CSDR - Settlement discipline regime:
Cash penalty system

DATE	VERSION	DESCRIPTION
05.2020	1.0	Creation of document
07.2021	1.1	Document update
09.2021	1.2	Document update, including mainly cash penalties on transactions with the participation of the CCP
06.2022	2.0	Amendments to update the text following the introduction of the cash penalty system on 1 February 2022. Amendments relating to penalties for participants for linked transactions (the party setting up the link). Other amendments relating to editing and formatting that do not affect the substance of the document.
05.2023	3.0	Change of deadlines: generation of PFOD instructions and collection/redistribution of penalties. Minor editing and corrections. *Amendments in relations to Version 2.0 of this document have been highlighted in the colour blue.*

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I   Introduction

1. As a part of the initiative to align with the requirements of "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 (CSDR)" and the technical standards on settlement discipline published on 13 September 2018, modifications have been introduced to the processing of cash penalties for late settlement.

II   Legislation and other documentation

1. 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 (CSDR).

2. 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 (RTS 2018/1229), as amended.

3. Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012.

4. Commission Delegated Regulation (EU) 2017/389 of 11 November 2016 supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council as regards the parameters for the calculation of cash penalties for settlement fails and the operations of CSDs in host Member States (RTS 2017/389).

5. ESMA Questions and Answers - Implementation of the Regulation (EU) No 909/2014 on improving securities settlement in the EU and on central securities depositories.

6. ECSDA SETTLEMENT FAILS PENALTIES FRAMEWORK – the source of information impacting system solutions under implementation; it is the intention of CSDs grouped in the ECSDA to apply common rules (market practice) for the cash penalties system; this documentation and the text herein includes references to the ECSDA Framework. Link: https://ecsda.eu/archives/12974

    UPDATE OF THE ECSDA SETTLEMENT FAILS PENALTIES FRAMEWORK - this document has been updated to reflect the shift by one day of the following deadlines: trade date in payment instructions (PFOD), and redistribution of cash penalties date.

    Link to the updated documentation:

    https://ecsda.eu/wp-content/uploads/2023/04/2023_04_28_ECSDA_Framework_update.pdf

III   General principles

1. The cash penalty system was introduced on 1 February 2022 and relates to the system for the calculation, collection, and redistribution of cash penalties for late settlement.

2. New ISO 20022-compliant messages are used in the cash penalty system to report late settlement and calculated penalties.

    Following amendments to the ECSDA Framework document, updates have been introduced from April 2023 /March reports/ in the trade date in payment instructions (PFOD) and payment realisation.

IV   Reference data for the cash penalties system

IV.1. General

1. In order to calculate cash penalties, reference data is uploaded to the KDPW system, in particular securities reference prices/market value.

2. Such values may not be available on the cash penalty calculation date; in such instances, the penalty amount is set to zero and the cash penalty amount is calculated at a later date when such data become available.

3. The latest time to provide data is the 11th business day ("PBD", penalties business day) of the month following the occurrence of an event subject to a cash penalty.

IV.2. List of instruments subject to cash penalties

1. Cash penalties apply in the case of transactions in the following instruments admitted to trading on a regulated market or trading venue (including MTF, OTF) or cleared by a CCP:
   1) **shares of companies** and other securities equivalent to shares of joint-stock companies, partnerships or other entities, and depository receipts relating to shares;
   2) **bonds** and other securitised debt, including depository receipts relating to such securities;
   3) **all other securities giving the right to buy or sell** any transferable securities or resulting in cash clearing in relation to transferable securities.

2. According to Article 7(13) of CSDR, the cash penalty system shall not cover settlement fails of shares where the principal venue for their trading is located in a third country.

3. The source of information for the list of instruments – information provided in the ECSDA Framework: point 3.3.

IV.3. Daily reference price used to calculate cash penalties

1. **Late settlement penalties** are calculated on the settlement fail date on the basis of **the market value of the security** which has had its settlement suspended or has failed to settle, irrespective of the type of transaction.

2. For securities traded on more than one market, the valuation depends on the type of securities.
   1) **for equity-type financial instruments** (i.e., shares, ETFs, certificates) admitted to trading in the European Union, the market value is based on the closing price on the **most relevant market in terms of liquidity**,
   2) **for other financial instruments admitted to trading in the European Union**, the market value is based on **the closing price on the EU trading venue with the highest turnover**,
   3) **for financial instruments other than those listed above**, the market value is based on **the price calculated according to a predefined method approved by the supervisory authority according to criteria relating to market data**, including market prices available from trading venues or investment firms.

3. The market price of securities is uploaded to the KDPW system from third-party data sources. Reference data used to calculate cash penalties are not published.

4. The reference prices used in the cash penalty system are applied independently of the existing rules for determining market value (§ 10 of the KDPW Rules).

5. Unit reference prices used in the cash penalty system are not made available in KDPW public online services, or transmitted in cash penalty system messages.

6. Source of information for the market value of instruments – information provided in the ECSDA Framework: point 5.2.

IV.4. **Supervisory reporting**

1. In accordance with the provisions of Annexes I and II to RTS 2018/1229 – KDPW reports predefined instances of settlement fails and associated cash penalties to the supervisory authority.

2. CFI codes are used in order to ensure the correct classification of instruments in reports.

3. Source of information for the classification of instrument types in reporting – information provided in the ECSDA Framework: point 5.3.

IV.5. **Liquid/illiquid instrument classification**

1. In order to calculate cash penalties, the KDPW system stores information on the liquidity indicator of specific financial instruments.

2. Source of information for liquid/illiquid instrument classification – information provided in the ECSDA Framework: point 5.4.

IV.6. **SME Growth Market indicator**

1. In order to apply the lower penalty fee, KDPW stores within its system information on whether the instrument/transaction is traded or has been executed on an SME Growth Market.

2. For the purpose of classification of transactions as subject to an SME Growth Market penalty rate, the "Place of trading" field in the settlement instruction must show an SME Growth Market.

3. Source of information for the SME Growth Market indicator – information provided in the ECSDA Framework: point 5.5.

IV.7. **Cash penalty rates**

1. The cash penalty rates are set out in the Annex to Commission Delegated Regulation (EU) 2017/389 of 11 November 2016 supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council as regards the parameters for the calculation of cash penalties for settlement fails and the operations of CSDs in host Member States (RTS 2017/389).

2. Cash penalty rates applicable to settlement fails (per business day):

Type of fail	Rate
1. Settlement fail due to a lack of **shares that have a liquid market** within the meaning of point (b) of Article 2(1)(17) of Regulation (EU) No 600/2014, excluding shares referred to in point 3	1,0 basis point
2. Settlement fail due to a lack of **shares that do not have a liquid market** within the meaning of point (b) of Article 2(1)(17) of Regulation (EU) No 600/2014, excluding shares referred to in point 3	0,5 basis point
3. Settlement fail due to a lack of **financial instruments traded on SME growth markets**, excluding debt instruments referred to in point 6	0,25 basis point
4. Settlement fail due to a lack of **debt instruments issued or guaranteed** by: (a) a sovereign issuer as defined in Article 4(1)(60) of Directive 2014/65/EU; (b) a third country sovereign issuer; (c) a local government authority; (d) a central bank; (e) any multilateral development bank referred to in the second subparagraph of Article 117(1) and in Article 117(2) of Regulation (EU) No 575/2013 of the European Parliament and of the Council ([1]); (f) the European Financial Stability Facility or the European Stability Mechanism	0,10 basis point

5. Settlement fail due to a lack of **debt instruments other than those referred to in points 4 and 6**	0,20 basis point
6. Settlement fail due to a lack **of debt instruments traded on SME growth markets**	0,15 basis point
7. Settlement fail due to a lack of all **other financial instruments** not covered in points 1 to 6	0,5 basis point
8. Settlement fail due to a **lack of cash**	Official interest rate for overnight credit charged by the central bank issuing the settlement currency with a floor of 0.

([1])Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

IV.8. Interest rate in instances of lack of cash

1. DvP settlement in KDPW is available only for PLN and EUR.

2. For the purposes of cash penalty calculation for lack of cash, the official interest rate of the central bank issuing the settlement currency is divided by 360 days in order to generate the applicable daily penalty rate.

3. The rate for PLN is the NBP Lombard rate (currently 0.50%).

4. The rate for EUR is the marginal lending facility rate (currently 0.25%).

5. Source of information for central bank interest rates – information provided in the ECSDA Framework: point 5.7.

IV.9. Currency conversion

1. Currency conversion may be required depending on specific cases.

2. This applies in instances where the reference currency of the cash penalty calculation is not supported by KDPW.

3. In practice, the requirement only relates to the cash penalty calculation for FoP settlement.

4. In such instances, amounts in a currency not supported by KDPW are converted into the default currency.

5. The default currency is PLN.

6. The foreign exchange rate is not published in daily or monthly reports made available by KDPW.

V General principles of cash penalty calculation

V.1. General

1. For events subject to penalties on a given date, the reference price of the instrument on the event date applies, including:
   1) **for SEFP (settlement fail penalty – lack of assets)** – the price on the fail date starting from the ISD (Intended Settlement Date), e.g., ISD=01.12 settled on 03.12, which means that the 01.12 price applies on 01.12 and the 02.12 price applies on 02.12

2) **for LMFP (late matching fail penalty)** – the price on each date from the ISD to the instruction matching date.

2. **LMFP** penalties may be calculated for **several days going back**, e.g., if instructions match on 05.12 and ISD = 01.12, the penalty is calculated at 05.12 for all days starting from 01.12. LMFP will be charged on a one-off basis for the entire period from ISD to the matching date.

3. **Cash penalties will be calculated per instruction and per business day**.

4. Cash penalties will be rounded up to two decimal places.

5. Invoices are not issued for cash penalties; instead, KDPW participants receive system reports.

6. KDPW calculates additional fees for the maintenance of the cash penalty system (calculating, collecting, redistributing penalties); for these fees, invoices are issued.

7. Non-standard solutions apply where cash penalties are calculated for CCPs and other CSDs which are KDPW participants (see below for details).

V.2. **Cash penalty currency**

1. **DvP instructions**:
   1) cash penalties are calculated in the currency of the settlement instruction that is subject to the penalty (PLN, EUR);
   2) the reference price may be in a different currency than the settlement currency of the instruction that is subject to the penalty; in such instances, the penalty is calculated by converting the reference price currency to the settlement instruction currency according to the rate of exchange from the reference price currency to PLN or EUR, i.e., the NBP or the ECB rate, respectively.

2. **FoP instructions**:
   1) **for debt instruments** quoted in nominal value, the penalty is calculated in the currency of the nominal value, unless the currency is not available in KDPW (see below for details);
   2) **for other instruments** (quoted in units), the cash penalty is calculated in the currency of the reference price, subject to availability of the currency in KDPW (see below for details);
   3) if the reference price is in a currency other than PLN or EUR, the cash penalty will be calculated in PLN. In such instances, the penalty is converted from the currency not supported by KDPW to PLN, according to the NBP or ECB exchange rate;
   4) PLN is the default currency of cash penalties for FoP operations.

3. Information provided in the ECSDA Framework: point 5.2.

VI   Processing cash payments – timeline

VI.1.   Business day definition in the settlement system

1. Applicable calendars:
   1) **depository system calendar** – cash penalties are calculated for those days when operations of a given type may be settled; as a result, penalties are calculated for instructions relating to, for instance, GPW transactions only for those days when the settlement of such transactions is available; no penalties are calculated for those days when the depository system is open but no settlement is available for specific types of operations (e.g., Good Friday: the system is open but GPW transactions are not settled);
   2) **clearing bank calendar** – relevant to DvP operations; in such instances, cash penalties are calculated for those days when the payment system is open for the given currency and KDPW supports settlement of the specific types of operations.

2. No cash penalties:
    1) FoP operations – if the settlement system is unavailable (closed) for the given type of operations;
    2) DvP – if the settlement system is closed on the day or settlement is not allowed for the specific types of operations.

3. As determined by ECSDA, **a PBD (Penalties Business Day) calendar** has been approved according to the following principles:
    1) **the calendar covers all days other than Saturdays, Sundays, 1 January, and 25 December**;
    2) **in the event of appeals** (Appeal Period), if an appeal deadline is a PBD which is a bank holiday in KDPW, such actions are to be taken on the KDPW business day **preceding** the deadline;
    3) in the event of **monthly reports on cash penalties**, if a reporting deadline is a PBD which is a bank holiday in KDPW, the report is provided on the KDPW business day **preceding** the deadline;
    4) in the event of **payment of cash penalties**, if the payment deadline is a PBD which is a bank holiday in KDPW, the payment is to be made on the KDPW business day **following** the deadline.

4. Information provided in the ECSDA Framework: glossary, PBD definition, points 2.1.2., 2.1.5 – 2.1.8.

VII Scope of application of the cash penalty system

VII.1.   **Instructions subject to penalties:**

1. **Cash penalties are calculated for late settlement of all types of transactions (including OTC trades) and all types of instructions (including FoP instructions)**, in particular instructions which meet the following conditions:
    1) **the instructions are matched**, either within or outside the KDPW system (e.g., CCP instructions);
    2) if instructions are matched **after the ISD** (intended settlement date), penalties also apply (see below for details);
    3) penalties are charged for settlement fails **on and after the ISD**.

2. **Exceptions** – instructions not subject to cash penalties:

    1) settlement orders **not related to change of ownership** of securities (subject to the definition of a transfer order in Directive 98/26/EC on settlement finality), e.g., PORT operations;
    2) **corporate action instructions** (in particular, ISO operation code CORP and other generated by KDPW);
    3) **technical instructions**;
    4) **assets status change instructions**.

3. Information provided in the ECSDA Framework: point 3.1.

VII.2.   **Penalty periods**

1. Penalties are calculated for the periods **between the ISD and the actual settlement date or the day the instruction is withdrawn** from the system.

2. **If an instruction is withdrawn**, the cash penalty is calculated even in the absence of settlement on the assumption that settlement was intended (as confirmed by the matching of instructions).

3. Penalties imposed where a settlement instruction is withdrawn from the system:
   1) if the instruction is cancelled **on day X before the cut-off time** – the penalty is not charged for day X;
   2) if the instruction is cancelled **on day X after the cut-off time** – the penalty is charged for day X.

4. Information provided in the ECSDA Framework: points 7, 7.1, 7.2.

VII.3. Types of cash penalties by cause

1. **Settlement fail penalties (SEFP) are imposed on each defaulting participant** (lack of assets for settlement: cash or securities).

2. **Late matching fail penalties (LMFP) are imposed on the participant who was last** to submit the settlement instruction, from the intended settlement date to the day of matching.

3. Instruction **"on hold"** after the intended settlement date – penalties are imposed on the **participant who flags the settlement instruction on "hold"**; where both counterparties flag the settlement instruction on "hold", the penalty is imposed **on each such participant**, from the intended settlement date to the day when the settlement instruction is flagged as "released". Specific terms concerning the identification of participants subject to cash penalties in the event of the "hold" status apply to transactions with the participation of the CCP as the central counterparty – see below for details.

4. **Determining the cut-off time** for cash penalties of a given type:
   1) **SEFP** – the closing of a settlement process including:
      a) batch system – end of session;
      b) RTGS – end of settlement available for the type of operations;
   2) **LMFP** – the latest time when instructions are accepted for settlement during the day:
      a) batch system – the opening of the session when the type of operations can be settled at the latest during the day;

5. RTGS – the latest time when the type of instruction is accepted for the current accounting day.

6. Information provided in the ECSDA Framework: points 4.1, 4.2.

VII.4. Calculating cash penalties: identifying the failing party

1. **SEFP - settlement fail penalty**
   1) the instructions are matched and ready for settlement
   2) the instructions have reached the ISD
   3) **the penalty is imposed on the participant who lacks assets**
      a) lack of securities – debit counterparty in the instructions
      b) lack of cash – credit counterparty in the instructions
      c) note: if lack of securities has been identified, this shall be deemed the reason for the settlement fail and the instructions are not processed to identify availability of cash, i.e., "lack of cash" status does not apply;
      d) in the case of "atypical" instructions resulting from securities netting, there can be a simultaneous lack of cash and lack of securities (Delivery with Payment instructions) – in such instances, the cash penalty is the sum of penalties for lack of cash and penalties for lack of securities.
   4) **the status is identified at the cut-off time on the business day** when instructions may be settled; if instructions are presented for settlement in the batch system only, it is the last

session for those given types of instructions, e.g., end of session at 15:30 for DvP instructions, end of session at 18:30 for FoP operations, end of RTGS settlement at 17:00 for DvP instructions and end of RTGS settlement at 18:30 for FoP instructions.

2. **LMFP - late matching fail penalty**
   1) calculated at the end of day when instructions can no longer match; in the KDPW system, in practice, after 21:00 (the cut-off time of system availability and consequently of matching under KDPW regulations);
   2) past the cut-off time for the settlement of instructions of a given type on the given day, e.g., instructions with ISD=12.12.2019 match at 19.00 on 12.12.2019 (after the settlement system has closed at 18.30).
   3) **calculated for the period from the ISD to the day the instruction matches** provided that:
      a) if the instructions match after the settlement cut-off time, penalties are calculated for the period from the ISD to the day the instructions match (inclusive), e.g., ISD=12.12, matched on 13.12 at 19.00 – charged for two days (settlement fail on 12.12 and 13.12).
      b) if the instructions match before the settlement cut-off time, penalties are calculated for the period from the ISD to the day before the day the instructions match, e.g., ISD=12.12, matched on 13.12 at 17.00 – charged for one day (settlement fail on 12.12, can settle on 13.12);
   4) penalties are imposed **on the participant who is last** to enter or modify the instruction in the system, based on the timestamp of instruction entry;
   5) if both counterparties enter the instructions after the ISD, the penalty is imposed on the counterparty who was last to enter the instruction;
   6) instructions entered in the system as matched, e.g., by a CCP – are processed as follows:
      a) KDPW cannot determine the failing counterparty;
      b) the default values are as follows:
         - if the CCP as the central counterparty is a transaction counterparty and the instruction issuer – the penalty is imposed on the other settlement counterparty other than the CCP;
         - if the instruction issuer is a settlement counterparty but it is not the CCP as a central counterparty – the penalty is imposed on the instruction issuer counterparty;
         - if the instruction issuer is not a settlement counterparty – the penalty is imposed on the counterparty debited with securities;
      c) the party on which the penalty is imposed may be changed following an appeal.

3. **The instruction is "on hold"**
   1) special SEFP penalty
   2) **"hold" is understood to mean lack** of assets
   3) status should be set to **"hold"** on the basis of a participant's instruction, or is applicable where a buy-in is initiated in relation to the settlement instruction which triggers the buy-in
   4) penalties are imposed on the participant who maintains the instruction "on hold"
   5) if both counterparties maintain the instruction "on hold", the cash penalty is imposed on both counterparties as failing parties:
      a) the debit counterparty for lack of securities;
      b) the credit counterparty for lack of cash.
   6) special case of putting on hold instructions/transactions with the participation of the CCP as the central counterparty (covered by the clearing guarantee system):
      a) the CCP as the issuer of a settlement instruction may, before initiating a buy-in, put the instruction which triggers the buy-in on hold – in such instances, the cash penalty is imposed on the CCP's counterparty which delivers securities while the CCP is the penalty beneficiary;

b) if an instruction where the CCP delivers securities is put on hold, the cash penalty is imposed on the CCP of the counterparty delivering the securities while the CCP's counterparty is the penalty beneficiary.

4. **Special case of LMFP**
   1) If a settlement order is entered for a buy-in, where the Intended Settlement Date (ISD) is earlier than the date when the order is entered into the CSD system in order to avoid a late matching penalty (LMFP), the BSSP flag must be indicated in the settlement instruction. KDPW does not enable such a solution to be applied.
   2) New instructions for some transactions where a buy-in fails should have other settlement date parameters (ISD) than the original instruction, which will help to avoid LMFP being imposed while the settlement instruction structure will remain unchanged.
   3) This practice is also allowed under the ECSDA Framework (see point 7).

5. **Information from the ECSDA Framework: point 7**

6. **Cash penalties for compound transactions** (as referred to in § 38 of the Detailed Rules of Operation of KDPW) used in the depository system:
   1) each component transaction is verified independently under the LMFP criteria in accordance with the standard solutions;
   2) for matched instructions forming part of a component transaction where the component transaction is incomplete – the calculation of the SEFP for late settlement is imposed on the party that established the link between the instructions. The establishment of the link, as a result of which other instructions were not directed to settlement, shall be treated as if the instruction were put on "hold".
      when the compound transaction is complete, the general terms of imposing SEFP apply.
      for matched instructions forming part of a component transaction and sent to settlement – the calculation of the SEFP for late settlement is imposed on the party on whose account there was a shortage of securities or cash, that established the link between the instructions. The establishment of the link, as a result of which other instructions were not directed to settlement, shall be treated as if the instruction were put on "hold".
   3) for matched instructions forming part of a compound transaction and sent to settlement, the calculation of the SEFP for late settlement shall take place as follows:
      a/ for the counterparty on whose relevant account there was a lack of securities or a lack of cash – for those instructions in which a lack of assets was identified
      b/ for the counterparty, which established the link between the instructions – for the instructions which were established as compound transactions in which a lack of assets was not identified, and the settlement failure is a unique consequence of the link between the instructions.

7. **Information provided in the ECSDA Framework on SEFP and LMFP: points 7, 7.1, 7.2.**

VIII Calculating debits and credits

VIII.1. **Daily gross amount**

1. The daily gross amount of debits and credits is calculated for each settlement instruction subject to cash penalties; the amount is calculated for a given day and there is no aggregation of amounts for different days relating to a given instruction.

2. The daily gross amount is calculated according to the KDPW system calendar rather than the PBD (Penalties Business Day) calendar applicable to actions taken after the closing of the month.

3. Information provided in the ECSDA Framework: point 2.1.3.

VIII.2. **Daily amount – bilateral netting**

1. In addition to the gross amounts referred to above, a bilateral net amount is calculated for each business day.

2. The amount for a participant is calculated per cash penalty currency and per counterparty/KDPW participant (as per the settlement instruction).

3. It is a component of all the penalties calculated on a given day for any cause.

4. Net amount = credits – debits; a positive amount is a daily credit per counterparty and per currency.

5. Information provided in the ECSDA Framework: point 7.3.

VIII.3. **Monthly aggregate amount**

1. The aggregate monthly amount of cash penalties per counterparty and per currency is calculated after the end of each month.

2. The calculation will be closed on the 14th PBD after the end of the relevant month according to the harmonised European CSD cash penalties calendar.

3. Information provided in the ECSDA Framework: point 7.4.1.

VIII.4. **Global net amount – amount due or receivable**

1. In addition to the monthly aggregate amount per counterparty, a global net amount is calculated which reflects the amount of cash flows in respect of cash penalties.

2. The calculation is closed on the 14th PBD after the end of the relevant month according to the harmonised European CSD cash penalties calendar.

3. The global net amount is calculated per currency (PLN and EUR).

4. Calculations are performed separately for:
   1) **intra-CSD operations**, i.e., settlements exclusively within the KDPW system;
   2) **any operational link established by KDPW with another CSD** – operations executed via such an operational link; in this case, KDPW is the Investor-CSD and uses information and calculations from another CSD (Calculating-CSD).

5. The Global Net Amount does not include transactions with the participation of the CCP as the central counterparty – such payments are processed by the CCP in relation to clearing members (see the section on: Payment of penalties for CCP transactions).

6. Information provided in the ECSDA Framework: glossary, definition of "Global Net Amount", point 7.4.2.

IX   Participants' appeals and corrections, recalculating cash penalties

IX.1. **Prior unavailability of reference data**

1. Reference data (e.g., instrument price on a given date) may in certain instances be unavailable. Once the data is obtained, the relevant conversion and calculation of the correct penalty fee value is performed.

2. Data may be updated no later than 11 PBD after the end of the relevant month.

3. Information provided in the ECSDA Framework: point 8.4.

IX.2.   **Removal of existing penalties**

1.   Calculated penalties may have to be removed due to events such as participants' appeals.

2.   Appeals are lodged by completing a form using a template available on the KDPW website, which will include the following information:
   1)   a reference to an instruction (instruction details) subject to a cash penalty;
   2)   the reason for lodging the appeal;
   3)   action expected by the party lodging the appeal.

3.   Appeals will be allowed per instruction and per day – gross corrections.

4.   Penalties may be removed up to 11 PBD after the end of the relevant month; participants may submit forms until the 10th PBD.

5.   The following reason codes are used for penalty removals (Information provided in the ECSDA Framework):
   1)   INSO – Insolvency
   2)   SESU – Settlement Suspended
   3)   SUSP – Trading status suspended
   4)   SEMP - Settlement on multiple platforms (applies in case the cash settlement is outside the CSD settlement system and the payment system is closed)
   5)   TECH – Technical impossibilities
   6)   OTHR – any other case (requires a narrative text to be added)

6.   Information on penalty removals are included in daily reports.

7.   Information provided in the ECSDA Framework: point 2.1.6, 8.1, Annex II point 4.

IX.3.   **Re-inclusion of previously removed penalties**

1.   Previously removed penalties may be re-included.

2.   This operation may be processed up to the 11th PBD after the end of the relevant month.

3.   In such instances, the penalty is recalculated; penalty reference data are amended.

4.   Re-inclusion of penalties is reported to participants (both counterparties).

5.   Information provided in the ECSDA Framework: point 8.2, Annex II point 4.

IX.4.   **Re-allocating penalties to other participants**

1.   Penalties may have to be reallocated as a result of participants' appeals to a different entity, in particular the other counterparty, if the penalised party is not the defaulting one.

2.   Following adjustment and recalculation, the parties will receive corrected reports.

3.   Information provided in the ECSDA Framework: point 8.3, Annex II point 4.

X   Cash penalties for inter-CSD transactions

X.1. **General**

1.   Penalties are calculated by a single CSD (the Calculating-CSD).

2.   The Calculating-CSD calculates penalties and reports them to all system participants including other CSDs.

3. KDPW calculates cash penalties for all KDPW participants in the event of settlement fails of operations to be settled in the KDPW system, i.e., where KDPW is the place of settlement.

4. The situation described in point 3 (KDPW as Calculating-CSD) includes in particular the following operations where KDPW is:
    1) **the issuer CSD** and the settlement fail occurs in KDPW, e.g., GPW transactions, OTC bond trades, etc.;
    2) **an investor CSD** but the instruction subject to the cash penalty is not a cross-border transaction, e.g., GPW transactions in securities recorded in KDPW via operational links.

5. KDPW may also receive information concerning cash penalties calculated in another CSD; in practice, for cross-border transfers. In particular:
    1) this concerns securities recorded in KDPW as investor CSD;
    2) penalties may be imposed where a KDPW participant orders a transfer with a past settlement date – LMFP penalties, matched after the ISD, KDPW acting on behalf of the participant is last to enter the instruction to a foreign CSD;
    3) a participant of a foreign CSD is late with a transfer, settled after the ISD because of the KDPW participant's fault.

       The following scenarios may apply:
    4) KDPW is required to pay a cash penalty, e.g., LMFP;
    5) KDPW receives a late settlement penalty from a foreign CSD – the counterparty delivered securities after the ISD.

       Collected or paid penalties are included in reports provided to KDPW participants after receipt of the foreign CSD's report. The Global Net Amount is calculated and cash penalties are charged and redistributed in processes separate from similar actions taken in relation to intra-CSD processes.

6. If securities are recorded in an omnibus account managed by KDPW for a foreign CSD, the following scenarios may apply:
    1) an instruction in the KDPW system does not settle on the ISD – the cash penalty is calculated as for any other KDPW participant;
    2) the settlement fails outside the KDPW system, e.g., internal settlement of securities in a foreign CSD, the penalty is not calculated by KDPW but by the foreign CSD which identified the settlement fail.

7. Information provided in the ECSDA Framework: point 9.1.

X.2. **Calculating cash penalties for KDPW participants (Investor CSD) which are CSDs (central securities depositories)**

1. The process is the same as for any other KDPW direct participants.

2. The Investor-CSD receives the cash penalty calculation from KDPW in standard daily and monthly reports.

3. The Investor-CSD does not itself calculate cash penalties for settlement fails in KDPW.

X.3. **Cash penalties calculated by other CSDs which manage KDPW's omnibus securities accounts**

1. As a participant of other CSDs, KDPW may act as intermediary in the payment of cash penalties for settlement fails of cross-border transfers.

2. In such instances, KDPW performs the role of the Investor-CSD.

3. KDPW receives cash penalty calculations from the Calculating-CSD.

4. In practice, the cash penalty system covers KDPW participants who instruct cross-border transfers and includes:
    1) debits (amounts due) – if a KDPW participant causes a settlement fail;
    2) credits (amounts to be received) – if a KDPW participant is affected by a settlement fail.

5. As a holder of an omnibus account in KDPW, KDPW will be credited/debited by foreign CSDs.

6. KDPW receives standard daily and monthly reports from foreign CSDs.

7. Cash penalties presented in reports from Calculating-CSDs are reported to KDPW participants who are the end recipients of such reports.

8. Reports sent to KDPW participants specify such payment amounts separately in respect of cross-border operations.

XI   Reporting to participants

1. **Daily reporting**
    1) calculation of cash penalties;
    2) generating daily reports for each participant where there are any new, amended, removed or recalculated penalties during the day according to the following principle:
       a) new cash penalties for events of the previous settlement day (DAIL, FWIS);
       b) modified penalties for the current or previous clearing month (DAIL, FWAM).

    Reports are aggregated for each counterparty;

    Reports are also generated indicating "no activity" (no penalty during the day);
    3) The distribution of reports takes place as follows:
       a) after the end of the cash penalty calculation process for the given day, i.e., after the closing of the settlement system (availability of settlement for SEFP and availability of matching for LMFP) and after the reference data are uploaded to the KDPW system as necessary to calculate cash penalties;
       b) no later than 12:00 on the day following the day for which cash penalties are calculated.

2. **Monthly reporting**
    1) Since:
       a) appeals and corrections may be lodged within 10 PBD following the end of the relevant month;
       b) data are recalculated on the 11th BD after the end of the relevant month at the latest;
       c) reports including adjustments (if any) are sent on the 12th BD after the end of the relevant month;

    The monthly aggregate reports are sent on the 14th BD after the end of the relevant month;

    2) Monthly reports aggregate net penalty amounts per currency and per counterparty;
       a) positive amount (credit) – expected to be paid to the counterparty;
       b) negative amount (debit) – expected to be paid by the counterparty.

3. **Information provided in the ECSDA Framework: points 2.1.4, 2.1.5., 2.1.7.**

XII   Cross-CSD reporting

1. CSDs which are KDPW participants receive daily and monthly reports in the same manner as all other system participants;

2. The Investor-CSD which receives information and reports from KDPW (as Calculating-CSD) forwards the information in its system to its system participants after receiving the KDPW report;

3. Monthly reporting is the same as for other CSD participants;

4. Participating CSDs have one more day to lodge an appeal (appeal period) and may do so by the end of the 11th PBD after the end of the relevant month to which the data relate;

5. Monthly reporting – the same as for other CSD participants; however, amounts in monthly reports are aggregated per currency, per counterparty and per CSD link;

6. Information provided in the ECSDA Framework: points 2.2.4 – 2.2.7.

XIII Exemption from cash penalties

XIII.1. Participant insolvency

1. Settlement fail cash penalties shall not apply to CSD participants against whom insolvency proceedings are pending.

2. Cash penalties calculated before the date of the announcement of the insolvency should be managed separately in monthly reporting and in the collection process, i.e., they should not be included in monthly reports.

3. Information provided in the ECSDA Framework: point 12.2.3.

XIV Reporting – system messages

XIV.1. General

1. KDPW uses ISO20022 standard messages.

2. KDPW makes available cash penalty system messages in the following communication systems:
   1) ESDI/ESDK – KDPW's systems;
   2) SWIFT network.

XIV.2. Format of KDPW system messages

1. KDPW complies with ISO20022 formats.

2. The message used in daily and monthly reporting is semt.044.

3. Information provided in the ECSDA Framework: point 11.1.1.

XIV.3. Reporting on payments

1. Daily and monthly reports contain no details of the final amount to be paid by the participant: daily reports include gross amounts per instruction; monthly reports include aggregate amounts per currency and per counterparty.

2. KDPW processes payments by means of PFOD (payment free of delivery) instructions.

XIV.4. Types of messages – summary

1. The following messages will be available for reporting:
   1) daily reports;
   2) monthly reports;
   3) payment amount messages, in particular PFOD instruction status.

2. Information provided in the ECSDA Framework: point 11.3 (and its subpoints).

XV Payment processing

XV.1. General

1. Payments are processed on the 17th BD after the end of the relevant month.

2. Cash penalties are collected and redistributed on one and the same business day. Where this day falls on a local bank holiday, the payment is made on the next business day following the 17th PBD.

3. KDPW only distributes amounts previously received from participants.

4. Tolerance levels shall not apply – the payment amount must exactly equal the monthly calculation amount.

5. Lack of payment on the part of the participant means that participant's complete exclusion from the calculations in a given period. The participant will also not receive any potential receivables that may be in his original "balance".

6. Information provided in the ECSDA Framework: point 12.2.4

7. KDPW will notify its participants of any late processing of payments.

8. Partial payments will not be processed; as a result, credit and debit amounts are processed whole without any deduction.

9. Cash penalties may only be paid in PLN and EUR; as a result, payments are processed in SORBNET2 or TARGET2, respectively.

10. Payments are processed no later than 11:00 on the 18th PBD.

XV.2. Generating and processing PFOD instructions

1. KDPW initiates payment orders with instruction code 644 for both the redistribution of cash penalties and their collection using the PFOD instruction with the PAIR (payment free of delivery) operation code.

2. PFOD instructions are based on monthly calculations; the instructions are issued in the global net amount due/to be received per currency.

3. The instructions are assigned the highest possible priority.

4. For cash penalties in respect of CSDs' internal operations, no matching is required. Instructions generated by KDPW are already matched.

5. Instruction settlement system: payments are processed in the RTGS system between 11.00 and 17.00.

6. Settlement is performed separately in PLN and EUR in the SORBNET2 or TARGET2 systems respectively.

7. In view of the selected method of collection and redistribution of cash penalties, the system will use bank accounts indicated by KDPW participants as default accounts per currency. Those accounts may be the participants' proprietary cash accounts or accounts managed by payment banks.

8. PFOD instruction contents:
   1) transaction date – 16th PBD (even if the 16th PBD is a bank holiday)

2) settlement date – 18th PBD (or KDPW's first business day after the 18th PBD when the settlement currency is supported if the 18th PBD is a bank holiday or a day when the settlement currency of the PFOD instruction is not supported)
3) ISIN code – the CSD expects to use a dummy ISIN: LU2128008567
4) settlement currency code – PLN or EUR depending on the currency of the cash penalty
5) settlement amount – net cash penalty amount
6) quantity of securities – always 0 (zero)
7) PFOD instruction settlement counterparties:
    a) charging penalties:
    - debit - KDPW (code 0001) is the party credited in cash
    - credit (pays) – participant with the payment obligation

    b) redistributing penalties:
    - debit - participant to receive a payment
    - credit - KDPW (code 0001)

8) operation code – the PAIR code has been defined in KDPW regulations
9) settlement system - RTGS

XV.3. Collecting cash from participants

1. Participants deposit cash in accounts before the deadline on the 18th BD.

2. Amounts collected are booked on KDPW's account in the clearing bank.

3. Amounts are redistributed after participants meet their payment obligations.

XV.4. Redistribution to participants

1. The process is initiated after the collection process is completed.

2. KDPW generates PFOD instructions which require no matching.

3. Payments are executed in the clearing bank on the 18th PBD.

XV.5. Information provided in the ECSDA Framework: points 10.1, 20.2, 10.3

XVI Payment of cash penalties for CCP transactions

XVI.1. General

1. According to the existing legal regulations concerning transactions to which a CCP is a counterparty, a special payment regime applies.

2. Within the scope of their clearing functions, CCPs are not charged cash penalties as part of the cash penalty system.

3. This approach relates to transactions where a CCP is a settlement counterparty following clearing novation, i.e., it concerns the CCP with the participation type of "central counterparty".

XVI.2. CCP payment processing

1. Daily and monthly reports include transactions in which the CCP is a participant and contain information necessary to identify transactions where the CCP is a participant, such as:

    a) the field <PnltyPerCtrPty>/<PtyId> contains the CCP's institution code, which is 0013 (for KDPW_CCP);

    b) the Counterparty Type field <PnltyPerCtrPty>/<PtyId>/<Tp> contains the code "CCPA"(central counterparty), which identifies the CCP as the central counterparty;

2. Transactions identified according to the aforementioned principles are excluded from the Global Net Amount for payment;

3. Payments in respect of cash penalties charged and redistributed by KDPW (as a CSD) do not include penalties for transactions where the CCP is participant;

4. The CPP uses reports provided by KDPW to make payments in respect of charging and redistributing cash penalties among CCP clearing members.

5. Information provided in the ECSDA Framework: point 12.3.