Monday 27 April 2015

Nasdaq's response to the EBA on CSD prudential requirements

This paper constitutes Nasdaq's response to the European Banking Authority (EBA) Consultation Paper of 27 February 2015 on draft Regulatory Technical Standards (RTS) under EU Regulation 909/2014 (hereafter the CSD Regulation or "CSDR").

Nasdaq owns and operates 4 CSDs in Europe, i.e. in Estonia, Iceland, Latvia and Lithuania. None of the Nasdaq CSDs operate with a banking license and will therefore not be subject to the RTS under articles 54 and 59, since these are specifically targeted at CSDs having a banking license and at designated credit institutions (DCIs).

Nasdaq's response thus deliberately focuses on the draft standards which apply to all CSDs (RTS under art.47 of the CSDR). It should also be noted that Nasdaq CSDs are members of ECSDA and the views set forth in ECSDA's response to this consultation are supported by Nasdaq and reflected in this response.

Amendment proposals included in this paper are presented in italics, with suggestions for additional wording in ***bold italics,*** and suggestions for deletions marked by ***~~a strikethrough~~***.

Executive Summary

Nasdaq supports harmonised and transparent capital requirements for central securities depositories. We are convinced that the CSD Regulation regulatory technical standards (RTS) have the potential to bring important improvements to the current situation, including by ensuring that:

- all EU-authorised CSDs with an identical risk profile are subject to similar capital requirements;
- the level of CSD capital is proportional to the risks arising from the activities of a CSD, as opposed to a fixed and arbitrary amount of capital.

We are not advocating the status quo or 'harmonisation by the bottom', and we recognise that some CSDs will need to increase their capital level as a result of the new standards. However, we regret that the draft standards currently proposed by the EBA are not sufficiently tailored to CSDs' specificities and

we fear that they will not be practically implementable unless they include some important adaptations.

In order to achieve solid and truly proportionate capital requirements, Nasdaq recommends that:

1. **Provisions coming from the framework in place for banks and/or CCPs and which are largely if not totally irrelevant in a CSD context should be removed from the draft RTS**. The vast majority of EU CSDs, including Nasdaq CSDs, do not provide cash credit and are thus not exposed to counterparty credit risk in relation to their participants. This is an important difference with banks and CCPs. This needs to be reflected in prudential requirements for CSDs. To give just one example, the notion of "*client short and long balances*" in Annex II of the draft RTS is simply not applicable in a CSD context, at least for CSDs without a banking licence.

2. **Custody risk in the Level 1 CSDR refers to a risk faced by the CSD itself, not by its participants.** Any potential risks that a CSD faces as a result of its participants' custody risk (whether in relation to securities held directly in the CSD or via a CSD link) are already covered under operational and legal risks. Duplicate requirements should be avoided.

3. **CSDs should only have to set aside capital for winding-down or restructuring their activities to the extent that this does not overlap with capital requirements for business risk.** International Principles allow CSDs to use the same capital for ensuring that the infrastructure operates as a going concern and for ensuring an orderly recovery or wind-down of critical operations. Given the lower risk profile of CSDs compared to CCPs, Nasdaq does not think that it was the intention of the EU legislator in the Level 1 CSDR to impose strict cumulative requirements clearly exceeding international standards.

4. **Some requirements should be recalibrated to reflect CSDs' low risk profile and specific arrangement**. For example, for assessing operational and legal risks, Nasdaq recommends a ratio of 10% instead of 15% as well as the possibility to take into account CSDs' specific insurance arrangements and/or guarantee schemes. For business risk, Nasdaq believes that the proposed 25% ratio is excessive in view of CSDs' low risk activities and that using gross expenses as a reference for the calculation is not appropriate.

5. **The predefined business risk and winding-down scenarios suggested by the EBA for determining capital requirements should be replaced by a more flexible approach** allowing CSDs to define reasonably foreseeable adverse scenarios relevant to their business model, subject to the approval of the competent authority.

6. **When assessing the quantitative impact of the new standards on existing CSD capital**

levels, the EBA should also look at the impact on the structure of CSDs' capital. Based on Nasdaq's preliminary assessment, we foresee that the draft RTS will result in a significant increase of minimum capital requirements for all Nasdaq CSDs, raising the bar far beyond current domestic and international requirements.

1. CSD capital requirements (art.47 CSDR)

This section refers to Title I of the draft RTS (p.18-24), as well as Annex I on winding-down or restructuring scenarios (p.67-68), Annex II on business risk scenarios (p.68), and Section 5.1(1) of the draft impact assessment (p.69-73)

Q1. What are the practical impediments of calculating capital requirements for custody risk as set out in Article 5?

Before considering the "practical impediments" for calculating capital requirements for custody risk, Nasdaq believes that the EBA needs to address fundamental conceptual flaws in the draft RTS.

(a) "Custody risk" in the Level 1 CSDR refers to a risk faced by the CSD itself, not its participants

First of all, Nasdaq believes that the draft RTS contain a misunderstanding of the notion of "custody risk" in the context of art.47 of the CSDR. Custody risk is not defined in the Level 1 CSDR, but it is important to remember that the notion was introduced in the CSDR in relation to the CSD's investment policy, to be consistent with Principle 16 of the CPMI-IOSCO Principles for financial market infrastructures (PFMI) on "custody and investment risks"[1]. Custody risk is not addressed in a separate article in the CSDR Level 1 text because **both types of risks (custody and investment risk) are covered under the same PFMI and because both types of risks were meant to be assessed in relation to the CSD's own assets.**

Whereas clearing members post margins to the CCP, CSD participants do not post assets to secure their obligations towards the CSD, and **CSDs typically do not invest their clients' assets.** Recital 11 is thus incorrect as far as most CSDs are concerned and is not relevant for any of the Nasdaq CSDs2. CSDs are different from banks and CCPs in that they are primarily exposed to operational

[1] In the PFMI, custody risk is defined as "*the risk of loss on assets held in custody in the event of a custodian's (or subcustodian's) insolvency, negligence, fraud, poor administration, or inadequate recordkeeping*." In other words, custody risk refers to the risk of losing own assets in the custody with a third party. This is a very remote risk and it is covered under operational risk in the banking regulations.

[2] Although Nasdaq did not carry out an analysis of the Recitals and decided to focus on suggesting alternative wording for the actual articles of the draft RTS, we note that the Recitals do not sufficiently distinguish between non-bank CSDs and CSDs offering banking type services. Recital 11 illustrates this problem with the statement that *"Investment risk is the risk of loss faced by a CSD when it invests its own or its participants' assets, such as collateral"*. Non-bank CSDs typically do not invest their clients' assets, even when they offer collateral management services under Section B of the Annex of the CSDR (collateral services "as agent"). The definition of investment risk provided in this Recital is thus misleading as it does not apply to

risk, with investment and custody risks being very marginal. Even for CSDs offering banking type services, investment and custody risks are typically very low compared to ordinary banks of the same size.

The custody risks faced by CSD participants (whether in relation to assets held directly in a CSD, via CSD links, or elsewhere in sub-custody) are covered by participants themselves. The risks to the CSD in relation to participants' assets, on the other hand, are fully covered under operational and legal risks. Should anything happen to the securities held by a CSD on behalf of its participants, the threat to the CSD's capital is indirect, either as a result of claims for compensation received from participants (legal risk) or operational incidents affecting assets held via links maintained by CSDs with other entities (operational risk). There is thus unnecessary duplication in art.5 of the draft RTS. Removing references to clients' securities is indispensable to ensure that the RTS are workable and consistent with the Level 1 text and the PFMI.

(b) CSD links should not be considered separately for the purpose of calculating capital requirements

As a result of the excessively broad interpretation of the notion of "custody risk", the EBA also suggests taking into account CSD links separately for the calculation of capital requirements. Nasdaq believes that such a proposal is not appropriate for two reasons:

First, CSDs typically do not invest client assets and do not face custody risk in relation to client assets, including assets held via CSD links. Custody risks are faced by the CSD's clients, and the CSD itself is subject to legal or operational risk, in case the loss of assets via a link would result in a claim towards the CSD. **The amount of CSD capital set aside for covering legal and operational risks already covers scenarios related to the loss or damage of client securities via a CSD link**, and so the consideration of custody risk in relation to clients' securities and CSD links creates unnecessary duplication.

Second, **there is nothing in the Level 1 CSDR or in the PFMI which requires (or even suggests) that custody risks faced by CSD participants, including via CSD links, should be considered for the purpose of CSD capital requirements.** For Nasdaq, the mention of "custody risk" under art.47 of the CSDR should be understood in the context of the PFMI, and both the CSDR and the PFMI contain separate and specific provisions (article 48 and Principle 20 respectively) on the risk assessment related

to CSD links. In fact, Principle 20 only refers to custody risk as an “additional risk” to be taken into account when CSDs use intermediaries to operate CSD links. Unlike links between CCPs, standard links between CSDs do not involve any credit exposures among the linked CSDs. This is why art.19(5) of the CSDR only requires an authorisation for interoperable links (such as the “bridge” between the two ICSDs) and allows CSDs to notify all other links, without having to request a prior authorisation from the competent authority. Removing the mention of CSD links in art.5 of the draft RTS would thus be fully consistent with the Level 1 CSDR, the PFMI and current supervisory practices (to our knowledge, national regulators do not currently assess CSD links outside of operational and legal risks’ considerations for the purpose of calculating CSD capital requirements).

(c) The proposed method for assessing custody risk is inappropriate

In addition to creating unnecessary duplication and introducing inconsistencies with the Level 1 CSDR and the PFMI, the proposed method for calculating custody risks under art.5 of the draft RTS is inadequate. It refers to the Capital Requirements Regulation (CRR) Standardised Approach for operational risk. When trying to apply the formula to their activities, CSDs face several problems. For example, it is unclear how CSDs' activities can be mapped to the business lines of a credit institution, as described in art.317 of the CRR. CSDs are not involved in the activities described (corporate finance, trading and sales, retail brokerage etc.) and thus they cannot select any of the listed business lines. So- called "agency services" are perhaps the only services that are conceivable in a CSD context, but then the definition provided in the CRR is different from the central maintenance service as described in the CSDR. Indeed, the type of custody services provided by other financial institutions are different from the safekeeping of financial assets by financial market infrastructures like CSDs, and are thus not comparable from a risk perspective.

Furthermore, no matter what numbers CSDs try to calculate using the Standardised Approach, the results always seem to be already included in the calculations under the Basic Indicator Approach for operational, legal and custody risk. This further confirms the duplication and shows that art.5 of the draft RTS should not only be amended in relation to clients' securities, but should be deleted entirely:

~~Article 5 - Level of capital requirements for custody risks~~
~~For the purposes of point (b) of Article 3(1), a CSD shall calculate its capital requirements for custody risks where it has its securities or its clients’ securities under custody by another CSD or an intermediary within a CSD link. It shall do so in accordance with the methodology referred to in Articles 317 to 319 of Regulation (EU) No 575/2013 on the standardised approach for operational risk.~~

Nasdaq recommends that references to custody risk should be included in art.4 of the draft

RTS instead, in line with the spirit of the Level 1 CSDR (see our proposed amendment under Question 2).

Q2. Is the level of capital requirements as proposed in these draft RTS (Articles 1-8) adequate to capture all the risks arising from the activities of a CSD? Are they proportionate for all the CSDs' business models? Please justify your answer.

Nasdaq agrees with the EBA that:

- All EU-authorised CSDs with an identical risk profile should be subject to similar capital requirements, ensuring a level playing field;
- The level of CSD capital should be proportional to the risks arising from the activities of a CSD. In other words, we support a risk-based approach, as opposed to a fixed and arbitrary amount of capital;
- Some CSDs will need to increase their capital level as a result of the new standards. Nasdaq is not advocating the status quo or 'harmonisation by the bottom'. We support solid capital requirements for all CSDs, but these must be fair, simple efficient workable and truly proportionate.

Against this background, some of the draft standards proposed by the EBA do not seem appropriate. In particular, some of the methods put forward for calculating the level of capital requirements of a CSD will not result in an accurate reflection of a CSD's risk profile, imposing a disproportionate burden on many CSDs, most of which are small or medium sized enterprises with a particularly low risk profile.

Title I of the draft RTS should be redrafted to reflect CSDs' specificities and to allow for a much clearer differentiation between CSDs based on their risk profiles. In particular, the standards need to take into account the low risk nature of activities performed by non-bank CSDs, which, unlike CCPs and banks, are not exposed to material credit risk in relation to their core activities. Relying on CRR approaches designed for banks, as is being proposed by the EBA, is not always workable and could make it difficult for competent authorities to determine the appropriate capital level for the CSD(s) they supervise. The proposed methods often put the focus on risks which are marginal for CSDs (investment, credit and liquidity risks) instead of allowing for a transparent and consistent assessment of operational risks which are at the core of every CSD's activities.

It is especially important to remember that the main risk faced by CSDs, operational risk, is mitigated mainly via the design and the procedures of the CSD's securities settlement system, not via capital requirements. No matter how well capitalised a CSD is, this does not in itself guarantee that the system is available to participants, hence the focus of CSD overseers on business continuity and

recovery planning.

In addition to these general comments, in order to be as helpful as possible, Nasdaq would like to put forward the following alternative solutions for the most relevant articles under Title 1 of the draft RTS:

- **Article 1: Overview of requirements regarding the capital of a CSD**

Nasdaq agrees with the drafting of art.1 of the draft RTS.

- **Article 2: Definition of capital of a CSD**

Nasdaq supports the proposed definition of “capital” under art.2 of the draft RTS (p.18).

- **Article 3: Level of capital requirements for a CSD**

(a) The treatment of custody risks

Nasdaq disagrees with art.3(1)(b) of the draft RTS. Point (b) is redundant and inconsistent, as explained in our response to Question 1. CSDR article 47 on capital requirements requires that a CSD *“is adequately protected against operational, legal, custody, investment and business risks (…)”.* This means that the capital of a CSD must be sufficient to mitigate the risks described under articles 43 (legal), 44 (business risk), 45 (operational) and 46 (investment and custody risk). It does not aim to include custody risks faced by CSD participants, and point (b) should thus be deleted altogether, especially since custody risks are already addressed under art.3(1)(a).

(b) The "cumulative approach"

Nasdaq agrees that a CSD's capital should be sufficient to ensure that a CSD can continue to operate as a going concern and to ensure that, if a restructuring or winding-down process is necessary, such process can take place in an orderly way to minimise market impact and preserve financial stability. However, we believe that the cumulative approach adopted by the EBA in relation to points (a) and (b) of CSDR article 47(1) is excessive and needs to be adjusted.

The problems with the proposed cumulative approach are as follows:

- There are overlaps between the approaches under points (a) and (b) of art.47(1), for example

as regards business risk under point (a) and winding-down under point (b). A given event (e.g. a substantial and unexpected loss of income) considered for business risk purposes might or might not fall under winding down scenarios, depending on the severity of the problem and whether it poses a threat to the operation of a CSD as a going concern. The same scenario might thus be considered twice, although with different degrees.

- The proposed cumulative approach is not consistent with Principle 15, Key consideration 3 of the PFMI, which allows the same capital to be used both for ensuring that the infrastructure operates as a going concern and for ensuring an orderly recovery or wind down of critical operations. Whereas we acknowledge that the EMIR standards go beyond the PFMI, given the specific role of CCPs as centralisers of risk in financial markets, we do not believe that it is the intention of the EU legislator in the Level 1 CSDR to impose significantly stricter requirements in the case of CSDs.

Taking into account the need for a consistent treatment of custody risk and the need to avoid an excessively strict interpretation of the "cumulative approach" for business risk and winding-down scenarios, Nasdaq recommends amending art.3(1) of the draft RTS as follows:

Article 3 - Level of capital requirements for a CSD

1. For the purposes of Article 1, a CSD shall hold capital, together with retained earnings and reserves, which shall be at all times more than or equal to the sum of:

(a) the CSD's capital requirements for operational, legal and custody risks, referred to in point (a) of Article 47(1) of Regulation (EU) No 909/2014, calculated in accordance with Article 4;

~~(b) the CSD's capital requirements for custody risks, referred to in point (a) of Article 47(1) of Regulation (EU) No 909/2014, calculated in accordance with Article 5 where it has its securities or its clients' securities under custody by another CSD or an intermediary within a CSD link;~~

(c) the CSD's capital requirements for investment risks, referred to in point (a) of Article 47(1) of Regulation (EU) No 909/2014, calculated in accordance with Article 6;

(d) the CSD's capital requirements for business risks, referred to in point (a) of Article 47(1) of Regulation (EU) No 909/2014, calculated in accordance with Article 7;

*(e) the CSD's capital requirements for winding-down or restructuring its activities, referred to in point (b) of Article 47(1) of Regulation (EU) No 909/2014, calculated in accordance with Article 8**, to the extent that these capital requirements are not already covered under point (d) above** (…)*

As regards art.3(3) and (4) of the draft RTS, Nasdaq understands that the wording has been copied from EMIR, but we wonder whether a notification at 110% is justified in the case of CSDs, given that a CSD's capital is typically very stable. Unlike CCPs, CSDs are not required to provide capital for managing a participant's default and they are thus not exposed to systemic risk to such an extent

that a minor loss of capital (e.g. 1%) would require urgent corrective actions and strict monitoring from a prudential perspective. This is especially true as such minor loss is very unlikely to lead to any disruption in CSD services. As a result, to avoid unnecessary notifications, Nasdaq recommends either lowering the notification threshold or providing more flexibility as regards the frequency of notifications to the competent authority (to be determined by each competent authority):

Article 3 - Level of capital requirements for a CSD

(…) 3. Where the amount of capital held by a CSD according to paragraph 1 is lower than 110 % of the capital requirements ('notification threshold'), the CSD shall immediately notify the competent authority and keep it updated ***regularlyat least weekly****, until the amount of capital held by the CSD returns to a level above the notification threshold. (…)*

- **Article 4: Level of capital requirements for operational, legal and custody risks**

The references to the CRR used in art.4 of the draft RTS are partly inappropriate when applied to non- bank CSD activities. Some adjustments are needed to allow for a proper reflection of CSDs' risk profile in their capital requirements.

(a) A re-calibration of the 15% ratio

Nasdaq supports the use of the Basic Indicator Approach for assessing operational and legal risks, but believes that **the 15% ratio used for banks should be recalibrated to 10% to reflect CSDs' lower risk profile.** Indeed, very few European CSDs have suffered any operational losses over the last 10 years, and, when there are any such losses, they tend to be extremely low.

Furthermore, Nasdaq believes **it should be possible to adjust the ratio to take into account the effect of CSD- specific insurance arrangements** covering operational and legal risks. Currently it is common both in the Nordic and the Baltic region where Nasdaq operates its CSDs, that some CSDs (e.g. Estonian CSD and Icelandic CSD) are obliged by law to subscribe special insurance arrangements against operational risks. Such arrangements protect the CSD's capital up to a certain amount should the risks materialise, and they are thus taken into account by national supervisors when determining minimum capital requirements for the CSD. Nasdaq CSDs are further covered by a group-wide professional liability insurance policies protecting regulated entities within the Nasdaq group against worst case loss-causing events in the area of operational and legal risks. These arrangements are a vital component of the CSDs' risk-management frameworks and should be recognised in the RTS.

Nasdaq

Nasdaq believes that, when CSDs have specific insurance arrangements to cover business and other risks, competent authorities should be allowed to take these into account (as well as any existing guarantee scheme, if applicable) when calculating capital requirements under art.4 of the draft RTS. This could be done, for example, by applying a lower ratio or by allowing CSDs to apply art.323 of the CRR (as regards the impact of insurance in the Advanced Measurement Approach) in the context of the Basic Indicator Approach calculations so that capital requirements for operational risk could be reduced by up to 20%.

Nasdaq thus recommends the following amendments to art.4 of the draft RTS:

Article 4 - Level of capital requirements for operational, legal and custody risks
*(…) 4. A CSD that is not authorised in accordance with Article 54(2) of Regulation (EU) No 909/2014 or a CSD that is authorised in accordance with point (a) of Article 54(2) of Regulation (EU) No 909/2014 but which does not have permission to use either the AMA as referred to in Articles 321 and 324 of Regulation (EU) No 575/2013, or TSA as referred to in Articles 317 to 320 of that Regulation, shall calculate its capital requirements for operational**, ~~and~~** legal **and custody** risks in accordance with the provisions of the Basic Indicator Approach as referred to in Articles 315 and 316 of that Regulation**, using a ten percent ratio**.*
National competent authorities shall be allowed to apply a lower threshold in the case of CSDs having a comprehensive liability insurance policy in place to cover operational and other risks. *(…)*

- **Article 5: Level of capital requirements for custody risks**

As explained in our response to Question 1, we believe that art.5 of the draft RTS should be deleted and that custody risk should solely be addressed under art.4 of the draft RTS.

- **Article 6: Level of capital requirements for investment risk**

CSDs, unlike banks, do not typically seek to generate income by investing client assets; client fees are the primary source of income. Investment and custody risks are thus very marginal compared with operational risk. Besides, given the restrictive investment policy imposed on CSDs by article 46 of the CSDR, in particular the obligation for a CSD to invest its assets in highly liquid instruments, investment risk is typically extremely low for CSDs. The EBA should thus be aware that some aspects of the proposed method for calculating capital requirements in relation to investment risk will not apply in the case of non-bank CSDs (e.g. CSDs typically do not enter into derivatives transactions).

Furthermore, Nasdaq wonders whether the consideration of tangible assets is adequate for CSDs. In particular, the fact that a CSD owns its office buildings (land and property used for the purpose of its own activities) should not result in a risk weight of 100% for assets as per art.134(1) of the CRR. Such property investments should not be considered in the context of investment risk (credit risk in particular) and the calculation of a CSD's risk-weighted exposure amounts for credit risk should be limited only to CSD's investment activities as described in art.46(3) of the CSDR ("*A CSD shall invest its financial resources only in cash or in highly liquid financial instruments with minimal market and credit risk*").

- **Article 7: Capital requirements for business risk and Annex II on business risk scenarios**

Given the nature of CSDs' businesses, in particular the fact that CSDs operate on considerably simpler and lower risk business models than banks or CCPs, Nasdaq believes that the 25% ratio for business risk is far too high. Using gross expenses as a reference is also inappropriate, as business risk should be primarily covered by net income (current or planned net income or EBIT). This would avoid unnecessarily high capital requirements, e.g. in case of a CSD that would remain profitable after the business risk scenarios described in Annex II have materialised. Equity coverage should only be required in case of net losses, hence there should be no 25% floor.

Nasdaq thus suggests amending art.7 of the draft RTS as follows:

Article 7 - Capital requirements for business risk
1. For the purposes of point (d) of Article 3(1), the capital requirements of a CSD ***together with retained earnings and reserves*** *for business risk shall be* ~~***the higher of the following:***~~
~~***(a)***~~ *the sum of all estimates resulting from the application of paragraph 2****.;***
~~***(b) 25% of the CSD's annual gross operational expenses.***~~ *(…)*

As regards Annex II (p.68) on business risk scenarios, Nasdaq is not convinced that predefined business risk scenarios are the most appropriate means to calculate capital requirements for business risk. We believe that a more flexible approach, similar to that in EMIR, allowing for example the use of reasonably foreseeable adverse scenarios relevant to the CSD's business model, as approved by the competent authority, could be more efficient and proportionate.

Should the EBA however decide to maintain Annex II and to impose the use of business risk scenarios, we believe that the following changes are necessary:

(1) The arbitrary percentages attached to each type of event should be removed. For example, an unexpected reduction of income of 30% will not necessarily affect the capital of a CSD,

and it should be possible for a CSD and its competent authority to assess the relevant fall in income that could require additional capital requirements, based on the CSD's own business model and risk profile;

(2) The reference to credit ratings should be removed in view of international and European initiatives calling for a progressive removal of references to ratings in regulation to reduce overreliance on them. Furthermore the EBA should be aware that several European CSDs, including the CSDs operated by Nasdaq, do not have credit ratings and do not issue debt. Annex II (a) will thus not be practically possible to apply for those CSDs. The CSDR does not require CSDs to obtain credit ratings, nor to issue debt.

(3) Points (e) and (f) of Annex II referring to long and short client balances should be removed as there are no such "balances" at CSDs and the notion is totally irrelevant for non-bank CSDs.

(4) Regarding contributions for pension plans under point (d), Nasdaq recommends that the EBA should make it explicit that this requirement only applies to defined benefit schemes and not to defined contribution schemes.

Nasdaq thus recommends either deleting Annex II entirely or amending it as follows:

Annex II - Business risk scenarios

The scenarios referred to in Article 35(2) for the calculation of the regulatory capital for business risks shall be:

(a) ***when CSDs have credit ratings****, the CSD's external rating downgrade of three notches by all the rating agencies that provide solicited ratings of the CSDs;*

(b) an unexpected ***substantial*** *increase of funding costs* ~~***of 10%***~~*;*

(c)) an unexpected ***substantial*** *reduction of income* ~~***of 30%***~~*;*

(d) ~~***10%***~~ ***substantially*** *higher than planned cash contributions for pension plans****, in the case of defined-benefits schemes****;* ~~***(e) an unexpected reduction of long clients' balances of 10%;***~~

~~***(f) an unexpected reduction in short clients' balances of 10%.***~~

- **Article 8: Capital requirements for winding-down or restructuring and Annex I on winding- down or restructuring scenarios**

As regards Annex I (p.67-68), Nasdaq agrees with the proposed definitions of restructuring (situations where the CSD no longer meets capital requirements but is able to continue to provide core services) and "winding-down" (situations where the CSD is no longer in a position to continue to provide all core services required under the CSDR licence) contained in paragraphs 1 and 2 respectively.

Nasdaq also welcomes the recognition, in paragraph 4, that *"the scenarios shall be commensurate with the nature of the business of the CSD"* and understands that CSDs with the simplest and

lowest risk profiles, including a low level of interconnectedness with non-domestic markets, will be able to assess capital requirements based on a shorter restructuring/winding-down period than CSDs with a more complex risk profile.

As regards paragraphs 5, 6 and 7, Nasdaq does not believe that the list of events proposed by the EBA is appropriate, especially for non-bank CSDs. For example, the "*failure of significant counterparties*" referred to in point (a) will typically not lead to a restructuring or winding-down of a CSD, since non-bank CSDs are not exposed to counterparty credit risk in relation to their participants, unlike CCPs. The same reasoning applies in case of a "*severe outflow of liquidity*". It will thus be impossible for most CSDs to include the listed scenarios in a meaningful way in their winding-down plan. Imposing that all CSDs include all scenarios, as suggested by the current wording of the Annex, does not make sense. As a result, Nasdaq suggests either removing all references to "*idiosyncratic events*" and "*systemic-wide events*", at least for non-bank CSDs, or allowing CSDs, together with their competent authority, to select and calibrate the relevant scenarios according to their own business models. This approach would be in line with the PFMI and EMIR.

Finally, CSDs should have the possibility to remove certain expenses from gross expenses, in particular:

- when these are not relevant in a winding-down situation, e.g. because they can be cancelled immediately from the moment the CSD enters into restructuring (e.g. bonuses, staff and commercial events, large projects);
- when these do not involve a cash outflow, such as depreciation and amortization expenses (see Principle 15 of the FMI, footnote 137 p.90).

Nasdaq recommends either deleting paragraphs 5, 6 and 7 entirely or alternatively making the following amendments to Annex I:

Annex I - Winding-down or restructuring scenarios

[…] ***~~5. When designing the scenarios, a CSD shall meet each of the following requirements:~~***

~~(a) the events foreseen in the scenario would threaten to cause the restructuring of the CSD operations;~~

~~(b) the events foreseen in the scenario would threaten to cause the winding-down of the CSD operations.~~

6. The plan ensuring an orderly restructuring or winding-down of the CSD's activities referred to in point (b) of Article 47(2) of Regulation (EU) No 909/2014 shall, ***where relevant,*** *include* ***~~all~~*** *the following scenarios ('idiosyncratic events'):*

(a) the failure of significant counterparties;

(b) damage to the institution's or group's reputation;

(c)) a severe outflow of liquidity;

(d) adverse movements in the prices of assets to which the institution or group is predominantly exposed;

(e) severe credit losses;

(f) a severe operational risk loss.

7. The plan ensuring an orderly restructuring or winding down of the CSD's activities referred to in point (b) of Article 47(2) of Regulation (EU) No 909/2014 shall, ***where relevant,*** *include* ~~***all***~~ *the following scenarios ('system-wide events'):*

(a) the failure of significant counterparties affecting financial stability;

(b) a decrease in liquidity available in the interbank lending market;

(c) increased country risk and generalised capital outflow from a significant country of operation of the institution or the group;

(d) adverse movements in the price of assets in one or several markets;

(e) a macroeconomic downturn.

- **Comments on the draft impact assessment (p.69-78)**

Nasdaq welcomes the EBA initiative to undertake a survey among CSDs, via national competent authorities, to assess the impact of the proposed measures on the current level of capital of CSDs. Given that the calculation method being proposed by the EBA for capital requirements is totally unprecedented for non-bank CSDs, it is all the more important that the EBA carefully estimates the quantitative impact of the proposed RTS on current capital levels of CSDs before the RTS are finalised. The simulation exercise is also important to identify potential problems and unintended effects prior to the finalisation of the standards.

In order to ensure a proper impact assessment, we recommend that the EBA considers not only changes in the amount of capital to be maintained by CSDs, but also changes to the structure of that capital. Indeed, art.46(3) and (4) of the CSDR state that the amounts of capital which are not invested in cash or highly liquid financial instruments with minimal market and credit risk shall not be taken into account for the purposes of art.47(1). This means that some CSDs might have to overhaul their asset structure without necessarily having to raise their capital, and we believe that such changes in the share of cash and highly liquid instruments in total assets should be reflected in the impact assessment.

We anticipate that the draft RTS would result in an increase of minimum capital requirements for all Nasdaq CSDs, raising the bar far beyond current domestic requirements and the PFMI. That said the impact of the RTS on the capital level of most CSDs should be limited by the fact that CSDs are often significantly overcapitalised on the basis of current minimum requirements. This should not prevent a few CSDs from having to raise a significant amount of additional capital as a result of the implementation of the standards, with possible repercussions on the level of CSD fees.

2. Capital surcharge for providing banking-type services (art.54 CSDR)

This section refers to Title II of the draft RTS (p.25-26) and Section 5.1(2) of the draft impact assessment (p.73-74) which relates to prudential requirements applicable to credit institutions or CSDs authorized to provide banking-type ancillary services. Since none of the Nasdaq CSDs operates banking type services we will not provide a response to the questions under this section.

Q3. What are the operational or practical impediments to the implementation of the proposed methodology for the calculation of the capital surcharge (Article 9)? Do you envisage any amendment to the proposed methodology that might lead to a better measurement and management of those risks?

No comment

3. Prudential requirements in relation to banking-type services (art.59 CSDR)

This section refers to Title III of the draft RTS (p.27-66) and Section 5.1(3) of the draft impact assessment (p.74-77) which relates to prudential requirements applicable to credit institutions or CSDs authorized to provide banking-type ancillary services. Since none of the Nasdaq CSDs operates banking type services we will not provide a response to the questions under this section.

Q4. To what extent do CSD-banking service providers have the capability to have a real-time view on their positions with their cash correspondents, based on compulsory information provided by those cash correspondents (Article 14)?

No comment.

Q5. What might be the practical, legal or operational impediments to the methodology set out in Sub-section on Collateral and other equivalent financial resources (Article 18)?

No comment.

Q6: What are the practical impediments of the implementation of Article 24?

No comment.

Q7. To what extent do CSD-banking service providers hold their intraday liquidity risk buffers independently to other liquidity risk buffers, such as the Liquidity Coverage Ratio (LCR)? If this is not currently done, are there any obstacles to ensuring this? Can CSD-banking service providers estimate the intraday buffer assets required to meet Article 35 compared to the assets that they currently hold that would qualify as eligible liquid assets under this Regulation beyond the minimum LCR standard?

No comments.