation by the end of 2008). On credit and liquidity risk controls, the former draft Standard 9 should be replaced by the (2001) CPSS/IOSCO Recommendation 9 for securities settlement systems. CESR and the ESCB were invited to adapt and finalise the draft by Autumn 2008.

The exercise provides a good illustration of the benefits of the approach but also of its limits. The draft recommendations can provide a good minimum harmonisation stratum for the supervisory authorities and could facilitate, among other things, the cross-border interpenetration of systems. However, as soon as important policy choices, even technical

---

118 http://register.consilium.europa.eu/pdf/en/08/st09/st09720.en08.pdf

119 The guidance given included among other things: the transformation of the Standards, addressed to providers of post trading services, into Recommendations for public authorities and the exclusion of custodians from the scope of application.

ones, are to be made, the process shows its limits; wider political agreements need to be reached at the legislative and political level.

5.8. The Commission's Price Monitoring Study (Study to monitor the evolution of trading and post-trading prices, costs and volumes)

In 2006, the Commission launched a study to monitor the evolution of trading and post-trading prices, costs and volumes. The first part of this project consisted of the development of a methodology. It was awarded to Oxera following a competitive tender and was concluded in Summer 2007. The second part consists of applying this methodology. Following a competitive tender, Oxera was awarded the contract to apply the methodology. It was started in Autumn 2007 and first results are due in late 2008.

The objectives of the study: The pricing of trading and post-trading services is complex. Several studies have attempted to shed some light.[120] Most have concluded that cross-border prices and costs are considerably higher than the corresponding costs and prices for domestic transactions. While useful, none of the results have been universally accepted as providing an accurate description. The objective of this study is therefore to develop a solid methodology that enables the Commission to more precisely follow the future evolution of prices, costs and volumes of post-trading activities and changes of the services offered within Europe. The European Commission believes such a solid methodology will contribute to improving transparency of the current market outcome and the identification of where market efficiencies are being delivered.

The debate in CESAME: In view of the study's objectives and the close cooperation of industry that is required, the study was discussed at several CESAME meetings. The following major themes came up.

- ***The value of the study***: In line with the principles of better regulation, public policy intervention should be based on sound analysis and be subject to evaluation. The study contributes on both fronts. It aims to provide the Commission with a solid understanding of the overall trading and post-trading value chain. It also aims at offering valuable data on the evolution of prices, costs and volumes, which will enable the Commission to assess the effect of its policy interventions. Overall, the ability to follow the evolution of trading and post-trading prices, costs and volumes is beneficial to us all. We believe that market participants will benefit from the application of this methodology in two ways. First, because they will have a clearer idea of overall price and cost developments over time in the trading and post-trading sphere. Second, because public policy action will be better informed, thereby focusing on the real problem areas.
- ***Costs and concerns of supplying data***: The methodology requires the collection of a significant amount of data. The Commission and Oxera rely on trading and post-trading market participants to supply the necessary data. Significant debate focused on the potential concerns of industry with supplying data (e.g. the internal collection of data will take time, be costly or the requested data may be commercially sensitive). Following a debate in CESAME and bilaterally between Oxera and data suppliers, Oxera is undertaking steps to address these concerns.

---

[120] E.g. Giovannini report (2001), CEPS (2001), NERA (2004). The European Commission's Draft Working Document on post-trading services (2006) provides an overview of this existing research.

- ***The full value chain***: An important objective of the study is to understand the micro-economic features of the trading and post-trading market structure. This requires that all actors covered by the methodology submit data.

5.9. External contributions by guests to the CESAME meetings

Frequently, guests have been invited to present relevant issues at CESAME meetings. The following examples might render a fair picture of the various issues discussed (others might be referred to elsewhere in this report, e.g. the **OMGEO** and **ICMA** presentation (see Barrier 6), the **ISIN fee issue** (see Barrier 8) or the **OXERA** study (see paragraph 5.8. of this report).

On the meeting of 10 June 2005, the **EIB** presented on difficulties regarding commercial paper and securitisation and explained as market participant the problems resulting from the fragmentation of euro short term paper and securitisation markets. Furthermore, **Euroclear** Group presented a status report on harmonisation implementation, i.e. their view on their experience gained on harmonisation while developing their technology platform integration project. On 24 October 2005, the Treasurer of **Siemens AG**, presented the position of a major industrial company and active user of financial services and on 20 February 2006, **Merrill Lynch** developed their views on European post trade infrastructure and on the impact that the ownership structure of infrastructures has on the growth and competitiveness of the EU capital markets; also **Professor's Alistair Milne of Cass Business School**, London view was heard with his economic view on standard setting in the area of clearing and settlement. Other aspects, such as the approach to IT convergence in the post-trading industry (by **Monte Titoli**) were covered on 12 June 2006 while on 12 February 2007 PensPlan, a regional pension scheme from Northern Italy vividly explained their experience as users of financial services.

Investment Funds Processing: The mutual investment fund market and its post-trading processing has traditionally been characterised by a lock of standardisation, high levels of manual processing for order trading and settlement, and the requirement to inter-face with multiple parties. The inefficiencies and complexities have long since been described and bemoaned. The investment funds area was covered on 20 February 2006 by **Robeco** and on 12 June 2006 by **EFAMA** and **BVI**.

5.10. Going beyond: the "16th Giovannini Barrier"

During the CESAME group discussion, it was mentioned occasionally that the 15 Giovannini Barriers had been identified seven years ago and that in the meantime – and because the Giovannini Barriers were actively addressed - other barriers had been identified which had not been addressed directly through the Giovannini Barrier removal process. Such issues were subsumed under the term "the 16th Giovannini Barrier". While not an exhaustive list, some of these barriers are explained below.

5.10.1. Netting issues

In general, netting is an agreed set-off of mutual positions or liabilities between business partners or participants. Netting reduces a large number of individual positions or liabilities to

a smaller number of positions or liabilities. Netting can take different forms. Claims resulting from netting are legally enforceable to a varying extent in case of default by a participant.

While the adoption and satisfactory implementation of the Settlement Finality Directive and the Financial Collateral Arrangements Directive has successfully solved the most frequent issue of netting (described in Barrier 14), i.e. bilateral netting, industry and legal experts have long since voiced the need for, and potential benefits of, a more encompassing European framework, e.g. on tri-party or multilateral netting. It is generally recognised that the provision in Article 7 FCD on close-out netting has contributed to eliminating Giovannini Barrier 14. It is worthwhile exploring the netting issue further, but this will require extensive legal research and discussion (in order to provide a solid provision which benefits the Single Market).

5.10.2. Different operating hours/settlement deadlines experienced by investors

Users of infrastructures have argued that even if all 10 standards on Barriers 4 and 7 are fully implemented throughout the EU, this still might not help users of these infrastructures, in particular when a chain of intermediaries has to be used. This is because infrastructures and intermediaries may apply different operating hours and settlement deadlines to their customers if trades have to be processed through various entities.

Thus, it has become clear that there are new operational barriers and obstacles (other than the ones identified by the Giovannini Reports) that impede efficient cross-border settlement and require further action regarding settlement activities that are typically conducted by CSDs as "investors' CSDs". Hence, while harmonisation of operating hours and cut-off times has been achieved at a domestic level, there is still a lack of harmonisation, especially at cross-border level where transactions are intermediated not just by an investor CSD but also often by intermediaries (such as banks) as well, making the chain of transactions complex.

To this aim, a full mapping of cut-off times for cross-border transactions for each country and for each CSD link is needed according to a jointly agreed methodology[121]: this mapping exercise will be prepared by ECSDA starting from background material provided by ECB and SIFMA and will focus on those CSDs for which cross-border traffic is particularly important: i.e. the ICSDs, the euro-area CSDs, and the CSDs in UK, Denmark, Sweden and Switzerland. Agents/custodians could (and should) be included at a later stage.

Based on the results of this mapping exercise, an action plan will be developed with the aim of harmonising cut-off times and operating hours to facilitate cross-system settlement. This action plan might result in a set of new standards/recommendations. This action plan identifying concrete proposals for harmonisation should be prepared in the beginning of 2009. ECSDA will take the lead in this project, but there will be a need for co-ordination with central banks and users of the systems.

[121] See ECB document of 6 May 2008; http://ec.europa.eu/internal_market/financial-markets/docs/cesame/other/20080616-barrier_7_en.pdf

5.10.3. Specific (CCP) clearing issues

During the period 2000 – 2001 when the Giovannini Barriers were identified, there were not many central counterparties (CCPs) for the equities market in Europe[122]. As a result, the barriers did not cover issues specific to clearing. Since then, more CCPs have been set up. Market participants active in multiple markets now need to cope with different CCP practices such as operating procedures, processing timing, margin posting and buy-in periods. Hence, there may be a need to identify areas where differences in how CCPs work cause higher costs and operational risks to market participants, and prioritise for harmonisation those areas that would yield the most benefits to market participants[123]. Already on 20 February 2006, LCH.Clearnet presented their views on CCP clearing to the CESAME group[124].

---

[122] Clearnet, formed in 1969 to clear contracts traded in Paris commodity markets, started clearing equities traded on the Paris Bourse in 2000. The London Clearing House (LCH), founded in 1888 to clear commodity contracts traded in London, began clearing of equities for Tradepoint (renamed virt-x) in 1995 and for the London Stock Exchange in 2001. Eurex Clearing was formed in 1998 when the DTB (Deutsche Terminbörse) and SOFFEX (Swiss Options and Financial Futures Exchange) merged; it started clearing equities in 2003. Cassa di Compensazione e Garanzia S.p.A. (CC&G), started in 1992 as CCP for bond derivatives, started to clear equities traded on Borsa Italiana in 2003. Four more CCPs that clear equities were launched in the last few years: SIS x-clear in 2003, Central Counterparty Austria GmbH (CCP.A) in 2005, European Multilateral Clearing Facility N.V. (EMCF) in 2007 and European Central Counterparty Limited (EuroCCP) in 2008.

[123] It has been mentioned that, on the providers' side, CCPs cope with obstacles they may encounter if they want to provide cross-border services, such as regulatory issues (e.g. the requirement of a banking licence or the setting up of local subsidiaries subject to 'host-state' supervision in order to offer local settlement services in other Member States). However, such issues are linked to the Code and are already dealt with by the relevant bodies, namely CESR (see section 5.4., in particular CESR's Post-Trading Expert Group, PTEG).

[124] See page 4 of the Report on the meeting of 20 February 2006: http://ec.europa.eu/internal_market/financial-markets/docs/cesame/meetings/20060220-report_en.pdf

C. Conclusions and outlook

6. Overview

The achievements regarding the barriers were outlined in paragraph 2.3. of this report, the following table briefly displays the outstanding issues which still have to be tackled:

Giovannini Barrier[125]	Outstanding issues	Timeline
1. **Diversity of IT platforms/interfaces**	Full implementation of the standard; potential positive impacts of TARGET2Securities ('T2S')	Standard setting: completed Implementation: 2011
2. ***Restriction on location of C&S*** & 10. ***Primary dealer restrictions***[126]	MiFID rules important legal background; effectiveness of the Code in providing additional possibilities at settlement/CCP clearing level; attitude of national supervisors/regulators; more comprehensive coverage of bonds and CCP clearing needed; potential positive impacts of T2S	Standard setting: 2009 Implementation: possibly 2013 (N.B. for settlement of bonds, work is ongoing and should be finished by 2010)
9. ***Restrictions on location of securities***	Adoption of appropriate EU and/or national measures; further detailed considerations of issues raised necessary	Standard setting: 2010 Implementation: 2013
3. **Different rules governing corporate actions**	Implementation of distributions standards; finalisation of the remaining standards (see Barrier 3) and their subsequent implementation: tackle corresponding legal and fiscal issues	Standard setting: 1st quarter 2009 Implementation: gradually, by 2012
4. **Absence of intra-day settlement finality &** 7. **Different operating hours/settlement deadlines**	Activity of investors CSDs to be included in the standards; implementation of all standards to be effected by infrastructures and their direct and indirect participants; potential positive impacts of T2S	Standard setting: completed (but under review) Implementation: of CSDs by 2008 (incl. new Member States' markets); outstanding parts by 2010
6. **Differences in standard settlement periods**	Barrier remains; reassess prioritisation; evaluate effectiveness of available partial solutions, e.g. same-day confirmation/matching	Standard setting: none Implementation: no date fixed due to low priority
11. ***Restrictions on withholding agents***	Adoption of recommendations by the Commission; implementation by Member States	Standard setting: Recommendations by 2009 Implementation: by 2011
12. ***Restrictions on tax collection***	Commission to discuss with Member States concerned	Standard setting: by 2009 Implementation: 2010
13. ***Absence of EU-wide framework of laws***	Adoption of appropriate EU and/or national measures; further detailed considerations of issues raised necessary	Standard setting: 2010 Implementation: 2013
15. ***Conflict of laws***	Comprehensive EU approach to be defined by the Commission	Standard setting: 2010 Implementation: 2013

[125] *public barriers in light italics*, **industry barriers bold and underlined**

[126] "collapsed" into barrier 2 by EFC Sub-Committee on EU Government Bonds

7. The CESAME2 Group

In order to ensure the continuation and proper completion of CESAME's successful work from 16 July 2004 to 16 June 2008 and to dismantle fully all remaining and any other or future obstacles identified in the cross-border post-trading area, a new group (CESAME2) was set up in Summer 2008. The group is again composed of high level representatives from various private entities and observers from public-sector bodies involved in the post-trading process. The chairmanship and secretariat is ensured by the Commission. The main objectives[127] of the follow-up group is to support and monitor in a transparent way the removal of the Giovannini Barriers hampering efficient post-trading in the EU. The group will continue to provide the transparent[128] interface between the private and public-sector bodies involved in the process of dismantling the Giovannini (and other) Barriers.

[127] CESAME2's mandate: http://ec.europa.eu/internal_market/financial-markets/docs/cesame2/mandate_en.pdf

[128] Via CESAME2's website: http://ec.europa.eu/internal_market/financial-markets/clearing/cesame2_en.htm

ANNEX 1: List of abbreviations

Abbreviation	Meaning	Information/webpage
AGC	Association of Global Custodians	http://theagc.com
AMTE	Association Marchés Taux Euro	http://www.aft.gouv.fr/article_784.html
ANNA	The Association of National Numbering Agencies	http://anna-web.com
BNP	BNP Paribas	http://www.bnpparibas.com/
CAJWG	Corporate Actions Joint Working Group (formed by EACH, EuropeanIssuers (previously EALIC), ECSAs, ECSDA, ESF, FESE)	See Operational Conclusions, Giovannini Barrier 3 (Corporate Actions)
CASG	Corporate Actions Steering Group (formed by EuropeanIssuers (previously EALIC), ECSAs, ECSDA, and ESSF)	See Operational Conclusions, Giovannini Barrier 3 (Corporate Actions)
CCBM	Correspondent Central Banking Model	http://www.ecb.int/paym/coll/coll/html/ccbm.en.html
C&S	Clearing and Settlement	http://ec.europa.eu/internal_market/financial-markets/clearing/index_en.htm
CCBM	Correspondent Central Banking Model	http://www.ecb.int/paym/coll/coll/ccbm/html/index.en.html
CCP	Central Counterparty	Association see "EACH"
CEECSDA	Central and Eastern European Central Securities Depositories Association	Merged with "ECSDA"
CESAME	Clearing and Settlement Advisory and Monitoring Experts' Group	http://ec.europa.eu/internal_market/financial-markets/clearing/cesame_en.htm
CESR	The Committee of European Securities Regulators	http://www.cesr-eu.org/
Civil Law Committee	Administrated by the European Council	http://consilium.europa.eu
COM	European Commission	http://ec.europa.eu/index_en.htm
CSB	(Standard & Poor's) CUSIP Service Bureau	https://www.cusip.com/static/html/webpage/welcome.html
CUSIP	Committee on Uniform Security Identification Procedures (also used for U.S. securities identification numbers)	http://en.wikipedia.org/wiki/CUSIP
CSD	Central Securities Depository	CSD Association see "ECSDA"
DG	Directorate General – within the European Commission (e.g. DG Internal Market)	
DENISA	Diagnostic European Numbers for International Securities Accounts (proposition by FBE)	See CESAME Synthesis Report of 12 June 2006
EACB	European Association of Co-operative banks	http://www.eurocoopbanks.coop/
EACH	European Association of Central Counterparty Clearing Houses	http://www.eachgroup.org/
EALIC	European Association of Listed Companies (name changed to EuropeanIssuers)	Previously: www.ealic.com
EBF/FBE	European Banking Federation / Fédération bancaire Européenne	www.fbe.be
ECB	European Central Bank	www.ecb.int
ECON	Committee on Economic and Monetary Affairs	http://www.europarl.europa.eu/committees/econ_home_en.htm
ECOSOC	European Economic and Social Committee	http://www.eesc.europa.eu/index_en.asp
ECSAs	European Credit Sector Associations, these	For links see: individual associations

	include EBF/FBE; ESBG, EACB	
ECSDA	European Central Securities Depositories Association	http://www.ecsda.com
EFC	Economic and Financial Committee	http://ec.europa.eu/economy_finance/efc_en.htm
EP	European Parliament	http://www.europarl.europa.eu/news/public/default_en.htm
EPDA	European Primary Dealers Association	http://www.bondmarkets.com/story.asp?id=1554
ERC	European Repo Council	http://www.icma-group.org/international1/european.html
ESBG	European Savings Banks Group	http://www.savings-banks.com
ESCB	European System of Central Banks	http://www.ecb.int/ecb/orga/escb/html/index.en.html
ESF	European Securities Forum (NOT identical to the European Securitisation Forum), as of April 1st 2008 integrated into SIFMA, the Securities Industry Financial Markets Association, and renamed ESSF (see below)	http://www.eurosf.com/
ESSF	European Securities Services Forum (previously ESF)	http://europe.sifma.org/affiliates.shtml
EU	European Union	www.europa.eu
EU Council	The Council of the European Union	http://www.consilium.europa.eu/showPage.ASP?lang=en
European Issuers	Previously EALIC	http://www.EuropeanIssuers.com/
FBE/EBF	Fédération bancaire Européenne / European Banking Federation	www.fbe.be
FCD	Financial Collateral Directive	Directive 2002/47/EC of 6 June 2002 on Financial Collateral Arrangements
FESE	Federation of European Securities Exchanges	http://www.fese.be/en/
FISCO	Fiscal Compliance Group	http://ec.europa.eu/internal_market/financial-markets/clearing/compliance_en.htm
FIX	The Financial Information eXchange Protocol	www.fixprotocol.com
G30	The Group of Thirty (Consultative Group on Internat. Economic and Monetary Affairs, Inc.)	http://www.group30.org/home.php
Hague Convention	The Hague Conference on Private International Law – Convention of 5 July 2006 on the Law Applicable to Certain Rights in respect of Securities held with an Intermediary	http://www.hcch.net/index_en.php http://www.hcch.net/index_en.php?act=conventions.text&cid=72&zoek=Securities
ICMA	International Capital Market Association	www.icma-group.org
IPMA	International Primary Market Association (IPMA and the International Securities Market Association (**ISMA**) merged on July 1, 2005 to become ICMA)	www.icma-group.org
ISIN	International Securities Identification Numbers (according to ISO standard 6166)	http://en.wikipedia.org/wiki/ISIN http://www.iso.org/iso/iso_catalogue/catalogue_tc/catalogue_detail.htm?csnumber=33446
ISO	International Organisation for Standardisation	http://www.iso.org/iso/home.htm
ISSA	International Securities Services Association	http://www.issanet.org/
IT	Information Technology	
JWGGM	Joint Working Group on General meetings (formed by EuropeanIssuers (previously EALIC), ECSAs, ECSDA and ESSF)	See Operational Conclusions, Giovannini Barrier 3 (Corporate Actions)
LCG	Legal Certainty Group	http://ec.europa.eu/internal_market/financial

		-markets/clearing/certainty_en.htm
MiFID	Markets in financial instruments directive	http://ec.europa.eu/internal_market/securities/isd/index_en.htm
MIGs	Market Implementation Groups	See Operational Conclusions, Giovannini Barrier 3 (Corporate Actions)
PTEG	Post-Trading Expert Group	Dedicated CESR working group
S&P	Standard & Poor's	http://www2.standardandpoors.com/
SFD	Settlement Finality Directive	Directive 98/26/EC of 19 May 1998 on Settlement Finality in Payment and Securities Settlement Systems
SIFMA	Securities Industry Financial Markets Association	www.sifma.org
SMPG	Securities Market Practice Group	http://smpg.webexone.com/
SWIFT	Society for Worldwide Interbank Financial Telecommunication	www.swift.com
TARGET2	TARGET 2 Project	http://www.ecb.eu/paym/t2/html/index.en.html
TARGET2-Securities	**(T2S)** TARGET 2 Securities Project	http://www.ecb.eu/paym/t2s/html/index.en.html
UNIFI	ISO Standard 20022 "Universal Financial Industry message scheme"	www.iso20022.org http://www.iso20022.org/index.cfm?item_id=42953

ANNEX 2: Mandate of the CESAME Group

Mandate for the Advisory and Monitoring Group on EU clearing and Settlement

The Commission Communication on Clearing and Settlement, adopted in April 2004, proposes the setting up of an advisory and monitoring group, composed of high level representatives of various private and public sector bodies involved in the clearing and settlement process and chaired by the Commission. The tasks of the group should be:

1. Supporting the project and ensuring transparency

The integration of European Securities Clearing and Settlement Systems requires coordinated actions by private and public sector bodies. The launching of these private and public sector-led actions will have important repercussions on the way clearing and settlement functions are performed throughout the EU for the foreseeable future. Strategies and policies of a variety of market participants and service providers will have to change as a result. For the success of the whole project, it is important that all the major bodies concerned are aware of the overall objectives and direction of the project, and transmit them to the market at large.

The group, chaired by the Commission, should help to ***support*** the project and to ***ensure*** wide dissemination to the public of all necessary information, explanations and reports on the state of reform. Transparency of the work of the group will be ensured at all times. The group will contribute to building awareness of the relevance of the project for the success of the EU's financial markets and for the attainment of the objectives incorporated in the Lisbon agenda.

2. Ensuring coherent action

The group should advise the Commission on the coordination of actions by the public and the private sector and on the sequencing for the removal the "Giovannini" Barriers for which the private sector has sole or joint responsibility. The group should also monitor the results of the whole process to help the Commission ensure that its efforts will be sustained at a pace consistent with private sector reforms and developments.

To ensure such consistency of actions, four tasks are expected to be accomplished by the group:

- The group should, first of all, ***interface*** between the private and public sector bodies involved in the process of removing the Giovannini Barriers with the aim of (a) defining interdependencies among the different barriers, (b) helping coordinate detailed action plans and timetables between the public and private sectors, (c) ensuring the consistency of the overall implementation process and (d) monitoring progress and sequencing of actions;
- In this context, the group will also ***informally assist*** the Commission through the provision, on request, of advice on specific technical issues;
- The group should also ***liaise*** with the groups of experts that will tackle, more specifically, the legal barriers and the barriers related to tax procedures which are expected to be more difficult to address.
- Finally, it will also need to ***liaise*** with the Group of 30 and other international bodies to ensure the consistency of initiatives in the EU with those developed at international level.

ANNEX 3: List of CESAME Group Meetings

1. 16 July 2004
2. 25 October 2004
3. 7 March 2005
4. 10 June 2005
5. 24 October 2005
6. 20 February 2006
7. 12 June 2006
8. 23 October 2006
9. 12 February 2007
10. 11 June 2007
11. 22 October 2007
12. 18 February 2008

Final 16 June 2008

ANNEX 4: List of CESAME Group members and participants

Chairman: David Wright/Mario Nava

Principal Policy Advisor: Alberto Giovannini

Secretary: Doris Kolassa

A. Members ('P' = participating in the meeting)

ARVIDSSON Kjell (P)
BARNES Robert (P)
BENITO Jesús (P)
BEZEMER Peter
BISIGNANO Frank (P)
BOEMCKE Nikolaus (P)
BOOK Thomas (P)
CHAN Diana (P)
CHIESA Orlando (P)
DE SWAAN Tom (P)
DE VIDTS Godfried (P)
DI NOIA Carmine (P)
DUDAS György (P)
FRANCOTTE Pierre (P)
FRANSENS Dorien (P)
FREY Werner (P)
GISLER Daniel (P)
GOIRIGOLZARRI José Ignacio (P)
HARDT Judith (P)
HARDY David
HARTSINK Gerard (P)
HUMPHERY Marye (P)
LIDDELL Roger
MAI Stefan (P)
MARSON Jacques-Philippe (P)
MERERE Joël (P)
MERRIMAN Alexander (P)
MILLSAP Marshall (P)
NARVAEZ José Maria (P)
NAWRATH Axel (P)
NICOL David (P)
PASSERA Corrado (P)
PERRAZZELLI Alessandra (P)
PONCELET Patrick (P)
RAVOET Guido
RENAULT Patrice (P)
SABATINI Giovanni (P)
SAMMONS Michael (P)
SCHUSTER Stephan (P)
SULTAN Naveed
TANTAZZI Angelo
THIRE Anso (P)
VANNI D'ARCHIRAFI Francesco
VERWILST Herman (P)
VICARIO Roberto (P)

B. Participating Representatives of Members

ARLMAN Paul
BARKSHIRE William
BISSARA Philippe
CITTADINI Paolo
CLELAND Victoria
CUNNINGHAM Rory
DAHLGREN Malin
DEROBERT Eric
DIJMARESCU Diana
LAMBERTI Hermann Josef
LAZZARI Valter
MARSAL Pierre
PASSAMONTI Francesca
PEETERS Ilse
PRUSKI Jerzy
SINGH Satvinder
SLEENHOF Ruud
SYMONS Paul

FARNHAM Adrian
FONTAN Florence
GAUTIE Sophie
GREBORN Bo
HEMON Christophe
KELLNER Julia
WALLIN-NORMAN Karin
WERNER Swen
XIMENEZ Santiago
ZEUSS Jürgen
ZICKWOLFF Marcus

D. Invited Guests

ATZWANGER Michael
ANFOSSI Claudio
AUSTEN Mark
BARNES Fod
BRENNAN Martin
CORREIA DA SILVA Luis
COSTA Paulo
COSTANTINI Giovanni
CUNNINGHAM Rory
DAMMERS Cliff
DE WOLF Joseph
DEAK Daniel
DELBECQUE Bernard
DOUGLAS Andrew
DUMONT Marie-Paule
ELOY Jean-Marie
FLODSTRÖM Ann
FREEMAN Tony
GRUNDELL Ella
HELLIER Charles
JENSEN Ove Sten
KINDLER Tomas
KUHNEL Dan
MILNE Alistair
MORITZ Peter
MUIR Andrew
O'GRADY Deirdre
POZNIAK Gregor
PREIMANIS Agris
REINA Volinka
RUTBERG Anne
SCHEPERS Manfred
SIEBEL Rudolf
VAN DIJK Reinder
WAGEMANS Norbert
WALLIN-NORMAN Karin
WIGLEY Bob
YOUNG Richard
ZINKEISEN Klaus

E. Observers

CLARK Alastair
FARKAS István (CESR)
JENKINSON Nigel
LARGE Andrew
MOELIKER Wim (CESR)
PRUSKI Jerzy
RUSSO Daniela (ECB)
SAPORTA Victoria
SENDEROWICZ Krzysztof
TUMPEL-GUGERELL Gertrude (ECB)
WYMEERSCH Eddy (CESR)

F. Commission Staff (*non-permanent, on temporary basis)

ARTEAGOITIA Juan
BAUR Dirk*
MAUERHOFER Gudrun*
MOREN Pekka

BERRIGAN John
BUFTON Rosalind
CABALLERO SANZ Francisco
DEGERBECK Eric
FRANCOIS-PONCET Florence
FRIESS Bernhard
GATELLI Debora
GIANNI Chiara*
GREENAWAY Sean
HROVATIN Sebastijan
HUEZ Jean-Marc
IDILI Maura*
KALLENBERGER Ute
KOSKINEN Jenni*
KUPFER Séverine
LEVIN Mattias
LO GIUDICE Salvatore*
LÖBER Klaus*
LOWE Angela
MARTINEZ RIVERO Eduardo
MULAROVA Denisa*
MURRAY Michael
NOLTE Nina*
PAECH Philipp*
PLANTA Fabrizio*
RAVIZZA Francesca*
SALTELLI Andrea
SCHULZE Niels
SCHWIMANN Irmfried
SVOBODA Marek*
THOMAS Martin*
THORSÉN Tomas
TOMARAS Konstantinos
ULLRICH Corinna
VAIGAUSKAITE Dovile
VEREECKEN Marc
VILLEGAS Manuel*
WALKNER Christoph
WEZENBEEK Rogier

ANNEX 5: Overview of the major global efforts on harmonisation and standard setting in clearing and settlement

Time	European	International
1977 (Oct.)	Study on a new system for the settlement of securities transactions within the EC	
1983 (Dec.)	Study by M. Hall and M.G. Duncan	
1988	Kessler Report (July)	ISSA 4 recommendations
1989		G30 Clearance and Settlement in the World's Securities Markets
1990		Report of the Committee on Interbank Netting Schemes of the Central Banks of the G10
1994 (Mar.)	Model Agreement between CSDs	
1998	European Monetary Institute, Standards for the use of EU Securities Settlement Systems in ESCB credit operations	
2000		ISSA Recommendations
2001	Publication of the First Giovannini Report (November)	CPSS IOSCO Recommendations for Securities Settlement Systems
2003	Publication of the Second Giovannini Report (April)	G30 Global Clearing and Settlement: A Plan of Action ("New G30 Recommendations")
2004	Second Commission Communication on Clearing and Settlement (April)	CPSS IOSCO Recommendations for Central Counterparties
2006	Industry Code of Conduct on Clearing and Settlement and announcement of TARGET2-Securities project	G30 Final Report on the Recommendations on Clearing and Settlement
2008	Launch of the TARGET2-Securities project	
Foreseen:		
2009	ECSB-CESR Recommendations	
2009	Commission Recommendations on Principles on improved procedures for obtaining withholding tax relief on securities income in the Member States	

ANNEX 6: Overview of Council Conclusions and European Parliament reports on clearing and settlement

(ECOFIN) Council Conclusions on Clearing and Settlement

3 December 2008: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/104451.pdf
3 June 2008: http://register.consilium.europa.eu/pdf/en/08/st09/st09720.en08.pdf
9 October 2007: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/96375.pdf
27 February 2007: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/92984.pdf
28 November 2006: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/91899.pdf
25 November 2004: http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/ecofin/82818.pdf

European Parliament Reports on Clearing and Settlement

In the **Andria report**[129] of 2003, the European Parliament supported largely the findings of the Giovannini Report and invited the European Commission to propose a directive regarding common rules for authorisation, control, freedom of establishment and provision of services as well as a common framework for infrastructures. The objectives were to lower the cost of cross border transactions while guarantying safe operations. The European Parliament considered that some post-trading services were of public interest and should be dealt with accordingly.

In its 2005 **Kauppi report**[130], the European Parliament reaffirmed its objectives of lowering cross border prices while limiting systemic risks, integrating systems by the elimination of competition obstacles and ensuring transparency and proper governance, thus ensuring a fair access to post market infrastructures. In this report, the European Parliament took a functional approach targeted at different levels of risk rather than at the type of actors involved. It also requested clear and coherent definitions in line with European practices as well as international standards.

[129] P5_TA(2003)0014, "Clearing and settlement in the European Union, European Parliament resolution on the communication from the Commission to the Council and the European Parliament entitled 'Clearing and settlement in the European Union: main policy issues and future challenges' (COM(2002) 257 — C5-0325/2002 — 2002/2169(COS)); OJ C 38E of 12 February 2004, p.265; http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2006:157E:0485:0490:EN:PDF

[130] P6_TA(2005)0301, "Clearing and settlement in the EU; European Parliament resolution on clearing and settlement in the European Union (2004/2185(INI))" OJ C 157E of 6 July 2006, p. 485; http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2006:157E:0485:0490:EN:PDF

ANNEX 7: Non-exhaustive overview of available glossaries concerning clearing and settlement terms

Glossary in the "Red Book" of the Committee on Payment and Settlement Systems (CPSS) regarding payment system terminology and the standard terms used in connection with payment and settlement systems.

http://www.bis.org/publ/cpss00b.htm

http://www.bis.org/publ/cpss00b.pdf?noframes=1

The ECB's "Blue Book" provides a comprehensive description of the main payment and securities settlement systems in EU Member States. It also provides a glossary (see page 437 in the edition of 2007).

http://www.ecb.int/paym/market/blue/html/index.en.html

http://www.ecb.int/pub/pdf/other/ecbbluebookea200708en.pdf

ECB occasional Paper No. 68 "The securities custody industry", by Diana Chan, Florence Fontan, Simonetta Rosati and Daniela Russo, August 2007

http://www.ecb.int/pub/pdf/scpops/ecbocp68.pdf

ANNEX 8: Description of corporate actions and background on "Record Date"

1. Corporate Actions *strictu senso*

a) Distributions

Distributions are defined as events where an issuer of a security delivers to a holder of those securities a particular benefit or resource (e.g. cash, securities, rights, etc.) and where the underlying holding which gave rise to the distribution is unchanged by the event. The key element in the distribution definition is the fact that the underlying holding and/or securities remain unchanged. The most obvious example of a distribution event is a cash dividend. In this event, the shareholder receives cash but his original shareholding remains unaffected. Other types of distribution include for example interest payments.

Distribution events can be further classified in **cash distributions** (cash dividend, interest payment), **securities distributions** (stock dividend) and **distribution in kind** (other type of benefits). Distributions can be mandatory or mandatory with options but cannot be voluntary. (This means that the event will happen, the only possible choice of the holder in a distribution with options is related to the type of benefit, he/she will get.)

b) Reorganisations

Reorganisations are defined as events where the underlying security is replaced by one or more different resource(s) (e.g. cash, securities).

Mandatory Reorganisations are events that occur, without any action required on the part of the holder of the security, when the issuer replaces all, or some, of the underlying security with one or more different resource(s).A typical example for a mandatory reorganisation without options is a stock split. In the case of a mandatory reorganisation with options, the holder of the underlying security can elect from the resources offered by the issuer.

Voluntary Reorganisations are events for which the holder of a security may choose whether or not to participate. If the holder decides not to participate, there is no change to its holdings in the underlying security. A typical example for a voluntary reorganisation is a merger or tender offer.

c) Transaction management

Transaction management is the collective set of processes to ensure that any parties involved in a transaction are assured of receiving the correct economic benefits due to them if the transaction relates to a security affected by a corporate action. Transaction management applies to both distribution and reorganisation events and covers market claims, transformations and buyer protection rules.

- **Market claims** are processes that redistribute corporate action proceeds where needed, so that the entitled party receives the benefit. This could be necessary due to the transaction itself (e.g. a fail) or positions (e.g. due to a lent position).
- **Transformations** are processes whereby a separate transaction is created to ensure that the proceeds of the corporate action reach the entitled holder, without changing the settlement details of the underlying transaction. This could be necessary in case of a corporate action involving a reorganisation of share capital.
- **Buyer protection** refers to the process by which the buyer instructs a seller to specify an election or acceptance on his behalf in case settlement happens beyond the record date and the buyer does not hold therefore the underlying securities.

2. General meetings

EuropeanIssuers (previously EALIC) had the lead on the second category, namely general meetings. Participants to the JWGGM are the ECSAs (EBF, ESBG and EACB), ECSDA, ESSF (previously European Securities Forum or ESF), EuropeanIssuers and FESE. A first draft of the standards was finalised on 30 April 2008.

General meetings (annual or extraordinary general meetings) are considered a part of Barrier 3 but as a special type of corporate event. General meetings encompas three phases namely the

1) "PRE" phase: covering all relevant actions preceding the general meeting,

2) "GM" phase: covering the meeting itself and

3) "POST" phase: covering the phase after the general meeting.

The industry decided that for the removal of the Giovannini barrier 3, it would be necessary to focus at the first phase. A further selection was made and finally three processes that were deemed the most important ones in the "PRE" (preceding the general meeting) phase were selected**:**

- **Process 1 deals with the notice from the issuer to convene the general meeting**
- **Process 2 deals with record date and entitlement, and**
- **Process 3 deals with the notification of attendance including advance voting.**

The standards on general meetings have to be compliant with the relevant legislation applicable in the European Union, especially with the Shareholders Rights Directive (SRD). In fact, the market standards can be seen as an important part of the operational implementation of the SRD.

In essence, the standards aim at introducing streamlined communication processes so as to ensure that information from the issuer can reach the shareholder - and *vice versa* - in a timely and cost efficient manner. The ultimate goal of the standards is identical to that of the SRD, namely to enhance shareholders' participation to general meetings in a cross-border investment environment. The goal is to be reached *i.a.* by removing operational barriers to the free flow of information between the issuer and the shareholder. These barriers are inherent to the system of intermediated shareholding, where a shareholder keeps his securities through book entry in a securities account with an intermediary. In a cross-border environment there is a chain of intermediaries between the issuer and the holder of bearer shares: the communication therefore has to go via the chain of intermediaries. The issuer and the shareholder depend on the intermediaries for passing on the information, so the process requires harmonised communication standards.

The standards for all 3 processes prescribe the details of the communication process: the content of the information (in line with the SRD), the parties involved, the information flow, the format of the communication, timelines, etc.

Process 1: notice to convene the general meeting: concerns the dissemination of information on an upcoming general meeting downstream, starting with the issuer and ending with the end shareholder. Process 1 is initiated by the issuer.

Process 2: entitlement: the standards are based on a record date system in accordance with the SRD. They prescribe how the voting entitlement should be determined and communicated to the end shareholder as well as the sequence of relevant dates. The information flow starts

with the (I)CSD and ends with the end shareholder. Process 1 is initiated by the (I)CSD. The issuer has no relevance here.

Process 3: notification of attendance: the main objective here is to assure the efficiency and integrity of the voting process. The notification covers in essence the following information:

- whether or not the shareholder will participate to the general meeting (identification of the shareholder and his relevant holding on the record date),
- the shareholder's chosen mode of participation (including in person, by proxy, by electronic means, by notification of attendance, etc.), and
- the shareholders votes or voting instructions (if any).

The flow starts with the end shareholder and ends with the issuer, possibly going through the chain of intermediaries. Process 3 is therefore the only process that depends entirely on the initiative of the end shareholder. If the latter does not act, nothing will happen.

Background issue: Variety of Record Dates

The term "record date" is used in two different meanings:

- either as a record date related to general meetings in order to determine who is entitled to participate and vote in the general meeting (in some cases the 'record date shareholder' will have sold the share(s) before the general meeting takes place),

- or as a record date related to clearing and settlement dates; in this case the record date is needed in order to determine the shareholder entitled to a dividend payment (e.g. on first June a dividend payable on the 30 June to shareholders on record on the 15 June is declared; after this 'record date' the share is traded 'ex-dividend').

1. The record date related to general meetings:

The current rules and regulations and market practices in relation to exercising voting rights in general meetings differ widely from country to country. The **record date** stands for the date that will be determining for the admission to the general meeting. Only persons who qualify as a shareholder on a given date will be admitted and can vote (even if he/she sells the shares between the record date and the general meeting). For instance, in the case of general meetings, recognising the concept of record date has clear advantages for ensuring a proper determination of entitlements and avoids conflicting entitlements. Even the recently adopted Directive on shareholders' rights[131] does not provide for a full harmonisation in this area of a standard common record date[132]: for instance, it does not say what positions should be looked at to determine entitlement, traded or settled, it does not mention the timing, i.e. the beginning

---

131 http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2007:184:0017:01:EN:HTML, http://europa.eu/rapid/pressReleasesAction.do?reference=IP/07/800&format=HTML&aged=0&language=EN&guiLanguage=en

132 The Directive introduces minimum standards to ensure that shareholders of companies whose shares are traded on a regulated market have a timely access to the relevant information ahead of the general meeting (GM) and simple means to vote at a distance. It also abolishes share blocking and introduces minimum standards for the rights to ask questions, put items on the GM agenda and table resolutions. The Directive allows Member States to take additional measures to facilitate further the exercise of the rights referred to in the Directive. However, European harmonisation in this Directive is a compromise and leaves Member States discretion to determine some very important areas, e.g. on setting certain dates like notice periods, record date etc. when implementing the Directive into their national legislation. Several stakeholders already raised their voices to promote a further harmonisation of these areas.

or the end of the day, it allows an exception for registered shareholders. It merely states that the record date must not be more than 30 days before the date of the general meeting to which it applies[133].

Furthermore the Directive only covers shares and not other forms of securities. The Shareholders Rights Directive aimed at abolishing the system of share blocking but did not lay down a standard uniform record date (and thus did not solve the discussion around a long or short period between record date and date of the general meeting; a long period has the benefit of giving time to intermediaries to process information but the disadvantage of an increased likelihood that the person voting will not be a shareholder by the time the meeting takes place thus requiring many updates of communications; the opposite applies regarding a short period).

Some stakeholders would appreciate a greater harmonisation across Europe and a smaller range of possible national record dates than between 30 and 0 days before the general meeting. Further harmonisation by industry standard setting of a shorter record date might however become difficult as there is no agreement among the various stakeholders and not even within a category of stakeholders on this issue. In addition it is not yet clear how the Member States will implement the Shareholders Rights Directive into national law, especially how they will use the given leeway in connection with the record date.

2. The record date related to trading and post-trading processing:

In most countries, there is a *de facto* record date, not always enshrined in the law or explicitly recognised by market practices (e.g. in Germany the "KV-Stichtag", or in Italy a record date which is calculated from the ex-date). Moreover, the record date timing is not always defined as an 'end of day date' (e.g. as in Estonia, Denmark). Although the existence of a single legal definition of the record date at EU level is – strictly speaking – not required, a common definition of the record date would greatly help in the processing of most corporate actions across borders, e.g. for the payment of dividends.

Several stakeholders would appreciate a greater harmonisation across Europe, even if, in practice, a harmonised concept can lead to different dates depending on the corporate event in question. In some countries (e.g. Greece, Austria), national legislation has been or is going to be adopted with a view to create a legal basis for determining the record date. In other countries, market participants believe that market practice alone can lead to a harmonisation of the record date and the sequence of key dates for processing corporate events.

[133] See Art. 7 (3) of the Directive. In implementing this provision, each Member State has to ensure that at least eight days elapse between the latest permissible date for the convocation of the general meeting and the record date.

ANNEX 9: Table on the state of standard setting on the 15 Giovannini Barriers in EU Member States (as of November 2008)

Barrier / Sub-phase	Fact finding	Standard setting	Endorsement	Overall progress
Barrier 1	100%	77%	75%	91%
Barrier 2/10	100%	60%	60%	70%
Barrier 3	100%	75%	0%	63%
Barrier 4/7	100%	100%	100%	100%
Barrier 5	100%	100%	100%	100%
Barrier 6	0%	0%	0%	0%
Barrier 8	100%	100%	100%	100%
Barrier 9	100%	40%	0%	35%
Barrier 11	100%	30%	0%	40%
Barrier 12	100%	30%	0%	40%
Barrier 13	100%	40%	0%	35%
Barrier 14	100%	100%	100%	100%
Barrier 15	100%	100%	100%	100%
Overall progress	**97%**	**68%**	**48%**	**69%**

ANNEX 10: Table on the state of implementation on the 15 Giovannini Barriers in EU Member States (as of November 2008)

Barrier / Member State	AT	BE	BG	CY	CZ	DK	EE	FI	FR	DE	EL	HU	IE	IT	LV
Barrier 1	67%	67%	58%	8%	0%	63%	28%	100%	67%	57%	0%	3%	25%	67%	100%
Barrier 2/10	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Barrier 3	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Barrier 4/7	100%	93%	43%	100%	0%	94%	100%	69%	100%	100%	88%	73%	100%	100%	92%
Barrier 5	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Barrier 6	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Barrier 8	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Barrier 9	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Barrier 11	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Barrier 12	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Barrier 13	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Barrier 14	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Barrier 15	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
Overall progress	**36%**	**36%**	**32%**	**29%**	**23%**	**35%**	**32%**	**38%**	**36%**	**35%**	**28%**	**27%**	**31%**	**36%**	**40%**

Barrier / Member State	LT	LU	MT	NL	PL	PT	RO	SK	SL	ES	SE	UK	EU
Barrier 1	5%	100%	15%	67%	42%	10%	2%	0%	50%	38%	80%	17%	**49%**
Barrier 2/10	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	**N/A**
Barrier 3	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0%**
Barrier 4/7	100%	100%	0%	92%	70%	100%	0%	50%	82%	72%	100%	100%	**94%**
Barrier 5	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	**100%**
Barrier 6	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0%**
Barrier 8	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	**100%**
Barrier 9	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0%**
Barrier 11	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0%**
Barrier 12	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0%**
Barrier 13	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0%**
Barrier 14	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	**100%**
Barrier 15	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	**0%**
Overall progress	**29%**	**40%**	**25%**	**36%**	**32%**	**30%**	**23%**	**26%**	**33%**	**31%**	**38%**	**30%**	**34%**