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TARGET2-Securities User Requirements Consultation

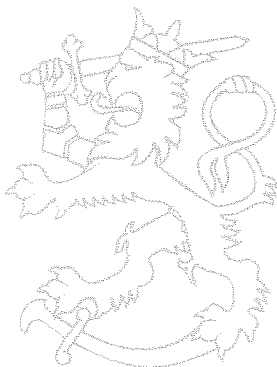
Dear Mr Godeffroy

The Finnish Ministry of Finance would like to thank the European Central Bank for organising the current consultation process in the context of TARGET2-Securities (T2S) User Requirements Documentation (URD).

In general, we are pleased to note that the ECB has chosen a transparent and consultative method with market participants and national authorities in preparing the T2S initiative. We appreciate the commitment the ECB team has shown to understand and handle the problems arising in the project, and we are grateful for all the information received.

The Ministry of Finance has been involved in the work of Finnish T2S User Group (FIN NUG) chaired by the Bank of Finland, and has been given the opportunity to participate in the drafting of FIN NUG's detailed comments on the URD. The Ministry of Finance fully shares the views expressed in the FIN NUG's reply and its enclosures. Therefore, we think there is no need for detailed feedback on the URD by the Ministry.

However, the Ministry of Finance would like to emphasize some issues especially relevant from our perspective:



The potential of T2S

There are several reasons to support a single settlement service in Europe. T2S could make securities settlement borderless and should be able to offer economies of scale to be shared by all participants. Furthermore, T2S could make the use of cash more efficient and increase liquidity on European securities markets. We therefore have a generally positive view of the goals and potential of T2S.

Settlement and asset servicing

We understand the T2S as a service engine and platform providing settlement services to Central Securities Depositories, but it does not itself constitute a system under the settlement finality directive (SFD) nor does it set-up a European CSD. In sum, book-entries are only 'technically' in T2S.

Yet, the General Principle 6 of T2S states "Securities account balances shall only be changed in T2S". Furthermore, the prevailing message from the ECB is that users need only a single account at one CSD to settle any transaction in securities in T2S. We think these premises can make the operation of T2S very challenging, and the separation of settlement and asset servicing is still partly blurred. One special area requiring further analysis is the handling of corporate actions in the context of T2S. In addition, we would like to mention that, as the SFD is implemented in a different way in several EU Member States, there might be problems for ensuring finality in a European level settlement service.

Direct holdings

The Finnish book-entry system is based on direct holdings. According to our national legislation, securities accounts must contain all the relevant information concerning securities holdings, including the respective rights and restrictions related to accounts and securities. We would suggest that incorporating a template for such data more generally in T2S could appreciably enhance the potential use of this EU-wide system in the future. For Finland, it would be particularly important that these requirements are fully met in the core service of T2S.

In addition, as stated in the ECOFIN Council Conclusions in February 2007: "The technical specifications should enable both direct and indirect holdings of securities in T2S, with the same efficiency and costs". We have the impression that the ECB is working on the system in this spirit, but we still hope to be able to receive full confirmation and clarity on these issues as soon as possible.

The Ministry would like to stress that the handling of direct holding systems is also a crucial matter in the pricing of services, as high costs per transactions and charges for individual accounts could make the participation of these countries in T2S economically almost impossible.

Outsourcing and legal aspects

The ECB underlines that T2S is only a technical platform where CSDs can outsource their settlement operations. Furthermore, it appears that the relationship between T2S and national CSDs is to be regarded as a contractual one. But, particularly in the case of a direct holding system, these views may not prove sufficiently operational. Therefore, it appears necessary to carefully analyse the legal and contractual framework to make T2S accommodate several legal systems.

In the case of Finland, the legal information received so far is not sufficient, for example, to make it possible to give to the national CSD a permission to transfer and outsource its responsibilities to ECB as a service provider. We also suspect that the implementation of T2S could lead to hitherto unforeseen need for legal change in Finland. Reassuringly, the ECB and the Eurosystem have indicated that further T2S legal work is under preparation, and we look forward to having this important legal output in the near future.

Economic feasibility and pricing

While T2S should lead to lower settlement costs, we find it worrying that, at this rather advanced stage of the planning process, the business case apparently is not yet fully proven to the satisfaction of potential participants. We think it is important, from several points of view, that the ECB rapidly finalizes a credible and transparent economic impact analysis, as we understand is intended.

Furthermore, it is important that T2S pricing principles and structures are clearly developed and evaluated as part of this analysis. We find it crucial that the pricing should not, directly or indirectly, give a competitive advantage to any national market, operator or any particular CSD market model. Since the T2S service is created and provided by a public EU institution, efforts to avoid distorting competition must remain beyond reproach.

Governance and supervision

There remains a lack of consensus to what extent T2S is simply a technical platform and to what extent it in reality casts the ECB in a new role of infrastructure provider in competition with private operators. To minimize the risk of appearing to do the latter, we think the ECB should consider governance issues very carefully at the outset.

Indeed, we think that creating a fully separate legal entity – eventually perhaps largely owned and administered by its customers – would go a long way in this regard. This would also make the adaptation to changes in the market environment easier and could make substantially more credible the declared lack of cross-subsidization in operations. Further, we think that a separate legal entity would help in organising the supervision that the service undoubtedly requires.

Multicurrency

To solve efficiency and cost problems in European cross-border securities settlement, T2S must be open to all European countries and currencies. We are pleased to note that the URD now rests on this idea, which is a very significant starting point from the perspective of Nordic-Baltic securities markets.

Market evolution

We have a feeling that the URD appears to be mainly focused on responding to present challenges. However, the system should be able to adapt to future needs flexibly and without major new costs. We consider that T2S could be planned so that it is more instrumental in helping to reduce Giovannini barriers, address stability and supervisory concerns, and increase market transparency, including shareholder transparency if and when so is desired. The possibility for such transparency would be greatly increased, if the T2S system architecture were built to fully accommodate individual accounts whenever national CSDs, authorities and political decision makers are ready to do so. Also, appropriate governance solutions would help retain flexibility.

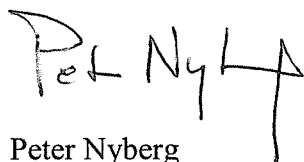
Conclusions

The Ministry of Finance considers the URD generally offering the ‘tracks’ on which T2S could run, but there are several key points which are not fully settled yet. We hope that the points mentioned in this letter could be reflected in the future work. In particular, we hope that the issue of legal aspects is further addressed in close relationship with the Member States. From the Finnish perspective, the most important legal question related to T2S is the national requirements of direct-holding book-entry accounts.

The Ministry of Finance accepts that this letter can be published on the ECB’s website in the same way as all the other URD comments.

Yours sincerely

Ministry of Finance
Financial Markets Department

A handwritten signature in black ink that reads "Peter Nyberg". The signature is written in a cursive style with a large, stylized 'P' and 'N'.

Peter Nyberg
Director General