

European Commission

Directorate-General for Financial Stability, Financial Services and Capital Markets Union

1049 Bruxelles

Belgium

February 2021

Dear Sir/ Madam

**RE: Targeted consultation on the review of Regulation on improving securities settlement in the European Union and on central securities depositories**

ISLA is a leading industry association, representing the common interests of securities lending and financing market participants across Europe, Middle East, and Africa. Its geographically diverse membership of over 160 firms includes institutional investors, asset managers, custodial banks, prime brokers, and service providers. ISLA sponsors the [Global Market Securities Lending Agreement (GMSLA)](http://www.islaemea.org/legal-services/) and the annual enforceability review in more than 65 jurisdictions.

ISLA welcomes the opportunity to provide feedback on this important initiative and fully supports the overall aim of CSDR to enhance settlement efficiency across EU capital markets. The response to this consultation was formulated by an industry working group representing 80 member firms and, throughout the working group’s review, one particular concern was repeatedly voiced that we would like to highlight in this letter.

Our members consider the introduction of a penalty mechanism to be an effective tool in reducing settlement failures across our industry, and strongly believe that this mechanism alone will help to achieve that objective. However, there is unanimous industry concern relating to the introduction of a mandatory buy-in. In particular, the current one size fits all proposal could be severely damaging to market liquidity, if applied to securities financing transactions. This activity provides crucial supply to the market and supports a recognised reduction of settlement failure. Members are also concerned that by introducing an additional risk for parties to securities lending transactions, asset owners that engage in securities lending as a low-risk discretionary activity may be deterred from lending their assets. This would reduce the pool of securities available to borrow, leading to less liquidity and increased settlement failure. In view of this, ISLA would strongly recommend that the entry into force of the settlement discipline regime be decoupled into two phases:

1. Penalties to go live as planned in February 2022 and,
2. Buy-in requirements to become effective at a later date, after policy makers have:
   1. conducted an in-depth assessment of the penalty mechanism to understand if it alone can achieve ‘target’ efficiency rates and grant ESMA the authority to recalibrate penalty rates where no significant improvement is shown; and
   2. clarify the scope of instrument types captured by the buy-in regime to ensure its effectiveness and, after further consultation with the industry, resolve any ambiguity in the current regulation.

Further concerns, regarding the mandatory buy-in, incorporate the timing and viability of its application. Implementing Article 25 of the RTS will require firms to expend significant legal and operational resources, in order to establish contractual arrangements with clients and counterparts. This represents a significant undertaking whilst providing little practical benefit, considering the securities financing master agreements (GMSLA & GMRA) contain contractual remedies addressing settlement failures. These remedies have been an effective means of governance for many years and members believe they match the objectives of the buy-in requirements under CSDR. Any amendments to the current documentation will result in a global repapering exercise, which will take considerable time.

ISLA would welcome a speedy deliberation and clear targeted regulatory amendments that provide sufficient and adequate time for industry adoption.

ISLA have provided, as part of this consultation response, an in-depth overview of the impacts on liquidity of the mandatory buy-in regime. We also include an outline of perceived negative market impacts, had the buy-in requirements been in place over the initial phases of the COVID 19 pandemic in early 2020.

Due to character limitations of the online response page, ISLA has submitted a full unabridged version of our response, highlighting examples, and providing supporting detail to our arguments.

ISLA would welcome the opportunity to discuss the response in this consultation in more detail.

Yours Sincerely

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