

## **European Short Selling Regulation: Article 15, Buy-in procedures**

### **Frequently Asked Questions**

Please see below a series of questions and answers containing information that will help clearing members better understand our buying-in operational processes and procedures as a result of the regulation.

#### **1. What is Article 15?**

The regulation advised by European Parliament and of the Council of the European Union, states the following:

A central counterparty in a Member State that provides clearing services for shares shall ensure that procedures are in place which comply with all of the following requirements:

- (a) where a natural or legal person who sells shares is not able to deliver the shares for settlement within four business days after the day on which settlement is due, procedures are automatically triggered for the buy-in of the shares to ensure delivery for settlement;
- (b) where the buy-in of the shares for delivery is not possible, an amount is paid to the buyer based on the value of the shares to be delivered at the delivery date plus an amount for losses incurred by the buyer as a result of the settlement failure; and
- (c) the natural or legal person who fails to settle reimburses all amounts paid pursuant to points (a) and (b).

A central counterparty in a Member State that provides clearing services for shares shall ensure that procedures are in place, which ensure that where a natural or legal person who sells shares fails to deliver the shares for settlement by the date on which settlement is due, such person must make daily payments for each day that the failure continues.

The daily payments shall be sufficiently high to act as a deterrent to natural or legal persons failing to settle

#### **2. When will the buy-in regulation commence & will Market Makers be exempt?**

LCH.Clearnet will implement the regulation from Monday 29 October 2012. All clearing members will be subject to the regulation of Buy-in initiation on ISD+4 however concessions have been made for registered Market Makers and subsequent market making business in their registered ISIN's. They will benefit from a delayed buy-in initiation of ISD+10 also reduced failed settlement costs

**3. What will the phased approach look like?**

LCH.Clearnet Ltd will move the buy-in timelines to allow members time to adjust to the regulation. Please review the buy-in presentation for full details across both LCH.Clearnet SA and LCH.Clearnet Ltd

**4. What are the costs associated with buying-in?**

Buy-in Administration charge of £125 Ltd / €150 SA  
 Buy-in dealing costs are included in buy-in consideration  
 Clearing and settlement costs are charged as cleared trades  
 There is also a fixed payment per failed settlement, per day of £20 Ltd / €15 SA.  
 There will be a fixed payment for Market Makers per fail, per day of £2.00 (Ltd only)  
 A variable, ad valorem charge of Reference benchmark interest rate + 1% charged on the net consideration of the failed settlement, for each business day of the fail.

**5. Will LCH compensate clearing members where LCH is unable to deliver?**

From February 2 2015, The EquityClear service will compensate clearing members with the Ad valorem charge, where EquityClear fails to deliver securities to its clearing members.

The Ad valorem compensation to be credited to members where EquityClear is net failing to deliver.

Compensation will be credited to members at a rate of 70% of the Ad valorem fee charged.

From 1st September 2016, LCH Ltd will remove the failed settlement compensation in the below markets.

| Market                     | CSD                    |
|----------------------------|------------------------|
| UK                         | Euroclear UK & Ireland |
| Norway                     | VPS                    |
| Denmark                    | VPC                    |
| Finland                    | Euroclear Finland      |
| Sweden                     | Euroclear Sweden       |
| Depository Receipts & ETFs | Euroclear Bank         |
| Switzerland                | SIS                    |

All credits and debits will be itemised within the existing month end report EREP0028- Fees- Fails charges

**6. What will LCH.Clearnet do with the cash generated from the buying-in costs?**

The administration charge and fixed payment cost will become revenue. However, the variable, ad valorem charge is subject to reimbursement

**7. What is the rationale for the charging levels?**

We have harmonised the administration charge across the group.

In the Article it states:

“The daily payments shall be sufficiently high to act as a deterrent to natural or legal persons failing to settle”

Therefore, we have set our fixed daily payment as above, which we feel is set at a suitable level to act as a deterrent

**8. Are the charges subject to VAT**

No, all additional costs are exempt of VAT.

**9. Are the costs subject to change?**

Yes, we will monitor the behaviour of our members and the resulting level of fails that require buying-in. If buy-in levels increase, we will discuss with the responsible parties and if necessary increase the daily fixed penalties to act as a deterrent. If buy-in rates decrease we can assume that the fixed penalties have acted as a suitable deterrent and could possibly be decreased

**10. Will LCH.Clearnet issue guidance or criteria for participants to better understand what would trigger a review?**

No

**11. Has LCH.Clearnet discussed/agreed the level of charges with other CCP's?**

No

**12. Will there be any charging of buy-ins between CCP's**

No

**13. Will LCH.Clearnet buy-in if clearing member is short Primary exchange but long MTF?**

No, the buy-in will not be processed if the clearing member is using the same CCP and the same settlement account at the CSD for both. However, if the clearing member is using different CCP's then yes, the buy-in will be processed. This also applies to members that are using LCH.Clearnet SA versus LCH.Clearnet Ltd

**14. Will LCH.Clearnet provide any modelling of old versus new buying-in costs?**

No

**15. Can LCH.Clearnet provide an example of a failing settlement charge?**

Example:

Settlement failing for 3 days and current value £1,000.00

Calculation:

Fixed payment X 3

£1,000.00 X 0.004% for Ltd, and 0.003% for SA, X 3

**16. Which products will be included in the regulation?**

As a result of the regulation we will reflect in our rules and apply to all EquityClear & continental cash securities markets. It will include all cleared equities and cash settled bonds traded on NYSE Euronext, Bourse de Luxembourg and Galaxy and cleared by LCH.Clearnet SA. It will also include trades that are due to settle as a result of option traded on NYSE Euronext and Turquoise but will not include result of options traded on NYSE Liffe London.

The regulation & our rules will not cover instruments cleared through our RepoClear or Swapclear services

**17. Will LCH.Clearnet include other trading venues?**

Yes, if they are included in the existing cash equity services

**18. Can clearing members partial to LCH.Clearnet?**

As is the case now, for LCH.Clearnet Ltd this depends on the service facilitated by the CSD. For LCH.Clearnet SA clearing members can partially settle open or failed positions

**19. Will a partial delivery reduce the cost of the variable, ad valorem charge?**

Yes, at the end of day we will process all open net positions to calculate the charges due.

**20. Can a clearing member pass on buying-in charges to a CCP?**

No

**21. From the proposed phased effective dates & subsequent implementation date, will all fails be subject to the rules within the Article?**

For LCH.Clearnet Ltd any fails that have been failing for more days than the buy-in timing, when the effective dates have been reached, will be subject to buy-in. For LCH.Clearnet SA we will apply a buy-in on all trades that have been failing for four days or more from 29 October. It should also be noted that we will only apply the daily charge from 1 November 2012

**22. Can a waiting buyer initiate a buy-in on ISD+5?**

No, from 29 October 2012 and at close of business on ISD+4, LCH.Clearnet will have automated processes in place to begin the buy-in procedure

**23. Will Cash out remain at ISD + 20 for LCH.Clearnet Ltd?**

We will review the cash out timeline and possibly harmonise between LCH.Clearnet Ltd and SA

**24. Will failed buy-ins be cash settled at 120% of the last available price?**

Yes, across both LCH.Clearnet Ltd & LCH.Clearnet SA.

**25. If the trade remains unsettled will the daily charge continue until cash out?**

Yes

**26. When LCH buy-in will the daily fail charge cease?**

No, the daily fail charge will cease upon settlement date of the buy-in.

**27. If I buy the position back to cover, will the daily fail charge cease?**

No, the daily fail charge will cease upon settlement date of the purchase

It should be noted that where a participant owes stock to LCH we will charge. However, if the participant owes the stock to LCH as a result of LCH not delivering the stock to the participant, we will not charge

**28. How will LCH.Clearnet notify clearing members of Buy-in costs and daily fails charges?**

There is no change to the LCH.Clearnet SA process. However for LCH.Clearnet Ltd all Buy-in costs, daily fails payments and any reimbursements will be detailed in the month end invoices

**29. Will the invoice contain charges at NCM level**

No, not at NCM level, however, for LCH.Clearnet Ltd we will advise detail at settlement firm ID level

**30. Other than the month end invoice what additional information will be provided?**

LCH.Clearnet SA will publish the Buy-in Information File (BIF) with record type 10, on ISD+3 and record type 20 will be published on ISD+4.

LCH.Clearnet Ltd issue a Fails Settlement report EREP0025 that contains the buy-in trigger dates. Buy-ins will be included in our existing EREP0006 report. We also issue a fails charges report EREP0028 that is produced at month end

**31. How will a buy-in be identified in the reports?**

No change to the LCH.Clearnet SA (BIF) files. For LCH.Clearnet Ltd all buy-ins will contain the value 'BUYN' within the 'tradeplace' field in both reports above.

It should be noted there will be no change to format of our reports

**32. Will LCH.Clearnet issue buy-in notifications to settlement agents?**

No, buy-in notifications will not be produced. Clearing members will be required to retrieve all buy-in details from our member reports

**33. Will LCH allow 5 days notice before buying-in?**

No, if the delivery remains open at COB on ISD + 4, we will attempt to buy-in the following day.

**34. What happens if I deliver the original sale after the buy-in has taken place?**

If the buy-in is successful, the stock will be delivered to the failing seller, whereby they will become owners of the stock.

**35. Will LCH net off future or outstanding purchases against the undelivered sale?**

For LCH.Clearnet Ltd yes, if a purchase of the same ISIN with the same settlement account details is made prior to the buy-in date, then the buy-in will not be processed. For LCH.Clearnet SA, there has been no change to existing process

**36. Will LCH net off the purchase if it is less than the outstanding sale?**

For LCH.Clearnet Ltd yes, if your failing delivery of 10shares is due to be bought in, but you have made a purchase of the same ISIN for 5shares, the buy-in will be for 5 shares. For LCH.Clearnet SA, there has been no change to existing process

**37. What is the last time to purchase the stock to avoid a buy-in?**

For LCH.Clearnet Ltd, the latest a member can purchase the stock is up to the close of business on ISD+4 or ISD+10. The purchase will avoid the buy-in.

However, if the purchase is made against a trading firm that uses the same GCM & Settlement Firm ID as the seller, then the new trades will net to zero and the buy-in will continue to be processed. Also, the purchase must not be off-set by a same day sale, as this will negate the delivery instruction in the CSD that is required by us, to ensure the buy-in is avoided.

For LCH.Clearnet SA you will be required to contact your local RM.

**38. If a member has multiple sales in the same ISIN due to be bought in, will LCH apply multiple buy-ins?**

No, a single netted buy-in and a single charge will apply, provided deliveries are due in the same settlement account at the CSD for the same settlement firm ID.

**39. Where can I review the new LCH.Clearnet Ltd report specification?**

The LCH.Clearnet Ltd report specification can be found using the following link:  
[http://www.lchclearnet.com/Images/EquityClear%20Member%20Reports\\_tcm6-47620.pdf](http://www.lchclearnet.com/Images/EquityClear%20Member%20Reports_tcm6-47620.pdf)

**40. Will the Article and subsequent LCH.Clearnet buy-in changes replace the current buy-in processes available from some trading platforms?**

Yes

**41. Will early buy-in remain?**

Technically early buy-in could take place from ISD+1. However, LCH.Clearnet will ensure that no buy-in will be processed before ISD+4.

**42. Is it possible that both the CSD and the CCP apply their charges to a single failing trade?**

For confirmation of how a CSD will operate its late settlement regime, we would advise clearing members to contact the CSD's directly.