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Market infrastructures in Luxembourg : overview of the applicable legal frameworks

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* The views of the authors expressed in this article do not necessarily reflect those of the *Banque centrale du Luxembourg.*

Introduction

1. The three core components of the financial system are markets, institutions and market infrastructures. Financial market infrastructures ("FMIs" or "market infrastructures") provide various services that underpin financial market activities, as they facilitate the handling of payments and the clearing and settlement of financial instruments, that is to say the process that finalizes a trade by transferring the ownership of the traded asset and the cash to pay for it.

2. According to the "Glossary of terms related to payment, clearing and settlement systems" published by the European Central Bank ("ECB"), "market infrastructures" are "systems used for the trading, clearing[1] and settlement[2] of payments, securities and derivatives".[3] More recently, the CPSS-IOSCO[4] defined in the Principles for financial market infrastructures ("PFMIs")[5] an FMI as "a multilateral system among participating institutions, including the operator of the system, used for the purposes of clearing, settling, or recording payments, securities, derivatives, or other financial transactions. FMIs typically establish a set of common rules and procedures for all participants, a technical infrastructure, and a specialised risk-management framework appropriate to the risks they incur".

3. These FMIs play a central role in the financial system's architecture, enabling a quick and effective settlement of financial transactions. However, if not properly organized and managed, they can pose significant risks to the financial system and be a potential source of contagion, particularly in periods of market stress, as such service providers might be the sole providers of such

[1] Clearing: the process of transmitting, reconciling and, in some cases, confirming transfer orders prior to settlement, potentially including the netting of orders and the establishment of final positions for settlement. Sometimes this term is also used (imprecisely) to cover settlement. For the clearing of futures and options, this term also refers to the daily balancing of profits and losses and the daily calculation of collateral requirements (see ECB Glossary defined below).

[2] Settlement: the completion of a transaction or of processing with the aim of discharging participants' obligations through the transfer of funds and/or securities. A settlement may be final or provisional (see ECB Glossary defined below).

[3] ECB, Glossary of terms related to payment, clearing and settlement systems, December 2009 (www.ecb.int) (the "ECB Glossary").

[4] Committee on Payment and Settlement Systems ("CPSS"), a committee of the Bank of International Settlement ("BIS"), and the Technical Committee of the International Organization of Securities Commissions ("IOSCO").

[5] See section describing the PFMIs in Chapter 2 below.

specialized services in the market they operate and are therefore often seen as essential utilities providing a service of common interest. Indeed, the failure of an FMI that has a critical size or position in a market could have immediate systemic implications, since its disorderly collapse would lead to considerable uncertainty that would destabilize markets – some segments might simply cease to operate. Such failure of an FMI would cause significant losses to other financial institutions. The contagion from a failure could spread rapidly, since FMIs are interconnected with their users and/or other FMIs.

4. FMIs may be payment systems ("PS") that are systemically important, central securities depositories ("CSD"), securities settlement systems ("SSS"), and central counterparties ("CCP"). Recently standards and European Union ("EU" or "Union") legislation have also covered over-the-counter ("OTC") derivatives CCPs[6] and trade repositories ("TR"), in particular, the Regulation on OTC derivatives, central counterparties and trade repositories ("EMIR").[7]

5. In the Grand Duchy of Luxembourg, apart from the Luxembourg component of the PS called TARGET2 – the real-time gross settlement ("RTGS") system[8] owned and operated by the Eurosystem[9] –, and a TR that has recently been established there,[10] the main market infrastructures are CSDs – including an international CSD ("ICSD")[11] – which also operate a SSS. This article will focus on CSDs and SSSs (Chapter 1), especially since three CSDs operating SSSs based in Luxembourg are subject to the oversight[12]

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6 As of mid-2013, there is no CCP based in Luxembourg. CCPs are regulated by EMIR (defined below).

7 Regulation (EU) No. 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories ("EMIR") (entered into force on 16 August 2012 but subject to further implementation measures).

8 Trans-European Automated Real-time Gross settlement Express Transfer system (see legal acts regarding TARGET2 on www.ecb.int and TARGET2-LU www.bcl.lu).

9 See for further developments on PS: T. Kokkola (ed.), *The Payment System: Payments, securities and derivatives, and the role of the Eurosystem*, European Central Bank, 2010; and *Payment and securities settlement systems in the European Union* (aka "Blue book"), Volume 1, Euro area countries, European Central Bank, August 2007 (esp. 'Luxembourg' section pp. 285 ff) (www.ecb.int).

10 Namely Regis-TR SA (www.regis-tr.com), which shall be regulated by EMIR (see also PFMIs, especially Section 1.14, p. 9 for the definition of TRs and the ESMA website, www.esma.europa.eu).

11 An ICSD is a CSD which was originally set up to settle Eurobond trades and is now active also in the settlement of internationally traded securities from various domestic markets, typically across currency areas. At present, there are two ICSDs located in EU countries: Clearstream Banking SA ("CBL") in Luxembourg and Euroclear Bank SA/NV in Belgium.

12 The oversight of payment systems, securities clearing and settlement systems are typical central bank functions whereby the objectives of safety and efficiency are promoted by monitoring existing and planned systems, assessing them against the applicable standards and principles whenever possible and, where necessary, fostering change.

and supervision, i.e. the regular assessment of their operations, of the *Banque centrale du Luxembourg* ("BCL"). Pursuant to Union law, the central banks of the Eurosystem – which encompasses the central banks of the European System of Central Banks ("ESCB") that are part of the euro zone (such as the BCL in Luxembourg) – have developed over the years crucial oversight and supervision functions of some FMIs (Chapter 2).

6. The introduction of the euro had promoted efforts to reshape and harmonize the market infrastructure for financial instruments in the euro area; especially as it had resulted in markets becoming larger and more liquid. EU legislation has, in particular, targeted SSSs following the implementation of the Settlement Finality Directive ("SFD")[13] and the Payment Services Directive ("PSD").[14] Following TARGET2, the SFD and the PSD, post-trade industry is also to be further harmonized with the planned implementation of TARGET2-Securities ("T2S"), the Eurosystem's single technical platform enabling CSDs and national central banks ("NCB") to provide core, borderless and neutral securities settlement services in central bank money in Europe, which shall go live in several migration waves as of 2015 (Chapter 3).

Chapter 1
Definitions and overview of the main market infrastructures in Luxembourg

7. Market infrastructures are complex notions, which deal with operations and concepts that constantly evolve. The legal regimes, standards and principles concerning FMIs – such as the recent PFMIs – have therefore been elaborated over time, in order to tackle the new risks inherent to FMIs. At EU level, even though the European Commission has long had the lead on the matter, the recent EU legislation – such as EMIR – has transferred regulatory

[13] Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems (*OJ* L 166, 11 June 1998, p. 45), amended by Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 (*OJ* L 146, 10 June 2009, p. 37) and Directive 2010/78/EU of the European Parliament and of the Council of 24 November 2010 (*OJ* L 331, 15 December 2010, p. 120).

[14] Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC (*OJ* L 319, 5 December 2007, pp. 1 to 36).

powers related to FMIs to the EU supervisory body for securities: the "European Securities and Markets Authority" ("ESMA").[15]

8. In Luxembourg, a PS and a SSS shall be designated by the BCL as payment systems and securities settlement systems and notified to ESMA[16] by the Minister responsible for the financial sector, in accordance with Title V of the law of 10 November 2009 on payment services, as amended (the "November 2009 Law").[17] The said Title V also applies to PS and SSS notified by the BCL to the European Commission before the entry into force of the November 2009 Law, in accordance with article 34-3 of the law of 5 April 1993 on the financial sector, as amended.[18] [19]

9. Thus, apart from the Luxembourg-leg of TARGET2, the main market infrastructures based in Luxembourg, which were notified or designated by the BCL and are mentioned on the official list of the latter,[20] are SSSs operated by the following CSDs: Clearstream Banking SA ("CBL"), VP Lux S.à r.l. ("VP Lux") and LuxCSD SA ("LuxCSD").[21]

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15 ESMA officially replaced the "Committee of European Securities Regulators" ("CESR") on 1 January 2011.

16 Until the Luxembourg law of 20 December 2011, the Minister responsible for the financial sector had to notify the designated PS or SSS to the European Commission.

17 See articles 107 ff. of the Luxembourg law published in *Mémorial* (Luxembourg Official Journal) A – No. 215 of 11 November 2009, p. 3698, as amended, in particular, by the law of 20 May 2001 and the law of 21 December 2012 implementing Directive 2010/78/EU of the European Parliament and of the Council of 24 November 2010 […] in respect of the powers of […] the European Supervisory Authority (European Securities and Markets Authority).

18 For the legal regime applicable pursuant to the January 2001 Law, see E. de Lhoneux *et al.*, "La banque centrale du Luxembourg: présentation juridique", *ALJB*, 2004 (para. 2-55 to 2-57) and M. Brouillet-Mc Sorley and L.-Ch. Van Burik, "Le cadre juridique des systèmes de règlement des opérations sur titres en droit luxembourgeois", *ALJB*, 2004.

19 For translations in English of most of the legislation mentioned in this article, see www.cssf.lu.

20 The BCL holds an official list of PS and SSS referred to in article 108 of the November 2009 Law. The official list is available on the website of the BCL and is updated regularly. It is published in the *Mémorial* at least every year-end (see article 110(2) of the November 2009 Law and ESMA website, www.esma.europa.eu).

21 Following an announcement in mid-July 2013, a fourth CSD is to be set up in Luxembourg by the London Stock Exchange Group (LSEG).

Section 1
Payment systems (PS)

Sub-section 1
The notions related to payments

10. A payment is, in a strict sense, a transfer of funds that discharges an obligation on the part of a payer *vis-à-vis* a payee. However, in a technical or statistical sense, it is often used as a synonym for "transfer order", which is an order or message requesting the transfer of assets – e.g. funds, securities, other financial instruments or commodities – from the debtor to the creditor.

11. A payment in a strict sense thus requires the use of payment instruments, be it a fiduciary currency – coins or notes – or other payment instruments like a bank transfer, a cheque, a debit or a credit card, or electronic money. Contrary to fiduciary money, which is directly exchanged, the use of payment instruments implies that the funds are transferred from the bank account of the payer to the bank account of the payee. As accounts are often held in different credit institutions, transfers from one institution to the other are executed through an interbank payment system.

12. According to the PFMIs,[22] a payment system is a set of instruments, procedures, and rules for the transfer of funds between or among participants; the system includes the participants and the entity operating the arrangement. Payment systems are typically based on an agreement between or among participants and the operator of the arrangement, and the transfer of funds is effected using an agreed-upon operational infrastructure. A payment system is generally categorized as either a retail payment system or a large-value payment system ("LVPS"). A retail payment system is a funds transfer system that typically handles a large volume of relatively low-value payments in such forms as cheques, credit transfers, direct debits and card payment transactions. Retail payment systems may be operated either by the private sector or the public sector, using a multilateral deferred net settlement ("DNS") or a RTGS[23] mechanism.[24] An LVPS is a funds transfer system that

[22] See PFMIs, Section 1.10, p. 9.

[23] An RTGS is a settlement system in which processing and settlement take place on a transaction-by-transaction basis in real time.

[24] The present article will focus on large-value (or systemic) payment systems. For retail payments, until 6 October 2006, LIPS-Net ("Luxembourg Interbank Payment System – Netting System") used to be the national compensation system for domestic cheques and credit transfers. The system started in 1994, as the substitute for a manual clearing house. Domestic and cross-border credit transfers and standing orders are processed in the pan-European system STEP2

typically handles large-value and high-priority payments. In contrast to retail systems, many LVPSs are operated by central banks, using an RTGS – such as TARGET2 – or an equivalent mechanism.

Sub-section 2
TARGET2 in Luxembourg

13. The BCL migrated to TARGET2 on 19 November 2007, date of the migration of TARGET to the "Single Shared Platform", the integrated central technical infrastructure on which TARGET2 is based. The BCL operates TARGET2-LU, the Luxembourgish component of TARGET2, which replaced LIPS-Gross.[25]

14. In TARGET2, only payment orders in euro are accepted. They are either national or cross-border, customer or interbank payments. Their settlement as RTGS is executed (i) one by one – for the gross amount, i.e. the amount mentioned in the payment order –, (ii) in real time and continuously, and (iii) in central bank money – that is to say recorded on the books of the central bank.[26] Payments settled in this way are subject to enforceability and irrevocability rules, in compliance with the November 2009 Law, which implements the SFD.[27] These notions of enforceability and irrevocability have been crucial since they contribute to one of the Eurosystem central banks' objectives: the maintenance of the financial stability. However, since the current legislation thereon is to be further harmonized – and thus further defined – in the upcoming European Commission proposal for a Regulation to introduce

since 9 October 2006. STEP2 is operated by the Euro Banking Association ("EBA") (see www.bcl.lu). These changes take place in the Single Euro Payments Area ("SEPA") framework that the financial sector, which is organized under the European Payments Council ("EPC"), strives to put in place under the aegis of the European Commission and the Eurosystem (see www.sepa.eu for further details).

25 LIPS-Gross ("Luxembourg Interbank Payment System – Gross Settlement") is the real-time gross settlement ("RTGS") system which was operated in Luxembourg from 1999 to 2007 and was a component of TARGET.

26 See also paragraph 16 of this article.

27 Article 111 of the November 2009 Law states that: "A transfer order may not be revoked or challenged any longer by a participant in a system covered by article 108 nor by a third party as from the moment of its entry in the said system." This article also provides that: "The moment of entry of a transfer order into a system covered by article 108 [of the November 2009 Law] shall be defined by the (functioning) rules of the said system." The Luxembourg legislator went beyond the text of article 5 of the SFD, as the Luxembourg implementation measure creates a link between the rule on irrevocability by the participant and third parties and the moment of entry into the system, whereas article 5 of the SFD only states that transfer orders are irrevocable by the participant or third parties, only as from the moment defined by the rules of that system.

common rules for CSDs which is meant to improve their safety and soundness ("CSDR"),[28] these notions will not be analysed in-depth in this article.

Section 2

Central Securities Depositories (CSD) and Securities Settlement Systems (SSS)

Sub-section 1

The notion of CSD[29]

15. CSDs are systemically important infrastructures in modern securities markets. They provide securities accounts, central safekeeping services and asset services, which may include the administration of corporate actions and redemptions, and play an important role in helping to ensure the integrity of securities issues – that means, ensure that securities are not accidentally or fraudulently created or destroyed or their details changed. A CSD can hold securities either in physical form, but immobilized, or in dematerialized form, meaning they only exist as electronic records. The precise activities of a CSD vary, based on jurisdiction and market practices. A CSD may maintain the definitive record of legal ownership for a security; in some cases, however, a separate securities registrar will serve this notary function.

16. CSDs may use, for settlement purposes, commercial bank money – which are commercial bank liabilities that take the form of deposits held at a commercial bank –, or central bank money – which are liabilities of a central bank – in the form of either banknotes or bank deposits held at a central bank, the latter being a safer means to secure payments. Furthermore, a CSD may also operate a securities settlement system or SSS, which is the case for the three Luxembourg CSDs.

Sub-section 2

The notion of SSS[30]

17. A SSS enables securities to be transferred and settled by book-entry according to a set of predetermined multilateral rules. When transfer is against payment, many systems provide delivery versus payment ("DvP"), whereby the settlement mechanism links a securities transfer and a funds

[28] See paragraph 51 of this article.

[29] See PFMIs, section 1.11, p. 8.

[30] See PFMI, section 1.12, p. 8.

transfer in such a way as to ensure that delivery occurs if – and only if – the corresponding payment occurs. Otherwise the delivery of securities is made free-of-payment ("FOP"), i.e. which is not linked to a corresponding transfer of funds. A SSS may be organized to provide additional securities clearing and settlement functions, such as the confirmation of trade and settlement instructions.[31]

Section 3
CSDs operating SSSs in Luxembourg

18. The CSDs operating SSSs in Luxembourg also act as central depositors for securities deposited by counterparties as collateral for monetary policy operations. In addition, these CSDs manage securities deposited by non-resident parties on behalf of other central banks of the ESCB, using the corresponding central bank model ("CCBM"), a mechanism established in 1999 to allow Eurosystem counterparties to make cross-border use of eligible assets.[32] The ECB holds the list of SSSs eligible for the settlement of collateral for Eurosystem credit operations on its website.[33]

Sub-section 1
CBL[34]

19. CBL, which has also a banking licence, acts as a national and international CSD (or ICSD) and operates an international SSS with commercial bank money. CBL was notified as SSS to the European Commission by the BCL in 2001. As LuxCSD will join T2S, CBL will not, as opposed to Clearstream Banking AG in Germany.

Sub-section 2
VP Lux[35]

20. VP Lux was established in 2008 as a CSD in Luxembourg following its notification as new SSS to the European Commission by the BCL. VP Lux,

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31 I.e. a process whereby the terms of a trade or a settlement are verified.

32 For further information in relation to the collateral management in the Eurosystem, see article of E. Simoes Lopes, with the collaboration of L. Schumacher, A. Vasiliu, c. Streiff, "Le régime des garanties de l'Eurosystème", *ALJB*, 2014.

33 www.ecb.int.

34 www.clearstream.com.

35 www.vplux.lu.

which is a fully-owned subsidiary of the Danish CSD "VP Securities Services", offers clearing, deposits and issuing services for Luxemburg and Danish participants. The latter thus have the possibility to issue, within a Eurozone country, securities eligible as collateral for Eurosystem monetary policy operations.[36] VP Lux shall join T2S.

Sub-section 3
LuxCSD[37]

21. LuxCSD is co-owned by Clearstream International SA and the BCL – the latter designated LuxCSD as SSS in October 2011 –, and has been an eligible SSS since February 2013 for the settlement of collateral in the framework of the Eurosystem's credit operations. As a CSD which is co-owned by the BCL, LuxCSD allows market participants to benefit from settling their securities transactions in central bank money, thereby mitigating the risks of settling these transactions with commercial banks. LuxCSD shall join T2S.

Chapter 2
Oversight and assessment of Financial Markets Infrastructures (FMIs) by the Eurosystem

22. One of the fundamental tasks of the Eurosystem central banks is the promotion of the smooth operation of payment systems. This entails the oversight and supervision – or assessment – of the security and efficiency of market infrastructures in the EU, in the light of the potential systemic nature of a system failure for the economy, the implementation of monetary policy, as well as the preservation of financial stability and of public confidence in the currency as a whole. These objectives are crucial during periods of market turbulences when operational reliability and resilience of market infrastructures are essential.[38]

[36] The BCL and the National Bank of Denmark (Danmarks Nationalbank) signed in 2008 a cooperation agreement ("Memorandum of understanding") related to the oversight of the system operated by VP Lux. This agreement defines the cooperation framework between the two central banks, in particular, the aspects related to the coordination and exchange of information between the two authorities.

[37] www.luxcsd.com.

[38] For a practical example of such impact, see BCL 2008 Annual Report (Section 2.7.2, p. 134): "The period of financial turbulences, which started in August 2007 and became more pronounced in 2008 following the bankruptcy of Lehman Brothers, was also challenging for market infrastructures. Some infrastructures had to handle increased volumes of transactions due to the uncer-

Section 1
The obligations pursuant to EU legislation

23. The promotion of the smooth operation of payment systems stems from article 127(2)[39] of the Treaty on the functioning of the European Union (the "TFEU") [ex-article 105(2) of EC Treaty] and articles 3.1[40] and 22 of the Statute of the ESCB and of the ECB (the "ESCB Statute"). Moreover, on the basis of article 22[41] of the ESCB Statute, the ECB and the NCBs may provide facilities and the ECB may make regulations to ensure efficient and sound clearing and payment systems within the Union and with other countries.

24. These provisions thus provide the main legal basis at EU level for the oversight activities by NCBs, exercised in accordance with the common oversight policy framework defined for the Eurosystem by the ECB Governing Council.[42]

Section 2
The obligations pursuant to Luxembourg law

25. In Luxembourg, in order to foster financial stability and maintain confidence of participants and users, a core mission of the BCL imposed by Union and national laws, as member of the ESCB, is thus to contribute to the smooth functioning of payment and securities settlement systems. The BCL oversees systems based in Luxembourg, but also contributes, at Eurosystem level, to the common oversight of SSSs, pursuant to article 2(5) of the Organic Law of the BCL, as amended (the "Organic Law").[43] [44]

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tainty, the high volatility in certain markets and an increased participation in monetary policy operations. Nevertheless, infrastructures showed a strong degree of operational robustness, supporting financial activity in a secure and efficient manner and thus implicitly, the liquidity situation of their participants."

39 "Article 127(2): The basic tasks to be carried out through the ESCB shall be: […] to promote the smooth operation of payment systems."

40 "Article 3.1: In accordance with article 127(2) of the Treaty on the Functioning of the European Union, the basic tasks to be carried out through the ESCB shall be: […] to promote the smooth operation of payment systems."

41 "Article 22 (Clearing and payment systems): The ECB and national central banks may provide facilities, and the ECB may make regulations, to ensure efficient and sound clearing and payment systems within the Union and with other countries."

42 See ECB, Eurosystem Oversight Policy Framework, July 2011 (www.ecb.int and, in particular, regarding the location policy and the regulatory power of the ECB).

43 Luxembourg law of 23 December 1998 concerning the monetary status and the Banque centrale du Luxembourg as modified (first published in the original French version in *Mémorial* A, No. 112 of 24 December 1998, p. 2980).

44 Article 2(5) of the Organic Law mirrors at national level article 22 of the ESCB Statute.

Sub-section 1
The Organic Law of the BCL

26. According to article 2(5) of the Organic Law "[i]n view of its tasks relating to the promotion of the smooth operation of payment systems, the Central Bank shall ensure the efficiency and safety of payment systems and securities settlement systems, as well as the safety of payment instruments. The means of coordination and cooperation employed for the performance of these tasks shall be the subject of agreements between the Central Bank and the *Commission de Surveillance du Secteur Financier* [('CSSF')], respecting the legal competences of the parties".

27. In addition, article 27-3 (Payment systems, securities settlement systems and payment instructions) of the Organic Law states that "[f]or the purpose of performing the tasks set out in article 2(5), the Central Bank may ask payment systems and securities settlement systems to provide any information relating to the operation of those systems which is necessary in order to assess their efficiency and safety and may also ask issuers of payment instruments to provide any information relating to those payment instruments which is necessary in order to assess their safety. The Central Bank shall be authorized to undertake on-site visits in order to collect the information referred to in paragraph 1. It shall coordinate with the [CSSF] to this end".

28. The said articles 2(5) and 27-3 of the Organic Law result from the implementation in the November 2009 Law of the PSD,[45] [46] to which the BCL contributed within a working group established by the Ministry of Finance, replacing the former law dated 12 January 2001 (the "January 2001 Law").[47] Previously, the BCL's competence was limited to the systems in which it participated.[48]

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[45] For the legal regime applicable prior to the implementation of the PSD in Luxembourg law, see T. Kokkola, *Payment And Securities Settlement Systems In The European Union* (aka "Blue book"), Volume 1, Euro Area Countries, European Central Bank, *op. cit.* (esp. the 'Luxembourg' section pp. 285 ff.).

[46] The PSD's goals are to regulate payment services uniformly within the European Union and to create a new category of financial institutions which will benefit from the European passport – the payment institutions. The PSD establishes a uniform legal framework for the achievement of the single Euro payment area (see Single Euro Payment Area project – SEPA – www.sepa.eu). The November 2009 Law also implements Directive 2000/46/EC, dated 18 September 2000, of the European Parliament and the European Council on the taking up, pursuit of and prudential supervision of the business of electronic money institutions.

[47] Luxembourg law published in *Mémorial A*, No. 16 of 6 February 2001, p. 681.

[48] See E. de Lhoneux *et al.*, "La Banque centrale du Luxembourg: présentation juridique", *ALJB*, 2004 (para. 2-55 to 2-57).

29. The previous Luxembourg legislation was enshrined in the law of 5 April 1993 on the financial sector, but was deemed not clear enough to ensure a proper oversight of market infrastructures; the ECB[49] welcomed the amendments in the then draft of the November 2009 Law, by pointing out that "a) they clarify the division of tasks between the CSSF and the BCL as far as payment instruments, payment systems and securities settlement systems are concerned, in line with article [127], paragraph 2, of the Treaty and article 3.1 of the ESCB Statute and b) they broaden the BCL's oversight role to cover all payment and settlement systems, regardless of their designation under Directive 98/26/EC."

30. In addition, the November 2009 Law takes over certain aspects of the SFD, which were previously part of the amended law of 5 April 1993 on the financial sector.

Sub-section 2

The Oversight Regulation of the BCL

31. In addition to the Organic Law, a BCL Regulation in the field of oversight (the "BCL Oversight Regulation") was adopted in 2010 and subsequently amended,[50] thus reinforcing the implementation of one of its core tasks – the promotion of the smooth operation of payment systems and securities settlement systems – in accordance with articles 2(5) and 27-3 of the Organic Law. The BCL Regulation details the BCL's tasks in the area of oversight of payment systems, securities payment systems and payment instruments in Luxembourg, as well as the general framework and the means by which it performs this activity and defines the general duties of the system operators, payment instrument issuers and governance authorities. The BCL Oversight Regulation and its subsequent amendments were published in the *Mémorial*; the consolidated version of the BCL Oversight Regulation is available on the BCL's website.[51]

32. According to the BCL Oversight Regulation, the BCL's oversight includes the system, comprising the operators or the issuers, the participants,

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[49] Opinion of the ECB on the broadening of the Banque centrale du Luxembourg's oversight role by a draft law on payment services, electronic money institutions and settlement finality in payment and securities settlement systems (CON/2009/46), paragraph 3.2.1, p. 3.

[50] Regulation of the "Banque centrale du Luxembourg" 2010/No 6 of 8 September 2010 concerning the oversight of payment systems, securities settlement systems, payment instruments, central counterparties and trade repositories in Luxembourg, consolidated version with the regulations of the "Banque centrale du Luxembourg" 2011/No 10 of 14 July 2011 and 2012/No 11 of 10 July 2012 (www.bcl.lu); which abrogated and replaced the provisions included in circulars BCL 2001/No 163 and 2001/No 168.

[51] www.bcl.lu.

the services, in particular, of operational and technical nature, provided by technical agents or third party entities.

33. In the annexes to the BCL Oversight Regulation, the principles and specific standards adopted by the Eurosystem are listed, upon which the BCL bases its assessment of the functioning of the systems and the instruments subject to its oversight, and in particular, the recently adopted PFMIs. In this context, the operators and issuers shall follow the applicable principles and put in place an organisation, adequate rules and a risk management framework aimed at reducing the risks associated with the system.

Sub-section 3

The Oversight means of the BCL

34. The oversight, which is periodically performed by the BCL in collaboration with the CSSF, is based on information of general, statistical, financial and internal control nature, required on a regular basis from the operators of the systems. The collected information is analysed, followed-up and complemented through regular contacts with the operators. The oversight aims at an assessment of the policies, practices and internal control procedures so as to maintain an adequate level of security and efficiency in the systems. In this respect, a particular focus is put on legal risk, liquidity risk, credit risk, operational risk and governance risk. This national oversight framework is also in line with European and international recommendations, standards and principles,[52] which have been developed over time in order to tackle the various risks inherent to market infrastructures. Different standards have been elaborated by various specialized institutions pursuant to various initiatives ; overseers in the Eurosystem now focus on the recently adopted PFMIs which have also been endorsed by the ECB.[53]

Section 3

The assessment of SSSs and the user standards of the Eurosystem

35. The Eurosystem is concerned about safe and reliable procedures for the use of collateral in monetary policy and credit operations in view of article 18[54]

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52 See annexes of the BCL Oversight Regulation and, in particular, the recent PFMIs.

53 See paragraph 48 of this article.

54 "Article 18 (Open market and credit operations): 18.1. In order to achieve the objectives of the ESCB and to carry out its tasks, the ECB and the national central banks may: […] conduct credit operations with credit institutions and other market participants, with lending being based on adequate collateral."

of the ESCB Statute, which requires that ESCB lending operations must be based on adequate collateral. Indeed, the Eurosystem collateral management services refer to the services/framework via which collateral can be mobilized by eligible counterparties for use in Eurosystem credit operations.[55] This is a crucial role of CSDs in the financing of the economy as almost all the collateral posted by banks to raise funds flows through SSSs operated by CSDs.

Sub-section 1

The common rules applicable to SSSs and links

36. The predecessor of the ECB – the European Monetary Institute ("EMI") – had, to this purpose, published Standards for the use of EU securities settlement systems in ESCB credit operations[56] (the "1998 User Standards"), on which the BCL and the ECB based their supervision of the SSSs via regular assessments. The 1998 User Standards comprised nine standards which are designed to limit the risk to which the Eurosystem is exposed in the handling of its credit operations and, in particular, the collateral provided by its counterparties.

Standard 1 of the 1998 User Standards laid down, *inter alia,* that SSSs and the links between them used by the Eurosystem must have a sound legal basis, ensuring not only that the settlement of payment and securities transfers are enforceable and irrevocable, but also providing for adequate protection of proprietary rights in respect of securities held in the accounts of such systems and through such links.[57]

37. When transferring collateral issued in a CSD or ICSD, counterparties make use of SSSs, which were regularly assessed against the 1998 User Standards (and as of now onwards by the Users Standards as defined below) to determine whether they are eligible for use in the collateralisation of Eurosystem credit operations. It shall be pointed out that several types of links connect SSSs.

38. In September 2013, the ECB published a new "Framework for the assessment of securities settlement systems and links to determine their eligibility

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55 See article of E. Simoes Lopes *et al.*, "Le régime des garanties de l'Eurosystème", *ALJB*, 2014, for further explanation concerning the use of Collateral in the Eurosystem and on the Luxembourg law of 5 August 2005 on the financial collateral arrangement, as amended.

56 Standards for the use of EU securities settlement systems in ESCB credit operation, European Monetary Institute, January 1998 (www.ecb.int / www.ecb.europa.eu/pub/pdf/othemi/sssstandards1998en.pdf).

57 More information on the User Standards and the up-to-date list of eligible SSSs can be found on the ECB's website (www.ecb.int).

for use in Eurosystem credit operations". The document describing the new approach and the assessment questionnaires replace the framework that has been in place since 1998 (the "User Standards").[58]

Sub-section 2

The various types of eligible links (direct and relayed)

39. The links between SSSs shall comply with the User Standards if they are to be used for cross-border securities transfers related to the collateralisation of Eurosystem credit operations. A link between two SSSs consists of a set of procedures and arrangements for the cross-border transfer of securities through book-entry process, that is to say a system which enables transfers of securities and other financial assets which do not involve the physical movement of paper documents or certificates. A link takes the form of an omnibus account, i.e. a securities account on which securities are held that belong to multiple investors, opened by a SSS, called the "investor SSS", in another SSS, called the "issuer SSS".

40. The Governing Council of the ECB periodically assesses links against the standards mentioned on the website of the ECB, pursuant to the methodology for the assessment of links and on the basis of the self-assessment of the relevant SSSs and of reports of the first and second assessor NCBs on the direct link.

§ 1. The direct links (unilateral or bilateral) and the notion of custodian for operated links

41. The link between two SSSs is unilateral when it is used only for the transfer of securities registered in one system to another. A bilateral link between two SSSs means that a single agreement regulates the transfers of securities in both directions. A direct link implies that no intermediary exists between the two SSSs and that the operation of the omnibus account opened by the investor SSS is managed either by the investor SSS or the issuer SSS.

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58 "In recent years, with the development of international and European regulatory and oversight standards for SSSs and CSDs/ICSDs, the Eurosystem has identified opportunities to streamline the user assessment framework by taking into account the outcomes of oversight assessments. By avoiding duplication in the conduct of oversight and user assessments against similar standards and requirements, the user assessments focus on a limited number of concerns and risks that are specific and unique to the Eurosystem user perspective. The new streamlined user assessment framework introduces considerable procedural simplifications, while also continuing to ensure a high level of protection for the Eurosystem against losses in the conduct of its credit operations" (See press release of the ECB dated 27 September 2013).

42. In an operated direct link, a custodian, i.e. an agent with the primary role of recording direct or indirect holdings of securities and acting as a registrar, is a third party in possession of the certificates that represents ownership, either in physical or electronic form, opens and operates an account in the issuer SSS on behalf of the investor SSS. The responsibility for the obligations and liabilities in connection with the registration, transfers and the custody of securities must however remain legally enforceable only between the two SSSs.

§ 2. The relayed links

43. Relayed links are contractual and technical arrangements for the transfer of securities involving at least three SSSs : the "investor SSS", the "issuer SSS" and the "intermediary SSS." In order to be eligible for assessment, a relayed link must be composed of two direct links that have already been assessed separately against the standards and found to be compliant. The methodology used for assessing relayed links is therefore based on the methodology used for assessing direct links and deals only with the specific conditions associated with relayed links.[59]

Sub-section 3
The nature of entitlement

44. A fundamental issue in the assessments is the nature of entitlement. As a professional custodian[60] of financial instruments, a CSD is an account keeper within the meaning of article 2 of the Luxembourg law of 1 August 2001 relating to the circulation of securities, as amended,[61] in particular, by the law of 6 April 2013 relating to the dematerialized securities[62] (the "August 2001 Law"). As a consequence, the participants of a CSD have, according to the number of securities entered in its securities account, a right *in rem*, i.e. a right of property against others, of an intangible – not physical – nature, over all the securities of the same description kept in the account by a CSD.[63] This right *in rem* may only be enforced by the participant against the CSD.

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59 The Governing Council of the European Central Bank decided in January 2005 that relayed links may be used in the collateralisation of the credit operations of the Eurosystem, but only after an assessment has been carried out against the Eurosystem's standards to ensure that the conditions set by the Governing Council have been met.

60 A custodian is an entity, often a credit institution, which provides securities custody services to its customers (*cf.* a depository).

61 Luxembourg law published in *Mémorial A*, No. 102 of 20 August 2001, p. 2036.

62 Luxembourg law published in *Mémorial A*, No. 71 of 15 April 2013, p. 890.

63 Article 3 of the August 2001 Law.

45. The securities received by deposit or held in a securities account with a CSD with no indication of numbers or individual identification information are treated as fungible – that is to say interchangeable.[64] Acquisition of securities by the account holder derives from the entry of these securities to the credit of his securities account.[65] In line with the provisions of the August 2001 Law, such securities form part of the global pool of securities held for the joint benefit of all participants of a CSD and each participant of the SSS holds a "co-ownership" interest in this global pool of securities.

Section 4

The development of standards/principles and EU legislation for FMIs

46. In order to tackle risks that may threaten the financial system, the market infrastructures shall be organized according to principles ; the primary purpose of which is to ensure their security. Such principles have been enshrined in Union law and also developed by the Committee on Payment and Settlement Systems ("CPSS"), a committee of the Bank of International Settlement ("BIS"), and the Technical Committee of the International Organization of Securities Commissions ("IOSCO"), which are specialized committees that have been working intensively in the field of settlement over the past decade.

Sub-section 1

The international principles of CPSS-IOSCO

47. CPSS and IOSCO issued the PFMIs in April 2012, and the related Disclosure framework and Assessment methodology in December 2012.[66] The PFMIs replace the three sets of principles and recommendations previously published, namely : the Core principles for systematically important payment systems ("CPSIPS") of 2001, the Recommendations for the securities settlement systems ("RSSS") of 2001 and the Recommendations for central counterparties ("RCCP") of 2004.[67]

64 Article 1(3) of the August 2001 Law.

65 Article 4(1) of the August 2001 Law.

66 *Principles For Financial Market Infrastructures ("PFMIs")* by the Committee on Payment and Settlement Systems (CPSS) and Technical Committee of the International Organization of Securities Commissions (IOSCO), April 2012 ; *Disclosure Framework And Assessment Methodology*, December 2012 ; available on the Bank of International Settlement (BIS) website (www.bis.org) and the IOSCO website (www.iosco.org).

67 See also the BIS website (www.bis.org) and the IOSCO website (www.iosco.org).

48. The PFMIs are designed to ensure that the infrastructure supporting global financial markets is robust and thus placed to withstand financial shocks. They apply to all systematically important payment systems ("SIPS"), CSDs, SSSs, CCPs and TRs. The FMIs collectively clear, settle and record transactions in financial markets. These revised standards provide important support for the G20 strategy to make the financial system more resilient by making central clearing of standardized OTC derivatives mandatory. The FMIs were expected to observe the PFMIs as soon as possible, whereas CPSS and IOSCO members strived to adopt the new standards by the end of 2012.[68]

49. The main public policy objectives of the CPSS and the Technical Committee of IOSCO in setting forth these principles for FMIs are to enhance safety and efficiency in payment, clearing, settlement and recording arrangements, and, more broadly, to limit systemic risk and foster transparency and financial stability. Indeed, poorly designed and operated FMIs can contribute to and exacerbate systemic crises if the risks of these systems are not adequately managed and, as a result, financial shocks could be passed from one participant, or FMI, to others. The effects of such a disruption could extend well beyond the FMIs and their participants, threatening the stability of domestic and international financial markets and the broader economy, due to their systemic nature. In contrast, robust FMIs have been shown to be an important source of strength in financial markets, giving market participants the confidence to fulfil their obligations on time, even in periods of market stress.

Sub-section 2
The evolution of EU legislation

50. In order to deal with the increasing importance of market infrastructures, and in view of the barriers to cross-border clearing and settlement

[68] The BCL adopted the PFMIs in July 2012 as an appendix to Regulation of the "Banque centrale du Luxembourg" 2010/6 of 8 September 2010 concerning the oversight of payment systems, securities settlement systems, payment instruments, central counterparties and trade repositories in Luxembourg, consolidated version with the regulations of the "Banque centrale du Luxembourg" 2011/10 of 14 July 2011 and 2012/No 11 of 10 July 2012 (www.bcl.lu); the Governing Council of the ECB adopted the PFMIs on 3 June 2013 (for the conduct of Eurosystem oversight in relation to all types of FMIs and published thereafter on its website – for consultation – a draft Regulation on oversight requirements for systematically important payment systems, in order to implement the PFMIs in a legally binding way).

identified in several reports, such as the Giovannini reports,[69] the European Commission has taken the lead over the past few years to regulate this industry via directives such as the PSD or the SFD. However, in the wake of the financial crisis, new proposals to further regulate the financial markets were launched and led to new legal instruments such as EMIR. In view of the issues raised after the implementation of the PSD or SFD, the European Commission has lately been more willing to propose legal instruments, which are directly applicable, namely EU regulations.

51. Even if these instruments, which are directly applicable, ensure harmonisation, they entail long negotiation procedures and discussions. Indeed, many technical concepts have to be defined in these instruments and the Members States may have conflicting views on matters related to settlement. This is the case with the European Commission proposal for a Regulation to introduce common rules for CSDs which is meant to improve their safety and soundness ("CSDR")[70]. The CSDR initiative is meant to be an important part of the European Commission's agenda to enhance the safety and soundness of the financial system. Together with EMIR – the Regulation on "OTC derivatives, central counterparties and trade repositories" that entered into force on 16 August 2012 and the Markets in Financial Instruments Directive (or MiFID) –, the CSDR shall form a framework in which FMIs are subject to common rules at a European level.[71] However, it shall later be assessed whether the multiplication of principles, standards, directives and regulations will finally cover all risks pertaining to FMIs and ensure a harmonized oversight and supervision, with a view to protect the financial markets and ultimately the retail investors.

[69] The Giovannini Group, Cross-Border Clearing and Settlement Arrangements in the EU ("First Giovannini Report"), November 2001 and 2nd Report on EU Clearing and Settlement Arrangements ("Second Giovannini Report"), April 2003; COM(2004) 312 final, 28 April 2004; Solutions to Legal Barriers related to Post-Trading within the EU – Second Advice of the Legal Certainty Group, August 2008 (www.ec.europa.eu).

[70] On 7 March 2012, the Commission adopted a "proposal for a Regulation on improving securities settlement in the European Union and on central securities depositories (CSDs) and amending Directive 98/26/EC". The Commission's proposal is as of mid-2013 still under consideration by the European Parliament and the Council.

[71] In parallel to the proposal made on recovery and resolution for banks, the European Commission is working on a possible broader framework for crisis management of systemic financial institutions other than banks, with a focus on CCPs and CSDs, in particular (the European Commission is involved in the international work-stream conducted on these issues, mainly by the G10 CPSS and IOSCO) (see www.ec.europa.eu).

Chapter 3
TARGET2-Securities (T2S) project of the Eurosystem

52. T2S is the securities settlement single platform which is being developed at Eurosystem level. It shall have a big impact on the post-trading landscape in Europe. It shall provide commoditized and harmonized DvP settlement in central bank money for securities transactions in euro and other currencies. T2S shall bring securities and dedicated cash accounts together on one technical platform for real-time gross settlement[72] and shall enable the use of the key legal concept of "autocollateralisation".[73]

53. Once T2S enters into operation in 2015, a single set of rules, standards and tariffs shall be applied to all transactions across all T2S markets. T2S shall thus help to overcome the complexity and fragmentation of the current European market infrastructure, composed of over thirty different securities settlement systems. T2S shall be neutral with respect to all countries and market infrastructures and all business models adopted by CSDs and market participants.

54. As a large number of stakeholders will therefore be affected by T2S, the Eurosystem has decided to build the platform in a transparent manner, involving all stakeholders to the highest extent possible. Given the international nature of the settlement services to be proposed by T2S to infrastructures based in and outside the euro area, a cooperative oversight framework will be set up regrouping the prudential supervisors and the central banks which are competent in this field, such as the BCL.

55. T2S is to be a service offered to CSDs and not a CSD itself. The mutual rights and obligations of the Eurosystem and CSDs relating to the use of the T2S settlement platform have been defined in the T2S Framework Agreement.

Section 1
The Framework Agreement

56. Following negotiations, the ECB and the European CSDs involved concluded the Framework Agreement, the contract which governs the legal

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[72] See Guideline of the European Central Bank of 21 April 2010 on TARGET2-Securities (ECB/2010/2).

[73] See article of E. Simoes Lopes *et al.*, "Le régime des garanties de l'Eurosystème", *ALJB,* 2014, for further explanation on the concept of "autocollateralisation".

relationship between the Eurosystem and each CSD participating in T2S.[74] The Framework Agreement regulates the scope of the control CSDs shall have over the IT functions outsourced to the Eurosystem, as well as issues such as liability, protection of intellectual property rights and confidentiality.[75]

Section 2
The impact of T2S on the participating CSDs

57. CSDs which have agreed to participate in T2S,[76] by signing the Framework agreement, will move their securities accounts to the T2S platform for settlement purposes. On these accounts, CSDs will hold all of their clients' securities positions for settlements. Similarly, T2S will maintain dedicated central bank money accounts for CSD customers through the national central bank chosen by the customer. Holding both securities and cash accounts on the platform will ensure DvP in real-time. CSDs, along with NCBs, have prepared their detailed feasibility assessments for T2S to adapt their IT systems and processes to T2S according to the T2S plan.

58. The CSDs will move their securities accounts to T2S for technical record-keeping and processing of settlement. However, they will remain the legal owners of these accounts and will be legally responsible for customer relations.

Section 3
The impact of T2S on banks

59. T2S will open up the European securities market for banks, making it more efficient and easily accessible. Benefits for market participants will range from the significant reduction of settlement fees for domestic and, above all, cross-border transactions, to the possibility to cut back-office costs by stream-

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74 All the documentation relating to T2S such as the Framework Agreement is available on www.t2s.eu.

75 The T2S Framework Agreement is comprised of the main document that contains all of the contractual provisions (the "core Framework Agreement") and the more technical and operational schedules that are annexed to the agreement and form an integral part thereof. The schedules cover, *inter alia*, the T2S programme plan, user testing, user migration, the Service Level Agreement, governance, change management, pricing and exit management. Each CSD shall enter into a separate but identical Framework Agreement with the Eurosystem, represented by the relevant national central bank or by the ECB (in the case of non-euro area CSDs).

76 As of mid-2013, the Luxembourg CSDs which have signed the Framework Agreement and thus will be participating in T2S are VP Lux S.à r.l. and LuxCSD SA.

lining interfaces and centralizing settlement activity. T2S will also lead to efficiency gains, enabling the banks to optimize their collateral and liquidity management. Moreover, T2S will provide new business opportunities for European banks and grant them access to new markets for asset-servicing.

60. Further benefits for the European banking community will derive from the harmonisation of market practices brought about and fostered by T2S. To ensure that T2S meets their needs, banks have been involved in the project since its very inception. In particular, they substantially contributed to the definition of the T2S User Requirements. In terms of project governance, banks are represented both at the European level, in the T2S Advisory Group and its substructures, and at the national level, in the National User Groups ("NUGs"). Via the NUGs, banks can actively contribute to the T2S project and respond to market consultations. Banks are constantly kept updated about T2S and are directly involved in the discussions through the T2S Info Sessions, the T2S "Technical Dialogues" and other events and workshops organized by the ECB and open to all interested stakeholders.

61. In T2S, all banks will maintain their business and legal relationships with the respective CSDs and will be able to settle all transactions through potentially one single CSD, with a consequent optimisation of systems and resources.

62. From a technical perspective, banks will also be offered the possibility, in agreement with their CSD, to become directly connected participants in T2S, i.e. to establish a direct network connection to the platform.

Section 4

The role of national central banks (NCBs)

Sub-section 1

The NCBs of the Eurosystem

63. The Eurosystem is the owner of T2S and will operate it on a non-profit basis to the benefit of all European market participants. The Eurosystem central banks are therefore key stakeholders in the project.

64. The central banks of the euro area will also be users of the services offered by T2S, as well as those non-euro central banks that decide to settle their currency in T2S. The NCBs will hold central bank money accounts for CSD customers on the T2S platform, so that the DvP settlement of securities transactions will exclusively take place in central bank money. These accounts

will be dedicated to settlement purposes only and will be linked to the cash accounts in the respective RTGS systems. For the settlement in euro, for instance, the T2S platform will be linked to the TARGET2 system, also operated by the Eurosystem.[77]

Sub-section 2

The participation of other currencies

65. T2S has been designed as a multi-currency system, performing central bank money settlement of securities transactions[78] not only in euro but also against other currencies. This is important to ensure that the market can maximize the benefits that T2S will bring from integrating settlement not only in the euro area but across the whole of the EU and beyond.

66. Those non-euro central banks that had expressed an interest in taking their currency in T2S were involved in thorough negotiations concerning terms and conditions of their participation. The contractual basis for their participation in T2S is defined in the Currency Participation Agreement, which was finalized in February 2012. Together with the Level2-Level3 Agreement and the Framework Agreement, this contract forms the final pillar of the main legal construction of T2S.

67. The National Bank of Denmark (Danmarks Nationalbank) signed the Currency Participation Agreement on 20 June 2012 and will make the Danish krone available in T2S in 2018. The other non-euro central banks that have taken part in the negotiations over the Currency Participation Agreement have decided not to join T2S for the time being.[79] Some of them have expressed an interest in joining at a later stage, as soon as their markets are ready.

68. Those non-euro area NCBs that sign the Currency Participation Agreement will be involved in the governance of the project, which ensures that NCBs retain control over their currency.

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[77] NCBs, along with CSDs, have prepared their detailed feasibility assessments for T2S to adapt their IT systems and processes to T2S and to do so according to the T2S plan. The assessments were conducted on the basis of the technical documentation provided by the Eurosystem, in particular, version 1.2 of the T2S User Detailed Functional Specifications, which was released in October 2011. As well as holding the cash accounts of CSD customers, some of the participating NCBs also offer CSD services themselves.

[78] See also paragraph 16 of this article.

[79] As of mid-2013.

Section 5

The involvement of other stakeholders and other post-trade harmonisation

Sub-section 1

The regulators

69. T2S will lead to a re-shaping of the European post-trading infrastructure, with the CSDs transferring their settlement activity to T2S. This process is closely followed by national regulators, and especially by ESMA, which participates in the T2S Advisory Group.

Sub-section 2

The European Commission and the other harmonisation initiatives

70. The European Commission has followed closely the progress of T2S by participating in the T2S Advisory Group, especially since T2S is viewed as having the potential to strengthen and integrate the European securities markets and thus foster economic growth.

71. The CSDR proposal, the aim of which is to enhance and harmonize the regulatory and operational framework of CSDs as well as of securities settlement in the EU, is a legal act which is of key interest to the T2S Programme as it grants CSDs the opportunity to outsource their settlement services to T2S and focuses on the safety and efficiency of their cross-border settlement activity. Furthermore, the provisions on market access and interoperability serve to improve the competitive environment within which CSDs and market participants will operate in T2S. The timely implementation of the CSDR and the relevant regulators' technical standards – so-called "level 2 legislation" – ahead of the T2S go-live date will help to ensure a level playing field among market participants.

72. Post-trade harmonisation is a key objective of T2S, supported by the T2S Community, the Governing Council of the ECB and EU public authorities. Progress in the harmonisation agenda will enable T2S to realize its full potential to benefit the European market, in terms of efficiency and level playing field. The objectives of T2S harmonisation are (i) to foster the creation of a single rule book for post-trade processes in the T2S Community and (ii) to protect the "lean T2S" concept, i.e. the exclusion of national specificities from the T2S operational blueprint, and to contribute to financial integration in Europe.

73. Post-trade harmonisation is an important component of the EU financial integration process. The integrated infrastructure provided by T2S will

bring about technical and operational harmonisation – which is a key ingredient for the creation of a single market for settlement services in Europe. It shall complement the legal and regulatory harmonisation agenda currently pursued by EU legislators.

Conclusion

74. Although market infrastructures performed relatively well during the financial crisis that started in 2007-2008, events and experience highlighted important lessons for effective risk management.

75. The safety and efficiency of the arrangements required to finalize securities transactions, and thus the rules regarding clearing and settlement, were already a crucial element of the Financial Services Action Plan launched in 1999,[80] which aimed to create an integrated and efficient European capital market. The said arrangements, largely invisible to the retail investor, lie at the core of all securities markets and are indispensable for their proper functioning.[81]

76. The legal framework regulating market infrastructures in the EU and the Eurosystem, in particular, have to be further developed, especially following commitments of the G20 governments. Indeed, in a globalized world where insolvencies of market participants are looming, the tightening of the rules protecting market participants has become of utmost importance, and entails an adaptation of the legislation at EU level in order to improve the transparency and security of operations. Following several reports[82] and legislation such as the PSD, the SFD and EMIR, the proposal for a Securities Law Legislation ("SLL") but also the CSDR proposal endeavour to regulate further market infrastructures of systemic importance which may threaten the financial markets, so as to improve the security of settlements and prevent credit and liquidity risks. These initiatives are necessary complements to EMIR which has recently tightened the legislation with respect to derivatives. Moreover, it shall be underlined that the recent PFMIs have also to be taken into account in the new proposals to harmonize the legislation of market infrastructures.

[80] See dedicated section on www.ec.europa.eu.

[81] Communication from the Commission to the Council and the European Parliament, Clearing and Settlement in the European Union – The way forward, Brussels, 28 April 2004, COM (2004) 312 final.

[82] See, in particular, the Giovannini reports referred to in paragraph 50 of this article.

77. The SLL proposal is still under discussion, due to the fact that this proposal deals with the harmonisation of the determination of models of sensitive subjects, such as conflict of law rules or the holding and ownership of securities concepts. The SLL proposal should clarify, in particular, that there is only one person who can own securities at a time and that only a uniform conflict of law rule could ensure that there is always one substantive law in the EU that addresses "who owns what". Such issues are to be agreed between the European Commission, the Members States and other stakeholders; however a consensus on these matters seems to be difficult to reach.[83]

78. In the same vein as the SLL, the CSDR proposal is the object of lengthy negotiations, especially since the proposal touches upon sensitive aspects, such as the harmonisation of settlement periods or the creation of penalties for market participants that fail to deliver their securities on the agreed settlement date and an obligation to buy those securities in the market and deliver them to their counterparties. It is also suggested that issuers and investors shall be required to keep an electronic record for virtually all securities, and to record them in CSDs if they are traded on stock exchanges or other regulated markets. Moreover, CSDs would have to comply with strict organisational, conduct of business and prudential requirements to ensure their viability and the protection of their users. An interesting feature of the CSDR proposal is that it is planned that authorized CSDs will be granted a "passport" to provide their services in other Member States; a CSD in the EU would have access to any other EU CSDs or other market infrastructures, such as trading venues or CCPs, whichever EU country they are based in. Other aspects, such as potential harmonisation regarding enforceability and irrevocability, and their impact on national legislation and the moment of entry, shall also be closely followed.[84]

79. Finally, the discussions on the SLL and CSDR proposals shall be also of relevance in the context of T2S, since the former proposals are bound to have an impact on the market infrastructures participating in the project, particularly with regard to the notions of links, enforceability and irrevocability. A comprehensive analysis of the legislation applicable to market infrastructures will thus be of utmost interest, especially for CSDs, once the SLL and CSDR are enacted and above all in the T2S context that sees a growing number of participants at the European scale.

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[83] See summary of the meeting of the Member States Working Group on Securities Law Legislation, Brussels, 19 November 2012 (www.ec.europa.eu).

[84] See paragraph 14 of this article.

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