

Minutes of the ERCC Committee meeting held on 22 February 2017 in London

Present:	Mr. Godfried De Vidts	BrokerTec (ERCC Chairman)
	Mr. Grigorios Markouzos	Citigroup (ERCC Vice Chair)
	Mr. Eduard Cia	UniCredit Bank (ERCC Vice Chair)
	Mr. Dan Bremer	BAML
	Ms. Emma Cooper	Blackrock
	Mr. Michael Manna	Barclays
	Mr. Andreas Biewald	Commerzbank
	Mr. Michel Semaan	Crédit Agricole
	Mr. Romain Dumas	Credit Suisse
	Mr. Ronan Rowley	Deutsche Bank
	Mr. Johan Evenepoel	Euroclear Bank
	Mr. Francois-Xavier Bouillet	Goldman Sachs
	Mr. Jean-Michel Meyer	HSBC
	Mr. Nicola Danese	JP Morgan
	Mr. Paul van de Moosdijk	PGGM
	Mr. Gareth Allen	UBS Limited
		Mr. Nicholas Hamilton
	Ms. Lisa Cleary	ICMA
	Mr. Richard Comotto	ICMA Centre
	Mr. Andy Hill	ICMA
	Mr. Paul Richards	ICMA
	Mr. David Hiscock	ICMA
	Mr. Alexander Westphal	ICMA (ERCC Secretary)
Guests:	Jean-Robert Wilkin	Clearstream
	Michel Bricq	Clearstream
	Rebecca Carey	Euroclear
On the phone:	Mr. Eugene McGrory	BNP Paribas
	Mr. Sylvain Bojic	Société Générale
Apologies:	Mr. Richard Hochreutiner	Swiss Reinsurance

1) Update from the ICSDs

Three representatives from the ICSDs, Euroclear and Clearstream, attended the meeting to provide an update on their recent discussions in relation to the Bridge.

They explained that while T2S brings cross-border settlement in Central Bank Money (CeBM) to new standards, it is also important to think of the Commercial Bank Money (CoBM) environment and how to align the two. Importantly this includes discussions on how to further enhance the link between the two ICSDs, the so-called Bridge. The key objectives of these discussions are to (i) maximize the settlement window between the ICSDs to support increased same-day and intra-day

settlement activity, (ii) move settlement windows & deadlines as close as possible to domestic cut-offs, and (iii) support settlement interoperability for triparty repo products, with Eurex GC Pooling. The agreed path for enhancing the Bridge involves three phases. The first phase was successfully implemented in September 2015, extending settlement deadlines and introducing a distinction between different currencies. This will be followed by a second set of enhancements which will further improve deadlines, allow for more frequent exchanges over the Bridge (48 instead of 17 possibilities to settle per day) and also improve the frequency of matching. This second set of enhancements will become effective on 19 June 2017. Subsequently, a third phase will be launched which should ultimately lead to a Real-time Bridge, the pre-condition for tri-party settlement interoperability. The necessary feasibility assessments for the real-time Bridge are expected to kick-off as soon as T2S is fully implemented, ie after September 2017. An important additional element to be taken into consideration in the context of the Bridge enhancements is the CSD Regulation (CSDR) which introduces certain requirements that could have a substantial impact on the settlement process. In particular, CSDR prudential requirements will constrain the ICSDs in their exposure to one another and thus require changes to the way the Bridge works today. The challenge is to optimise the settlement process in a way that reduces the need for intraday credit exposure between the ICSDs, while at the same time keeping settlement as efficient as possible and avoiding a significant shift of volumes from the night-time batch to day-time settlement. The ICSDs are currently working on a model which is hoped to achieve these objectives, but which might require increased usage of intraday credit lines on the side of participants.

In relation to the optimisation of intraday credit usage, members remarked that the success of this crucially depends on the individual settlement behaviour of market participants. It was thus suggested that in a second step, it might still have to be considered whether some agreed market best practices would be needed to better coordinate the timing of settlement. In this context, there might also be a case for additional batches to optimise settlement. Members also remarked that the real discussion on settlement optimisation should probably take place once T2S is fully implemented and the settlement environment stabilises. At this point it will become clearer to what degree settlement will shift from CoBM to CeBM, in which case the discussion on the Bridge could become less urgent. Although it was also acknowledged that this is likely to remain an important issue given existing constraints for certain counterparties to access CeBM. In this context, members also discussed the role of custodians, on applicable settlement cut-off times for market participants on the one hand, but also more fundamentally on the choice of settlement location which is mainly determined by the custodian.

The Chairman thanked the ICSDs for the presentation and welcomed the progress that is being made on the Bridge. In terms of next steps, it was agreed that the ERCC Operations Group should follow-up with the ICSDs on this issue. At a later stage this work should also be extended to involve CCPs and Trading Venues. Mr. Hamilton agreed with the suggested approach and added that there is a need for the ERCC Operations Group to better understand sequencing issues with the settlement process as a basis for developing recommendations. He suggested that the Group should work on specific use cases regarding the timing of the process. In this context, he also mentioned the ECB's new Advisory Group on Market Infrastructure for Collateral and Securities (AMI-SeCo) on which he represents the ERCC and which will be a useful forum to drive this agenda as it includes infrastructures and central banks, as well as market participants.

2) Minutes from previous meetings

Members approved the minutes of the last Committee meeting, held on 25 January in Luxembourg, without further comments.

Members were asked to vote for the Chairman and the two Vice-Chairs of the Committee. Mr. De Vidts was confirmed as Chairman of the ERCC Committee for another year. Members also unanimously renewed the mandates of the current Vice-Chairs, Mr. Markouizos and Mr. Cia, for another year.

The Chairman welcomed the two newly elected members of the ERCC Committee, Ms. Cooper and Mr. van de Moosdijk and added that he was particularly pleased to note that there are now 3 members from the buy-side on the new Committee. Following up on recent discussions in the Committee regarding buy-side representation, members were asked whether they still see a need to invite additional buy-side members as observers to the Committee, as had been agreed previously. Members decided that the outcome of the elections and the resulting significant increase in buy-side membership should address the concerns previously raised and that there was no need to invite additional observers to the Committee at this stage.

3) Updates from recent meetings with regulators

The Chairman and other members reported back from a number of recent meetings between ERCC delegations and regulators.

a) CGFS: On 30 January, an ERCC delegation met a group of CGFS members in London to follow up on previous discussions with them on their ongoing work in relation to repo. Mr. Hill commented that the meeting was relatively productive. He had presented the findings from the ERCC study on year-end repo market conditions. Although mostly in listening mode, CGFS members clearly seemed to be worried by the observed market frictions. It is though not expected that the CGFS work will lead to any immediate follow-up actions. The findings from the report will not feed into the ongoing Basel consultation on LR, but are rather intended to inform subsequent work to be undertaken in the course of 2018-2019.

b) ECB: On 15 February, following the publication of the ERCC year-end study mentioned above, a small ERCC delegation went to Frankfurt to present and discuss the findings from the report with the ECB. Mr. van de Moosdijk reported back from the meeting, noting that he was surprised by the large number of participants on the side of the ECB, although most of them remained rather passive. A couple of participants led the discussion on the side of the ECB and asked critical questions on the report. In response, ERCC participants clarified a number of important points, including that regulation may impact the market even where not yet fully in force, as market participants tend to anticipate new rules in order to smoothen implementation. In addition, ERCC members explained that from a systemic risk perspective it was not only relevant whether the market fully clears or not, but also at what size and at what price. In this regard, the events around year-end can be seen as a very clear warning sign. Overall, the ECB seemed to acknowledge that there is a problem in the repo market, although some of their assessments related to reasons and possible solutions differ from the view of market participants. As regards the role of the ECB more generally, some members remarked that their ability to improve the situation is limited given that the relevant lending programmes are fully in the responsibility of national central banks. However, it was also remarked that the lending programmes are not the only possible tool to improve the situation and that the ECB is a powerful voice in all the relevant discussions, so that it remains important that we have now provided the evidence that the market is seriously challenged - which is something that the ECB and other authorities have always insisted on seeing.

c) Commission: On 16 February, an ERCC delegation also met with officials from the European Commission, again mainly to discuss the market dislocations around year-end 2016. A summary of that meeting has also been shared with Committee members.

More generally, members discussed the right approach towards regulators in relation to the December events. While some members cautioned that we should not rely too much on the single year-end event, others insisted that the December dislocations were critical given their likely longer-term impact having destroyed trust in the reliability of the repo market more broadly, particularly on the buy-side. Also the fact that dealers basically stopped fulfilling their critical role in the market around year-end should be seen as an important warning sign by regulators. Members agreed that it was crucial at this stage to keep the pressure up and to continue to highlight the challenged market conditions. When dealing with authorities, the ERCC should focus on practical issues arising from the market conditions both for buy-side and dealers.

The upcoming ERCC AGM on 20 March in Zurich will be another occasion to keep up the momentum on the various important challenges for the market. The Chairman noted that the AGM agenda reflects this very well, including a presentation by Mr. van de Moosdijk on the buy-side perspective on the repo market, as well as a presentation by Mr. Hill on the ERCC year-end study. Overall, there seems to be an increasing awareness among regulators that there is a problem in the repo market. Pressure is also increasing on national central banks, hopefully leading to some necessary improvements in the relevant lending programmes.

4) Legal update

Ms. Cleary provided an update on recent developments in relation to legal issues. Given the ever-growing legal agenda, she suggested to set up a formal ERCC legal sub-group which would reflect roughly the agenda and meeting frequency of the Committee. This would thus formalise the current set up which is based on ad hoc consultations with legal experts from member firms. As a basis for setting up the new group, Ms. Cleary will circulate to Committee members a list with her current legal contacts at member firms for review. In terms of legal developments, Ms. Cleary covered the following five topics.

The idea to develop a **standardised corporate annex to the GMRA** has been considered for several years now. The purpose of such an annex would be to facilitate certain types of transactions with buy-side. However, discussions so far have not led to any significant progress. Legal and risk departments in some sell-side firms remain generally opposed to the idea of a standardised annex and the discussions are also difficult due to confidentiality issues. Committee members discussed whether and how to take the initiative forward. While generally supportive of the idea, members acknowledged that unanimity on this issue was probably impossible to achieve given the reluctance in some firms. In order to move forward, a sub-set of firms will probably have to go ahead. As regards the scope of the annex, members agreed that the most promising avenue would be to limit the annex to tri-party transactions. Considering existing ICSD documentation in this space, Ms. Cleary explained that both ICSDs are part of the working group and have expressed openness towards any standardised solution developed by ICMA, provided that it works and is generally accepted in the market. In terms of immediate next steps, Ms. Cleary will draft a note for Committee members which will set out the current state of the discussions as well as the key disagreements and sticking points. In addition, she will circulate a list of member firm representatives who have been involved in the discussions. In the meantime, Committee members are encouraged to discuss the issue with their relevant legal colleagues. At the same time, ICMA will consider undertaking further work with its buy-side constituency in order to get a better idea of the potential demand and to identify key issues with current GMRA documentation.

Ms. Cleary reminded members that ICMA is thinking to discontinue the **coverage of the GMRA 1995 in the legal opinions** as of 2018. Considering that this decision had already been reversed once, it is important for ICMA to receive a clear indication from member firms whether this deadline can be a hard deadline or whether the industry is not ready for such a move yet. As it is clear that many firms still use the 1995 version of the GMRA, a protocol has been developed in 2008 to facilitate the transition. However, industry take up of the protocol has been very limited so far. Some members confirmed that their firms are indeed reluctant to sign the protocol and are instead aiming to repaper all their existing 1995 agreements. It is not clear though whether this will be achieved in time for a 2018 deadline. Before deciding on whether a hard deadline to discontinue GMRA 1995 coverage is practical, members agreed that there needs to be a discussion on the reasons for firms' reluctance to sign up to the protocol. It was decided to have this discussion at the next Committee meeting in May. Members are encouraged to raise this issue with their legal colleagues ahead of that meeting.

Ms. Cleary explained that article 71(8) of the BRRD contains specific record-keeping requirements for firms related to their resolution plans. Among other things, the rules require firms to indicate the degree to which certain transactions, including repo, can be subject to bail-in. It was suggested by one member firm that these rules might require standardised industry guidance to ensure that the information is provided in a consistent way. It was agreed that this issue should be further discussed by legal experts in the ERCC's new legal sub-group.

As a final item, Ms. Cleary informed members about ongoing discussions within ISLA to develop standard documentation for pledge based securities lending. She asked members whether there was a business case for a similar initiative related to repo, which would require the development of a new master agreement type as well as related legal opinions. Mr. Hiscock added that this issue had also been discussed at the most recent ISLA Board meeting which he attended. During that meeting it was clarified that the current proposal would be a new agreement covering the entire transaction. In a first step, the idea is to limit the scope of the proposal to cover English, Belgian and Luxembourg law. Members discussed potential benefits of a similar structure for repo, but concluded that there does not seem to be a sufficient business case for developing this. Some members remarked that such an initiative might also lead to other problems, in particular as it raises new questions in relation to re-use. The only scenario where a pledge structure for repo might make sense is for the posting of IM. However, this should not be referred to as repo. It was concluded that ICMA should continue monitoring the ISLA discussions. At the same time, members are asked to provide further feedback. Discussions will be picked up by the new legal sub-group.

5) MiFID II Best Execution requirements for SFTs

Mr. Hill updated members on the latest discussions around the applicability of best execution requirements under MiFID II to SFTs. The ERCC has sent two letters to the relevant authorities to request clarification on the scope of the best execution requirements (in particular the ones set out under RTS 27) as it is not clear from the legal text whether these apply to SFTs. So far, no response has been received from either ESMA or the Commission. However, a small ERCC delegation met with the FCA to discuss the topic. They appeared broadly sympathetic and are understood to have subsequently raised the issue at a meeting with ESMA and other NCAs. Given the stage of the legislative process, it is however not clear whether ESMA has a mandate to resolve the issue. More likely, this will thus have to be addressed by the European Commission. While there is some hope for RTS 27, the FCA's feedback on the requirements under RTS 28 was less promising as they recognise that the current text is clear in that it applies to SFTs. Members

commented that this means essentially that the principle of best execution, as counterintuitive as it seems, would apply to SFTs, ie firms would need to prove for all repo trades that they have been executed at a price that is within an appropriate range. Members also briefly discussed the scope of RTS27, in particular whether these requirements apply only to agent business or more broadly.

6) CCP Recovery and Resolution

Mr. Hiscock updated members on the latest developments in relation to Recovery and Resolution Planning for CCPs. Two separate relevant initiatives address this issue: First, at EU level the European Commission published on 28 November 2016 an EU Draft Regulation on CCP Recovery and Resolution. This is now going through the regular legislative process during which both European Parliament and Council can suggest amendments to the initial draft law and will then agree on a final text. This process provides an opportunity for the ERCC to raise any concerns with the current text to the relevant contacts in the European Parliament and/or in the Council, through national Ministries of Finance. Second, at global level, on 1 February 2017 the FSB published a consultation on draft Guidance for CCP Resolution. This follows up on a discussion note published in August 2016 and contains some high level principles to be taken into account by national regulators when drafting their respective national rules. Given that Europe is ahead of the curve on this topic in that the related draft Regulation has already been published, Mr. Hiscock suggested that it probably makes sense for the ERCC to focus its attention directly on the EU Regulation and its advocacy with European legislators. In this context, it will be important for members to carefully consider the current proposals and decide whether we need to advocate any changes. So far, he has only received limited feedback. The one issue that seems to stand out is the proposal on variation margin haircutting which is considered inappropriate for SFTs. Members explained that the logic of margining in the case of SFTs where variation margin covers the principal risk is very different than for most derivatives where this applies to the respective P&L of the trade only. Applying variation margin haircutting to SFTs would thus create serious issues for SFT markets and may also negatively affect end users. Members agreed that the ERCC should approach the relevant contacts in the European Parliament, in particular rapporteur Ms. Kay Swinburne, with a letter outlining our concerns on the specific issue of margin haircutting.

7) NSFR

Mr. Hiscock introduced a short discussion on NSFR. The related Commission legislative proposal, published on 23 November 2016, is now going through the regular EU legislative procedure. Any concerns with the current proposals will thus have to be raised with the two EU co-legislators, the European Parliament and the Council. In the Parliament, this will be primarily be Mr. Peter Simon (S&D Group), the rapporteur for the file, as well as shadow rapporteurs from other political groups. The proposal itself includes some helpful improvements in relation to repo as compared to the previous Basel proposals in that it reduces the asymmetry in the treatment of repo and reverse repo trades, although not removing it fully. The ERCC should thus continue to advocate the removal of any asymmetry at a minimum, if a full exemption for repo from NSFR is not achievable. It was agreed that the Secretariat should draft a letter to the relevant MEPs on this issue.

8) ERCC Operations Group update

Mr. Hamilton, Co-chair of the ERCC Operations Group, provided an update on the work of the Ops Group. The Group is currently heavily focused on the upcoming implementation of the SFTR reporting rules. ESMA is expected to submit the final draft RTS by the end of March to the

Commission. The actual reporting is then expected to go live in Q4 2018. Given the extensive requirements this will be a very short window for the industry to prepare implementation. In order to kick off the necessary cross-industry discussions, on 8 March the ERCC Ops Group held a first SFTR event, organised jointly with ISLA and hosted by JPM. The event was well attended with over 200 participants, both from the industry and relevant vendor firms. The discussion helped to highlight some of the key problem statements and to start discussions on the dynamics of the operating model. One of the key issues in a complex and competitive environment with multiple matching engines and trade repositories will be to ensure a sufficient level of interoperability between the different systems. Moreover, it will also be important to continue pushing for consistent product definitions for SFTs, both at a firm level but also at the clearing and settlement layer. These and other aspects have to be developed more fully over the coming months. At the upcoming ERCC AGM on 20 March in Zurich, Mr. Hamilton will give a short presentation highlighting some key aspects to consider for the target operating model for SFTR reporting. This will be followed by a panel discussion. In relation to the SFTR, other Committee members confirmed the scale of the upcoming task and remarked that the reporting is not limited to banks but will have to be implemented by all market participants, including from the buy-side, which will add to the challenge.

In terms of other focus areas for the ERCC Ops, Mr. Hamilton also informed members of a newly established ERCC Ops FinTech WG, led by Mr. Sanjiv Ingle (SocGen). The aim of the group is to develop a better view on existing and emerging FinTech tools in the collateral operations space. Given the very active ERCC Ops agenda, Mr. Hamilton concluded with a request for Committee members to reach out to their operations colleagues to encourage participation in the ERCC Ops Group. As a basis for this, Mr. Westphal will circulate a list of current ERCC Ops membership to Committee members.

9) AOB and further dates

Mr. Comotto informed members about some recent work he has undertaken in relation to the impact of CSDR on CCP-clearing. This work has shown that CCPs will likely have to break up netting sets for repo trades in order to be able to apply the CSDR buy-in exemption for short-dated repo trades (<30 days) correctly. As a result, CCPs will probably not be able to net exempt and non-exempt trades. While most CCP-cleared repos would appear to be exempt, the overall effect of this change is currently hard to quantify. Members commented that the markets most impacted by such a change would be the French and German markets. It was thus suggested to first raise the issue with regulators and central banks in France and Germany, which are likely most interested to address the issue. This should also be coordinated with the SMPC's efforts to raise further concerns with the upcoming CSDR buy-in rules from a market liquidity perspective.

The Chairman raised an idea that he had discussed with Mr. Comotto related to the upcoming SFTR reporting regime. He suggested that ERCC member firms could share on a confidential basis some of reported data in an aggregated form also with the ERCC. This could be done for instance as part of the regular Repo Survey and would allow the ERCC to enrich its survey analysis and to limit likely future information asymmetries between market participants and regulators as ESMA is planning to publish only a very limited subset of the SFTR data.

As a follow-up from the discussion at the previous Committee meeting, Mr. Westphal asked members to reconsider the application of IHS Markit to become an ERCC member. Considering relevant precedents, members approved the application and agreed the following general approach for ERCC applications from service providers (vendors): (i) Vendors should be allowed to join the ERCC as associate members, where their services are considered relevant and (ii) they will be invited to join a specific vendor working group under the ERCC Ops Group (but not the Ops

Group directly). The aim of the latter will be to facilitate closer collaboration between ERCC Ops members and the relevant vendors in the SFT space, something that is considered particularly important in the context of the upcoming SFTR implementation.

In view of the upcoming Brexit negotiations, while probably still too early to have a proper discussion in the Committee on the likely impacts on the repo market, Mr. Hiscock raised the idea to launch some preparatory work in order to develop a better view in numerical terms of the geographical distribution of the market and thus the potential impacts from Brexit. For that purpose, he suggested that Mr. Comotto could prepare a few additional questions for the European Repo Survey which could be added to the June survey. While in principle supportive of the idea, members remarked that the questions would need to be sent to firms as soon as possible, in order to allow firms sufficient time to make the necessary system changes to collect that additional information. Mr. Comotto agreed to prepare some additional questions for members' review.

Mr. Hill announced that he will soon launch a short ICMA study in relation to credit repo. The purpose of this new study will be to inform the ERCC but it will also feed into the SMPC work in relation to secondary market liquidity. Mr. Hill will approach ERCC members on this issue in the course of the next weeks.

- **20 March (13:00 – 16:00 CET):** ERCC AGM in Zurich, hosted by SIX Repo AG
- **3 May (15:00 – 17:30 CET):** ERCC Committee meeting in Luxembourg, hosted by EIB
- **20 June (time tbc):** Joint ERCC Committee – ISLA Board meeting in Berlin (in the margins of ISLA's 26th Annual Securities Finance and Collateral Management Conference)
- **14 November (14:00 – 17:00 CET):** ERCC GM in Brussels (in the margins of the Euroclear Collateral Conference)

The ERCC Chairman:

The ERCC Secretary:

Godfried De Vidts

Alexander Westphal