Reply form

**on the** **call for evidence on shortening of the settlement cycle**

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

* respond to the question stated;
* indicate the specific question to which the comment relates;
* contain a clear rationale; and
* describe any alternatives ESMA should consider.

ESMA will consider all comments received by **15 December 2023.**

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input - Consultations’.

Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

• Insert your responses to the questions in the Consultation Paper in this reply form.

• Please do not remove tags of the type < ESMA\_QUESTION\_SETT\_0>. Your response to each question has to be framed by the two tags corresponding to the question.

• If you do not wish to respond to a given question, please do not delete it but simply leave the text “TYPE YOUR TEXT HERE” between the tags.

• When you have drafted your responses, save the reply form according to the following convention: ESMA\_CP1\_SETT \_nameofrespondent.

 For example, for a respondent named ABCD, the reply form would be saved with the following name: ESMA\_CP1\_SETT \_ABCD.

• Upload the Word reply form containing your responses to ESMA’s website (**pdf documents will not be considered except for annexes**). All contributions should be submitted online at *www.esma.europa.eu* under the heading *‘Your input - Consultations’.*

**Publication of responses**

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

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Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘[Data protection](https://www.esma.europa.eu/about-esma/data-protection)’.

**Who should read this paper?**

All interested stakeholders are invited to respond to this consultation paper. In particular, ESMA invites market infrastructures (CSDs, CCPs, trading venues), their members and participants, other investment firms, issuers, fund managers, retail and wholesale investors, and their representatives to provide their views to the questions asked in this paper.

# General information about respondent

|  |  |
| --- | --- |
| Name of the company / organisation | Finance Denmark |
| Activity | Associations, professional bodies, industry representatives |
| Are you representing an association? |[x]
| Country / Region | Denmark |

# Questions

1. : Please describe the impacts on the processes and operations from compressing the intended settlement date to T+1 and to T+0. Please:
2. provide as much detail as possible on what issues would emerge in both cases and how they could be addressed with special attention to critical processes (matching, allocation, affirmation and confirmation) and interdependencies. Where relevant please explain if these are general or asset class/instrument/ trade specific.
3. Identify processes, operations or types of transaction or financial instrument class that would be severely impacted or no longer doable in a T+1 and in a T+0 environment.

**Please, suggest if there are legislative or regulatory actions that would help address the problems. Where relevant please explain if these are general or asset class/instrument/ trade specific.**

<ESMA\_QUESTION\_SETT\_1>

Introduction remark on securities settlement in Denmark:

Denmark migrated to the T2S platform for DKK and EUR settlement back in 2018 which means that many processes at CSD level are harmonised according to European T2S standards.

However, considering the Danish market practise of having a segregated account structure rather than an omnibus account structure at CSD level (which is more common in the European securities settlement landscape), it was decided - at the time of migration to the T2S platform - that the securities accounts belonging to retails clients and the securities settlement of retail clients were to remain on the original proprietary platform in the Danish CSD and to settle accordingly on this platform. An ECB derogation was granted allowing up to 5 % of total settlement volume to be settle on the proprietary platform.

Hence, there are two settlement platforms for securities settlements in Denmark, i) the T2S platform with settlement cycles, ii) the proprietary platform referred to as the 'Classic' platform with batch settlement. Both platforms are operated by the Danish CSD, Euronext Securities Copenhagen.

Note: Settlement on the Classic platform is supported in DKK, EUR and SEK. For settlement in either of the three currencies you must as a participant of the Danish CSD have access to liquidity of relevant currency either directly yourself or via a payment bank.

Issues in relation to shortening of settlement circle may differ depending on which platform the transaction is settling.

Comments in the following text, will generally be referring the T2S platform unless otherwise is stated.

(i)

Late trading will challenge the possibility to settle T+1. Suggestion will be to close the Stock Exchange earlier than today.

Shortening the settlement time on T2S in DKK will be possible with a minimum of changes; but the problem will be to get the liquidity in time, especially where customer use another bank to cover liquidity than the one used for settlement in T2S. The Danish market have an 'interbank agreement', with a cut-off for liquidity moves betwen the banks and its customers.

When it comes to the post trade processing on behalf of custodians and foreign investors, we do have some observations in regards to the timing of which all aspects can be managed. Settlement needs to be compressed ie Instructions for match and settlement need to enter the market sooner, liquidity and cash funding for settlement purposes depend on reporting abilities between the market, CSD/T2S, the agent/subcustodian, the global custodian(s) and possible the fund manager or others acting either as investor or investors representative. The window within which, the custodian receives matching status from the agent/subcustodian enabling adequate assessment and consequent payment instructions, for funding of the related cash account at agent level narrows down. There may even be a need for trading fx in between. Furthermore, custodians operate on a global scale, and may be impacted by differences in time zone between market and operations. If operation or back office functions lie east to the market, this window may narrow even further. At least on short term we will probably see a decrease of a settlement ratio (increased fails) a higher demand for securities lending, cash penalties etc.

(ii)

For T+0: Missing local infrastrucure support on mass settlement, e.g., seen in settlement of dividends, which has a limit of maximum 2.500 linked settlement transactions in same ISIN. A T2S change is needed and will be a prerequisite for shortening the settlement cycle.

In a Cross Border environment, several challenges arise. Different market structures, different rules between f.ex US and EU. A few examples of differences; Cut off times not mandatory in DTC per se, late matching penalties not applicable in US compared to EU CSDR. US is based on penalizing inefficincies through additional costs. There's no US equivalent to the EU Settlement Finality Directive (SFD). Processing wise cross border transactions are not handled STP, volumes are low in comparison, however important to mention.

<ESMA\_QUESTION\_SETT\_1>

1. : What would be the consequences of a move to a shorter settlement cycle for (a) hedging practices (i.e. would it lead to increase pre-hedging practices?), (b) transactions with an FX component?

<ESMA\_QUESTION\_SETT\_2>

We support information from ICMA and AFME. For non-EUR countries there is a need for more currency exchanges with shorter settlement to follow the security settlement cycle. This will most likely put a pressure on the operational processes and lead to more expensive currency trading.

<ESMA\_QUESTION\_SETT\_2>

1. : Which is your current rate of straight-through processing (STP ), in percentage of the number and of the volume of transactions broken down per type of transaction or per instrument as relevant? In case STP is used only for certain processes/operations, please identify them. Which are the anticipated challenges that you envisage in improving your current rate of STP?

<ESMA\_QUESTION\_SETT\_3>

We assess STP (Strait Through Processing) as the level of automation and not as settlement efficiency, which is something else. It is difficult to estimate a general STP ratio for the Danish market as this often depend on type of instrument, underlying customer sending the original transaction/swift and intermediary institution(s) forwarding the instruction to the CSD/T2S for settlement. Our rough estimate is that we are well above 95% and base this on very high-level input from a large part of the membership banks in Denmark. This said our experience is that the level of STP is a bit higher on national transactions than on transactions that involves custodian transactions or cross-border transactions, and our guess is that this is due to a longer chain and in general our experience is that STP rates goes down the further from the CSD that we are in the transaction chain. But STP rates also vary between the different institutions and the different clients.

Regarding settlement efficiency:

ES-CPH Danish CSD advised that the settlement rate in October 2023 was 97.6% and the T2S settlement was 97.9%. The batch flow punctuality was 99.0%. In October two batches were delayed due to minor disturbances.

In November, the ES-CPH settlement rate was 98.9% and the T2S settlement was 98.0%.The batch flow punctuality was 98.5%.

<ESMA\_QUESTION\_SETT\_3>

1. : Please describe the impacts that, in your views, the shortening of the securities settlement cycle could have beyond post-trade processes, in particular on the functioning of markets (trading) and on the access of retail investors to financial markets. If you identify any negative impact, please identify the piece of legislation affected (MiFID II, MiFIR, Short Selling Regulation…) and elaborate on possible avenues to address it.

<ESMA\_QUESTION\_SETT\_4>

Customers who buy/sell from own bank (inhouse) is extremely effective in Denmark. But when it comes to third party trading the settlement include more participants, with respective processes that can delay instruction and settlement in the Post Trade chain.

Non-inhouse settlement consequently increases the complexity rate for each external party in the Post Trade chain which on the other hand decreases the STP rate.

<ESMA\_QUESTION\_SETT\_4>

1. : What would be the costs you would have to incur in order to implement the technology and operational changes required to work in a T+1 environment? And in a T+0 environment? Please differentiate between one-off costs and on-going costs, comparing the on-going costs of T+1 and T+0 to those in the current T+2 environment. Where relevant please explain if these are general or asset class/instrument/ trade specific.

<ESMA\_QUESTION\_SETT\_5>

Costs would be contingent on the roadmap and timeline that is ultimately agreed but are generally expected to be accrued in the short-term. Costs will not be borne equally, and we need to consider that smaller market participants may generally have to undertake more significant levels of preparation for T+1 thus incurring greater costs. One-off costs would involve making operational changes like additional staff if required and technical changes like process optimization, 100% automation, to cater to T+1 and eventually T+0 scenario in EU. On-going cost could be the requirement of additional staff should the level of unmatched or unsettled trades not return to previous levels after introduction of a shorted settlement cycle.

<ESMA\_QUESTION\_SETT\_5>

1. : In your view, by how much would settlement fails increase if T+1 would be required in the short, medium and long term? What about T+0? Please provide estimates where possible.

<ESMA\_QUESTION\_SETT\_6>

We expect with the introduction of shorter settlement cycles that settlement fails would increase at the initial introduction and startup phase by roughly 25% since the biggest issue today is lack of securities which we anticipate will increase with a shorter settlement cycle. We would expect a rise in penalties especially related to late matching. After the introduction period it is our assumption that these numbers would begin to decrease. We also expect a change in the penalties moving from Late Settlement to more penalties being received for Late Matching. With reduced settlement cycles reduced time frames are available whereby counterparties would have less time to agree on SSI's and general trade details. Should T+0 come into play the risk for late matching and settlement would increase as any delay from counterparties would relate in late matching and subsequent late settlement.

<ESMA\_QUESTION\_SETT\_6>

1. : In your opinion, would the increase in settlement fails/cash penalties remain permanent or would you expect settlement efficiency to come back to higher rates with time? Please elaborate.

<ESMA\_QUESTION\_SETT\_7>

Based on our experience from the T+3 to T+2 move we would expect that in the short term the number of matching fails could increase, especially if the market has a short time to adapt to shortened settlement cycles. We expect that the actual settlement fails impact would be more limited. In the longer term we would expect the number of settlement fails to decrease. This requires that market participants are able to speed-up their processes for trade allocations and related instruction processes. If the number of matching fails could be reduced that would also have positive impact on settlement fails. In most cases settlement fails are inventory issues due to high interlinkage of trades, i.e., one is not able to deliver, because he has not received the securities as scheduled.

<ESMA\_QUESTION\_SETT\_7>

1. : Is there any other cost (in particular those resulting from potential impacts to trading identified in the previous section) that ESMA should take into consideration? If yes, please describe the type of cost and provide estimates.

<ESMA\_QUESTION\_SETT\_8>

As we have seen with the introduction of T+1 in U.S and Canada for the EU markets, Asset Managers and other intermediaries outside European time zones may need to adapt their location or working hours to accommodate shortened processing times. The FX trading could require a change of working hours for relevant staff and a change of cut-off times in national banks.

<ESMA\_QUESTION\_SETT\_8>

1. : Do you agree with the mentioned benefits? Are there other benefits that should be accounted for in the assessment of an eventual shortening of the securities settlement cycle?

<ESMA\_QUESTION\_SETT\_9>

Yes, we agree with the named benefits of reduced counterparty risk and related collateral needs. In addition, the requirement of more automated solutions to achieve T+1 and T+0 Settlement will bring benefit to the operational processing space with the potential reduction of manual intervention and potential cost savings.

<ESMA\_QUESTION\_SETT\_9>

1. :Please quantify the expected savings from an eventual reduction of collateral requirements derived from T+1 and T+0 (for cleared transactions as well as for non-cleared transactions subject to margin requirements).

<ESMA\_QUESTION\_SETT\_10>

We hope that long term cost savings would arise from lower collateral requirements and improved settlement efficiency in the processes related to the post trade environment.

<ESMA\_QUESTION\_SETT\_10>

1. : If possible, please provide estimates of the benefits that you would expect from T+1 and from T+0, for example the on-going savings of potentially more automated processes.

<ESMA\_QUESTION\_SETT\_11>

Too early to provide estimates of the benefits from moving to shorter settlement cycle. We may be in a better position to share this once T+1 is live in North America.

<ESMA\_QUESTION\_SETT\_11>

1. : How do you assess the impact that a shorter settlement cycle could have on the liquidity for EU markets (from your perspective and for the market in general)? Please differentiate between T+1 and T+0 where possible.

<ESMA\_QUESTION\_SETT\_12>

Shortening settlement cycle from T+3 to T+2 had some positive effects adding liquidity generally in the market. Accelerating the settlement period to T+1 or T+0 should have a similar effect. Similar effect could be seen for banks and other investors at large. However, we expect the impact on liquidity being minor. Further there might be a rebalancing of activity that has moved to the US as a consequence of the US T+1 move, some of that activity might move back to the EU.

<ESMA\_QUESTION\_SETT\_12>

1. : What would be the benefits for retail clients?

<ESMA\_QUESTION\_SETT\_13>

Retail investors would receive securities or cash from their transactions earlier. Also, likely that interest and dividend payment cycles would be shortened respectively. This would be in line with the expectations of more "instant" services from the retail customer base.

<ESMA\_QUESTION\_SETT\_13>

1. : How would you weigh the benefits against the costs of moving to a shorter settlement cycle? Please differentiate between a potential move to T+1 and to T+0.

<ESMA\_QUESTION\_SETT\_14>

We see the main benefit of a shorter settlement cycle being a more automated process along the value chain. In order to achieve cost savings automation for processing would be required along the whole value chain thus improving processing from an operational perspective and hopefully reducing cost by removing manual processes such as trade input and corrections. Although we expect to see an increase in penalties in the initial phases due to late matching and settlement, we would expect these to reduce to normal levels within a short time frame after introduction. It is hard to list benefits in relation to T+0 at this time as better automated solutions would be required by all parties to achieve a seamless processing flow which entails additional startup costs. Benefits achieved from a move to T+1 would need to be analysed prior to moving to T+0 to ensure cost efficiency.

On the cost side we expect increased cost for developing automation in a T+1 scenario while T+0 scenario will require a new and different infrastructure which will be very costly.

<ESMA\_QUESTION\_SETT\_14>

1. : Please describe the main steps that you would envisage to achieve an eventual shorter securities settlement cycle. In particular, specify: (i) the regulatory and industry milestones; and (ii) the time needed for each milestone and the proposed ultimate deadline.

<ESMA\_QUESTION\_SETT\_15>

In our opinion first step before even talking about shortening settlement cycles, should be working on a higher settlement efficiency. Not particularly in Denmark, but across Europe. If this is not taken in consideration before moving to T+1, the settlement fails would most likely increase. We are aware that UK might be moving to T+1 in 2026 but that should not lead to a forced or hastily implementation in EU. We would prefer an alignment with UK go-live if UK would be willing to wait for EU which is a more complex market.

With that said the first step should be for the legislators to incorporate T+1 in a common European regulation, f.ex. CSDR which also implemented moving from T+3 to T+2. To see that European Countries implement at the same time. Implementing one country at a time would be chaotic.

A timeline could be a legislation draft is made and proposed end 2024 - beginning of 2025. Evaluation and review during 2025, final legislation beginning of 2026 and Implementation date 18 months later. Beginning of 2027 at the earliest. 2028 is probably more feasible due to the work that needs to be in place.

<ESMA\_QUESTION\_SETT\_15>

1. : Assuming that the EU institutions would decide to shorten the securities settlement cycle in the EU, how long would you need to adapt to the new settlement cycle? And in the case of a move to T+0?

<ESMA\_QUESTION\_SETT\_16>

In Denmark and in the Nordics markets we believe that we could be ready for T+1 in a rather short time, as trading and settlement have a high STP rate and settlement efficiency. But that is if we are talking about domestic trades i DKK. The cross-border settlement would require more time for adaption.

A way to ensure quality and a high settlement rate could be to implement the use of pre-matching more broadly in Europe. Less time for manual handling requires more automation. Implementing this requires time. We would need at least 1,5 to 2 years after final decision.

Moving to T+0 either immediately from T+2 or shortly after T+1, would be very challenging and it is not possible as it would definitely require full STP and automation. In other words, a completely different settlement system with no manually handling of settlement issues, as there wouldn't be enough time for it.

<ESMA\_QUESTION\_SETT\_16>

1. : Do you think that the CSDR scope of financial instruments is adequate for a shorter settlement cycle? If not, what would be in your views a more adequate scope?

<ESMA\_QUESTION\_SETT\_17>

Yes, we do think the scope in the CSDR is adequate. But it would be preferable if derivatives and FX trading moved standard spot settlement towards T+1 as well. Even if standard settlement cycle for FX is not a rule but a convention, it should be considered. In a T+1 scenario for security transactions the market participants will have to trade their liquidity earlier (T+0 or T+1) to avoid misalignment and increased CSDR penalties due to lack of cash. As long as the convention or market practice on FX spot is T+2, FX trading will be more expensive.

<ESMA\_QUESTION\_SETT\_17>

1. : Is it feasible to have different settlement cycles across different instruments? Which are the ones that would benefit most? Which least?

<ESMA\_QUESTION\_SETT\_18>

From a settlement point of view, it is not feasible. The misalignment would cause more problems than benefits. To take some of the financial instruments from CSDR Scope out and not move it to T+1 would in our opinion create an unfortunate misalignment and we see no advantages.

<ESMA\_QUESTION\_SETT\_18>

1. : Which financial instruments/ transaction types are easier to migrate to a shorter settlement period in the EU capital markets? Does the answer differ by asset class? Should it be feasible/advisable to have different migration times for different products/markets/assets? If yes, please elaborate.

<ESMA\_QUESTION\_SETT\_19>

We do not see any instruments or transaction and we would advise not to have different migration times for different products as explained above in our reply to Q18.

<ESMA\_QUESTION\_SETT\_19>

1. : Do you think that the settlement cycle for transactions currently excluded by Article 5 of CSDR should be regulated? If you think that the settlement cycle of some or all of these transactions should be regulated, what would be in your view an appropriate length for their settlement cycle?

<ESMA\_QUESTION\_SETT\_20>

We do not believe that it would be any advantage to begin to regulate the transactions out of scope in CSDR art. 5. They should remain out of scope.

<ESMA\_QUESTION\_SETT\_20>

1. : Please describe the impact(s) that the transition to T+1 in other jurisdictions has had or will have on your operations, assuming the EU remains on a T+2 cycle.

<ESMA\_QUESTION\_SETT\_21>

The most significant challenge is the timing misalignment between the different jurisdictions. The market participants in EU will need to deal with a compressed time window between trade execution and settlement. This will create operational complexities, especially for FX transactions, cross-border trades and liquidity management.

Also, if the EU remains at T+2 whereas other markets move to T+1, investment funds would face a significant impact. More specifically, investment fund would experience UCITS breaches in relation to subscriptions and redemptions. For subscription the funds will for larger subscriptions breach current 10% limit of overdraft. For larger redemptions the funds will risk breaching 20% of cash allocation limits. This will be a direct consequence if the EU does not move to T+1 when other larger markets do, which would increase costs from overdrafts and operational complexity.

<ESMA\_QUESTION\_SETT\_21>

1. : Can you identify any EU legislative or regulatory action that would reduce the impact of the move to T+1 in third countries for EU market participants? Please specify the content of the regulatory action and justify why it would be necessary. In particular, please clarify whether those regulatory actions would be necessary in the event of a transition of the EU to a shorter settlement cycle, or they would be specific only to address the misaligned cycles.

<ESMA\_QUESTION\_SETT\_22>

Inspired by the US, the impact of the move to T+1 in third countries might be reduced by a EU regulatory demand for pre-matching of trades for EU based investment firms. Implementing mandatory pre-matching would most likely reduce operational risk for both misaligned cycles and for a transition for the EU to a shorter settlement cycle. This would also increase the settlement efficiency rate in the EU which would be a good step in preparing the EU for a T+1 settlement cycle, see also our response to Q15.

<ESMA\_QUESTION\_SETT\_22>

1. : Do you see benefits in the harmonisation of settlement cycles with other non-EU jurisdictions?

<ESMA\_QUESTION\_SETT\_23>

Standardizing settlement cycles with e.g., USA will bring many benefits to EU Capital Markets. It will streamline the operational processes and reduce the complexity for EU participants when trading with US based participants. Furthermore, if the two most liquid capital markets are aligned once again, we should expect the smaller Non-EU Jurisdictions to follow, leading to a higher harmonization degree for EU participants. We would also expect some rebalancing of activity and alignment of cash to happen, pls. see also responses to Q12 and Q21.

<ESMA\_QUESTION\_SETT\_23>

1. : Would reducing the settlement cycle bring any other indirect benefits to the Capital Markets Union and the EU's position internationally?

<ESMA\_QUESTION\_SETT\_24>

An increase market efficiency will lead to an increase in liquidity in EU. Faster allocation of capital and quicker access to funds for investors would improve the attractiveness of the EU Capital Markets compared to T+2 jurisdictions. Moving from T+2 to T+1, will also decrease the time the participants are exposed to potential counterpart defaults.

<ESMA\_QUESTION\_SETT\_24>

1. : Do you consider that the adaptation of EU market participants to the shorter settlement cycles in other jurisdictions could facilitate the adoption of T+1 or T+0 in the EU? Please elaborate.

<ESMA\_QUESTION\_SETT\_25>

Adapting to the shorter settlement cycles in other jurisdictions would mean changes to the settlement processes to facilitate the shorter settlement cycle of the jurisdictions in question. The implemented changes to the settlement process will most likely be the exact same changes needed for a general adaption of T+1, thus, lowering the extra cost of operating in markets with shorter settlement cycles.

<ESMA\_QUESTION\_SETT\_25>

1. : Would different settlement cycles in the EU and other non-EU jurisdictions be a viable option?

<ESMA\_QUESTION\_SETT\_26>

Different settlement cycles across the EU and non-EU jurisdictions will create operational complexities, especially for FX transactions, cross-border trades and liquidity management. The option of differing settlement cycles as a permanent state would lead to complex and costly settlement procedures since the procedures would differ between the different settlement cycles. We would expect a permanent loss of competition for EU institutions to happen in a case a where EU would keep the T+2 settlement cycle while most other jurisdictions would be on a T+1 settlement cycle and no rebalancing of activity would happen as well.

<ESMA\_QUESTION\_SETT\_26>

1. : Please elaborate about any other issue in relation to the shortening of the securities settlement cycle in the EU or in third-country jurisdictions not previously addressed in the Call for Evidence.

<ESMA\_QUESTION\_SETT\_27>

We would highly prefer and recommend a T+1 solution to a T+0 solution since that would be a very complex move that we do not see possible currently. We strongly recommend that a potential move to T+1 in EU is done after an thoroughly investigation of processes and potential impacts and taking into consideration the complexity of the EU market. Any decision should also be based on the experiences and lessons learned from the US T+1 move and not be rushed in a chase for alignment as fast as possible.

<ESMA\_QUESTION\_SETT\_27>