

Overcoming the barriers in cross-border settlement in Europe - a progress report

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The deficiencies that stand in the way of efficient clearing & settlement and custody cross-border processes in Europe are well known; the Giovannini Group has comprehensively analysed and defined them in their report published in 2003. The European Commission has endorsed this analysis in its Communication on Clearing and Settlement in the European Union of 2004. Its objectives of liberalisation and integration of the post-trade systems through the removal of existing barriers to significantly reduce costs and risks have been met with unanimous approval.

What has been achieved to date?

The private sector has taken up its responsibility to remove six of the fifteen barriers without delay: ECSDA, the European Central Securities Depositories Association, has worked out detailed solutions for harmonised settlement deadlines, operating hours and intraday settlement finality. SWIFT recently published a consultation paper presenting a Europe-wide protocol aimed at removing national differences in the information technology and interfaces. IPMA, the International Primary Market Association, is far advanced in removing primary market barriers. The European Association of Listed Companies (EALIC), the European Banking Federation (EBF), ECSDA and the European Securities Forum (ESF) have entered into a close cooperation to develop and implement harmonised and standardised processes in the complex area of corporate action events.

In the public sector the European Commission has set up three expert groups: CESAME, the Clearing and Settlement Advisory and Monitoring Expert Group, the Legal Certainty Group and the Fiscal Compliance Group. The mandate for the CESAME Group, composed of high level representatives of private and public sector bodies, focuses on the support of the project to integrate clearing and settlement systems in Europe, to ensure transparency and warrant coherent action through coordination. The Legal Certainty Group is tasked with analysing legal uncertainties in the context of clearing and settlement and with proposing adequate solutions to such problems of legal uncertainties. The tax barriers outlined in the Giovannini Report are the basis of the mandate conferred upon the Fiscal Compliance Group. At the same time, to our knowledge hardly any action has been taken at the level of national authorities to contribute to the removal of the barriers for which the responsibility is assigned to the public sector.

In essence: the work of removing the barriers has started, however, the time required to reach a broad consensus and to implement agreed solutions should not be underestimated.

What are the main risks and impediments in this process aimed at making the European post-trade processes internationally competitive?

Change will be required to eliminate the current fragmentation and diversity. In most cases change will not be for free and costs and benefits will not be evenly distributed. More generally, the lack of will and commitment caused by commercial and national interests must not be underestimated. Neither is there room for ill-conceived competition between financial centres nor for the 'not invented here' syndrome.

Why is a close cooperation between the private and the public sector deemed key for success?

For the following seven reasons:

- The public sector is faced with an unusual degree of complexity - e.g. corporate action events or matching processes - in an area in which it lacks in depth expertise and know-how.
- The private sector on the other hand lacks the authority to enforce the removal of key impediments to higher efficiency and lower costs and risks, such as legal diversities.
- In reality most barriers have multiple roots of an operational and legal, fiscal and/or regulatory nature.
- Only solutions supported by the public and the private sector will be sustainable.
- Resistance to change within the public and the private sectors will require action in concert.
- The timely and cost-effective implementation of agreed solutions depends on coordination and cooperation by responsible public and private sector institutions.
- A European clearing and settlement and custody landscape that is globally competitive, cost efficient and safe is in the interest of both, the private and the public sector.

What are essential lessons learnt so far?

To define and agree on the deficiencies of the European cross-border post-trade environment has been important showing the way to high level objectives. However, only by breaking these high level objectives down into concrete actions, by working out detailed solutions that are widely accepted and by implementing them will the benefits of reduced cost and risk be achieved.

Bespoke alliances of private and public sector organisations help to mitigate the resource issue and to steer clear of duplicate efforts.

A relentless drive of agents of change is and will be required to overcome inertia and to avoid playing into the hands of those who perceive change as a threat - it has to be acknowledged that the harmonisation, standardisation and integration will imply asymmetric cost-benefit effects.

What are the important milestones in the way forward?

An important part of public sector activities has been taken up by ESCB-CESR, the Joint Working Group of European central banks and securities regulators. Its report published in 2004 - containing 19 standards for securities clearing and settlement in the European Union that are based on the respective recommendations of CPSS-IOSCO - has partly been heavily criticised by market users and infrastructure organisations alike. Although the respective authorities have agreed on the standards they have not come into force yet. By mid July an additional ESCB-CESR document - essentially covering the assessment methodology by which systemically important market participants are to be defined - will be published. This document will be subject to an open consultation process for three months and it will be the topic of a public hearing mid September. We would hope that the controversies on some of the standards will not distract from what we deem an essential objective: the harmonisation, standardisation and integration of regulation and supervision throughout Europe.

At the beginning of 2006 the European Commission intends to decide on whether or not it will take legislative action by way of a framework directive. An important basis for this decision will be an impact assessment that is currently under way. First results of this analysis demonstrate the significant amount of excess costs caused by the current post-trade fragmentation in the amount of EUR 3 to 5 bn p.a. and the sizeable benefits the markets could generate in an integrated clearing and settlement environment. In our view, legislative action, if deemed required, should be restricted on the removal of those barriers for which the public sector takes responsibility such as ensuring open access and harmonising the legal, tax and regulatory environment.

A continuing effective cooperation between the private and the public sector - for the reasons outlined above - including the phase of implementation, which will last for years to come, will be a key requirement for success.