

# **KELER - Depository Announcement 9-24**

## **On the Detailed Rules on the Management of Penalties**

**Entry into force: 17 March 2022**

## Table of Contents

_Toc971425211.....	Introduction	2
2. Definitions used in the Depository Announcement.....		2
3. Application of penalties.....		2
3.1. Legal background .....		3
3.2. Financial instruments and instructions subject to cash penalties.....		3
3.3. Types and calculation of penalties .....		4
3.3.1. LMFP (Late Matching Fail Penalty).....		5
3.3.2. SEFP (Settlement Fail Penalty).....		6
3.3.3. Calculation methods and penalty rates.....		6
3.3.4. Currency of the penalties .....		9
3.3.5. Daily reference price of the security.....		9
3.4. Penalty reporting, reports.....		10
3.4.1. Daily report .....		10
3.4.2. Monthly report .....		11
3.4.3. Reporting of penalties from foreign CSDs .....		11
3.4.4. Zero report.....		11
3.5. Life cycle of penalties, penalty calendar.....		12
3.6. Appeals, modification of penalties .....		13
3.7. Settlement of penalties.....		15
3.8. Procedure to be followed in insolvency procedure .....		17
3.9. Handling of penalties due for transactions cleared by the central counterparty .....		18
4. Contact details .....		18
5. Transitional provisions .....		19
6. Appendix.....		21

## 1. Introduction

The purpose of this Depository Announcement is to set out the details of the sanction mechanism for penalties that KELER is obliged to apply in order to enforce the settlement discipline in conjunction with the provisions of Chapter II.4.9 on Settlement Discipline of the General Business Rules of KELER (General Business Rules). The application of the sanction mechanism is provided based on the CSDR<sup>1</sup> and the related Settlement Discipline Regulation (SDR)<sup>2</sup>, and the provisions established by KELER in this Depository Announcement are aligned with these rules.

Among the measures affecting settlement discipline, this Depository Announcement details the process and conditions for the application of penalties, the sending of the related reports, and the way in which penalties are collected and distributed.

## 2. Definitions used in the Depository Announcement

The terms and expressions used in this Depository Announcement shall have the meaning ascribed to them in the General Business Rules (General Business Rules) and in the relevant legislation and the ECSDA Framework.

## 3. Application of penalties

Pursuant to Article 7(2) of the CSDR, KELER shall impose penalties on Account Holders causing failed settlements in the Settlement System.

The penalty, as one of the sanction mechanisms provided for by law, does not form part of the revenues of KELER, but is passed on to the innocent Account Holder in the failed settlement.

With regard to the management of penalties, KELER also follows the recommendations of the European Central Securities Depositories Association (ECSDA)<sup>3</sup>, i.e. it applies the guidelines summarised in the ECSDA CSDR Penalties Framework document.

**From 2 May 2022, KELER will start to fully apply the Penalty Mechanism for settlement instructions failed in its own Settlement System, but at the same time it will have to implement**

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<sup>1</sup> Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012

<sup>2</sup> Commission Delegated Regulation (EU) 2018/1229 of 25 May 2018 supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council with regard to regulatory technical standards on settlement discipline

<sup>3</sup>Detailed information on penalties is provided in the ECSDA CSDR Penalties Framework document. (The latest version available at the time of editing this Depository Announcement is available here: [https://ecsda.eu/wp-content/uploads/2021/10/2021\\_10\\_05\\_ECSDA\\_CSDR\\_Penalties\\_Framework.pdf](https://ecsda.eu/wp-content/uploads/2021/10/2021_10_05_ECSDA_CSDR_Penalties_Framework.pdf))

the ex-post collection or distribution of penalties for failed settlement instructions with a detection date on or after 1 February 2022.

For details of the transitional arrangements, see Chapter 5.

However, as from 1 February 2022, KELER will forward the penalties incurred by foreign CSDs to its clients and will collect and distribute the penalties within the prescribed time limits.

### **3.1. Legal background**

KELER has developed the rules and processes for penalties based on the following legal provisions, industry recommendations and other documents:

- Regulation (EU) No 909/2014 of the European Parliament and of the Council on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (CSDR)
- Commission Delegated Regulation (EU) 2018/1229 supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council with regard to regulatory technical standards on settlement discipline (SDR)
- Commission Delegated Regulation (EU) 2017/389 supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council as regards the parameters for the calculation of penalties for non-compliance with the settlement and the activities of CSDs in host Member States
- Regulation (EU) No 600/2014 of the European Parliament and of the Council on markets in financial instruments and amending Regulation (EU) No 648/2012
- ESMA Questions and Answers - Implementation of the Regulation (EU) No 909/2014 on improving securities settlement in the EU and on central securities depositories.
- ECSDA CSDR Penalties Framework

### **3.2. Financial instruments and instructions subject to cash penalties**

Penalties apply to trades made on both trading venues and on the OTC market.

Penalties may be imposed on matched<sup>4</sup> settlement instructions that have not been settled on the intended settlement date and are for the settlement of MiFID II/MiFIR financial instruments (transferable securities, money market instruments, units in collective investment undertakings, emission allowances) that:

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<sup>4</sup> Unmatched settlement orders are not subject to penalties, i.e. they can only be taken into account for the purposes of applying a penalty after the order has been successfully matched. For details see chapter 2.3.

- are tradable on an EU trading venue, or
- may be cleared by an EU CCP
- except shares whose primary trading venue is in a third country.

The above criteria for determining whether a financial instrument should be considered subject to a penalty are determined on the basis of the databases maintained by ESMA:

- Instruments admitted to trading venues in the EU are included in the Financial Instruments Data System (FIRDS)<sup>5</sup> database.
- The list of shares whose primary trading venue is outside the EU can be determined on the basis of the Short Selling Regulation (SSR)<sup>6</sup> list.

New or changed data in the ESMA databases are taken into account from the business day following the change.

KELER calculates the penalty for all instructions failed in its own settlement system, including for intra-CSD settlements on the T2S platform. However, no penalties apply to securities blocking transactions, as these transactions do not constitute settlement instructions and do not result in the transfer of financial instruments between accounts.

If the settlement fail does not take place in the settlement system of KELER but in the system of a foreign CSD subject to CSDR through the intermediation of KELER, the calculation and reporting of the penalties for these settlement instructions is the responsibility of the CSD concerned. KELER receives these reports from its external account servicers (currently SIX SIS - Switzerland and KDPW - Poland).

KELER also sends daily and monthly reports to its clients on the penalties received from foreign CSDs, and the settlement of penalties levied and passed on by these external settlement venues is also performed by KELER by debiting or crediting the client accounts with KELER.

Account Holders are responsible for allocating, reporting and passing on the penalty amounts to their clients.

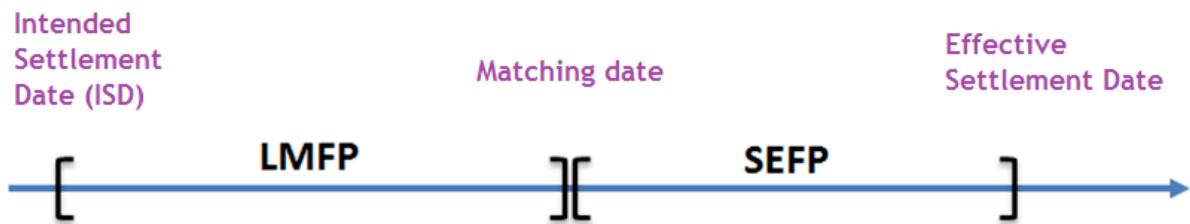
### **3.3. Types and calculation of penalties**

The following two types of penalties are distinguished, depending on when the matching of the settlement instructions concerned took place in relation to the intended settlement date or cut-off date.

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<sup>5</sup> [https://registers.esma.europa.eu/publication/searchRegister?core=esma\\_registers\\_firds](https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_firds)

<sup>6</sup> [https://registers.esma.europa.eu/publication/searchRegister?core=esma\\_registers\\_mifid\\_shsex](https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_mifid_shsex)



1. Figure 1 - Types of penalties depending on the intended settlement date

### 3.3.1. LMFP (Late Matching Fail Penalty)

If settlement instructions are successfully matched on the business day following the intended settlement date (ISD), or the matching takes place on the intended settlement date but after the settlement cut-off time, before the close of the relevant business day, a late matching penalty may be imposed retroactively for up to several business days (N) at a time, from the intended settlement date to the matching date.

The Account Holder who was the last to submit a settlement instruction shall be liable to pay the penalty. (Even in the case where both Account Holders submitted their instructions after the ISD cut-off time.)

The penalty detection date in case of LMFP is the same as the date of matching.

Calculation formula for DF, RF, RVP, DVP (i.e. instructions resulting in actual securities movement), where the projection basis for the penalty is the market value of the failed security quantity:

$$\text{LMFP} = \sum_{n=1}^N (\text{Penalty rate} * \text{Securities daily reference price} * \text{Securities quantity})$$

Calculation formula for PFOD instructions (i.e. instructions with no actual securities movement):

In this case, the basis for calculating the penalty is

$$\text{LMFP} = \sum_{n=1}^N (\text{Penalty rate (daily borrowing rate)} * \text{Settlement amount})$$

Therefore, the penalty calculated for late matching is the sum of the individual penalties calculated for each penalty date (business day).

If an already matched settlement instruction is submitted late, in default the selling (transferring) Account Holder in the instruction is the at-fault party and the penalty is charged to the seller. However, the selling Account Holder, if approved by the receiving Account Holder, may request KELER to reallocate the penalty to the other party through an appeal. If the failure was caused by the

third party - trading venue - that submitted the instruction, the Account Holders concerned may claim directly from the trading venue the reimbursement of the amount of the penalty, outside the penalty mechanism operated by KELER.

Please note that for securities accounts where the Account Holder has enabled automatic transfer crediting, - i.e. where a transfer order (FOP TRAD) from the transferring Account Holder causes KELER to generate a matching settlement instruction on behalf of the receiving Account Holder - in the case of a failed settlement instruction submitted by the transferring party after the ISD cut-off time, the receiving Account Holder is considered at fault, given that the instruction automatically generated on its behalf has the subsequent acceptance timestamp!

### **3.3.2. SEFP (Settlement Fail Penalty)**

Penalty calculated for the period between the intended and effective settlement date(s), payable for settlement instructions that are matched until the applicable cut-off on the intended settlement date, but are not settled on the intended settlement date or on the following business day(s). On a business day, only the SEFP for that day will be charged, i.e. in the case of consecutive failures over several days, penalties will be calculated separately for each business day.

The penalty detection date for a SEFP-type penalty is the same as the date of settlement failure.

The penalties (SEFPs) are determined on the basis of the status and reason for failure of the settlement instruction concerned at the end of the settlement window (i.e. cut-off time) relevant for the transaction type concerned. This reason determines whether a penalty is to be imposed on the instruction and which counterparty is subject to the penalty.

*Accordingly, for example, in the case of a DVP-type settlement instruction, KELER will look at the relevant settlement cut-off, i.e. the status at 17:30: the seller may be subject to penalties due to lack of securities (LACK), the buyer due to a shortage of funds (MONY), and both parties may be subject to penalties simultaneously for instructions held in hold status (PREA, BOTH) (if both parties' instructions are held).*

Calculation formula for DF, RF, DVP, RVP (i.e. instructions resulting in actual securities movement) instructions:

$$\text{SEFP} = \text{Penalty rate} * \text{Securities daily reference price} * \text{Securities quantity}$$

Calculation formula for PFOD instructions (i.e. instructions with no actual securities movement):

$$\text{SEFP} = \text{Penalty Rate (overnight credit rate)} * \text{Settlement Amount}$$

### **3.3.3. Calculation methods and penalty rates**

The calculation method to be used determines the type of penalty rate.

- **A SECU-type calculation method** shall be used for the following types of settlement instructions resulting in actual securities movements:
  - DF: Delivery Free of Payment
  - RF: Receipt Free of Payment
  - DVP: Delivery versus Payment

The penalty is calculated on the basis of the market value of the quantity of securities failed, i.e. the quantity of securities multiplied by the reference price of the security on the date of failure.

In the case of partial settlement, only the remaining outstanding amount of securities is taken into account.

The applicable penalty rates are set out in Table 1 (see below)

Under the SECU-type calculation methodology, a penalty may be calculated if the settlement instruction of the party at fault has one of the following settlement reason codes at the settlement cut-off time on the relevant business day:

- PENF (FIng) / LACK: lack of securities
- PENF (FIng) / PREA or BOTH\*: withheld (alone or by both parties)
- PENF (FIng) / INBC: related settlement instruction in the same pool missing (possible for FOP transfers)
- PENF (FIng) / LINK\*\*: related settlement instruction in the same pool has failed (possible for FOP transfers) or when, in the case of repo transactions, the maturing leg has not been settled due to the failure of the initial leg.
- PENF (FIng) / OTHR: in case of other reasons for failure

**Table 1: Penalty rates to be used for the calculation of penalties (basis point)<sup>7</sup>**

(In brackets, the classification of the financial instrument concerned according to the CFI code under the CSDR)

<i>Liquid shares (SHRS)</i>	<i>1.00 bp</i>
<i>Illiquid shares (SHRS)</i>	<i>0.50 bp</i>
<i>Government securities (SOVR)</i>	<i>0.10 bp</i>
<i>Corporate bonds (DEBT, MMKT)</i>	<i>0.20 bp</i>
<i>Financial instruments traded on SME growth markets (e.g. BSE Xtend), excluding bonds* (SHRS)</i>	<i>0.25 bp</i>

<sup>7</sup> For details see: Regulation EU 2017/389



Bonds* traded on SME growth market (DEBT,MMKT)	0.15 bp
For other financial instruments (SECU, ETFS, UCIT, EMAL, OTHR)	0.50 bp

1 basis point (bp) = 0.01 %

Transactions in the SME growth market are identified by KELER on the basis of the MIC code of the Place of Trade in the settlement instruction, if this information is provided.

Illiquid shares are defined on the basis of the ESMA FITRS<sup>8</sup> database (Financial Instruments Transparency).

- The **MIXE calculation method** is used for RVP (Receive versus Payment) type settlement instructions. In this case the market value of the failed securities is the basis for calculation. In this case, the penalty rate is the official interest rate charged by the central bank issuing the settlement currency for overnight credit<sup>9</sup>, which may not be less than 0. (That is, in the case of a negative interest rate, the amount of the penalty is 0.)

For each business day, the 1/360th of the published annual interest rate is used for the calculation, i.e. the daily interest rate, and the daily interest rate is also used in the penalty reports.
- CASH type calculation method** is used for PFOD type settlement instructions. Since there is no actual movement of securities in these transactions and therefore no market value of the securities can be interpreted, the basis for the calculation of the penalty is the matched settlement amount.

In this case, the penalty rate is also equal to the official interest rate charged by the central bank issuing the settlement currency on a daily credit basis, which cannot be less than 0. (That is, in the case of a negative interest rate, the amount of the penalty is 0.) See above.

Under a MIXE or CASH type methodology, a penalty may be imposed if the settlement instruction of the party at fault has one of the following fail reasons on the settlement cut-off date of the payer's settlement instruction on the relevant business day:

- PENF (FIng) / MONY: Money uncovered (Buyer)
- PENF (FIng) / PREA or BOTH\*: withheld (alone or by both parties)
- PENF (FIng) / LINK\*\*: in the case of repo transactions, the maturing leg has not been settled due to the failure of the initial leg (only for MIXE calculation method)
- PENF (FIng) / OTHR: in case of other reasons for failure

<sup>8</sup> [https://registers.esma.europa.eu/publication/searchRegister?core=esma\\_registers\\_fitrs\\_files](https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_fitrs_files)

<sup>9</sup>For HUF see: <https://www.mnb.hu/letoltes/repo-idosor-hu.xls> (O/N covered loan rate), for EUR: <https://www.ecb.europa.eu/home/html/index.en.html> (Marginal facility rate)

\*If both parties' instructions are on hold at the relevant cut-off time, both the delivering and the receiving party will be charged a penalty according to the relevant calculation method. On this basis, for FOP-type instructions, the amounts of each penalty will be the same but of opposite sign, so that they will ultimately sum to 0.

In the case of withholding of settlement instructions against payment by both parties (BOTH reason), different calculation methods and penalty rates applied to DVP and RVP instructions may result in different penalty amounts!

\*\* In case of a LINK failure reason, the penalty will be automatically charged to both parties involved. However, only the Account Holder who caused the failure of the related (linked) settlement instruction will be considered as the party at fault. The determination of the Account Holder to be actually penalised and the correct assessment of the penalty will be done manually. KELER will subsequently remove the penalty charged to the at-fault Account Holder. The Account Holder(s) concerned may submit an appeal to KELER to have the automatically calculated penalty corrected.

### **3.3.4. Currency of the penalties**

The currency in which the amount of the penalties (and also the collection or distribution) calculated by KELER is denominated in the case of failed settlements between KELER accounts (intra-CSD):

- if the type of the original settlement instruction is FOP, then HUF (also for transactions in securities denominated in foreign currency or for reference prices recorded in foreign currency),
- if the settlement method is DVP, the penalty is also calculated in the original currency of the settlement instruction.

The currency denomination of the penalties incurred by foreign CSDs is determined by the respective CSDs, and KELER shall report and settle the penalties in the currency in which they are received from the external account servicer.

### **3.3.5. Daily reference price of the security**

For the purpose of calculating the penalty, the market value (price) on the day of fail is determined as follows:

- For equity-type financial instruments, the closing price of the most relevant trading venue (MRM - most relevant market) in terms of liquidity is used, if available. The MIC code indicating the MRM market is contained in the ESMA FITRS database.
- For other financial instruments, the price of the EU trading venue with the highest turnover is used. ESMA will publish a list of the trading venues with the highest turnover assigned to ISINs on a quarterly basis for each financial instrument, based on trading data from the previous quarter, starting in February 2022.
- If the closing price from the most relevant/trading venue with the highest turnover is not

available for a given fail date, the last available closing price from that trading venue will be considered to apply. In the absence of a closing price not more than 30 days old for the trading venue assigned to the security, KELER may use a price determined in accordance with its own methodology, including prices published by depositaries and market makers or calculated on a net asset value basis, or, in the absence of an available market price, may use a valuation of the securities at par value.

KELER may also adjust ex-post the penalties previously calculated due to a change in a reference price already used in the reference price system, if the change in the reference price relates to a business day for which a penalty has already been calculated.

In accordance with international practice, the market prices used for the calculation and their sources are not shown in the penalty reports.

### **3.4. Penalty reporting, reports**

For each penalty, KELER identifies the defaulting Account Holder, i.e. the party at fault, who is liable to pay the penalty, and the innocent party, who will be the beneficiary of the penalty. For the purposes of penalties, counterparties are always identified per KELER Account Holder (per KELER Main Account, i.e. based on the first 4 characters of the Central Securities Account Number), and therefore the penalty reports are always prepared at this level, i.e. KELER does not provide a sub-account or underlying principal/clearing member breakdown in its reports.

KELER reports penalties by default in the form of MT537 or semt.044 (via KID). (The message types are the same for daily and monthly reports.)

In case the message format chosen by the client is not available for technical reasons, KELER may alternatively, as a substitute, send notifications of the relevant penalty items by electronic mail to the contact persons previously notified to KELER.

The Account Holder may request changes to the setting and subscription rules for reports (channel, zero report) by sending a duly signed electronic document to [clientservice@keler.hu](mailto:clientservice@keler.hu) via the KELER Central Client Service.

#### **3.4.1. Daily report**

KELER will send a daily report on the newly detected penalties and the details of the related settlement instructions, following failures in its own settlement system, no later than 12:00 noon on the Business Day following the day on which the penalty was detected, as scheduled, and on the previous Business Day, to be paid by or credited to the Account Holder.

If a previously recorded penalty is amended or cancelled on a business day, the next report will also include these amendments with the original date of detection of the penalty.

The daily reports issued by KELER will include both new penalties for that day and penalties amended

or cancelled on that day.

### **3.4.2. Monthly report**

The monthly report is based on the finalised penalty data for the previous month, i.e. it includes those penalty items with an active status whose penalty detection date falls in the month preceding the month in which the report is sent. (For example, a monthly report in April would include penalties detected between 1 and 31 March.)

The monthly reports include the aggregated net amount of penalties per currency and per settlement partner, as well as the global net amount of penalties actually to be settled against the Account Holder.

Important: The amount to be settled by KELER (global net amount) does not include the amounts of penalties calculated for transactions cleared by the CCP, with regard to Article 19 of EU Regulation 2018/1229.

The monthly report does not include the details of the calculation of the individual penalty amounts and the details of the corresponding settlement instruction.

### **3.4.3. Reporting of penalties from foreign CSDs**

If a cross-border instruction of a KELER Account Holder to an external (EU) settlement venue fails, the corresponding penalty is calculated by the foreign CSD and reported directly to KELER as participant or, in case of an indirect link, to the external account servicer of KELER. KELER will process this information and reports to produce separate daily and monthly reports on external penalties. Thus, a KELER Account Holder who is affected for a given business day (or month) not only by a failure within KELER but also by cross-border transactions as reported by the foreign securities depository will receive several reports for a business day or month.

The reports will be prepared separately at the level of the external account servicers of KELER (SIX SIS and KDPW) and these reports on external penalties will be sent by KELER to the Account Holder concerned by 14:00 on the Business Day following the Business Day in question, as scheduled.

Please note that KELER can only send reports on penalties calculated by foreign securities depositories if it has received and processed them itself. The processing of foreign penalties may sometimes take some time due to the different data content of the reports provided by the individual account servicers or underlying CSDs and the multiple actors involved in the settlement chain.

For this reason, KELER's reports on foreign penalties may contain different levels of detail than the penalties from KELER's own Settlement System, i.e. for example, certain calculation details or certain data on the underlying instruction may not be provided to our Account Holders!

### **3.4.4. Zero report**

Upon request, the Account Holder may also request zero (daily and monthly) reports, which are also

prepared for business days on which no new penalty was recorded or no previous penalty was amended (daily report), and a zero monthly report is generated even if the Account Holder did not have an active status penalty for the relevant month.

The zero daily report is scheduled to be completed by 14:00 on business days, taking into account any penalties from foreign securities depositories.

By default, a zero report is not generated for all Account Holders, only on request.

### **3.5. Life cycle of penalties, penalty calendar**

KELER determines the days for reporting, appealing and settling penalties on the basis of a standardised Penalties Business Calendar, harmonised between countries, in line with the ECSDA CSDs Procedures. Accordingly, all days except Saturdays, Sundays, 25 December and 1 January are considered as Penalties Business Days (PBD).

KELER also sets the following dedicated days and deadlines for penalties affecting its own Settlement System. *(All dedicated business days listed below should be interpreted as PBDs.)*

- 1) The Account Holder may appeal to KELER on the 10th business day of the month (by 17:00) with regard to the penalty for the previous month. \*
- 2) A foreign CSD (investor CSD) Account Holder holding an account with KELER can appeal to KELER on the 11th business day of the month (by 17:00) regarding the penalty for the previous month.
- 3) The last day on which KELER may make adjustments to the penalty calculated for the previous month is the 12th business day of the month.
- 4) The monthly report, including aggregates based on the finalised penalties for the previous month, is sent to Account Holders by KELER on the 14th business day.
- 5) On the 15th business day, (PAIR type) PFOD instructions are generated and sent to the settlement system, with the intended settlement day of the 17th business day.
- 6) The collection and distribution of penalties is scheduled for the 17th business day of the month. This day will be the intended settlement date for PFOD (PAIR type) transactions.

If a PBD day listed in Sections 1 to 5 falls on a day that is not a KELER business day (i.e. no settlement service is provided by KELER), the given transaction is due on the last day before the given PBD, which is also a business day for KELER.

If the 17th business day of the month that is relevant for penalty management (PBD) is not a KELER business day, the settlement of PFOD instructions for the settlement of penalties (Section 6) is due on the next KELER business day.

\*In the case of an appeal of a penalty calculated by a foreign CSD, the deadline for receipt of the

appeal by KELER is 17:00 on the 9th PBD (if the 9th PBD is not a KELER business day, the deadline for the appeal is 17:00 on the preceding KELER business day.)

### 3.6. Appeals, modification of penalties

KELER Account Holders are expected to check the penalty reports on a daily basis and to report to them any penalties due to or payable by their underlying clients.

An Account Holder may appeal if they do not agree with the calculated penalty and the reason for their appeal is one of the following.

The grounds for appeal may include the following:

- *Calculation error*: A discrepancy between the amount of the penalty reported by KELER and the amount determined by the Account Holder. Typically, this may be due to errors in the master data, e.g. the classification of the financial instrument, its liquidity, the calculation of the penalty rate applied, etc., which may lead to an incorrect result.
- *Missing penalty*: Where the failed settlement instruction is not included in the daily report sent by KELER, but the financial instrument included in the order is subject to a penalty.
- *The party at fault is disputed*: In rare cases, it is only after the automatic calculation of the penalty that it can be decided ex-post which of the participants involved in the settlement instruction is the party actually at fault and liable to pay the penalty. Such cases may include the following:
  - o In the case of an already matched order submitted late by a Market Infrastructure, the LMFP will be automatically allocated to the transferring party as the party at fault.
  - o In case of failure of linked FOP transfers or repo transactions due to a LINK reason, both parties may be automatically issued a penalty.
- *Wrongly charged penalty*: In the exceptional cases listed in the ESMA CSDR Q&A<sup>10</sup>, a central securities depository may waive the application of a penalty:
  - o Insolvency proceedings are opened against the failing participant
  - o Trading or settlement of a financial instrument with the relevant ISIN code is suspended due to unjustified security creation discovered during reconciliation.
  - o In the case of a settlement instruction where the cash settlement takes place outside the

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<sup>10</sup> <https://www.esma.europa.eu/press-news/esma-news/esma-updates-csdr-qas-10> (Settlement Discipline Questions 4 - Cash penalties: scope)

Settlement System and the relevant payment system has a settlement holiday on the intended settlement date.

- A technical problem in the system of the Central Securities Depository that prevents settlement on time, e.g. in case of failure of infrastructure components, cyber attack, network problems.

KELER may reject an appeal in the event of a discrepancy between the reference price of the security used for the calculation of the penalty and the price contested by the Account Holder, provided that the discrepancy between the prices indicated by the Account Holder and those applied by KELER does not exceed 20%.

Deadline for appeals: Account Holders may submit an appeal from the receipt of the daily report until the designated deadline of the month following the month in question. (see Section 2.5)

In all cases, we kindly ask our esteemed clients to **notify KELER of their appeal requests** and comments **as soon as possible** in case of any alleged errors or circumstances giving rise to an appeal, in order to allow sufficient time for the investigation of the same. We would like to draw your attention to the fact that the procedures for penalties calculated by foreign CSDs may take considerably longer due to the length of the settlement chain.

If the foreign account servicer (CSD) charges any fees in connection with an appeal initiated by a KELER Account Holder, for example for an unfounded appeal, KELER is entitled to pass on these fees to the Account Holder concerned.

The Account Holders can request a review of the penalties by sending an e-mail to [penalty@keler.hu](mailto:penalty@keler.hu). The appeal must include in the e-mail all data and information necessary to identify and verify the penalty in question. This includes, but is not limited to:

- the account holder's securities account number with KELER,
- the unique or common penalty reference reported by KELER
- the reason for the appeal,
- the details of the calculation that the account holder considers justified
- in the case of a missing penalty item, the identification of the failed settlement instruction,

The appeal is examined by KELER and, if the appeal is justified, KELER amends, re-includes or removes the calculated penalty. (In the case of an appeal concerning a foreign CSD, it forwards the appeal to the external account servicer.)

The result of the appeal is communicated by KELER in a reply letter to the party that submitted the appeal and, in the case of a modification or cancellation of a penalty, the modified (new) record is also shown in the next daily report, keeping the original date of detection but with a new penalty status or reason.

KELER may also make changes to the calculated penalty items without appeal, at the latest by the 12th business day of the month (PBD), if a master data or parameter used for the calculation (e.g. market price of the security, type of security) subsequently changes in its own system or if it

discovers an error affecting the calculation of the penalty on its own initiative. (Alternatively, if it receives a change notification from a foreign securities depository.)

If a penalty item is amended or subsequently recorded by KELER, the item appears in the next daily report to be sent to the Account Holders concerned.

### **3.7. Settlement of penalties**

Dedicated cash accounts for the settlement of penalties, where the collection and distribution can be settled by KELER using PFOD instructions, are set up for each Account Holder according to the following default set of rules:

- In the case of HUF:
  - for credit institutions: MNB account number
  - for different clients: own type of KELER account number (unless the MNB account number is currently the default settlement cash account under a separate contract)
- Other currencies: for all clients: own type of KELER account number

If you require a different configuration from the above, please contact the Client Service of KELER at [clientservice@keler.hu](mailto:clientservice@keler.hu).

Please note that for the settlement of penalties, the Account Holder must have a settlement account in the currency of the penalty.

After the netting of the penalty amounts for the previous month, on the 15th business day of the month (PDB), KELER prepares the future value dated and already matched PFOD (transaction type: PAIR) instructions, which will be used to collect and distribute the penalties on the 17th business day of the month (PBD) or, if this day is not a KELER business day, on the next KELER business day.

If a cross-border transaction of a KELER Account Holder is also subject to a penalty by a foreign CSD, the amounts payable to the external KELER account servicer will be settled by a separate PFOD order, in addition to the penalties calculated by KELER.

The netting of penalties incurred by foreign CSDs is performed at the level of the external account servicers of KELER (per currency), even if the KELER Account Holder has incurred penalties at several EU CSDs through the given external account servicer in the given month.

KELER will generate as many PFOD instructions per Account Holder as there are penalties incurred by the Account Holder and as many currencies in which the penalties are due for collection/distribution. (In terms of netting, it is currently possible at the level of KELER, SIX SIS and KDPW.)

Once PFOD instructions with this PAIR transaction code have been accepted by the settlement system, KELER informs the client of the amount to be actually settled and the account number to be



debited or credited by means of the order status message (MT548, sese.024).

Based on this notification, the account holder to be debited shall, on the intended settlement date of the PFOD instruction, until the start of the settlement period (07:00), ensure that the amount in their account for the collection of penalties is at least sufficient to cover the settlement of the penalty to be paid.

After the opening of the 17th business day, KELER attempts to collect the amount of the penalties through the PFOD transaction. Instructions to debit penalties are sent to the settlement system in released status and instructions to credit penalties to Account Holders are sent to the settlement system in hold status.

On the basis of successfully settled PFOD instructions, the amounts collected are held by KELER in a dedicated cash account until all outstanding penalties are settled. The crediting of penalties to eligible Account Holders, i.e. the release of PFOD instructions kept in hold state, will only commence once all debits (collections) have been successfully settled for all Account Holders. Also, penalties from foreign CSDs will only be credited if the amount has been credited to KELER's account.

The PFOD instructions for the settlement of penalties are generated by KELER with the following main data:

Transaction type	PAIR
ISIN	LU2128008567
Trade date	PBD 15 (possible deviation due to holidays)
Intended settlement date	PBD 17 (possible deviation due to holidays)
Settlement quantity	0
Settlement amount and currency	Global net amount (based on monthly report)
Account Holder's securities account number	XXXXPENLTY <i>where 'XXXX' denotes the first 4 characters of the participant's central securities account number (main account number) and 'PENLTY' denotes the dedicated sub-account for the settlement of the penalty (last 6 characters of the central securities account number)</i>
Settlement counterparty securities account number	9999PENLTY
Settlement counterparty matching BIC	KELRHUHBXXX

The following procedure is applied by KELER in the **handling of possible penalty defaults**:

No Account Holder receives a penalty credit on the 17th business day (PBD) until KELER has collected the amounts due in full from all Account Holders, that is, the settlement of the relevant PFOD instructions will be suspended by KELER until such time (in hold status).

- If a PFOD Order is not settled by 9:00 on the 17th business day (PBD) at the latest due to a lack of funds, KELER will declare a default and send a notice to the defaulting Account Holder by electronic mail. (After the transaction, a default fee will be charged!)

- If the debit remains unsuccessful within 13:00 on the given day, KELER will notify all Account Holders of the default through the usual communication channels (website, KID).
- If the debtor Account Holder is still in default at 09:00 on the next business day, KELER will declare a new day of default and send a new notice to the Account Holder. (At the same time, a new default fee will be charged for the transaction.)
- If the debit has not been settled by 13:00 on the business day following the intended settlement date, KELER will recalculate the payment items of the defaulting and all affected Account Holders in a special procedure and generate new PFOD instructions. (One based on the available amount expected to be settled if there is an available cash account balance, and a second one for the amount not settled).

At the same time, the original PFOD instructions for crediting all Account Holders that would have expected to be credited based on the amount to be debited from the defaulting Account Holder are also cancelled.

Together with the recalculation and the generation of new PFOD instructions, the other non-defaulting Account Holders are credited with the amounts collected so far, i.e. the settlement instructions that were held back until then are released for settlement (hold->release).

- The PFOD instructions created as a result of the recalculation and still pending on the last business day of the month in question are cancelled from the system by KELER before the close of the last business day of the month. A default fee is charged for each business day, including the day of cancellation, for the outstanding debit PFOD instruction until cancellation.
- After the month-end cancellation of PFOD instructions by KELER, the Account Holders (and their clients) concerned may pursue their claims against each other bilaterally outside KELER's penalty mechanism.

Repeated breaches of payment discipline may lead to suspension and termination of KELER membership. Furthermore, the cases concerned may be reported to the competent national authority, with the Account Holder's name.

KELER also applies the rules relevant to penalty defaults if for reasons attributable to the Account Holder the securities or cash account needed for the settlement of the PAIR PFOD instruction is missing.

KELER charges the fees indicated in the applicable Fee Schedule in connection with the penalty procedures and may pass on the fees charged by the foreign CSD to the Account Holder concerned

### **3.8. Procedure to be followed in insolvency procedure**

KELER does not charge a penalty for a default caused by an Account Holder who is subject to an

insolvency procedure for settlement fails occurring after the date of notification of the procedure.

The penalties calculated until then are handled separately in the monthly report and in the penalty collection by KELER, i.e. they are not taken into account in the determination of the global net amount.

### **3.9. Handling of penalties due for transactions cleared by the central counterparty**

The details of the penalties due for failed settlement instructions cleared by the CCP pursuant to Article 19 of Regulation (EU) No 2018/1229 shall be reported by the CSD to the CCP (KELER CCP) and the participants concerned, and the collection and distribution of these penalties to each clearing member shall be performed by the CCP. The central counterparty reports the result of the collection and distribution to the clearing members to the CSD.

As set out above, the details of the relevant failed instructions and calculated penalties are reported by KELER to both the participant concerned and KELER CCP. In such cases, the CCP is reported with the 'CCPA' Party Capacity Indicator in the penalty reports. When determining the global net amount calculated by KELER per account holder, these penalty amounts are excluded from the calculation and thus do not form part of the (PFOD-type) penalty settlements initiated by KELER.

## **4. Contact details**

- **KELER:**

The following contact details are available to Client to pose questions or report problems related to penalties:

- daily operational matters, appeals: [penalty@keler.hu](mailto:penalty@keler.hu)
- setting up and changing report subscription rules: [clientservice@keler.hu](mailto:clientservice@keler.hu)
- error reporting related to the delivery of reports, technical problems: [servicedesk@keler.hu](mailto:servicedesk@keler.hu)

- **Account Holder:**

We would like to inform our clients that all reports, information and notices related to penalties are sent by KELER to the operational contact person(s) for settlements by default. In the absence of a dedicated operational contact person, notifications are sent to the person(s) indicated on the Counterparty's master data form.

If you would like to notify additional persons for the purpose of handling penalties or to expand the number of persons to be notified (e.g. by providing a group e-mail address), please indicate your wish using the form available on the KELER website:

<https://english.keler.hu/KELER/KelerContactList/>

KELER excludes its liability in the event that the Account Holder fails to comply with its obligation to change and notify data, and in the event of damages and consequences resulting from the failure to notify or the notification of the incorrect contact person.

## 5. Transitional provisions

**KELER must ensure the collection and allocation of penalties for failed settlements retroactively from the date of entry into force of the original legislation, i.e. from 1 February 2022, before the date of the activation of the penalty mechanism.**

Based on the above, the following transitional procedure will be followed to ensure the ex-post collection and allocation of penalties:

KELER plans to continue the full operation of the penalty mechanism from 2 May 2022, but for the transitional period, i.e. for the months of February, March and April 2022, the penalties will be settled in one lump sum retrospectively.

The details of the penalties for the three months concerned will be prepared and made available to account holders by KELER by 31 May 2022 in the aggregated form, which will be sent to the designated contact persons by e-mail in an excel sheet.

The deadline for appealing the three monthly penalties concerned is different from the normal procedure: 30 June 2022

However, given that KELER is scheduled to provide penalty reports in a live environment already in April 2022, our clients will be informed of some of the penalty amounts before the excel sheet report in May. Thus, we kindly ask our clients to send any comments or appeals related to the reported penalties to KELER as soon as possible after their occurrence, so that the necessary corrections can be made.

Following the appeal deadline and any adjustments, the **penalties will be collected and distributed by 31 July 2022**. (The exact date will be communicated separately via the usual communication channels at a later stage.)

Prior to the settlement of the penalties, all Account Holders will receive a repeat report (in an excel sheet) on the (net) amount of penalties actually to be settled and the main details of the underlying penalties.

At the same time, please note that in the live environment, during the dry run, monthly penalty reports may be generated, but these are for information purposes only, as they are generated for one month periods under normal, simulated dry run, operations and the payment requirements indicated in the monthly reports will not be fulfilled and no PFOD instructions will be generated by KELER.

The settlement of the initial, normally scheduled first (PAIR) PFOD instructions, for penalties

affecting KELER's Settlement System, after the penalties detected in the month of May 2022 will be due on 23 June 2022, i.e. on the 17th PBD day.

Please also note that **the settlement of penalties foreign CSDs will continue to be settled on a monthly basis according to the normal schedule.** Thus, the first PFOD debit and credit transactions will be entered into the system with a intended settlement date of 23 March 2022 and will be notified in advance (monthly reports) to the Account Holders concerned. (Until the ISO format reports are available in a live environment, also in excel sheet format.)

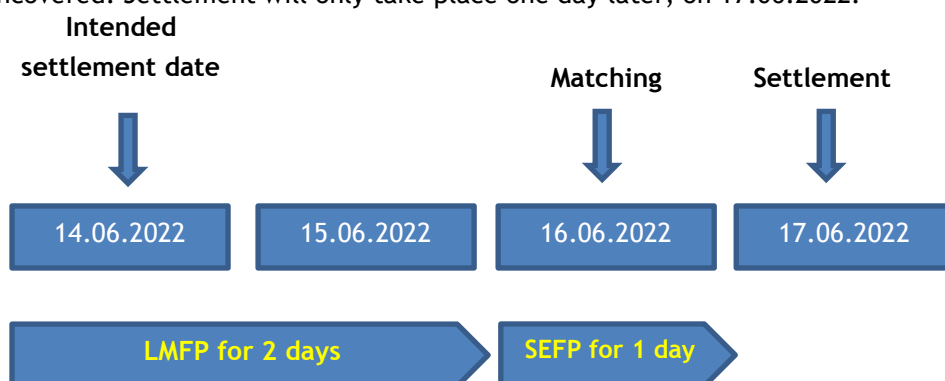
## 6. Appendix

### Example:

The details of a failed (fictitious) transaction are the following:

- Intended settlement date:	14.06.2022
- Settlement method:	Against payment (APMT)
- Settlement currency:	HUF
- Securities quantity to be settled:	25,000
- Securities type:	Liquid shares (SHRS)
- Penalty rate:	1.0 bp (=0.0001)
- Market price of the security on each day:	
o 14.06.2022:	HUF 15,000
o 15.06.2022:	HUF 15,300
o 16.06.2022:	HUF 14,600
- Overnight credit rate (HUF):	4.9%
- Timestamp of acceptance of the Seller's (DVP) order:	16.06.2022 13:00:00
- Timestamp of acceptance of the Buyer's (RVP) order:	14.06.2022 08:05:00
- Matching date:	16.06.2022 13:00:01

The Seller in the example submits their order two business days later than the intended settlement date, so the successful matching of the two parties' instructions can only take place on 16.06.2022. However, on 16.06.2022, the transaction is not settled because the Buyer's cash account is uncovered. Settlement will only take place one day later, on 17.06.2022.



Based on the above, the first time a failure can be detected is on 16.06.2022, as only from this date onwards can the instructions be considered as matched. On the following business day (17.06.2022) the following penalties will be calculated by KELER.

- For 2 business days between 14.06.2022 and 16.06.2022: LMFP, party at fault: the Seller. The penalties for the two business days are calculated cumulatively. Since the instruction type is DVP, the calculation method is the following: SECU, i.e. the daily reference price of the security and the penalty rate, determines the amount of the penalty:
  - 14.06.2022: 25,000 pcs x HUF 15,000 x 0.0001 = HUF 37,500
  - 15.06.2022: 25,000 pcs x HUF 15,300 x 0.0001 = HUF 38,250

For 2 days in total: HUF 75,750 (LMFP)

2. On 16.06.2022, the Buyer's RVP order is uncovered (with PENF / MONY status) at the end-of-day cut-off time, therefore the party at fault is the Buyer, and the amount of the penalty for 1 day is calculated based on their instruction. The calculation algorithm = MIXE, i.e. the penalty rate is 1/360 of the daily O/N HUF credit rate, which is calculated by applying the market value of the failed security quantity:

$$25,000 \text{ pcs} \times \text{HUF } 14,600 \times (0.049 / 360 = 0.000136111) = \text{HUF } 49,681 \text{ (SEFP)}$$

The above penalties will be reported by KELER with the Penalty Detection Date of 16.06.2022, by 12:00 on 17.06.2022 via the daily penalty reports.