

Clearing and Settlement Impact Assessment

Chapter 1, 3 and 4

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Chapter 1: Importance of C&S

- Financial Market integration
 - Liquidity
 - Diversification
 - Competition
- Benefits
 - Lower costs for borrowers
 - Higher returns for investors
 - Better growth prospects for EU
- Promise only to be fulfilled with integrated C&S

Importance of C&S II

Empirical: financial integration more advanced in unsecured segments – where securities have to be transferred -suggesting that C&S is key for integration

- Derivatives market
- Money market
- Bond market
- Equity market

Can CESAME provide evidence on this?

Importance of C&S III

- Public policy interest in **efficient** and **safe** post-trading arrangements
- Efficiency:
 - Direct costs
 - Indirect costs
 - Opportunity costs
- Safety:
 - Legal certainty: conflict of laws
 - Counterparty creditworthiness
 - Liquidity risk
 - Operational risk

All exacerbated in cross-border context, interruption of C&S has systemic consequences

Chapter 3: Current Situation

- Current C&S
 - Monopolistic
 - Segmented along national lines, but efficient and safe
 - Low level of remote access or bilateral links
- Reasons → Giovannini barriers:
 - Technical requirements/market practice
 - Tax procedures
 - Legal certainty

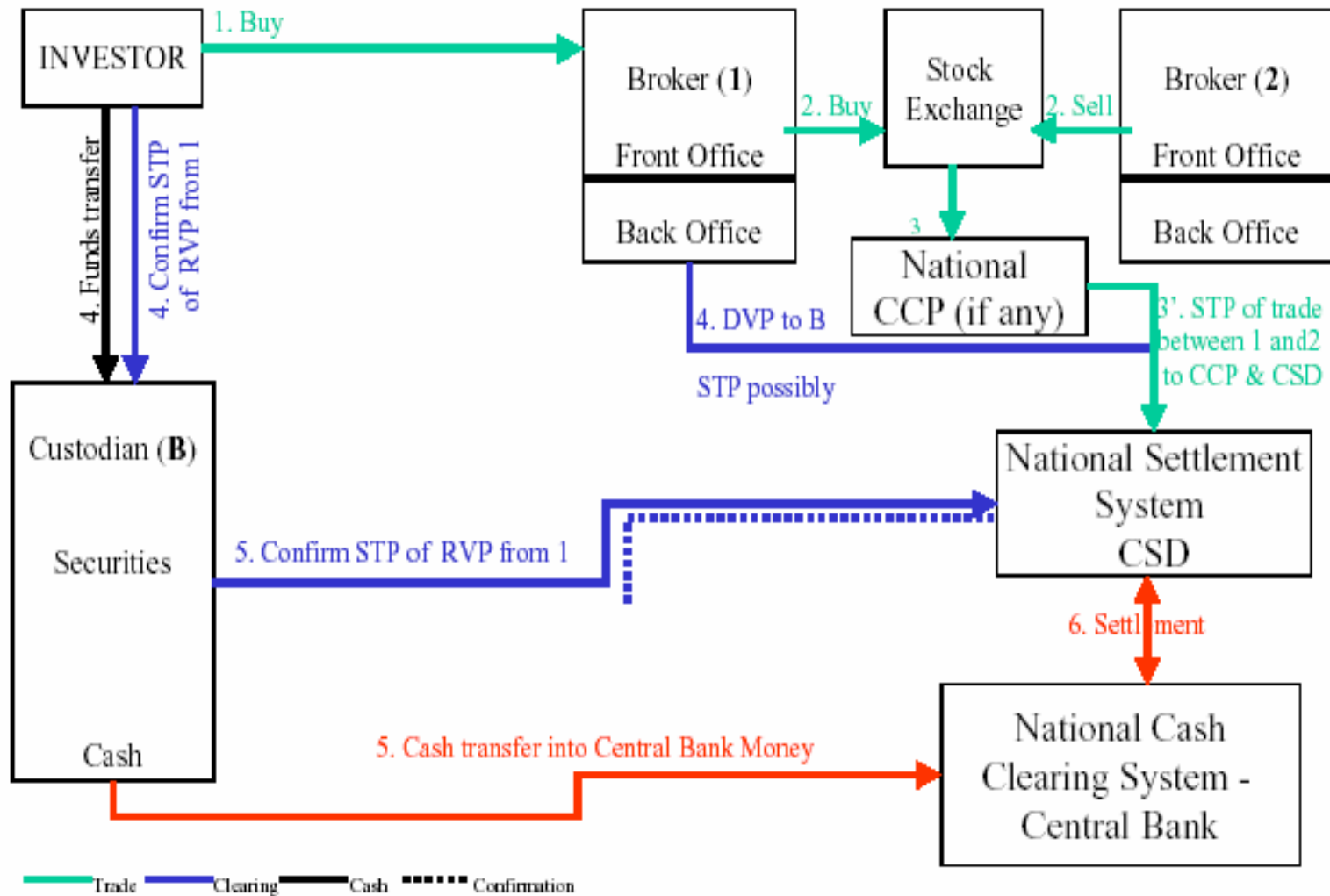
Current Situation II

- Intermediaries circumvent these barriers
 - Local agents with membership in national CSD
 - ICSDs*
 - Global custodians*
- (*Single access point to national markets)

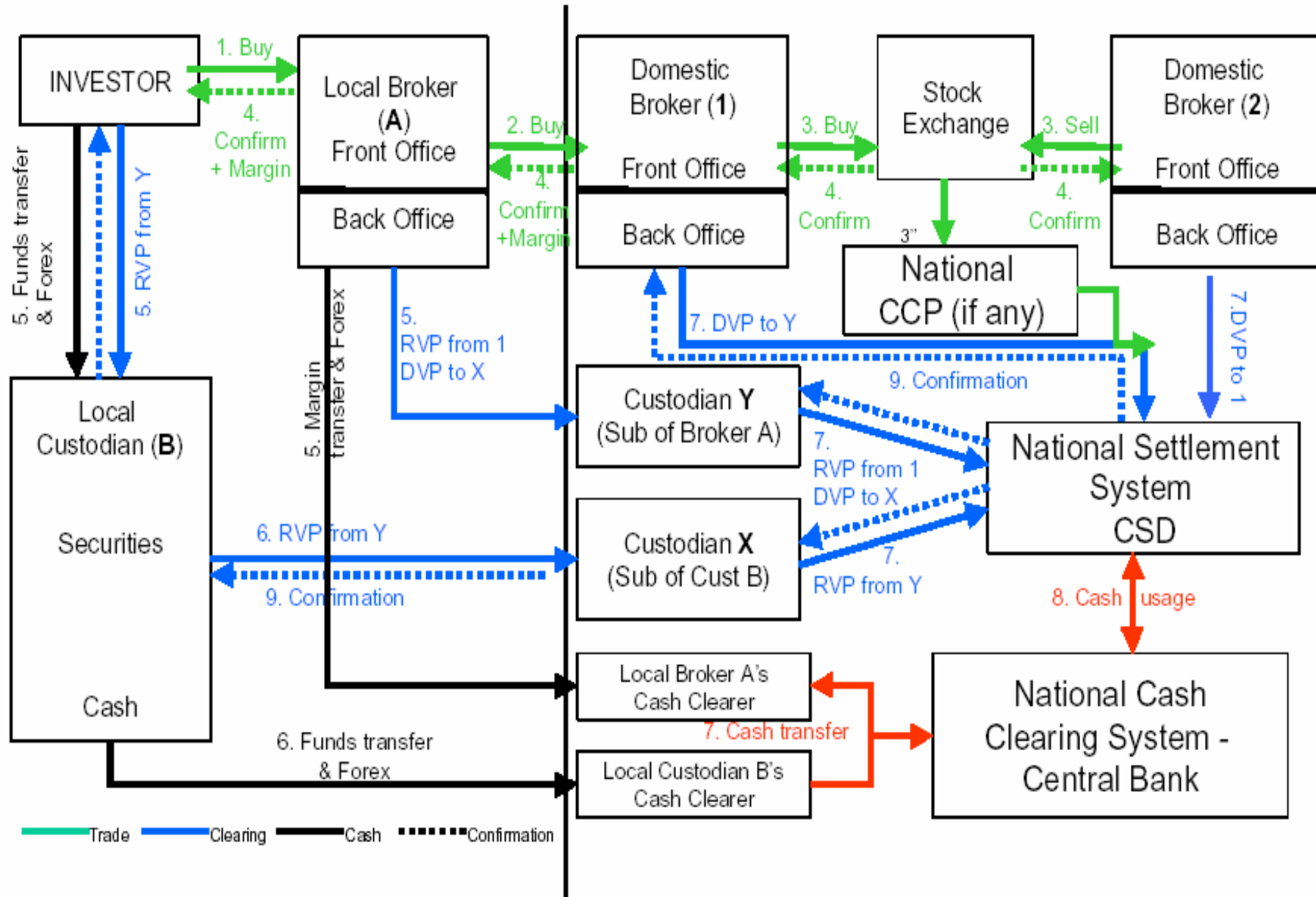
Current Situation III

- Use of intermediaries enable market to function across borders:
 - Benefits
 - Risk-diversification for investors
 - Economics of scale for C&S
 - Better resource allocation for economy as a whole
 - Costs
 - Added complexity
 - Added risk

Domestic C&S



Cross-border C&S



Current Situation IV

Market Consolidation impacting competition issues

C&S is network industry, i.e. users prefer systems that provide

- Access to the maximum number of other users and
- Access to maximum range of other securities

Current Situation V

Network industries:

- Tippy → co-existence of different providers may be unstable equilibrium
- Switching costs → users will try to link with a dominant provider in advance

Expectations of ultimate size of network
crucial for success

Current Situation VI

Public authorities have time consistency problem:

- Relevant market today is national monopolistic market
- Relevant market tomorrow might be EU market

Current Situation VII

- Cross-border consolidated C&S might find it difficult to overcome public sector Giovannini barriers (9 out of 15)
 - Barrier 2: restriction on location of C&S
 - Barrier 5: impediments to remote access
 - Barrier 9: restrictions on location of securities
 - Barrier 10: primary dealer restrictions
 - Barrier 11: restrictions on withholding agents
 - Barrier 12: Restrictions on tax collection
 - Barrier 13: absence of EU-wide framework of law
 - Barrier 14: legal treatment of netting
 - Barrier 15: conflict of laws
- Difficulties for market functioning, especially in times of market stress
 - ➔ cross-border liquidity might dry up

Current Situation VIII

A number of studies & reports contributed to growing awareness of the need to act:

- Giovannini Group
- European Association of Clearing Houses (EACH)
- CPSS / IOSCO
- Group of 30
- ECB/CESR
- Commission Communication (82 responses)

Current Situation IX

Collective action problems:

- Diverse, opposite interests
- Keeping some barriers in place might benefit one group at the expense of another
- Absence of sound legal basis, enforcement problems
- First mover has investment costs, but no legal certainty that others will follow

Chapter 4: The Commission's overall approach and objectives

- Will briefly deal with the Communication and market responses
- Restates the objectives and the interrelation of the measures proposed in the Communication

The Communication I

- Choice of proposed policy measures based on two underlying considerations:
 - EU already possesses numerous efficient and safe, albeit different, national securities clearing and settlement systems
 - Their inventiveness and excellence need to be supported and not stifled

The Communication II

- Policy measures intended to form a coherent and interdependent whole in order to foster efficiency, safety and a level playing field
- Combined effects sought so as to tackle shortcomings at different levels and from different angles
- Remain neutral so as to avoid:
 - the creation of regulatory imbalances
 - the promotion of particular models, structures and approaches

Market responses I

- Wealth of comments both on the approach and the particular measures proposed
- Diverging views on a number of issues
- The development of appropriate definitions was considered of utmost importance for any further discussion and analysis

Market responses II

- The Commission is considering the relevance and the coherence of the various suggestions in developing its future policy.
- These suggestions will feed into the discussion on the various options the impact of which are to be tested in the following chapters.

Objectives I

- General objectives
 - Promotion of an efficient and safe Clearing and Settlement framework
 - Level playing field

Objectives II

- Specific objectives
 - Integration
 - Investor protection
 - Financial stability

The objectives and the interrelation of measures

| Objectives | Specific objectives | Policies and measures | Rationale | Practical initiatives |
|--|--|---|--|--|
| <p data-bbox="260 1529 308 2072"></p> <p data-bbox="308 1529 1390 2072">Efficiency</p> <p data-bbox="938 1592 1018 1749">Level playing field</p> | <p data-bbox="260 1207 1390 1529">Integration</p> <p data-bbox="1390 1207 1514 1529">Financial stability and investor protection</p> | <p data-bbox="260 887 384 1207">Ex-post competition policy</p> | <p data-bbox="260 445 384 887">Possible abuse of dominant positions - discrimination</p> | <p data-bbox="260 168 384 445">Ex-post competition policy</p> |
| | | <p data-bbox="392 887 780 1207">Dismantling of barriers</p> | <p data-bbox="392 445 780 887">Liberalisation in the cross-border distribution of C&S services, increasing competition and driving down costs</p> | <p data-bbox="392 168 491 445">CESAME (market Barriers)</p> <p data-bbox="491 168 590 445">Legal expert group</p> <p data-bbox="590 168 673 445">Tax expert group</p> <p data-bbox="673 168 780 445">Options to be tested in RIA</p> |
| <p data-bbox="788 1529 1514 2072">Safety</p> | | <p data-bbox="788 887 1098 1207">Ex-ante competition legislation</p> | <p data-bbox="788 445 1098 887">To increase pricing and cost transparency as a means to make easier to detect possible abuses of market power, and therefore distortions of competition, by SSSs/CCPs.</p> | <p data-bbox="788 168 1098 445">Options to be tested in RIA</p> |
| | | <p data-bbox="1106 887 1514 1207">Common regulatory and supervisory framework</p> | <p data-bbox="1106 445 1514 887">Facilitate the integration of systems by avoiding that diverging treatment of similar concerns is adopted by national authorities</p> | <p data-bbox="1106 168 1514 445">Options to be tested in RIA</p> |