IFLR

Firms should not neglect mandatory buy-ins

By Lucy Frost July 04, 2022

The Central Securities Depositories Regulation (CSDR) went live at the beginning of this year without the controversial mandatory buy-in requirements but the delay only creates more uncertainty ahead

The three-year delay to the introduction of mandatory buy-ins (MBIs) announced by the European Securities and Markets Authority (ESMA) will come around quickly, warn market participants.

The mandatory buy-in arrangement has been delayed thrice already due to heavy criticism from industry groups, especially those in the securities financing space who maintain MBIs will not solve the underlying issues.

“The delay to mandatory buy-ins was three years, which seems like forever but it's really not,” said Andy Wiblin, chief product officer at GLMX, a securities financing trading platform. “The market is certainly in a better position now than last month when MBIs were hanging over as a looming threat, but some serious investment will still need to take place for firms to be ready for this in three years’ time.”

The delay was received well across the industry.

“There’s no doubt the industry breathed a collective sigh of relief at this output from ESMA,” said Michelle Bedwin, chief compliance officer at Coremont, a portfolio management services provider.

However, this won’t be the end of the concerns.

“The delay to the MBIs has prevented new potential issues from emerging rather than solving any problems,” said Rui Ferreira, product owner at Torstone, a post-trade services provider. “However, the European Commission is retaining it, signalling to the industry that improvements to the settlement efficiency rates still need to be achieved.”

If that does not happen in the coming years, then the MBIs will likely still be enforced, albeit with some changes to what was envisaged in the original legislation, he added. “The Commission’s intention has been to show that it has listened to industry feedback and has given the industry some motivation to work on improving the systems, but at the same time, it has retained the possibility of using the proverbial stick later if not enough change is observed.”

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Industry impact

A key concern for market participants is the uncertainty created by the numerous delays.

“By the end of the three years which the MBIs have now been delayed, firms will need to understand what is actually going to happen,” added GLMX’s Wiblin. “The longer that remains under discussion or ambiguous, the preparation time for firms begins to drop and that shortens the period firms have to make their investment decisions.”

In a world where there are many challenges and demands on budgets, trying to satisfy regulatory needs or just reacting to changing market conditions is going to be a tough one for the different market participants, he added.

Others agreed with this concerned approach to the buy-in delay. “This delay gives the European Commission and co-legislators more time to finetune and ratify the rules,” said **Coremont**’s Bedwin. “However, it remains to be seen what exactly the three-year delay to the regime will bring. It’s clear that key stakeholders are focused on determining the best way forward to improve settlement efficiency.”

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Wider concerns

While the EU signalled from the end of last year that MBIs would not come into force with the rest of the CSDR in the first quarter of this year, other parts of the regulation, including cash penalty requirements, have been in place since then.

“The first few months of the Settlement Discipline Regime enforcement have highlighted that there are definitely still underlying aspects to be worked on and enhanced across the industry,” said Torstone’s Ferreira. “The one key problem that is still causing concern is the lack of wider standardisation on the usage of the MT537 penalties messages. The industry has seen some central securities depositaries and custodians taking different approaches that ultimately force further changes on every entity that needs to process such messages.”

A key part of the CSDR is using technology to make post-trade more efficient. This will also be key to fulfilling reporting requirements swiftly.

“Automated data management has emerged as an important factor in achieving timely settlement,” said Matt Johnson, director at Depository Trust & Clearing Corporation (DTCC). “Automation of standing settlement instructions (SSIs), which guarantee that trade settlements, margin and payments are sent to the correct account, has been highlighted as an important post trade process contributing to settlement efficiency. SSIs change frequently, therefore, unless this process is automated, it can be responsible for trade fails, late settlement and inaccurate settlement reporting.”

The adoption of partial settlement optimisation to help minimise financial penalties and to ensure they are charged only for the outstanding amount which has failed to settle hasn’t been adopted as broadly as it could have, he added. “It’s vital for participants to use post-trade tools, such as partial settlement, to keep settlement penalties as low as possible.”

Other market participants emphasised the importance of digitisation in the industry. “We've really been pushing the digitisation agenda to allow the trading to take place electronically, which means it's more efficient from everyone's perspective and offers secondary benefits in terms of transparency and speed of execution,” added Wiblin.

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