Minutes of the European Repo Committee meeting held on 23 August 2011 in London

Present:  
- Mr. Godfried De Vidts  ICAP (Chairman)  
- Mr. Stefano Bellani  JP Morgan  
- Mr. Rajen Patel  Morgan Stanley (substitute)  
- Mr. Olly Benkert  Goldman Sachs  
- Mr. Simon Tims  UBS AG  
- Mr. Jean-Michel Meyer  HSBC  
- Mr. Michel Semaan  Nomura  
- Mr. Sylvain Bojic  Société Générale  
On the phone:  
- Mr. Tony Baldwin  Daiwa Capital Markets  
- Mr. Eugene McGrory  BNP Paribas  
- Mr. Andrea Masciovecchio  Intesa Sanpaolo  
- Mr. David Nicholls  Deutsche Bank  
- Mr. Mats Muri  BarCap  
- Mr. Romain Dumas  Credit Suisse  
Also Present:  
- Mr. Tony Platt  Morgan Stanley (Chair, ERC Ops)  
- Mr. Kevin McNulty  ISLA  
- Ms. Lalitha Colaco-Henry  ICMA (Secretary)  
- Ms. Lisa Cleary  ICMA  
- Mr. Paul Richards  ICMA  
- Mr. John Serocold  ICMA  
- Ms. Serena Vecchiato  ICMA  
- Mr. Richard Comotto  ICMA Centre  
Apologies:  
- Mr. David Hiscock  ICMA  
- Mr. Eduard Cia  Unicredit Bank AG (Vice Chairman)  
- Mr. Andreas Biewald  Commerzbank  
- Mr. Edward McAleer  Morgan Stanley (Vice Chairman)(substitute)  
- Mr. Johan Evenepoel  Dexia Bank Belgium  
- Mr. Herminio Crespo Urena  Caja de Madrid  
- Mr. Grigorios Markouizos  Citigroup  

**Welcome by the Chairman**

The Chairman thanked everyone for attending and dialling into the meeting.
1. **Minutes of the previous meeting**

The draft minutes of the last ERC Committee meeting held on 30th June 2011 in Portugal, were sent to the ERC Committee on 3rd August 2011. It was noted that the Committee had agreed, at the June meeting, for minutes of Committee meetings to be published on the ICMA website. The June minutes were unanimously approved without comment and accordingly will be published on the ICMA website.

2. **Repo Cash Settlement**

The Chairman reported on the meeting with the ECB held on 14th July. The Chairman, Mr. Comotto and Mr. Platt had presented a draft of the Repo Cash Settlement Study. The study was carried out by Mr. Comotto as a way for the ERC to inform the discussion of reform of European financial market infrastructure relevant to repo. The study is also relevant to ongoing discussions on the interoperability of triparty repo services. Ms. Daniela Russo, Directorate General Payments and Market Infrastructure at the ECB, welcomed the study as a valuable contribution. The paper is currently being reviewed prior to publication on 14th September, the date of the next ERC Council meeting being held in Paris.

The Chairman had circulated to the Committee a draft of his foreword for the publication of this latest study and asked whether the Committee had any comments regarding the three priorities for the ERC, namely, the development of interoperability for triparty repo between both ICSDs, unfettered access by all types of trading venues to all CCPs irrespective of the location of the collateral and improved European-wide access to liquidity, fully respecting the level playing for all users. The Committee agreed that these are the priorities for the ERC.

Mr. Comotto noted that the main point of the paper is to examine the relationship between commercial bank money (CoBM) and central bank money (CeBM). CeBM is synonymous with systemic stability while CoBM extends the reach of the system to a greater number of participants such as international participants and those who are unable or unwilling to open up a direct account with a central bank or need to settle in foreign currency or cross-border. As the study shows, CoBM prudently used, can be an adequate alternative to CeBM. Mr. Comotto went through a slide presentation which showed various combinations of CCP, depository and payment systems. The models set out four broad categories of systems. The conclusion of the study is that in order to extend the system beyond the top tier of banks or cross-border, CoBM is required. It was also noted that almost all the diagrams apply to both cash and repo markets. Prior to publication, the study will be shown to the European Commission, LCH.Clearnet, LCH.Clearnet SA, Eurex Clearing and CC&G. MeffClear had also been invited but no response had been received to date. Clearstream and Euroclear will receive a copy prior to publication in recognition of their valuable input as members of ECSDA.

3. **Composition of European collateral pool**

Discussion of this item was postponed as the working group had been unable to prepare. A proposal will be submitted at the next ERC Committee meeting on November 7th in Denmark.
4. **Possible amendment of the ERC acceptable General Collateral (GC) List**

Ms. Colaco-Henry said that at the last Committee meeting, the ERC Secretariat had been tasked with updating the ERC acceptable general collateral list (“List”) by adding the bonds and bills of Estonia and Slovakia as well as issues of the European Financial Stability Facility. In starting to carry out this task, it became clear that the task was perhaps not as simple as first thought. The List has been in existence for at least 12 years and sets out the issuers/security types which are deemed by the ERC to be acceptable as collateral on GC repo and buy/sell transactions. In the past, the list has included government bonds from a variety of countries such as Japan and Canada. Moreover, for certain EU Member States, the list had contained caveats on the types of bonds that would be acceptable, e.g., French index-linked were excluded from the list in 1999 unless otherwise agreed by the counterparties prior to the transaction. The current list now comprises government bonds of member states that are in the Euro and government bonds from the UK, Denmark, Sweden, Norway and Switzerland.

The last time the List was scrutinised in detail by the Committee was September 2006. Minutes of that meeting reveal that the discussion focused on (1) whether total volume of the sovereign issuer or the size of the individual bonds would be a better criterion; (2) that a decisive criterion should be whether the bonds are already included in the ICSDs; (3) the fact that even if the ECB accepts bonds as collateral this would not mean that they would be accepted by clients. It was agreed at that meeting that the ERC committee should refrain from any political statement such as recommending the inclusion or exclusion of bonds from certain countries or with certain ratings from EURO GC eligibility. Accordingly, the committee had concurred that it would abstain from such a recommendation.

Returning to the present, given that it is unclear whether the list is used by the market in practice, the Committee agreed that the list should no longer be published on the ICMA website. The Chairman agreed to inform the European Banking Federation of this decision.

5. **Repo margin guidelines**

Mr. Platt led a discussion of the latest draft of the Repo Margin Best Practices paper. He noted that the answer to question 2 (how is mark-to-market calculated) had been amended to take into account the use of different methodologies within a portfolio. The answer to question 6 (how is interest paid on cash margin) had been amended to include a reference to RONIA. The answer to question 8 (is a substitution of margin collateral possible) had been amended to make it clear that substitution should be bilaterally agreed.

Mr. Platt also noted that the wording in the answer to question 9 (which trades have to be included into the daily “mark-to-market”) had been changed to make it clear that the calculation of daily “mark-to-market” should only include those trades that have actually settled, as opposed to including those trades where there is assumed settlement. Therefore, the answer now provides: “All trades that had a settled on-side with settlement date of T-1 or earlier should be included in the margin calculation, all trades with a failing on-side as of this time should be excluded from the calculation. All trades with a settled off-side with settlement day of T-1 or earlier should be
excluded from the calculation, all trades with a failing off-side as of this time should be included in the calculation.” It was commented that fails should be added back into the exposure calculation and that many firms at this time do not have the ability to monitor for failed trades, though this functionality is being developed. It was agreed that all ERC Committee members should agree to adopt the Best Practice guidelines in a coordinated fashion. The Chairman also noted that regulation is moving the market to T+2 settlement, which will come into force by the end of 2012. Mr. Platt agreed that he would raise this issue at the ERC Council meeting in September as it was important to start educating market participants about the need to implement appropriate systems in order to adopt the Best Practice guidelines. This issue would also be discussed by the ERC Operations Group to understand the extent to which member firms will be able to adopt the Best Practice guidelines by June 2012.

The Committee also discussed the answer to question 11 (how are forward trades included in marking to market), which specifies that forward starting repo will be excluded from the calculation. After much discussion, it was agreed that further work is needed to consider the appropriate treatment for such repo trades.

Mr. Platt also noted that regarding question 15 (what happens if margin collateral is not delivered (event of default)), the answer had been amended to take into account the concerns raised in the June 2011 Committee meeting.

It was agreed that the Repo Margin Best Practices paper should be finalised in advance of the January 2012 European Repo Council annual general meeting.

6. **Interest Calculation for floating-rate repos**

Mr. Comotto led a discussion regarding how the rate of interest in floating rate repos should be calculated. He advocated that there is a need for clarification about the way market participants calculate the floating-rate and specifically the timing of the fixing of the rate they use for the daily margin calculation.

The Committee concluded as follows - it has proved difficult to establish a single common pattern that could be said to represent market practice and instead, different market participants use different conventions. To add to the lack of consensus on this issue, there appears to be some confusion about what EONIA is. The Committee agreed that this is a topic that requires clarification. Accordingly, it will be discussed at the next Committee meeting.

7. **Coupon re-investment on buy/sell-backs**

Mr. Comotto addressed a discussion on the coupon re-investment calculation on buy/sell-backs done by LCH.Clearnet SA, which seemed to differ from the calculation method used by the trading venue and the information vendor. In particular, it was noted that the trading venue and information vendor count 17 days for the re-investment calculation against 19 days counted by LCH.Clearnet SA which had included the weekend in the calculation. The Committee agreed with Mr. Comotto’s analysis that the market would calculate 17 days and the seller would not be any worse off. It was agreed that a letter should be sent to LCH.Clearnet SA asking for clarification on
this matter.

8. **Eurepo® and quality of quotes and launch of Eurepo benchmark by EBF**

Mr Andrea Masciovecchio noted that a new definition of Eurepo® has been developed. However, the Committee agreed that the development of an objective benchmark would be very beneficial for the market, based on government bonds rather than corporate bonds. The Committee also agreed that the ideal benchmark would be based on weighted average trades rather than a fixing. One option could be to use repo trades on GC using a central counterparty. The Chairman agreed to discuss this matter with the European Banking Federation.

9. **Repo Code of Conduct**

Given the lack of progress regarding the Repo Code of Conduct, it was agreed that this item would be removed from agenda for the ERC Council meeting in September. Instead, Mr. Comotto would seek to finalise the Code in advance of the January 2012 European Repo Council annual general meeting.

10. **ERC Operations**

Mr. Platt gave an update on the work conducted by the ERC Operations group. The trade matching guidelines have now been published on the ICMA website. They can be accessed [here](http://www.icmagroup.org/ICMAGroup/files/2e/2eba29d5-2084-4c77-97d4-a4d7e1192fe8.pdf). The next step will be to consider how they should sit alongside electronic platforms.

A letter is being drafted to Monte Titoli regarding their recent system outage. Monte Titoli have experienced two catastrophic failures in the past six months. The letter will ask for improved reporting of outages to the market and also reassurances that system improvements designed to rectify the problems will be robust. There was a brief discussion regarding the fact that Monte Titoli is proposing the imposition of fail penalties, though it was recognised that the documentation accompanying the proposal requires greater scrutiny.

Other issues that the ERC Operations Group are considering include agent lending disclosures and legal entity identifiers.

11. **Legal update**

Miss Cleary noted that the 2011 legal opinions have been published. The GMRA working group is currently reviewing a number of the Annexes to the GMRA 2011 which are due to be published alongside guidance notes to the GMRA 2011 by the end of September 2011.

12. **AoB and Upcoming meeting dates**

Alternatively, see: [http://www.icmagroup.org/ICMAGroup/files/2e/2eba29d5-2084-4c77-97d4-a4d7e1192fe8.pdf](http://www.icmagroup.org/ICMAGroup/files/2e/2eba29d5-2084-4c77-97d4-a4d7e1192fe8.pdf)
**Buy-ins** – the Committee discussed the situation where if you have a repo cash termination on a fail to deliver versus guaranteed buy-in on an outright fail to receive, you end up long in the bond outright in market risk. The Committee discussed what the possible remedy might be for the person in the middle – sell the bond outright in the cash market, or end up with two cash market fails? The Committee recognised that this may become a growing problem as the volume of fails (repo terminations) is increasing. Some cash desks are refusing to be appointed as buy-in agents, especially for other brokers in respect of very tight bonds. It was agreed that the problem rests on the cash side rather than on the repo side. Mr. Serocold noted that he was in discussions with participants active in the secondary cash market. One possibility for resolving the issue could be to have a cash option as a first process prior to initiating a buy-in. However, this could potentially turn the cash market into a derivatives market. Mr. Serocold agreed to continue discussions with ICMA’s Secondary Market Practices Committee and also engage with the EPDA as the issue is more problematic for government bonds than for corporate bonds. The Committee agreed that if there could be greater harmonisation between the repo and cash sides, which could help to reduce the number of fails, this would be well received by those regulators in Brussels who are considering short selling legislation.

**Mini Close-out** – the Committee considered the issue of the materialisation of bond exchanges on existing repo transactions (as per the forthcoming Greek bond exchange programme). The Committee considered that in relation to corporate events, the instructions need to be passed on to those who have borrowed the paper. In repo transactions this is accepted, although not desirable. As the securities lending market operates differently, there may be some benefit in looking at the legal documentation to see if provisions pertaining to corporate events can be amended so they are voluntary instead of mandatory.

**Research Project** - ICMA, together with ISDA and AFME have commissioned a research project on sovereign collateral that is being carried out by ECMI (the European Capital Markets Institute). It is expected that the study will be published sometime in mid-September.

**Relationship with ISLA** – Mr. McNulty noted that he will try to attend ERC Committee meetings more regularly. He recognises that many of the regulatory issues affecting securities lending also concern repo. ISLA is currently focused on ETFs, short selling, Solvency II (which could also impact on repo), and the FSB investigations into how shadow banking should be regulated. Agent lending disclosures are no longer on ISLA’s radar but Mr. McNulty understands the concerns of Committee members especially in relation to the trading desk being able to identify clients for purposes such as anti-money laundering legislation and the Terrorist Asset-freezing Act. Mr. McNulty undertook to consider these concerns further.

**Further dates:**

The ERC Council general meeting is being held on 14th September in Paris, hosted by BNY Mellon. The agenda is available [here](http://www.icmagroup.org/ICMAGroup/files/eb/ebb15253-2669-4777-819f-3212cd75ae2e.pdf).

The ERC Committee meeting will be held on 7th November in Copenhagen, at the invitation of Danske Bank.

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The Professional Repo and Collateral Management Course will be held on 21-22 November, hosted by BondLend in London.

The Chairman:  

[Signature]

Godfried De Vidts

The Secretary:  

[Signature]

Lalitha Colaco-Henry

London, 23 August, 2011