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CR-653 (Partial release functionality)

AMI-SeCo Meeting
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Overview

1	Background information
2	Outcome of T2S governance consultations
3	Functional clarifications
4	Elements for further AMI-SeCo discussion

Background information

- High level description of the partial release functionality (see CR-653 for full details)
  - Currently, hold/release functionality in T2S is at settlement instruction (SI) level – the entire SI is either on hold or released (i.e. allowed to settle, if resources are available)
  - With CR-653, T2S actors (e.g. custodians with omnibus accounts) could release a SI on Party Hold for a specific quantity, i.e. part of the securities remaining to be delivered
  - Cost of the CR: EUR 1,499,457.21 (development) / EUR 146,020.66 (yearly)
  - Scoped for T2S Release 3.2

- The objectives of CR-653 are:
  - to improve the settlement efficiency of T2S;
  - to minimise the impact of the CSDR penalties;
  - to reduce the operational workload compared to the current process

While these objectives may materialise if partial release is widely used, quantifying them is technically difficult.

T2S governance consultation outcome

- CRG: no functional objections, but
  - ➢ **Monte Titoli** and **Banca d'Italia** pointed out the very high development and adaptation costs for the market and the existence of alternative ways to cover the business need. They (plus **SIX**) further called for additional cost-benefit analysis

- RMSG/PMG: support for deployment in T2S release 3.2 (11/2019), from a planning perspective

- OMG: no objections on operational grounds

- AMI-SeCo written procedure:
  - ➢ **State Street, Deutsche Bank and JP Morgan** requested further analysis regarding the expected benefits from the CR while questioning its impact on current market practice. **Bank of Slovenia** also supported a more detailed cost-benefit analysis
  - ➢ **BNYMellon** and **Clearstream** explicitly expressed support for the CR (without response, other members were also deemed to support it)

- CSDs Steering Group: adopted a resolution in favour of the approval of CR-653 and its inclusion in T2S release 3.2 (November 2019)

Functional clarifications

As a receiving party is it possible to opt out from the CR introduced partial release functionality?

➢ There is no T2S specific feature for opting out of the partial release directly, however, the receiving party can ensure that any partial release request from its delivering counterparty is rejected by not allowing partial settlement in its Settlement Instructions

➢ The **delivering party** may always send a partial release request to T2S, subject to some checks (e.g. instruction must be matched, on hold, intended settlement date reached..)

➢ If the objective is to opt-out, the **receiving party** can ensure that the delivering party's partial release requests are unsuccessful. If the receipt instruction is originally flagged by the receiving party with '**NPAR - Partial settlement not allowed'** T2S will not execute the deliverer's partial release (otherwise T2S logic assumes partial settlement is allowed). Such flagging is to be done by the receiving party **for each receipt instruction (RvP)** – also possible via amendment instruction once its instruction is already in T2S.

➢ As a side-effect, it needs to be considered that those 'opted out' transactions will not become available for partial settlement during the partial settlement windows in T2S, which could affect negatively the settlement efficiency

Functional clarifications

What is the potential impact of not opting out?

➢ When the partial release request sent by the delivery party is successful or when settlement takes place, T2S *will* send a status update to both parties (delivery and receiving) with **new data** in the existing sese.024 message New data due to the CR: the **released quantity** and the **remaining on hold quantity**

➢ Furthermore, **new T2S error codes** (due to the CR) may be reported to both parties (delivery and receiving) in case the partial release process is cancelled in T2S

➢ Parties connected to T2S should analyse the impact this new information may have on their systems and business models, e.g. legacy/local systems may need to manage the new data and error codes

Elements for further AMI-SeCo discussion

- Considering the T2S governance outcome and the functional clarifications, AMI-SeCo members are invited to:
  - Confirm their support for the CR implementation.
  - Consider whether further work should be organised within the AMI-SeCo and its sub-structures in order to ensure that the T2S community reap the benefits expected from the new Partial Release functionality.

Thank you for your attention

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Annex 1 – CRG, AMI-SeCo, CSG comments (1/4)

Comment number	Date of comment	Respondent	Comment
1	15/05/2018	NBB-SSS (CRG)	Agreed
2	15/05/2018	Monte Titoli (CRG)	As anticipated in the last CRG conference call Monte Titoli will not support the development of the CR 653 for the following reasons: i) the CR 653 has a very high financial impact and returns for Italian community are very low compared the required investment. ii) The CR 653, unlike other CRs, won't have a neutral impact on CSD/T2S participants infrastructure. Regardless from benefits, all T2S stakeholder in the securities side will be called to update the software to manage the new functionalities. In the past other CRs even with low or null benefits at least didn't required developments and tests. iii) Several features are available in T2S to control settlement risks including the drawing in the mass. iv) Other CRs with a greater priority (e.g. 654) are on hold for the reason that some csds are not considering to receive benefit and wouldn't share costs, the same consideration can be raised for the CR653.
3	15/05/2018	Banca d'Italia (CRG)	As anticipated during the CRG telco held 7 May, Banca d'Italia does not support the inclusion of CR 653 in the Release 3.2 for the following reasons: i) CR 653 has a very high financial impact. When a CR is flagged as "common" and has a very high financial impact, it should be supported by all CSDs; otherwise, it should be put on hold, as it recently happened for CR 654 (in this case, what is more, the CR would have allowed to overcome a serious issue: the lack of harmonization when CSDs calculate settlement penalties in T2S); ii) Alternative solutions are already available in the platform to meet the same business needs addressed through CR 653, namely a more extensive usage of segregated securities accounts instead of omnibus accounts; iii) T2S users are already concerned about the expected increase of the T2S fees. Before deploying expensive CRs, the Eurosystem should evaluate the impact on cost recovery and carry out a cost-benefit analysis for the whole T2S community.
4	15/05/2018	Clearstream (CRG)	We recommend approval of the CR, and inclusion into T2S R3.2.
5	15/05/2018	Euroclear (CRG)	We confirm our approval of CR 653 and the strong support of our markets for its implementation We agree with the proposed recommendation to the steering level to approve the implementation of the CR for release 3.2
6	15/05/2018	SIX SIS (CRG)	I hereby confirm that SIX recommends the approval of CR-653 and its inclusion into R3.2 to the Steering Level with the remark that it could be beneficial for similar cases to perform cost benefit analysis

Annex 1 – CRG, AMI-SeCo, CSG comments (2/4)

Comment number	Date of comment	Respondent	Comment
7	22/05/2018	State Street (AMI-SeCo)	As a custodian bank managing client assets, we would typically set up a CSD account with an NPAR flag, and allow clients in certain cases to send their instructions to us to flag that that they wish to make the transaction eligible for partial settlement. In most cases however, clients prefer to disable partial settlement. As a result, this functionality would have very limited use to the institutional business in the segment global custodians support (Asset manager, insurance firms ie buy side) – typically a broker would wish to deliver assets partially, but the buy side would not wish to receive partials therefore partial settlement would not happen. Given the recent pricing discussions around T2S, I would advise against building this functionality as it seems to me that the functionality is not widely beneficial and would require each firm to build additional logic to support it (whilst a cancel & reinstruct logic is common market practice and could be supported by most clients already today if they wish to do so). So my main concern with this change request is that it would require a significant logic change for many participants who currently would use a cancel & reinstruct process (and thus may not lead to higher settlement efficiency since only a subset of T2S users is likely to make use of it). I noted the comments that 2 CRG members expressed their opinion that additional cost benefit analysis would needed: it would be useful to understand how many T2S accounts are set up with no partial (out of total – and how much transactions those accounts represents), and how many partial indicators are sent on transactions against accounts with NPAR vs total PART delivery instruction, and why this change causes additional running costs (and if we can see how all the CRs that led to real functional changes have accumulated so far, both in terms of running and change costs), and if we think this CR would lead to additional transaction volume (i.e. what's the payback time .. we expect XX more partial settlement priced at x).

Annex 1 – CRG, AMI-SeCo, CSG comments (3/4)

Comment number	Date of comment	Respondent	Comment
8	22/05/2018	Deutsche Bank (AMI-SeCo)	In principle we support the desired outcome of CR 653, i.e. increased settlement efficiency in omnibus accounts. This will become even more important with the introduction of the CSDR penalty regime. However, from an operational perspective the current proposal of the CR requires significant adaptations in the systems of market participants throughout the value chain (e.g. end client - … – Global Custodian – Local Custodian – CSD - T2S) in order to build additional logic to integrate the partial release functionality in the existing automated disposition logic. Within this context the benefit of this CR needs to be further assessed on all levels of the value chain compared to the already existing market practice, i.e. cancellation and re-instruction with the available quantity. The current process is viewed as cumbersome, because the original end clients must initiate a cancel / new in order to reshape the delivery into 2 parts – This reshaping must be agreed by both parties and communicated down the chain to the CSD / T2S. From our perspective the future process is effectively no different. In general, custodians act upon client' instructions. The CSD participant/ custodian cannot initiate the partial release process as the custodian may not know the available stock for the end client within the omnibus account of the custodian' client, i.e. the global custodian/ GC. Therefore the GC would have to instruct the CSD participant on the initiation of the partial release process based on their understanding of if their client has the available stock. Depending on their client, the GC may also need to pass this decision up the value chain. Ultimately, the partial release still needs to be initiated by the participant with the direct view of the end client position and then processed by each level of the value chain down to the CSD level. Even if the end client indicates (via this new process) that they wish to do a partial release, if their counterparty has instructed with NPAR, no partial settlement will occur. To check if a partial is possible, the end client would still need to speak to their counterparty to see if the instruction on the other side is set to allow partial settlement. Currently, the buy side – the primary user of the omnibus account structure - usually does not want to receive partials as opposed to brokers who typically would wish to deliver securities partially. Without a change of the buy side behaviour to increasingly use partial release functionality e.g. in light of the CSDR penalty regime, this CR may not result in greater settlement efficiency of omnibus accounts and hence the investment costs on all levels of the value chain and the additional T2S costs for this CR may not be justified. Given the recent T2S pricing discussions, we would advise to make sure the process is going to bring real value in process and efficiency. With respect to this we would propose to set up a task force comprising representatives from all levels of the settlement chain to analyse all implications and the future market demand. From our point of view all participants require further understanding on the operational impact to the entire value chain (where there are omnibus accounts at various levels), and whether the new process is in fact any more efficient or less cumbersome than the current one.

Annex 1 – CRG, AMI-SeCo, CSG comments (4/4)

Comment number	Date of comment	Respondent	Comment
9	24/05/2018	Bank of Slovenia (AMI-SeCo)	Based on the estimation of (high) development and operational costs we are hesitant to support the proposed CR without additional cost-benefit analysis conducted. Furthermore, as the functionality will not be used by all NCBs/CSDs, we would prefer the CR to be reclassified as a specific CR, i. e. paid by the requestor and the (optional) users of the functionality, rather than as a common change request, paid by all.
10	24/05/2018	JP Morgan (AMI-SeCo)	We have also discussed the proposed changes and would be supportive of a task-force to look into more details on the cost-benefit of this CR for the wider T2S user community.
11	24/05/2018	Clearstream (AMI-SeCo)	We recommend approval of the CR, and inclusion into T2S R3.2.
12	24/05/2018	BNY Mellon (AMI-SeCo)	BNY Mellon supports the majority view of the CRG. The CR is desirable in itself, and will become more desirable, if not mandatory, with the future CSDR settlement discipline requirements.
13	24/05/2018	Monte Titoli (CSG)	As already stated in the CRG, MT is not in favor of recommending CR653 since: 1) its overall impact is not neutral since it will imply changes to systems and messages also for those Actors (CSDs and Participants) not using it 2) its potential benefits are not justified by the significant adaptation costs not only for T2S but also for the Market 3) alternative solutions are already available in the platform to meet the same business need, namely a more extensive usage of segregated securities accounts instead of omnibus accounts Consequently we would like to propose a) an additional cost-benefit analysis in light of the low benefits expected for the T2S community and b) an assessment of alternative ways for managing such business needs