Settlement Discipline: Frequently Asked Questions

December 2019
## Definitions and Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td><strong>BNY Mellon</strong></td>
<td>This is the corporate brand of The Bank of New York Mellon Corporation and may be used as a generic term to reference the corporation as a whole and/or its various subsidiaries generally</td>
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<tr>
<td><strong>RTS</strong></td>
<td>Regulatory Technical Standards</td>
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<tr>
<td><strong>ISD</strong></td>
<td>Intended Settlement Date</td>
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<td><strong>RTP</strong></td>
<td>Receiving Trading Party</td>
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<td><strong>FTP</strong></td>
<td>Failing Trading Party</td>
</tr>
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<td><strong>LMFP</strong></td>
<td>Late Matching Fail Penalty</td>
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<td><strong>SEFP</strong></td>
<td>Settlement Fail Penalty</td>
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<tr>
<td><strong>SFT</strong></td>
<td>Securities Financing Transaction</td>
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<tr>
<td><strong>CSD</strong></td>
<td>Central Securities Depository</td>
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<td><strong>CCP</strong></td>
<td>Central Counterparty</td>
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<tr>
<td><strong>EEA</strong></td>
<td>European Economic Area covers the European Union and the three additional countries of Norway, Liechtenstein, and Iceland</td>
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<td><strong>ESMA</strong></td>
<td>European Securities and Markets Authority</td>
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Background Information

On 13 September 2018, a delegated regulation setting out regulatory technical standards on settlement discipline, was published in the Official Journal of the European Union (EU). Under the current timetable, this delegated regulation will enter into force on 13 September 2020.

The CSDR rules on the settlement discipline regime introduce a number of measures to prevent settlement fails by ensuring that all transaction details are provided to facilitate settlement, as well as further incentivising timely settlement by cash penalty fines and buy-ins. In addition, CSDs are required to provide functionality to participants to ensure harmonisation and automation of settlement processes across all European Economic Area markets to improve settlement efficiency.

This document seeks to address the FAQ’s being asked by clients in order to assist their understanding of the CSDR settlement discipline regime, how it will impact them and how BNY Mellon is responding.

Further information on CSDR can be found on the BNY Mellon website.

- What is the Central Securities Depositories Regulation (CSDR) settlement discipline regime?
  The CSDR settlement discipline regime covers two main sets of measures:
  a. measures to prevent settlement fails by improving matching and settlement rates, and
  b. measures to address settlement fails: cash penalties and mandatory buy-ins.

- Who is affected by CSDR settlement discipline regime?
  All parties in the settlement chain involved in transactions in European securities will be affected by the settlement discipline regime, including where the trading parties are not located in the European Economic Area (EEA). The regulatory obligations will affect both the receiving and delivering parties in a given failing transaction.

- When will the settlement discipline regime enter into force?
  Under the current official timetable, the new settlement discipline regime will take effect on 13 September 2020. It is, however, expected that the European authorities will shortly announce a new starting date of November 2020 or possibly January 2021. The reason of the delay is due to the November 2020 SWIFT release, on which CSDs have a dependency for facilitating the cash penalty reporting and payments, and the delivery in November 2020 of a centralised penalty calculation mechanism for CSDs using TARGET2-Securities. The decision to delay beyond September is within the European Commission’s remit.

Measures to prevent settlement fails

Written allocations and confirmations:

1. What does the regulation require?

   The regulation sets out detailed rules relating to the message flows between an investment firm (typically, a broker) and its client, once an investment firm has executed a trade on behalf of its client. The regulation requires that the investment firm include these rules in the contractual arrangements with its client.

   Once the investment firm has sent the confirmation of the execution to a professional client, the client is obliged to confirm its acceptance of the terms of the transaction. The client is also obliged to send to the investment firm a set of specific details relating to the allocations of securities or of cash. The client is obliged to send both these messages by a specific deadline (see below for details). The client can combine both messages in a single message.

   Investment firms shall confirm receipt of the confirmation and allocation messages within two hours of receipt.

   Investment firms are under the obligation to offer their professional clients the option of sending the confirmation and allocation messages electronically using international communication standards.
What is the impact to clients?

Professional clients will need to ensure that they provide the investment firm with the confirmation message, and with all required information in an allocation message within specified timeframes. The investment firm should receive the confirmation and allocation messages by close of business on the business day that the transaction took place. If the two parties are in time zones with more than a 2 hour difference, or if the order has been executed after 18:00 CET, then there is an extension of the deadline until 12:00 CET on the following business day.

Any contractual agreements between a professional client and BNY Mellon as an investment firm, must include the communication requirements of the confirmation and allocation messages, the information to be provided, what method of communication will be used, and the timeframes by which messages should be sent.

How will BNY Mellon support?

Where BNY Mellon acts as an investment firm, we will provide a confirmation to the professional client where required, and offer clients the option of sending via an electronic messaging method.

Matching and population of settlement instructions

2. What does the regulation require?

CSDs are required to provide functionality to participants with fully automated, continuous real-time matching of settlement instructions.

CSDs require their participants to populate additional fields in their settlement instructions and have made the following changes:

i. Transaction type:

The transaction type will now become mandatory on settlement instructions to CSDs.

The transaction type field is the Type of Settlement Transaction Indicator (SETR) on SWIFT settlement instruction messages.

| 22F | :41c(8c)/41c | :(Qualifier)/((Data Source Scheme))/(Indicator) | :SETR//TRAD |

ii. Place of Trade and Place of Clearing:

In some instances CSDs will also require participants to instruct the place of trade, and the place of clearing.

The place of trade will be used to derive the correct cash penalty rate for the relevant financial instrument for Small Medium Enterprise (SME) growth markets. If clients do not notify this, then they may be subject to receive a higher cash penalty, as CSDs will default the transactions as not having been executed on a trading venue.

The place of clearing is used to identify if the transaction was cleared through a central counterparty (CCP). Depending on the outcome of current discussions with ESMA, this may be used to identify who is responsible to manage the collection and distribution of cash penalties (the CSD or the CCP).

What is the impact to clients?

Clients will need to ensure that they instruct all relevant details necessary as this could affect whether their transactions settle on time and are subject to settlement discipline penalty or buy-in. The Transaction Type should always be populated, and we recommend that the Place of Trade field is also populated as a matter of good practice. The Place of Clearing should be completed for transactions settling with a CCP.

How will BNY Mellon support?

BNY Mellon is making changes to its SWIFT MT54x settlement instruction message processing to enable clients to instruct these fields.

BNY Mellon will provide further information on whether fields are mandatory and/or matching as the market infrastructure makes this available.
CSD functionality to assist matching and settlement

3. Tolerance matching – what does the regulation require?

CSDs will need to have a functionality to allow matching even if the cash amounts on the two settlement instructions differ. In such a case, matching will occur providing that the difference in cash amounts is not greater than a standard tolerance level. There will be two bands of tolerance:

- EUR 2 for up to EUR 100,000 or currency equivalent
- EUR 25 for over 100,000 or currency equivalent

Any settlement instructions with a broker cash amount above these tolerances will not match until one party amends their instruction to within the tolerance level.

What is the impact to clients?

Clients will not need to make any changes to their existing settlement instruction process.

How will BNY Mellon support?

BNY Mellon already supports the matching process and any mismatches will be notified to clients through their existing settlement status messaging.

4. Bilateral cancellation – what does the regulation require?

CSDs are obliged to operate a bilateral cancellation facility that requires participants to bilaterally cancel matched settlement instructions.

Most EU/EEA CSDs currently operate with bilateral cancellation and those remaining unilateral cancellation markets will be updated to follow the new process.

What is the impact to clients?

Clients will need to ensure that both parties to a matched settlement instruction will need to instruct a cancellation of the settlement instruction in order to prevent the transaction from settling.

How will BNY Mellon support?

BNY Mellon already supports bilateral cancellation. BNY Mellon will send out a communication to clients if there are any market changes.

5. Hold and release – what does the regulation require?

CSDs must provide a hold and release mechanism to facilitate blocking pending instructions from settling, as well as the capability to release pending settlement instructions that are blocked and therefore allowing them to settle.

The regulation also requires Failing Trading Parties to use the hold and release mechanism when settlement instructions are subject to buy-ins (see also question 35).

What is the impact to clients?

Clients will need to request BNY Mellon to place all delivery instructions on hold upon receipt of a buy-in notification from the Receiving Trading Party (RTP).

How will BNY Mellon support?

BNY Mellon will provide the ability for clients to request a settlement instruction that is subject to a buy-in to be placed on hold or release from hold via SWIFT MT530 or NEXEN.

BNY Mellon will provide further details to clients of the SWIFT messaging formats and fields that will be required once the information has been published.
6. Partial settlement – what does the regulation require?

CSDs are required to provide participants with functionality to partially settle transactions. Early partial settlement (between intended settlement date (ISD) and buy-in deadline date -1) can reduce the penalty fines payable by the delivering party.

On the deadline date of the buy-in extension period (e.g. ISD +4 for liquid securities) the regulation states that any available stock must be used to partially settle, unless the settlement instruction is on hold.

What is the impact to clients?

BNY Mellon is expanding its partial settlement service to enable clients to maximise settlement of their transactions as detailed below. This is in line with industry working group, e.g. AFME, recommendations on the use of partial settlement.

How will BNY Mellon support?

BNY Mellon currently defaults all T2S market instructions not to partially settle, however we do offer clients with the ability to instruct partial settlement. Partial settlement can occur on all CREST (Euroclear UK and Ireland CSD) settlement instructions. For all other markets where partial settlement can occur, including through BNY Mellon’s sub-custodian network, we do not currently automate partial settlement. Clients can instruct the settlement transaction condition indicator to partial or non-partial where the market allows. If a transaction is placed on hold then partial settlement will not occur.

BNY Mellon’s service will be expanded to allow partial settlement at all EU/EEA markets for all instructions (receipts and deliveries), unless the instruction is place on hold.

BNY Mellon will also introduce partial release functionality on deliveries from omnibus accounts, which will be driven by the position control process within BNY Mellon’s settlement system application.

7. Settlement instruction status update reporting – what does the regulation require?

CSDs are required to provide participants with access to real-time information on the status of their settlement instructions. CSDs must also offer participants either a minimum of three settlement batches spread across the business day or real-time gross settlement throughout the business day.

What is the impact to clients?

Clients will not need to make any changes to their existing settlement instruction process.

How will BNY Mellon support?

BNY Mellon already supports real-time settlement status messaging to clients, so there will not be any impact on clients.

8. Consistent and systematic failure to deliver securities – what does the regulation require?

CSDs will need to identify the criteria by which a participant is deemed to be a consistent offender of late matching and settlement failure. CSDs will need to establish a system that enables them to monitor the number and value of settlement fails over a period covering 10% of days of activity during the course of a year.

If settlement efficiency falls below 15% of that securities settlement system, then a participant will be deemed to be a consistent offender. Working arrangements will be set up with participants who cause high levels of settlement fails within the CSD.

What is the impact to clients?

Clients should monitor their fails to ensure that they maintain a high settlement rate.

How will BNY Mellon support?

BNY Mellon can provide Management Information Statistics (MIS) on settlement rates to support client oversight management of their fails, and help clients identify their settlement fails through fail management reporting. For further details, please contact your relationship manager.
Measures to address settlement fails

I. Cash Penalties – general information

9. What does the regulation require?

CSDs are required to establish penalty mechanisms for late matching and failed settlement and will debit failing CSD participants and credit the non-failing CSD participant.

10. Which type of instructions will be subject to cash penalties?

All settlement instructions, free or against payment, settling at a EU/EEA CSD, which are matched on or after their Intended Settlement Date (ISD), and failing to settle on and after their ISD.

11. Which type of instructions are not subject to cash penalties?

- Redemptions (i.e. REDM);
- Corporate actions on stock (i.e. CORP);
- Technical instructions (e.g. T2S automatic realignments)

12. What are the types of cash penalties?

   a. _Late Matching Fail Penalty (LMFP)_; penalty that applies due to the matching taking place after the ISD.
   b. _Settlement Fail Penalty (SEFP)_; penalty that applies due to the non-settlement of a matched transaction on or after its ISD.

13. What instruments are in-scope for cash penalties?

All transferable securities are in scope where admitted for trading or traded on an EU/EEA trading venue or Cleared by an EU/EEA CCP as follows:

   i. transferable securities as defined in point (a) of Article 4(1)(44) of Directive 2014/65/EU;
   ii. sovereign debt as defined in Article 4(1)(61) of Directive 2014/65/EU;
   iii. transferable securities as defined in point (b) of Article 4(1)(44) of Directive 2014/65/EU, other than sovereign debt referred to in point (ii);
   iv. transferable securities as defined in point (c) of Article 4(1)(44) of Directive 2014/65/EU;
   v. exchange-traded funds (ETFs);
   vi. units in collective investment undertakings, other than ETFs;
   vii. money-market instruments, other than sovereign debt referred to in point (ii);
   viii. emission allowances;
   ix. other financial instruments

14. What is the difference between a late matched and settlement fail trade?

A late matched trade is any trade settling at an EU/EEA CSD that matches after intended settlement date. The last party to match the trade, post settlement date, is liable for the late matching fail penalty.

A settlement fail is any matched trade settling at an EU/EEA CSD that has not settled on the intended settlement date (ISD) where the reason for failure is either due to a lack of securities or cash.

15. What are the Settlement fail cash penalty rates?

The daily cash penalty rates use the basis points in the following table:
<table>
<thead>
<tr>
<th>Reason for failure</th>
<th>Type of Security</th>
<th>Rate</th>
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<tbody>
<tr>
<td>1.</td>
<td>Settlement fail due to a lack of shares that have a liquid market within the</td>
<td>1.0 bps</td>
</tr>
<tr>
<td></td>
<td>meaning of point (b) of Article 2(1)(17) of Regulation (EU) No 600/2014,</td>
<td></td>
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<tr>
<td></td>
<td>excluding shares referred to in point 3</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Settlement fail due to a lack of shares that do not have a liquid market within</td>
<td>0.5 bps</td>
</tr>
<tr>
<td></td>
<td>the meaning of point (b) of Article 2(1)(17) of Regulation (EU) No 600/2014,</td>
<td></td>
</tr>
<tr>
<td></td>
<td>excluding shares referred to in point 3</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Settlement fail due to a lack of financial instruments traded on SME growth</td>
<td>0.25 bps</td>
</tr>
<tr>
<td></td>
<td>markets, excluding debt instruments referred to in point 6</td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Settlement fail due to a lack of debt instruments issued or guaranteed by:</td>
<td>0.10 bps</td>
</tr>
<tr>
<td></td>
<td>a. a sovereign issuer as defined in Article 4(1)(60) of Directive 2014/65/EU;</td>
<td></td>
</tr>
<tr>
<td></td>
<td>b. a third country sovereign issuer;</td>
<td></td>
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<tr>
<td></td>
<td>c. a local government authority;</td>
<td></td>
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<tr>
<td></td>
<td>d. a central bank;</td>
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<td></td>
<td>e. any multilateral development bank referred to in the second subparagraph of</td>
<td></td>
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<tr>
<td></td>
<td>Article 117(1) and in Article 117(2) of Regulation (EU) No 575/2013 of the</td>
<td></td>
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<tr>
<td></td>
<td>European Parliament and of the Council1;</td>
<td></td>
</tr>
<tr>
<td></td>
<td>f. the European Financial Stability Facility or the European Stability Mechanism.</td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Settlement fail due to a lack of debt instruments other than those referred to</td>
<td>0.20 bps</td>
</tr>
<tr>
<td></td>
<td>in points 4 and 6</td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Settlement fail due to a lack of debt instruments traded</td>
<td>0.15 bps</td>
</tr>
<tr>
<td>Discount rate per</td>
<td>currency with a floor of 0</td>
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</table>

### 16. How are cash penalties calculated?

Cash penalties are calculated daily and per day as from the ISD until the actual settlement or cancellation date of the instruction:

- For Settlement Fail Penalty: once the instruction is matched, penalties apply earliest from the ISD or the matching date to the date of actual settlement or cancellation of the instruction
- For Late Matching Fail Penalty: penalties apply retroactively from the ISD until the actual matching date.

The formulas to calculate the penalty imposed by a Settlement Fail Penalty (SEFP) are the following:

a. **For a failing DVP, DF or RF Settlement Instruction (including when on hold):**

\[
SEFP = \text{Security Penalty Rate} \times \text{Reference Price} \times \text{Quantity}
\]

b. **For a failing RVP Settlement Instruction (including when on hold):**

\[
SEFP = \text{Cash Discount Penalty Rate} \times \text{Reference Price} \times \text{Quantity}
\]

The same penalty calculation method applies to Late Matching Penalties and Settlement Fail Penalties.
17. Will BNY Mellon pass on cash penalties to its clients?

Yes, BNY Mellon intends to pass on the late matching and late settlement penalties to its clients.

18. When will CSDs report, and collect cash penalties?

- Cash penalties will be reported by CSDs daily per transaction to the CSD participant. Where BNY Mellon is direct in the market the CSD will report directly to BNY Mellon. Where BNY Mellon uses a sub-custodian the CSD will report directly to the sub-custodian who will then provide reporting to BNY Mellon.
- Net cash penalties will be reported by CSDs monthly to the CSD participant.
- Net cash penalty amounts will be collected and distributed by CSDs each month to the CSD participant’s cash account.

19. How does BNY Mellon intend to report cash penalties to clients?

BNY Mellon will offer its clients the choice to receive daily cash penalty reporting via either MT537 or MT548 and/or via NEXEN. On a monthly basis BNY Mellon will offer clients the choice of MT537 or NEXEN reporting of the net cash amount. SWIFT formats for MT537/548 (PENA) messages have been published in the SWIFT Release 2019 and can be referenced [here](#).

What is the impact to clients?

Clients may want to prepare to receive daily SWIFT cash penalty reporting messages or use the NEXEN report, as well as any internal processes to identify and manage the penalties.

How will BNY Mellon support?

BNY Mellon will provide further details to clients of the SWIFT messaging formats and fields that will be populated, and also how this will show on your invoice.

20. How will BNY Mellon’s invoices apply cash penalty fees?

BNY Mellon will provide an aggregated monthly cash penalty amount as an out of pocket expense on client’s invoices, together with a detailed, transaction level breakdown of each penalty.

21. Will CSDs charge for administering the penalties regime and will BNY Mellon pass on the CSD’s charges?

CSDs have the option to charge separately to recover the costs of operating the cash penalty mechanism. A number of CSDs have stated that they intend to charge a fee for operating the penalty mechanism, but it is not yet clear how they will communicate these charges and what will be the basis of their calculation for the charges. BNY Mellon is reaching out through its CSD and sub-custodian network, and through industry working groups, e.g. AFME, to obtain more information regarding the approach and fees to be charged. At point of publication Euroclear UK and Ireland, Euroclear Bank, the National Bank of Belgium, and Monte Titoli have said that they will charge their participants.

What is the impact to clients and how will BNY Mellon support?

Once we receive more information from CSDs and sub-custodians then BNY Mellon can determine its approach and further communications will be sent to advise our clients.

22. How can clients submit an appeal to dispute a penalty, and what information should be included?

CSDs have set out that they will require an appeals to be made within 10 business days from the beginning of the month after the penalty was calculated. The details of the appeal process have not yet been defined by CSDs however it is likely that CSDs will require the reasons for making the appeal and the information of the underlying transaction.

BNY Mellon is working with its sub-custodians to identify timeframes and will provide a further update once more information becomes available.

23. Will BNY Mellon accept appeals for cash penalties?

BNY Mellon will implement a process for clients to raise any appeals related to penalties received, investigate and support relevant penalty appeals made against the market. If it is determined that BNY Mellon was at fault, then erroneous fees will be reversed.
24. Will BNY Mellon agent lenders accept liability for any financial detriment to the client (including penalties, price differences on buy-in and losses on subsequent disposal of stock in falling markets), where the stock is not returned in time to deliver against a trade?

BNY Mellon is actively engaged in industry working groups to determine how the regulation impacts open loans versus term loans. As soon as we have more information, BNY Mellon will be communicating with our agency lending clients.

25. Where BNY Mellon provides a collateral management service, will the custodian accept liability for any financial detriment to the client (including penalties, price differences on buy-in and losses on subsequent disposal of stock in falling markets), where the stock is not returned in time to deliver against a trade?

Under the triparty collateral management service, BNY Mellon can only return client securities pledged to client counterparties when sufficient alternative collateral securities have been made available and there has been sufficient time to effect a substitution. In circumstances where either insufficient client alternative securities are available or where insufficient time has been allowed, BNY Mellon will not accept any liabilities where stock is not returned in time to deliver against a trade.

26. Where the client uses a third party collateral manager, will BNY Mellon be able to automatically pass any penalties on to the collateral manager agent where the stock is not returned in time?

BNY Mellon will pass on late matching and late settlement fines to our clients. Where clients believe a fine has been incurred due to the error of a third-party collateral manager it will be the clients’ responsibility to discuss directly any resulting penalties with that collateral manager.

II. Mandatory Buy-in and Cash Compensation

27. What does the regulation require?

CSDR imposes a mandatory buy-in process on any financial instrument which has not been delivered within a set period after the intended settlement date (ISD). CSDR places an obligation on the Receiving Trading Party (RTP) to invoke a buy-in within set timeframes and sets out 3 different processes for buy-ins to occur, dependent upon where the transaction is cleared and how it is executed.

28. What is a buy-in?

In the event of a settlement fail, a buy-in process provides a buyer of securities with the right to source the securities elsewhere, cancel the original instruction(s), and settle between the two original counterparties any differences arising from the net costs of the original transaction and the buy-in transaction.

29. What are the timeframes of the mandatory buy-in requirements?

The extension period for initiating a buy-in varies based on asset type, liquidity or whether quoted on an Small and Medium Enterprise (SME) Growth Market:

- ISD+4 for liquid securities
- ISD+7 for illiquid securities
- ISD+15 for SME Growth Markets

ESMA maintain a register of SME Growth Markets which can be accessed here.

What is the impact to clients?

Clients should be prepared to be able to identify when securities are due to be bought in and establish communications procedures with their counterparties.

How will BNY Mellon support?

BNY Mellon’s reporting of clients failed trades will include the number of days since Intended Settlement Date (ISD) that a transaction has been failing.
30. Will BNY Mellon be notified of a buy-in by the CSD?

No, CSDs will not notify participants of settlement instructions that are due for buy-in.

31. Who executes the buy-in process?

CSDR mandates the Receiving Trading Party (RTP) to initiate a buy-in for the outstanding, undelivered stock at the expiration of the extension period. In the case that the transaction is cleared by a central counterparty, then they will be responsible for initiating the buy-in.

If the buy-in is unsuccessful, the process will be settled by means of cash compensation.

What is the impact to clients?

Clients need to prepare for buy-ins by establishing internal processes to identify buy-ins and the management of them. One important consideration for clients will be whether they will execute the buy-in themselves or if their broker will execute on their behalf.

How will BNY Mellon support?

See below for further information on how BNY Mellon will support clients.

32. What trading activity is in scope for buy-ins?

- Transactions cleared by a central counterparty (CCP)
- Transactions not cleared by a central counterparty (CCP) but executed on a trading venue
- Transactions not cleared by a central counterparty (CCP) and not executed on a trading venue

What is the impact to clients?

Clients will need to be able to identify how their transaction was cleared and where executed in order to follow the correct buy-in process.

How will BNY Mellon support?

See below for further information on how BNY Mellon will support clients.

33. Do mandatory buy-ins apply to securities financing transactions?

The regulation provides an exemption for securities financing transactions (SFTs) where the term of the SFT is less than 30 business days. This applies to securities lending and collateral management transactions and includes both start and end legs. Longer term SFTs of 30 business days or more, however, are in scope for buy-ins.

What is the impact to clients?

Clients will need to be able to identify securities financing transactions and therefore when they could be subject to buy-in.

How will BNY Mellon support?

BNY Mellon already provides a range of settlement status reporting through SWIFT status messages and in NEXEN which shows the transaction type and settlement date period. Please contact your relationship manager for further information.

34. What instruments are in scope for buy-ins?

Only securities which are listed in the ESMA database registers are in scope instruments. These financial instruments can be found here.

What is the impact to clients and how will BNY Mellon support?

Clients will need to be able to identify whether the financial instruments are in or out of scope and the timeline for when they will be due for buy-in by reviewing the ESMA database registers.
How will BNY Mellon support?

Clients can use the link provided above to identify whether financial instruments are in scope for buy-ins.

35. What actions will clients need to take in relation to mandatory buy-ins?

a. Allow Partial Settlement:

On the last day of the extension period (i.e. ISD +4, ISD+7, ISD+15), the Failing Trading Party (FTP) must offer partial delivery of any available securities to the Receiving Trading Party (RTP) which cannot refuse.

b. Set instruction on Hold/Unhold:

At the end of extension period, it is mandatory for the Failing Trading Party (FTP) to place delivery instructions on hold upon receipt of buy-in notification from the Receiving Trading Party (RTP). This is in order to ensure that settlement cannot be released even if the stock becomes available until either the RTP advises, or the instruction is bilaterally cancelled.

For a Receiving Trading Party it is not mandatory to put the receive trade on hold by its clients, however it will be market practice in order to prevent the original trade from settling.

c. Verify that buy-in is possible

On the next business day of the extension period (i.e. ISD +5, ISD+8, ISD+16), the Receiving Trading Party (RTP) must verify that a buy-in is due to be initiated by checking the following:
- Security is on list of in-scope instruments (see ESMA database)
- Transaction is settling through an EU/EEA CSD
- The nature of the trade (i.e. Transaction Type) is an actual trade

d. Buy-in Agent appointment:

The Receiving Trading Party (RTP) must appoint a Buy-in Agent and inform the Failing Trading Party (FTP) of the appointment.

The Failing Trading Party sets his instruction on hold and inform its CSD participant.

Buy-In Agent confirms the appointment for “guaranteed delivery” and goes to the market to purchase the instruments subject to buy-in.

e. Buy-in execution:

The Buy-in agent confirms the execution of buy-in to the Receiving Trading Party (RTP) and immediately transmits to its CSD participant the information to instruct the bought-in instruments.

f. Cancellation of original instruction:

Upon the delivery of securities from the buy-in agent, the Receiving Trading Party (RTP) instructs failing party to cancel the original instruction and transmits to its agent new information to match buy-in agent on the market.

After the buy-in has settled the Receiving Trading Party (RTP) issues invoice on buy-in costs to the Failing Trading Party (FTP).

g. Buy-in costs and Cash compensation:

All buy-in costs and/or cash compensation arrangements should be agreed between the trading parties. Cash compensation may include the Buy-in agent fee, price difference where the Receiving Trading Party was disadvantaged, FX rate change, and corporate event entitlements due to the Receiving Trading Party.

36. When does the buy-in execution need to be completed by?

The Receiving Trading Party (RTP) will be given a period of business days equal to the same number of business days before the buy-in was invoked e.g. an equity due for buy-in after ISD +4 would have an extension period of 4 business days.
What is the impact to clients?
Clients will need to identify when a buy-in is due to occur in order to meet with their buy-in obligations.

How will BNY Mellon support?
BNY Mellon will provide the number of days that a transaction is unsettled after Intended Settlement Date on its NEXEN fail settlement reporting to support clients in identifying when a buy-in may be due.

37. What happens if the buy-in is ineffective?
If the buy-in is unsuccessful, the process will be settled by means of cash compensation. This will require the original trade to be cancelled and a payment being made by the failing trading entity to the failed-to trading entity based on the difference between the current market price and the original transaction price.

What is the impact to clients?
Clients will need to be prepared in the event that a buy-in may not succeed and result in cash compensation.

How will BNY Mellon support?
BNY Mellon already supports the processing of cancellation instructions.

38. Does BNY Mellon plan to update their contractual arrangements with clients?
Yes, BNY Mellon will amend client contracts for buy-ins and cash penalties, as required under Article 25 of the Delegated Regulation on Settlement Discipline (EU 2019/1229). More detail will be communicated in due course.

What is the impact to clients?
Clients will receive notification of any contract changes and can review and refer any questions to their BNY Mellon relationship manager.

How will BNY Mellon support?
BNY Mellon will provide clients with notification of contract changes and address any queries raised.

39. What are the Buy-in status reporting requirements?
CSDs are required to report the number and the value of Buy-ins executed to their National Competent Authority.

Receiving Trading Parties must report the Buy-in status to the CSD at the latest on the last business day of the buy-in extension period.

Status information to be provided in the buy-in reporting for each buy-in will be:
- Successful Buy-in
- Failed Buy-in
- Partially Executed Buy-in

A request has been submitted by industry working group AFME to facilitate buy-in reporting using the SWIFT MT530 Transaction Processing Command message type.

What is the impact to clients?
Clients who are the Receiving Trading Party will need to report the buy-in status to BNY Mellon.

How will BNY Mellon support?
BNY Mellon will support this requirement by providing clients with the ability to communicate the buy-in status via either SWIFT MT530 message type once developed by SWIFT, or our NEXEN webportal, and BNY Mellon will forward the message to the CSD or sub-custodian.
40. Will BNY Mellon provide a Buy-in service?

BNY Mellon will not be providing a buy-in execution service. Clients should therefore establish appropriate arrangements to cover their buy-in obligations.

BNY Mellon’s approach to CSDR as our clients’ custodian and settlement agent is to focus on enabling our clients to reduce their failing trades and therefore minimise the impact to clients of the settlement discipline rules.

Contact Us:

For further information and/or clarification, please either contact your Relationship representative, otherwise inquire here.