ESCB-CESR STANDARDS FOR SECURITIES CLEARING AND SETTLEMENT SYSTEMS IN THE EUROPEAN UNION

General comments

The Finnish Bankers' Association (FBA) considers it pivotal for the development and competitiveness of the European securities market that the operational framework for the securities clearing and settlement system is sufficiently uniform. With uniform standards, i.a. the stability and transparency of the markets can be improved. However, when establishing the framework, one should ensure that unjustified limitations not be imposed for market-based development of markets and systems.

In the proposed draft for standards, custodian banks have in many respects been exposed to similar requirements as have for instance central securities depositories (CSDs). The FBA does not find this to be an appropriate starting point. As a matter of principle, the same standards that apply to those who maintain the systems cannot be applied to those who use it. Custodian banks are the users of the systems, not the maintainers.

The FBA wishes also to point out that the application of several requirements in the standard imposed on custodian banks is tied to the status of a dominant position in the local market. Criteria related to the local market only may, in the integrated European markets, distort the competition between the companies providing custodian services.

In the draft, the concept of systemically important systems is tied to percentage limits for market shares. The FBA does not consider this as an appropriate starting point. It would result in different obligations for different service providers depending on their being just above or below the set limit. It would also affect the competitive position of service providers. The aim should be to apply a purely functional definition providing similar obligations to all service providers in the same business irrelevant of their size.

Standard specific comments

Standard 3

In item 6 of the explanatory part of the standard, it is proposed that, i.a. CSDs should harmonise their operating days and hours using the TARGET operating hours as the benchmark. The harmonisation of operating times is in itself a justified principle. However, when harmonising operating times, the costs should be weighted against the benefits. From this point of view the harmonisation of operating days might - at least in the short term - be a difficult goal to achieve. Instead, the harmonisation of operating hours should be carried out as soon as possible.

Standard 5

In the standard for securities lending, the need to remove barriers inhibiting securities lending is emphasised. Indeed, it is essential for the functioning of the securities lending markets that national barriers , such as those related to taxation, be removed. The FBA

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suggests that an explicit statement concerning the removal of barriers related to taxation be added to the explanatory part of the standard.

In several points, the draft emphasises the benefits of centralised securities lending system, e.g. in reducing settlement failure. The FBA does not believe that the benefits of establishing centralised securities lending facilities are as significant as the draft implies. Competition is also in securities lending the best way to increase efficiency and hence promote product development and reduce costs. Decentralised securities lending may be efficient from the markets' point of view, as well. Consequently, we think that the explanatory part of the standard should be modified and objectively describe the advantages and disadvantages of a centralised versus a decentralised securities lending arrangement respectively.

Standard 6

The FBA finds it important that CSDs endeavour to avoid risk taking as suggested in the standard. The resources of CSDs should not be directed towards activities competing with the users of their services or to producing extra services that increase their risks. CSDs should stick to providing basic services necessary for the functioning of the market.

Standard 9

The standard stresses that systemically important systems extending credit to participants should in principle always fully collateralise their credit exposures. Uncollateralised credit should, in accordance with the explanatory part of the standard, be limited only to specifically determined situations. The FBA does not find this at all justified from a custodian operations point of view.

Credit risk management lies at the heart of banks' operations, and customer risk relating to custodian operations cannot be distinguished from banks' overall management of customer risk. Banks assess their customer risks as a whole. Here, reference can also be made to the new Basel II capital requirements, which emphasise banks' responsibility of managing credit risk. There are no grounds to introduce specific requirements for credit risk management relating to custodian operations. If implemented, the standard would unjustifiably impair the operational prerequisites of custodian banks and could lead to corporate restructuring due to regulation, and thereby to overall inefficiency.

Standard 11

The standard regulates the management of operational risk. In this respect, its relationship to the Basel recommendations remains unclear. Contingency plans etc. are already part of normal operations.

In item 6 of the explanatory part of the standard there is a requirement implying that an entity should outsource clearing and settlement operations or functions to third parties only after prior approval of the relevant competent authorities. This proposal could unnecessarily restrict business development. A notification should be sufficient.

Standard 13

The standard would apply to custodians with a dominant position in a specific market. The FBA does not consider it justified that different custodian banks should be subjected to different requirements in a local market. Even though a bank has a significant position in a particular market, it may be insignificant at the European level. In this case market-specific requirements would lead to distortions in the local market. Possible problems arising from a dominant position can also be effectively dealt with by the competition authorities and competition legislation.

Standard 14

The standard proposes that the principle of open access be applied, in addition to CDSs, also to custodian banks with a dominant position.

CSDs are central for the maintenance of the basic infrastructure of the securities market. For the smooth and undisturbed functioning of the market, open access to CSDs is, indeed, essential. All participants fulfilling the criteria set out in the standard should have open access to the services of CSDs. A possible decision to deny such access should be substantiated and given in writing. The decision ought to be submittable for examination of a third party. The reason for denial could only be based on the management of system risk.

However, the principle of open access cannot be applied to custodian banks. Custody services are only a part of the services offered to customers and of the overall customer risk. Consequently, the pricing of the services also varies from customer to customer. If imposed in the proposed form, the standard would probably lead to unnecessary standardisation of services, and to extensive distortion of competition in the local market, as the requirement of open access and the ensuing obligations would only apply to some of the banks engaged in custodian operations.

Standard 17

The standard proposes that the requirements of transparency be extended to custodian banks with a dominant position. In the market with true competition between custodian banks, the proposal would remarkably distort the competition as it would only apply to part of the service providers.

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