SIX SECURITIES SERVICES

Unit G2 - Financial Markets Infrastructure
European Commission
DG Internal Market & Services
Rue de Spa/Spastraat 2
1000 Brussels
Belgium
By e-mail to: markt-consultation-csd@ec.europa.eu

SIX Securities Services
Brandschenkestrasse 47
CH-8002 Zurich

Mailing address:
P.O. Box 1758
CH-8021 Zurich

T +41 44 288 4511
F +41 44 288 4512
www.six-securities-services.com

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PUBLIC CONSULTATION ON CSDs AND THE HARMONISATION OF CERTAIN ASPECTS OF SECURITIES SETTLEMENT

Dear Sirs

SIX SIS AG (SIX SIS), with address details as above, is writing to you in response to the above consultation. We thank the Commission services for launching the consultation on this important issue at this time and for the opportunity of responding to it. We are not registered with the Commission as an "interest representative". We are replying as (i) both an issuer and investor CSD, (ii) as the operator of the securities settlement system SECOM, and (iii) as a provider of a wide range of CSD services, including safekeeping, custody and banking-type services. We are also active members of ECSDA, whose position we also support.

Why are SIX SIS interested?

SIX SIS offer, as a CSD, settlement, custody and asset servicing to clients throughout Europe, including the Member States of the European Union. We are both an Issuer and an Investor CSD. As part of the SIX Group (see below), we are strong promoters of an open market, encouraging links and access throughout our open architecture model. SIX Swiss Exchange is one of the top 5 largest regulated equity markets within Europe and we operate the largest warrants and structured products market within Europe – Scoach, as well as the derivatives exchange, Eurex, both as joint ventures. In the clearing segment, SIX x-clear AG is active as a CCP service provider across Europe, with SIX x-clear AG and LCH.Clearnet Ltd having first extended an interoperable service to the London Stock Exchange in 2008. We believe that the Commission should not only focus on EU securities traded, cleared and settled in the EU, but also on non-EU securities traded, cleared and settled within the EU borders.

About the SIX Group

SIX SIS are part of the SIX Group which operates Switzerland's financial market infrastructure and offers on a global scale comprehensive services in the areas of securities trading, clearing and settlement, under the brand of SIX Securities Services, as well as financial information and payment transactions. The company is owned by its users (150 Swiss and foreign banks) and, with its workforce of approximately 3,700 employees and presence in 23 countries, generates annual revenues of the equivalent of approximately 1.3 billion Swiss Francs.

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Executive Summary and Overall Approach

SIX SIS supports the reply of ECSDA to the public consultation dated 1 March to the Commission. We support ECSDA in their emphasis that the main focus of the legislation should be safety and soundness for a CSD, and in particular with the Commission's objective of establishing a harmonised authorisation regime for CSDs. We note, however, that during the recent financial crisis market infrastructures proved themselves to be very resilient. EU legislation should be mindful of the need to ensure that market infrastructures do not lose the capacity to support the official sector and the market in general, and indeed to react dynamically to the demands of the market, e.g. through product innovation. The issues we would like to bring to your attention, in addition, (these are all amplified in our detailed responses contained in the accompanying document and Appendix), are as follows:

(i) treatment of Third Country CSDs, where specific provision under the authorization and supervision requirements for these entities should be made;
(ii) the mitigation of financial risks including collaterisation of credit exposures;
(iii) the use of commercial bank money, which should continue to be accorded its status in the post-trading value chain;
(iv) segregation of assets, where investor protection can be achieved through other means;
(v) settlement discipline, where we do not favour harmonisation at the EU level; and
(vi) mandating a settlement cycle, where progress is being made, which should be left to market forces.

Following our meeting with the Commission on 3 February, we have included additional material in our response on the inclusion of Third Country CSDs in the scope of legislation. We are still researching, the figures on cross-border settlement flows, and producing a comparative table on the lien system mentioned in our answer to question 41, and will submit these to the Commission in the forthcoming weeks.

I We hope these remarks are of help. If you require any further information at this stage, may I suggest that our Head of Market Policy, Alex Merriman (contact: Alexander.Merriman@six-group.com or on +41 58 399 4583) would be pleased to assist.

Yours sincerely

SIX Securities Services

Thomas Zeeb
Chief Executive Officer

Alex Merriman
Head of Market Policy

SIX SECURITIES SERVICES

SIX SIS RESPONSE TO CONSULTATION ON CSDs AND HARMONISATION OF CERTAIN ASPECTS OF SETTLEMENT IN THE EU

[SIX Securities Services cover the clearing, settlement and custody arms of the SIX Group. Reference is made in our replies to SIX SIS, the CSD of the Group]

Part 1: Appropriate regulatory framework for CSDs

1. SCOPE AND DEFINITIONS

1. What is your opinion on a functional definition of CSDs?

If a functional approach is to be adopted, then we believe that this is appropriate. We do not believe that, through EU legislation, a new and separate category of "CSD" needs to be created. Please also see our response to question 5.

2. What is your opinion on the scope of the possible legislation and providing for any exemptions (such as for central banks, government debt management offices, transfer agents for UCITS, registrars, account operators)?

As noted in our letter to the Commission of 6th January, we believe that there are pro's and con's for the exemption of central banks. For the other entities mentioned, such as standalone registrars, they could be excluded from the scope of the legislation.

3. What is your opinion on the above description of the core functions of a CSD?

We find them acceptable.

4. Which core functions should an entity perform at a minimum in order to be qualified as a CSD?

The undertaking of a minimum of two out of the three core functions strikes us as a reasonable compromise to qualify as a CSD, taking into account the diversity of core functionality among CSDs in Europe. It is essential, however, that in order to qualify as a CSD, this entity undertakes the settlement and safekeeping functions.

5. Should the definition of securities settlement systems be reviewed?

No. We believe that the current definition in the Settlement Finality Directive (as amended in 2009) still has merit and serves us well. The operation of a securities settlement system conveys upon the operator a distinct and unique personality. This is also important in terms of identifying systemically important payment and settlement systems.

6. What is your opinion of the above description of ancillary services of a CSD? Is the list above comprehensive? Do you see particular issues as to including one or several of them?

We believe that they are broadly acceptable and comprehensive as currently stated. But we would not wish to see this list diluted and we suggest that the following ancillary services should also be included:

(i) Triparty collateral management services not related to settlement, but to other activities undertaken by CSD participants; and
(ii) repo services.

EU legislation should make it clear, however, that other categories of services can be offered by CSDs and that CSDs are not prevented from offering a wide range of CSD services throughout the EU. We suggest in this regard that a comprehensive list of services is included in the Legislation as an Annex. So broadly, we support a "long" list of core and ancillary services. In particular, CSDs do not want to be in a position where they will have to approach either their Home or Host supervisors each time they require to offer a new product.

2. AUTHORISATION AND ONGOING SUPERVISION OF CSDS

7. According to you, could the above mentioned cases impact a future regime of authorisation and supervision? Yes? No? No opinion? Please explain why. Are there other cases which could have an influence on a future regime of authorisation and supervision?

The Commission's list is comprehensive. Particularly important are the ability to undertake cross-border business through links and, in future, via branching as well (as CSDs currently have to maintain separate legal entities in each EU jurisdiction). We also thank the Commission for taking into account the earlier comments from ECSDA about the need for a relatively straightforward authorisation and supervision regime for CSDs; nonetheless respecting the involvement of Home and Host supervisors, on a case-by-case basis.

We comment, however, that the Commission's framework described in paragraph 2.2 does not explicitly cover the provision of services in and out of the EU by CSDs from Third Countries such as SIX SIS. We believe that the legislation should make allowance for this and we pick up this point at various junctures in our response. We add that Swiss law already enables CSDs from other jurisdictions to offer services on its territory. Further justification for the inclusion of Third Country CSDs in the forthcoming legislation is outlined in Appendix I.

8. What other elements should be submitted as part of the initial application procedure by a CSD?

No further comment on this.

9. According to you should the authorisation procedure of a CSD be distinct from the designation and notification procedure under Art. 10 of the SFD? Yes? No? No opinion? Please explain why.

The two processes should be kept distinct, but designation should be a core part of what constitutes a CSD. However, it strikes us that this distinction is valid only for established and currently authorised CSDs that are designated by national competent authorities. This says nothing of the situation of an entity that might be authorised, but not have SFD designation (e.g. because the nature of its business is not considered systemic). ECSDA has stressed in its replies to the Commission on the need for a level playing field, so that new (CSD) entrants to the market do not face additional hurdles to establishment and operation.

10. What is your view on establishing a register for CSDs?

We have no objection to this being kept by ESMA, as this is consistent with responsibilities in other financial sector services. The register should also include Third Country CSDs which are authorized to provide services in the EU.

11. What is your view on the above proposal for a temporary grandfathering rule for existing CSDs?

We agree that this is desirable and consistent with the similar provisions in EMIR. Where CSDs from Third Countries provide services in the EU, they should also be grandfathered, provided that they have been appropriately authorised, and are supervised, on an equivalent basis by their Home State authority. In Appendix I, we suggest the necessary conditions for equivalence.

12. According to you, does the above approach, concerning capital requirements, suit the diversity of CSDs? Yes? No? No opinion? Please explain why.

Yes, given the diversity of business undertaken by CSDs in Europe, there needs to be an element of flexibility in the capital adequacy regime, addressing only those risks which a CSD is exposed to. In relation to the offering of banking-type services, a CRD-lite regime might be contemplated. In other words, not all aspects of the CRD (for instance trading book requirements) need apply to CSDs which already have banking-type licences. Care should also be taken to ensure that CSDs offering banking-type services are not subject to two sets of conflicting measures in the Regulation and the CRD, for instance in relation to operational risk.

13. According to you, should the competent authorities have the above mentioned powers? Yes? No? No opinion? Please explain why.

Yes. This list of powers is comprehensive. It seems essential to us that competent authorities should in particular be enabled to exchange information about CSDs offering services in their territory especially given the essential role played by CSDs in the financial market system, and particularly their contribution in mitigating systemic and other contagion risks. As CSDs offer services to the entire market place, it should be made clear that their core services should not fall under any outsourcing regulation, so as to not to limit the independence of the CSD.

14. Would a special purpose banking license be appropriate for "banking type services"?

Please see our answer to question 12 on how a CRD-type regime might apply in this respect.

15. Which of these three passporting options would you support? Full passporting? Limited passporting? Opt out regime? Please explain why.

We support a full passporting regime. In other words, all those (core and ancillary) services, including banking-type services, for which the CSD has been authorized to provide in its home state can be passported into the rest of the EU. This also tallies with our remark in answer to Question 6 on the offering of future services. In our view, a full passporting regime s would be the simplest way of ensuring a level playing field in the EU, and obviate the need for CSDs to obtain permissions each time. Such a regime should be extended to CSDs from Third Countries.

3. ACCESS AND INTEROPERABILITY

16. What is your opinion about granting a right for market participants to access the CSD of their choice?

We agree that participants should have choice, and believe that users already have free access to most EU CSDs, though we wonder whether the relevant MiFID provisions (Articles 34 and 46) need to be made more explicit in this respect. However, this should not prejudice the ability of the CSD to ensure that the participant fulfils all the conditions necessary to become an account holder at the CSD.

17. What is your opinion on the abolition of restrictions of access between issuers and CSDs?

We broadly support the removal of Barrier 9. However, we would point out that this could lead to some further uncertainties which would need to be tackled, for instance: (i) which national ISIN would apply, that of the issuing company or the CSD; (ii) which governing corporate law would apply to the issue in question, and (iii) general aspects such as reconciliation of the issue.

18. According to you, should the removal of Barrier 9 be without prejudice to corporate law? Yes? No? No opinion? Please explain why.

EU legislation could have a catalyzing effect to give choice to issuers, and facilitating the wider issuance, listing and holding of shares, through the removal of barriers in domestic corporate law. It appears from the consultative paper, that the Commission believes that national corporate law does play a role in channeling an issue into the domestic CSD. We wonder therefore whether a further amendment to the Prospectus Directive might not be the place to undertake this.

19. How could the integrity of an issue be ensured in the case of a split of an issue?

We are not against the idea of splitting issues and indeed multilateral issues already exist, for instance bond issues between Euroclear and Clearstream. As the Commission points out, this

can lead to some complex issues in the cross-border settlement of these securities, for instance in realignment, or reconciliation where more than one registrar is required. The key issue from our perspective is that where an issue is split, and is assigned a unique identifier, such as an ISIN number, or is badged as a Global Certificate, then that identity should be valid in more than one market. In other words, it should be just a matter for CSDs to handle split issues via routine processes such as *nostro* and *vostro* accounts.

20. What is your opinion on granting a CSD access rights to other CSDs and what should their scope be?

We believe that this segment of the Commission's paper is over-engineered and over-complicated. We notably do not think that those requirements identified in bullets numbered one on a reinforced legal assessment, and six – harmonization of account structures, should be pursued. CSD to CSD links are already very common and arise through a business case. For instance, SIX SIS already enjoys links with Euroclear, London and Brussels (ESES), Clearstream Frankfurt and Luxembourg, VP Denmark, OeKB, Monte Titoli and Keler. In addition, technical interfaces such as Link-up Markets have facilitated the development of direct cross-border access between CSDs, both inside and outside the EU. Where access has been turned down, it has usually occurred because the requesting CSD has not met the admission criteria. We do not believe that EU legislation should harmonise in detail proposed aspects such as securities accounts structures or dictate a common set of access requirements: the latter are already laid down in relevant (e.g. CPSS-IOSCO) recommendations. Providing such access rights in legislation might also have the unintended consequence of limiting CSD access only to CSDs, which might discriminate against other market participants that wish to open accounts at the CSD. We would welcome more clarity from the Commission of the type of problem they believe they are trying to fix.

21. What is your opinion on a CCP's right of access to a CSD?

A CCP should have unlimited access to any CSD and therefore should be free to choose the provider of its settlement services in the same way as trading venues appear to be able to choose their CCP. We stress here the advantage of the SIX Group's open architecture model, where we can offer clearing and settlement services to a range of trading venues across the EU.

22. What is your opinion on access conditions by trading venues to CSDs? Should MiFID be complemented and clarified? Should requirements be introduced for access by MTFs and regulated markets to CSDs? Under what conditions?

We believe that access should be allowed. Once the review of MiFID has put all trading venues (recognized markets, MTFs, crossing networks and systematic internalisers) on a parallel footing in terms of regulatory and other requirements, then it will be possible to ensure that the conditions for access to CSDs are similarly even.

23. According to you, should a CSD have a right to access transactions feeds? Yes? No? No opinion? Please explain why.

We do not believe that this should be an automatic right, but should be permitted to the extent that it is needed by a CSD to perform its settlement. CSDs current compete against each other for trading feeds and this is a continuingly desirable feature of the market.. In our experience, granting access to multiple CSDs without a business case does not make sense as implementing such a model increases legal and technical complexity and therefore costs to the execution venue and to the CCP. The latter would need to support settlement of the same product across multiple locations necessitating the use of additional funding to operate accounts and cross border costs to transfer and maintain position to facilitate orderly settlement. One of our subsidiaries SWX Europe Limited used to offer choice of settlement location for Swiss, UK and Pan European Products. It was possible to settle in SIX SIS, Euroclear UK & Ireland (formerly Crest) and Euroclear Bank. This choice has associated maintenance costs, as suggested above, and was never used in any material way by the participants in the 6 years the choice existed.

24. What kind of access rights would a CSD need to effectively compete with incumbent providers of CSD services? Should such access be defined in detail?

Please see our answer to question 9. Initial authorization conditions should be the same for incumbents and new entrants.

4. PRUDENTIAL REQUIREMENTS

25. Do you think that the legal framework applicable to the operations performed by CSDs needs to be further strengthened?

No. Please also see our response to question 5.

26. In particular should all settlement systems operated by CSDs be subject to an obligation of designation and notification?

We believe that this is already being done. For instance both our securities settlement system, SECOM, and the inter-bank payment system linked to it, SIC, are designated and overseen by the Swiss National Bank. It should be left up to individual national competent authorities/overseers of payment and settlement systems to decide which system, because of local (or cross-border) characteristics, qualifies for designation. There is enough advice (e.g. through CPSS-IOSCO principles and CESR-ESCB recommendations) to ensure that a consistent approach is adopted throughout the EU and beyond. Please also see our remark in the covering letter about the need for EU legislation to safeguard the ability of CSDs to support the official sector and innovate.

27. What do you think of the general elements of these requirements, particularly with respect to the obligation for CSDs to facilitate securities lending and the obligation of counterparties to securities loans to put in place adequate risk controls?

We do not think that the legislation should mandate CSDs to be active in this area, as securities lending tends to be an activity conducted between market participants, and it should be up to the market whether the CSD is requested to offer this service. In addition, it rather depends on the type of settlement optimization run through the SSS. This function is not supported by a number of CSDs, for perfectly understandable reasons such as the thinness of the market for such products.

From our perspective, SIX SIS supports a fail driven securities lending & borrowing ("SLB") facility on settlement date as principal. Loans to borrowers are only granted on a collateralized basis. But this collateral cannot be used to collateralize the lenders to SIX SIS. This generates a limitation on the loan volume (clean credit lines) as well as the access to lenders and its positions. SIX SIS being an agent lender would not practicable as there is no SLB market for agents in Switzerland. In addition, a SLB facility linked to naked short selling does not yet exist. This would require blocking positions in the lending pool already at trade date and consequently short selling would be allowable only if the position is successfully blocked and confirmed.

28. What do you think about the requirement for issuers to pass their securities through a CSD into a book entry form? If such an obligation were considered, which securities should it concern? Only listed securities? All securities with an ISIN code? Only equities? Eligibility approach?

We support the passing through of securities in book entry form. The Netherlands is the latest EU country to announce the abolition of certificated securities by end-2013, and in general a fully dematerialized system is to be encouraged (on grounds of efficiency, safety and a level playing field for investors). We believe that the Commission might continue to catalyze this trend by introducing a requirement that all securities being introduced to a listed market in the EU (either as a new issue above a certain threshold – or a further release of an existing listed security) be in book entry form. This should certainly apply to equities in the first instance, and markets should be free to add other categories of assets, where these are already in fully dematerialized form (structured products in the case of Switzerland).

29. What is your opinion with respect to grandfathering?

We are not against it. Each CSD/system should ensure that it has procedures in place to deal with certificated securities.

30. What do you think about the requirements above for DVP? Do you see any issues in respect of the different DVP models?

We undertake DvP settlement in real-time settlement (please also see our answer to question 41). Different models of DvP can be accommodated through differential cut-off times. We were unclear about the Commission's definition that transfer of cash and securities might not occur simultaneously, thus implying that DvP does not occur.

31. What are your particular views on the grandfathering principle coupled with the

requirement for the introduction of a guarantee fund?

We would have no objection to a grandfathering period to enable the non-DvP CSDs to catch up, subject to the conditions mentioned by the Commission.

32. What do you think about a preference of settlement in central bank money? Should such a preference be applied equally to all types of securities?

We can live with a formulation which does not expressly prohibit the use of commercial bank money, such as the Commission's suggestion of "whenever practicable and feasible" for central bank money. We do not agree with the ECB's view (as expressed in its Opinion in EMIR dated 13th January) that central bank money should be used at all times in the post-trading environment. As explained in our letter of 6th January, and through the position paper submitted by ECSDA, we stressed that the use of commercial bank money is necessary for a variety of situations, particularly cross-border corporate action transactions, when central bank money may not be available. To do otherwise will severely restrict the availability of liquidity for infrastructure and participant alike. Paradoxically, there are some markets (see answer to question 34) where there is no routine use of central bank money for settlement, and where CSDs should have the right to access this. In our view, these parts of the system should be encouraged to develop this functionality, while maintaining access to commercial bank money.

33. Do you think that the principles outlined above could be transposed in future legislation?

We agree that these principles are fit for transposition.

34. What is your opinion about the extent of the requirements that should be imposed when commercial bank money is used?

We suggested a number of controlling mechanisms in our letter to the Commission of 6th January. In essence, the CSD should subject settlement in commercial bank money to equivalent parameters to settlement in central bank money, notably appropriate daylight counterparty limits and caps, real-time monitoring, and appropriate security and queuing arrangements. We would also draw the Commission's attention that in at least one market we are aware of, settlement occurs only in commercial bank money, obliging market participants to hold accounts with that commercial bank. In this particular case, it could be that greater use of central bank money should be promoted.

35. What do you think about the rules above?

We have no problem with the proposal on **reconciliation**, since we have a real-time capacity. However, we question the need for an elaborate system of physical **segregation** of proprietary assets, assets belonging to the participant, and the participant's customers' assets. In particular CSDs are not set up to segregate participants' clients' assets. To introduce this requirement would impose a significant burden on CSDs. As we wrote in our 6th January letter, this

segregation can be equally well achieved through proper control and monitoring of account balances, together with robust underpinning law, which ensures that if there is any doubt about the ownership of assets held in an omnibus account, then these default to the client. Although, as a CSD, as explained above, we have the means to segregate adequately our own assets and those of our clients, we also believe that any participant in a CSD should be to segregate its proprietary assets and its client assets in an omnibus account as well. Forcing CSDs to segregate their participants' clients' assets will be very costly in terms of systems adaptations. The CSD can offer an appropriate accounting structure/system, but should not be made responsible for the client's mistakes.

We otherwise agree that appropriate audit requirements, ensuring that client securities are only used according to the rules of the system and therefore with the clients' given consent, and preventing the creation of securities debit balances are desirable objectives.

36. Are further rules needed in order to ensure reconciliation and segregation?

No.

37. Do you think that these six basic principles cover sufficiently operational risks?

Yes. These are adequate.

38. What do you think about the eight principles above, particularly with respect to board composition and the need for a risk committee?

We do not have any objection in principle. However, should EU legislation mandate for instance the composition of CSD Boards, e.g. in the number of independent directors, then credit should be given to parallel and equivalent governance and supervisory structures, for instance, in an integrated group, if the CSD's activities are overseen by the Group Board. A similar comment could be made in relation to a group risk function.

39. According to you, should CSDs be subject to a principle of full responsibility and control on outsourced tasks? Yes? No? No opinion? Please explain why.

While the tasks can be outsourced or delegated to third parties, we agree that the CSD must retain ultimate responsibility and control for these tasks. Please also see our comment under question 13 on the outsourcing of core services.

40. Should there be any other exemptions from the principle of responsibility and control of CSDs on outsourced tasks?

Yes. We believe that that exemptions should be possible for both public and private bodies, where tasks are outsourced to a like-industry provider, such as T2S, (where CSDs will be solely outsourcing the settlement function to the Eurosystem) or to a technology/messaging network such as Link-up Markets. Some years ago, the Bank of England also outsourced government

bond settlement to what eventually became CREST (now EUI). Under T2S, maintenance of accounts etc will still remain the responsibility of the CSD.

41. What is your opinion on the above prudential framework for risks directly incurred by CSDs (which offer banking-type services)?

We agree that a CSD should manage its financial risks prudently, including those associated with counterparty, liquidity, market and custody risk. We do not think that the offering of credit (i.e. banking-type services) poses any special risks, as long these are monitored in real time and are actively managed. We do not offer uncollaterised overnight credit, and intra-day credit is secured by means of a lien (with appropriate haircuts) on the participants' assets. This lien is fully enforceable in the event of non-return of cash by the participant. If you are a bank like SIX SIS, and you operate a real time (not overnight batch) system, with final settlement across the books of the central bank, then there is a need for short-term credit facilities to smooth payment flows. We advance that operating a batch system (with overnight settlement) is systemically more risky.

We are also not in the business of creating large additional amounts of liquidity and do not encourage our clients to deposit excess cash surpluses with us. We have never experienced a liquidity drain and believe that our system is comprehensively robust. In terms of custody risk, as noted in our reply to question 35, there is an adequate legal underpinning where ownership of assets is queried. We also repeat our earlier comment about the need to tweak the application of the CRD to the relevant risks.

42. What do you think about the principles above (for CSDs as Facilitators)?

CSDs generally do not take credit risk as agents.

43. What do you think about including these elements of the Code in legislation?

We have no problem with the Code itself, which had laudable objectives, and we believe that we have adhered to its provisions. However, the Code, as a self-policed measure, has not been rigorously enforced, nor breaches sanctioned, nor problems resolved quickly enough. We therefore do not believe it is a matter of simply replicating the Code in EU legislation (and anyhow there would be an inconsistency as similar requirements are neither proposed in MiFID, nor are contained in EMIR for CCPs), and that it would probably be preferable if the Code was declared invalid and an alternative approach adopted.

PART II: HARMONISATION OF CERTAIN ASPECTS OF SECURITIES SETTLEMENT IN THE EUROPEAN UNION

As a general observation, we reiterate that the aspects covered here are not under the control of CSDs, but rather the entire market. As such we do not think it would generally be appropriate to capture all of them in EU legislation.

44. According to you, is the above described harmonisation of key post trade processes important for the smooth functioning of cross-border investment? Yes? No? No opinion? If yes, please provide some practical examples where the functioning of the internal market is hampered by absence of harmonisation of key post trading processes. If no, please explain your reasoning.

For the reasons outlined below, we do not believe that settlement discipline should be harmonized at the EU level. We are nonetheless pleased that the Commission has separated these notions from the desire, in the Short Selling Regulation, to link failed short sales with settlement discipline.

45. Do you identify any other possible area where harmonisation of securities processing would be beneficial?

Yes. The Commission and Member States should concentrate on removing the public barriers to the efficient cross-border settlement of securities. We also believe that it would be useful to harmonise the processes (e.g. deduction at source, withholding) relating to taxation requirements, covering notably capital gains, local-only tax requirements and stamp duty. This will notably ensure that investors in different jurisdictions are not discriminated against.

46. According to you, is a common definition of settlement fails in the EU needed? Yes? No? No opinion? Please explain why. If yes, what should be the key elements of a definition?

Yes. We believe that a high level common definition of a settlement fail could be beneficial. Given the small number of fails (less than 2% on average across all markets, a much more harmonized regime would be costly to implement and would not be robust on cost benefit grounds. Where some harmonization might be desirable is in relation to equalizing the treatment (discipline fees) between exchange traded and OTC products, so that regulatory arbitrage does not occur.

47. According to you, should future legislation promote measures to reduce settlement fails? Yes? No? No opinion? If yes, how could these measures look like? Who should be responsible for putting them in place? If no, please explain.

No: we do not support the use of legislation in this area. Measures are already in play in many venues which promote settlement efficiency and therefore reduce settlement fails. Measures such as pre-matching, settlement matching discipline regimes, auto-borrowing functionality, settlement efficiency functionality (to ensure items are settled in the CSD) such as auto partial settlement, settlement fail discipline regime; even the use of central counterparty clearing it a further measure to promote efficiency in settlement. However, we do not believe that legislation in this area will help. No CSD or participant willingly encourages settlement fails. Fail can occur which are not the direct fault to the participant, such as securities being transferred across depositories being delayed, the end investor is incapacitated during the process resulting in settlement of their investment being frozen (Probate), a temporary shortage of the product in the

markets or stock not released from collateralized undertakings. Persistent settlement fails caused by e.g. a participant are sanctioned subject to the rules of the system. This should be maintained at the level of the CSD. Our own experience of settlement fails is that they are a tiny proportion of our volumes: 0.002%.

48. What do you think about promoting and harmonising these ex-ante measures via legislation?

We are not in favour of this approach. We are concerned about what use should be made of this information (e.g. notifying it to the regulator), beyond regularizing the relationship with the participant.

49. What do you think about promoting and harmonising these ex-post measures via legislation?

We are not in favour of this approach. Buy ins should be left to national markets.

50. According to you, is there a need for the harmonisation of settlement periods? Yes? No? No opinion? Please explain why

We support the idea of harmonizing the settlement cycle, and notably shortening the equities settlement cycle from T+3 to T+2. Functionally, we can undertake this. However, we suggest that market forces might be a better way of achieving this, rather than a legislative initiative, particularly as we do not believe a full business case has been made, nor has a full CBA on the end-to-end impact been undertaken. Where markets for other products, such as bonds, are already on a settlement cycle of less than T+2, then clearly these should be left alone.

51. In what markets do you see the most urgent need for harmonisation? Please explain giving concrete examples

There are a number of markets in the EU which could benefit from greater harmonization, so a true pan-European securities market is created. We are notably pleased that the Spanish authorities are taking steps to introduce a CCP and reform their Registration system.

52. What should be the length of a harmonised period? Please explain your reasoning

Please see the answer to question 50 above. Studies have demonstrated that a move to T+2 strikes a balance between the reduction in (a) participants' collaterisation requirements (and the potential for settlement fails) with (b) the cost of system improvements (including faster collateral and liquidity placement) required to move to a faster settlement cycle. Moving to T+1 would not necessary improve these aspects further, and the savings and benefits would be small.

53. What types of trading venues should be covered by a harmonisation? Please explain your reasoning

On level playing field grounds, the same minimum settlement period should exist for a particular segment (e.g. cash markets), regardless of execution venue. However, there may be a need to vary the settlement period, depending on the different product types and investor requirements.

54. What types of transactions should be covered by a harmonisation? Please explain your reasoning

Please see our answer to question 50.

55. What would be an appropriate time span for markets to adapt to a change? Please Explain

We agree with the deadline of December 2013 being proposed by the Harmonisation of Settlement Cycles Working Group. We note however that migration by different markets must be orderly so that the impact on all infrastructures and participants can be minimized.

56. According to you, how should the principles examined in the communication on sanctions apply in the CSD and securities settlement environment?

In our view, the principles described in the Commission's Communication on "Reinforcing Sanctioning regimes in the financial services sector" should not be applied to the operations of post-trading market infrastructures. The reason for this, as explained above, is that relations between operators, such as CSDs, and participants are governed by (commercial) contract. Sanctions are applied to participants in the event that the rules of the system are broken, for instance for the posting of insufficient collateral (which would incur a basis point charge), or for late settlement and settlement fails. Such (financial) penalties form part of the overall financial relationship between the participant and the infrastructure, and are simply added to the participant's invoice of charges for a given time period. In certain circumstances, they can be appealed and reversed, but they certainly should not give rise to sanctions under either a civil or criminal code. The infrastructure does have the ultimate sanction of withdrawing the participants' membership of the system if the participant, after repeated warnings and failings, does not co-operate with the infrastructure. But this is rare; usually the threat of such action is sufficient to restore correct behavior. In any event, the participant is usually anxious to preserve a relationship with the CSD, since there are few immediate alternatives, and so both parties will work towards a mutually satisfactory outcome. Similarly, we do not believe that CSDs should be sanctioned by regulators in the way proposed in the Commission's Communication.

SIX SIS AG
28 February 2011

APPENDIX: JUSTIFICATION FOR INCLUSION OF THIRD COUNTRY CSDS IN SCOPE OF EU LEGISLATION

We believe that provision should be made to include Third Country CSDs in the Scope of the CSD Regulation, for the following reasons:

(i) CSDs, and particularly Investor CSDs undertake a considerable amount of cross-border business. This international business is rarely confined to one jurisdiction and because of the complexity of some value chain transactions (such as corporate actions), involving a number of intermediaries such as CSDs, transfer agents and custodians, this business snakes in and out of the EU, and not only in and out of Switzerland.

(ii) As the market place continues to be globalised and products commoditized, legal certainty about the status of Third Country CSDs to provide services in the EU will continue to offer institutions and investors in the EU the widest choice and provide a level playing field for CSDs in the EU and Third Countries (where reciprocity exists). This includes the preference and ability of certain intermediaries to open accounts directly with CSDs, as opposed to relying on sub-custody arrangements. Were this trend to continue (for instance accelerated by T2S), then this could lead to more efficiency in the industry. For instance, the South African CSD, State, is a member of Link-up Markets, and more participants from this continent and elsewhere can be anticipated;

(iii) Further cross-continental consolidation of trading venues will also provide an impetus to settle in fewer CSDs, which already have multi-currency capabilities; and

(iv) As supported by our major clients, both Swiss banks active in the EU, and EU banks active in Switzerland, it is the intention of SIX SIS to put our settlement business into T2S. By participating in T2S, we will aid the smooth flow and settlement of transactions throughout Europe, thus consolidating the use and promulgation of securities in euros and other currencies. This will benefit EU institutions, end users, investors and consumers alike, enhancing the single capital market.

Grandfathering

It is our view that the current Home State authorization of Third Country CSDs should be recognized under forthcoming legislation and grandfathered for a period after the entry into force of the Regulation, before being subject to re-authorization by ESMA. This will mirror similar provisions in EMIR. Grandfathering should be subject to reciprocity (in the Swiss case, we already allow EU CSDs to operate in our market) and to demonstrable equivalence between EU requirements and the Third Country's (see below). Grandfathering should be possible as SIX SIS is a well regulated entity, subject to supervision by the Swiss financial services supervisor, FINMA, and, as the operator of systemically important payment and settlement systems, to oversight by the Swiss National Bank.

Equivalence

Equivalence requirements are set out in a number of EU Directives, for instance in MiFID Articles 19(6), 24 (2) and (4), 47, 48 (3) and 63, and in the latest draft of EMIR (Articles 3.0 and 23 (3) and (4). We would anticipate that something similar to the requirements in EMIR will emerge in the CSD Regulation. Given, however, that some Third Country regimes may not be as developed as those of the EU, we suggest that the equivalence framework could be based on the following generic requirements:

(i) A comparable authorization and supervision regime, including a clear application of an institutional license, such as for banking;
(ii) Reciprocity;
(iii) As a CSD, designation under a similar measure to the Settlement Finality Directive;
(iv) A robust domestic legal framework for the holding and disposition of securities in accounts, for instance replicating the key provisions of the Geneva and the Hague Conventions
(v) Meeting substantively CPSS-IOSCO Recommendations for CSDs, including risk management;
(vi) Permitted information exchange between relevant EU and Third Country (Home state) supervisors; and
(vii) Where relevant, the convening of a college to discuss cross-border issues.

As noted above, this assessment of equivalence would hold good until re-authorization by ESMA.