

Minutes of the ERCC Committee meeting held on 20 June 2017 in Berlin

Present:	Mr. Godfried De Vidts	BrokerTec (ERCC Chairman)
	Mr. Dan Bremer	BAML
	Mr. Michael Manna	Barclays
	Ms. Emma Cooper	Blackrock
	Mr. Eugene McGrory	BNP Paribas
	Mr. Grigorios Markouizos	Citigroup (ERCC Vice Chair)
	Mr. Andreas Biewald	Commerzbank
	Mr. Michel Semaan	Crédit Agricole
	Mr. Romain Dumas	Credit Suisse
	Mr. Nicola Danese	JP Morgan
	Mr. Tom Wells	Morgan Stanley
	Mr. Paul van de Moosdijk	PGGM
	Mr. Sylvain Bojic	Société Générale
	Mr. Richard Hochreutiner	Swiss Reinsurance
	Mr. Gareth Allen	UBS Limited
	Mr. Eduard Cia	UniCredit Bank (ERCC Vice Chair)
	Mr. Ed Donald	Standard Chartered (ASIFMA)
	Mr. Richard Comotto	ICMA Centre
	Ms. Lisa Cleary	ICMA
	Mr. David Hiscock	ICMA
	Mr. Alexander Westphal	ICMA (ERCC Secretary)
On the phone:	Mr. Ronan Rowley	Deutsche Bank
	Mr. Jean-Michel Meyer	HSBC
	Mr. Nicholas Hamilton	JP Morgan (Co-Chair ERCC Ops Group)
	Mr. Andy Hill	ICMA
Apologies:	Mr. Johan Evenepoel	Euroclear Bank

Welcome

The Chairman welcomed members to the second session of the day and thanked Commerzbank for hosting the meeting. Following up from the preceding joint session with the ISLA Board, members had a brief discussion on the implications of MiFID II best execution requirements and the related time pressures, noting that in the absence of any clarification from regulators as to whether the rules actually apply to SFTs many firms already had to go ahead and start working on the implementation to ensure compliance.

On the impact of MiFID II more generally members commented that the one positive expected effect of the rules is likely to be a push towards the use of more technology and an increasing electronification and automation of repo operations as regulation requires firms to focus and rethink their back-office process.

1) Minutes from previous meetings

The Committee approved the minutes of the last Committee meeting held on 3 May 2017 in Luxembourg with one minor amendment.

2) Pledge based repo and other legal updates

Members picked up the discussion from the joint session with the ISLA Board on the standard documentation for pledge based securities lending which is being developed by ISLA, focusing on the potential implications for repo. Ms. Cleary shared some initial observations related to the ISLA proposals, stressing in particular the need to protect the integrity of existing documentation and to avoid confusion in the market and among regulators between the different legal structures.

Members remarked that ISLA's pledge work responds to some real concerns in the market, specifically related to capital costs, large exposure concerns and netting. It is thus important for the ERCC to be supportive of ISLA's efforts to address these problems. If no solution is found, there is a risk that in the near future a significant part of the securities lending market could be lost. While the main added value of a pledge based structure is seen for securities lending, members noted that there appears to also be a case for some pledge documentation in certain repo scenarios. The rationale for developing such documentation would be different though. One potential use case is related to funding with counterparts who do not transact in classic repo, ie the borrowing of cash (versus pledged securities collateral), which would not be well-suited to the agreement currently considered by ISLA. This would be more akin to a secured loan and would have to be very clearly distinguished from classic repo under the GMRA. A second case is to allow for a classic repo at par with a side agreement to pledge securities in relation to the initial margin or haircut applicable. This structural adaptation alters the risk, accounting and regulatory treatment, leading to a better outcome. Members discussed whether the ERCC should try to work together with ISLA to extend their current legal structure to also cover the use cases mentioned above, as a way to keep the number of required legal documents as limited as possible. While members were in principle supportive of a close cooperation with ISLA on this topic, it was also remarked that we are solving for different problems and that such significant change to the scope of the legal documentation might not be possible, especially at this relatively advanced stage in the process. It was agreed that ICMA should approach ISLA to discuss the question.

Ms. Cleary informed members that the first meeting of the newly established ERCC Legal Working Group will be held on 27 June and encouraged members to make sure that their legal colleagues are represented in the Group.

3) Macroprudential policy and repo

Members discussed increasing pressures from certain officials to consider the implications of repo for macroprudential policy, especially related to haircuts and collateral reuse. In particular, Mr.

Markouizos reported back from the Second Annual Macroprudential Policy and Research Conference which was held on 11 May in Frankfurt, and where ECB Vice-President Constancio, during his speech made repeated reference to the need to further regulate and restrict collateral reuse. Members agreed that it will be important to address the arguments put forward by Vice-President Constancio and to pro-actively counter these. While some of the remarks seem to be based on misperceptions, especially those related to collateral chains (reuse versus re-hypothecation), it is important not to dismiss the concerns entirely as some of the points, particularly those related to the risks of excessive leverage, are clearly relevant. The ERCC should instead stress the amount of improvement that has been achieved since the crisis and how this has already addressed the fundamental concerns expressed. It will be important for the ERCC to be vocal on this topic and to send a consistent message. The ERCC's upcoming General Meeting in November will be a very good opportunity to do so. Committee members are encouraged though to also take up other speaking opportunities to discuss the question of re-use.

In this context, members also discussed ongoing work in relation to mandatory haircuts for SFTs. Mr. Hiscock explained that while progress on this topic has been limited so far, the issue is still an unactioned recommendation from the FSB and will be picked up eventually. The work on haircuts is considered to be an important part of the overall discussion given that this would be a way to address concerns about leverage created by non-banks, not subject to the same comprehensive prudential requirements as banks, and should thus also mitigate concerns about reuse. If this was the case, members commented that the industry would be supportive of additional requirements related to haircuts in line with the FSB's recommendations. It was also mentioned though that the ECB's macroprudential policy considerations might be more problematic as they seem to go beyond the FSB's proposals for minimum haircuts by considering haircuts as a macroprudential policy tool, i.e. countercyclically to control the amount of credit in the economy.

More generally, members commented that it seems surprising that the discussion on re-use seems to be entirely focused on repo, given the importance of collateral re-use for the wider banking system beyond repo.

4) Upcoming ERCC study on the importance of repo for the real economy

Following up on discussions at the previous Committee meeting, the buy-side members in the Committee updated other members on their ongoing initiatives to raise awareness of the positive impacts and importance of repo for the real economy.

- Blackrock is working on a white paper on the importance of repo which they expect to finalise after summer. It is planned to set up at least two events in September (including in Brussels and London) to present the conclusions of the paper.
- SwissRe has reached out to the wider insurance industry through the relevant bodies, e.g. Insurance Europe, to raise awareness of the potentially significant (indirect) negative impacts on their business from a non-functioning repo market.

- PGGM (together with the Chairman) have met authorities in the Netherlands (Ministry of Finance and Central Bank) to discuss the importance of functioning repo markets for pension funds, following up on their feature article in ICMA's Quarterly Report.

The aim of the work undertaken by the buy-side will be to set the scene for the ERCC General Meeting on 14 November, which is currently being prepared. The Chairman presented the [draft agenda](#) for the event and asked Committee members for feedback. Members were generally very pleased with the ongoing preparations and the draft agenda. It was remarked that it would be important to have a tangible basis for the panel discussions, setting out concretely the key issues and questions for discussion, e.g. in the form of an academic presentation prior to the panels. Mr. Comotto explained that the idea is to have one or more discussion papers ready for the event and to use them as inspiration for the panelists. The moderators could possibly go through some of the key findings ahead of their panels to introduce the discussion. Another idea raised by the Chairman would be to ask Mahmood Pradhan from the IMF to cover some of the key points and conclusions from the paper(s) in his opening keynote speech.

Following today's discussion, the ICMA Secretariat together with the Chairman and other participants will finalise the agenda and start promoting the event. Once published, Committee members are invited to spread the word and pass on the event details to anyone they consider important to have in the room.

5) Regulation

a) **CRD IV review**

Mr. Hiscock mentioned the recent report of the US Treasury which sets out some far-reaching recommendations for financial reform in the US, including some concrete proposals (e.g. in relation to LCR and LR) that could be highly relevant for repo markets. This is seen as an important development, also in the context of ongoing discussions in relation to the finalisation of the Basel framework and concerns expressed in Europe, e.g. by both Commission and the European Parliament, that the proposed global rules risk to put European banks at a competitive disadvantage as compared to their US counterparts.

b) **CCP Recovery and Resolution**

Mr. Hiscock introduced a discussion on the latest proposal by the European Commission for more robust [supervision of CCP activities](#) in the EU, published on 13 June as part of the EMIR review. The most controversial aspect of the proposal is the question of CCP location in the context of Brexit. While the Commission proposal does not go as far as requiring forced relocation of euro clearing from London to other EU Member States post-Brexit, it does give ESMA substantial additional powers in relation to the supervision of CCPs, which include the right to impose a relocation if deemed necessary for financial stability purposes. While in the context of derivatives ISDA and other associations have been quite vocal in opposing any forced relocation ICMA has thus far focused its comments on the risks of market fragmentation and disruption post-Brexit.

Members remarked that purely from a repo perspective, a consolidation of business in a single CCP would be beneficial. Members were confident though that any desirable relocation can probably be achieved by the market without regulatory intervention. Members also discussed the sequencing implications of any relocation of activity. While from a market wide perspective a big bang migration on a specified date would clearly be preferable to a gradual shift, members also remarked that further analysis is needed as regards the impact on balance sheet netting. Some market participants currently seem to face problems in this regard and there is also some uncertainty about the potential for netting within T2S, i.e. whether this depends on the location of the underlying issuer CSD. Currently, the netting potential still seems to depend very much on the operational setup of each individual firm. It was suggested that the ERCC should approach LCH on this question, as it would be important to better understand the relevant factors and to clarify the netting potential in T2S. It might make sense to also involve the ICSDs in this discussion.

In the context of Brexit, members acknowledged that the focus of the CCP relocation discussion was primarily on derivatives, which requires a differently nuanced discussion than for repo. On the broader question of regulatory involvement in the relocation of euro clearing, members agreed that the ERCC should maintain its current stance.

The Chairman noted that the Italian market was due to move the following week to classic repo (instead of buy/sell-backs). Members commented that this change was generally welcome and indeed overdue and was not expected to cause any disruptions.

c) CSDR

Andy Hill updated members on the latest developments in relation to the CSDR settlement discipline regime and ICMA's advocacy on this issue. On 15 May, ICMA published its latest [position paper](#) related to CSDR, arguing for a suspension of mandatory buy-ins and an increase of the proposed penalty rates in return. Mandatory buy-ins have also been among the key themes discussed in the Commission's Expert Group on Corporate Bond Market Liquidity in which ICMA is represented. Given their likely detrimental impact on bond market liquidity, the suspension or removal of mandatory buy-ins should be among the key recommendations of the Group's final report. Finally, the risks from mandatory buy-ins also feature prominently in the recently published [ICMA Credit Repo Market study](#) given that they are expected to provide a major disincentive for potential lenders of securities, in particular where these are less liquid.

As regards the relevant CSDR RTS on settlement discipline, currently still under review by the Commission, there have been some indications that the Commission is planning to adopt the final standards after the summer. The regime would then be implemented two years after their publication, i.e. towards the end of 2019 or early 2020. While it is unlikely that the Commission will make any substantial changes to the mandatory buy-in requirements in the draft RTS (and whether this is even possible given that the underlying problem is in the Level 1 text), the fact that the

implementation of the regime continues to be pushed out provides some hope. Members also remarked that the Commission is clearly very keen to make CMU a success and might thus be ready to compromise on the question of mandatory buy-ins given their highly detrimental impact on capital markets which would seem to be in contradiction to the CMU objectives. Mr. Hill remarked that it was clear from the discussions at the Expert Group that the Commission's primary concern in relation to CSDR is to improve settlement efficiency in Europe, as this is seen as the key objective of the settlement discipline regime. If the industry can come up with constructive alternative solutions to reduce settlement fails this would certainly help convince the Commission to explore ways to suspend the mandatory buy-in proposals.

6) Benchmarks

The Chairman informed members about a consultation launched by the European Money Markets Institute (EMMI) on 15 June on ["A New Reference Index for the Euro Repo Market"](#). The Secretariat sent out a message to all ERCC members encouraging them to respond to the consultation. Members took note of the consultation and expressed support for the work which is hoped to provide the basis for a robust benchmark for the euro repo market.

Members also discussed the Bank of England's work on a sterling risk-free interest rate (£RFR) benchmark. On 28 April, the Bank of England [revealed](#) that the Working Group on Sterling Risk-Free Reference Rates has announced the Sterling Overnight Index Average (SONIA) as its preferred £RFR benchmark. Mr. Manna who has been a member of the relevant working group explained the reasons why the group chose SONIA over the two secured alternatives. In his view, the decision was mainly due to the perceived implementation risk of a switch to a secured benchmark. While the Group acknowledged that a secured benchmark would make sense as a concept, concerns prevailed that the switch to a secured rate would introduce a number of additional risks as compared to the reformed SONIA. These include the need to define the new benchmark, the resulting reliance on a third-party provider (other than the Bank), and the need to adopt the concept in the swaps market (which already clears on SONIA) and futures market as well as the future LIBOR transition. There was also a concern among some non-dealers that a secured (repo) benchmark might introduce excessive volatility in banks' loan books. The Bank of England will hold a workshop on this topic on 6 July to which the ERCC was asked to nominate a few representatives.

7) ERCC Operations Group update

Mr. Hamilton, Co-chair of the ERCC Operations Group, updated members on the latest ERCC Ops Group initiatives. The ERCC Ops work can be framed in four main pillars:

1. Regulation: Currently heavily focused on SFTR and led by a dedicated ERCC Ops SFTR Task Force chaired by Jonathan Lee (JP Morgan). On 31 May the group launched a [bilateral reconciliation exercise](#) for repo and buy/sell-backs encouraging all ERCC member firms to participate. The exercise aims to identify the most critical transaction types and reporting

elements and is hoped to serve as a good basis for further industry implementation work, e.g. on UTIs. The Group is also coordinating closely with other industry bodies, in particular ISLA, in order to achieve a level of consistency across SFT markets. In addition, the Task Force has been working with a consultancy on an SFTR industry readiness survey, which is hoped to provide some useful insights and should be published in due course. Mr. Hamilton encouraged all members to ensure that they are appropriately represented in the SFTR TF given the substantial focus and resources that firms will have to dedicate to this project over the next couple of years.

2. Market infrastructure: The key focus of the work on market infrastructure is the ERCC Ops' involvement in the ECB's new Advisory Group on Market Infrastructures for Securities and Collateral (AMI-SeCo). This group was created in the context of the recent reform of the ECB's advisory group structure, merging the tasks and responsibilities of the now discontinued T2S Advisory Group and the COGESI. Mr. Hamilton is representing ERCC Ops on the AMI-SeCo. The first meeting of the group was held in March, followed by a workshop on 11 May which focused specifically on several impactful ECB initiatives in relation to their collateral framework, including a project with the ICSDs to make euro-denominated Eurobonds available for settlement in T2S. The workshop itself was followed up by a short written consultation to which the ERCC Ops responded on 15 June. The ERCC Ops focus has now shifted to the preparation for the next regular AMI-SeCo meeting which is due to be held on 4-5 July.
3. FinTech: The ERCC Ops FinTech Working Group is working on a mapping of existing FinTech tools in the collateral operations space. This work is progressing well. The draft mapping now covers around 60 FinTech solutions across various categories and provides a useful overview for firms of existing technology solutions available to help firms achieve a more consistent and efficient back-office process.
4. Best Practice and education: Another important pillar of the Ops work is around best practice and education. Mr. Hamilton stressed the important positive contribution of the ERCC Repo Guide in the standardisation of the repo market and the need for firms to fully embrace the Guide, in their internal processes as well as their educational setup. A useful complement to the Guide is ICMA's educational offering which provides a range of relevant courses in the Ops space.

8) AOB and further dates:

The Chairman mentioned that the latest ERCC Repo and Collateral Management Course was held on 1-2 June, kindly hosted by UBS in London. The event was well attended and feedback has been generally very positive. We are still looking for a host for the next edition of the event, which should be held in Q1 or early Q2 2018. Any members who are interested to host the event are invited to

reach out to the Secretariat as early as possible so that we have sufficient time to promote the event.

Mr. Hiscock informed members that the next meeting of the ERCC Repo Guide Review Working Group is due to meet on 5 July, hosted by SocGen in London. Although the latest comprehensive update of the Repo Guide was published earlier this year, a number of additional issues have already been raised for consideration by the Group. As a few members recently dropped out of the Group, it would be good if we could add a few further representatives from both ERCC Committee and ERCC Ops to the Group. Mr. Hiscock asked interested members to get in touch with him.

In terms of next ERCC meetings, the following meetings have been scheduled so far:

- **12 September, 14:00 – 17:00 (UK time):** ERCC Committee meeting in London, hosted by HSBC
- **14 November, 14:00 – 17:00 (local time):** ERCC General Meeting in Brussels, hosted by Euroclear in the margins of their Collateral conference

The ERCC Chairman:

The ERCC Secretary:

Godfried De Vidts

Alexander Westphal