

Minutes of the ERCC Committee meeting held on 13 December in London Hosted by Credit Suisse

Present:	Mr. Godfried De Vidts	BrokerTec (ERCC Chairman)
	Mr. Dan Bremer	BAML
	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. Nicola Danese	JP Morgan
	Mr. Harald Baensch	UniCredit Bank
	Mr. Richard Comotto	ICMA Centre
	Mr. David Hiscock	ICMA
Mr. Alexander Westphal	ICMA (ERCC Secretary)	
On the phone:	Mr. Michael Manna	Barclays
	Ms. Emma Cooper	Blackrock
	Mr. Eugene McGrory	BNP Paribas
	Mr. Grigorios Markouizos	Citigroup (ERCC Vice Chair)
	Mr. Jean-Michel Meyer	HSBC
	Mr. Tom Wells	Morgan Stanley
	Mr. Sylvain Bojic	Société Générale
	Mr. Richard Hochreutiner	Swiss Reinsurance
	Mr. Nicholas Hamilton	JP Morgan (ERCC Ops Co-Chair)
	Mr. Adam Bate	Morgan Stanley (ERCC Ops Co-Chair)
Ms. Lisa Cleary	ICMA	
Apologies:	Mr. Paul Van De Moosdijk	PGGM
	Mr. Gareth Allen	UBS Limited
	Mr. Eduard Cia	UniCredit Bank (ERCC Vice Chair)

Welcome

The Chairman welcomed members to this seventh Committee meeting of the year and thanked Credit Suisse for hosting the meeting.

1) Minutes from previous meetings

Members approved the minutes of the last Committee meeting held on 2 November 2017 in London with one minor amendment.

2) Repo and the real economy: Follow-up from ERCC GM and update on buy-side initiatives

The Chairman briefly reported back from the recent ERCC General Meeting held on 14 November in Brussels which went very well and delivered some helpful messages related to the main theme of the meeting, the importance of repo for the real economy. This theme has also been picked up by ERCC buy-side members through different helpful contributions, including an upcoming White Paper that is being prepared by Blackrock. Once published, the ERCC will support Blackrock in spreading the key messages of the paper, e.g. by setting up roundtable events in different European centres. In this context, the Chairman noted that awareness among policy makers regarding repo seems to have grown already, including in the European Parliament where it is increasingly acknowledged that there is a need for the regulatory framework to take better account of the specifics of repo. On a related note, Mr. Hiscock mentioned that ICMA's upcoming Quarterly Report (to be published on 10 January 2018) will include two pieces that are highly relevant for these discussions, an article on "The importance of SFTs to insurance companies" contributed by Mr. Hochreutiner and a personal view by ERCC Chairman Godfried De Vidts, calling for further supportive action by regulators particularly in the post-trade space.

3) Balance sheet netting in T2S

As agreed at the previous Committee meeting, a letter was sent to the ECB on 16 November to request clarification in relation to balance sheet netting opportunities in T2S. The ECB confirmed that they are looking at the issue, but no formal response has been received yet.

4) Daily settlement of term trades for repo markets

Mr. Hiscock introduced a discussion on potential benefits linked to the daily settlement of term repo trades. In mid-August, US regulators published some guidance in relation to cleared derivatives trades which essentially confirmed that firms that choose to settle on a daily basis open derivatives positions instead of exchanging variation margin will be subject to a more favourable treatment in terms of capital requirements. As reported subsequently in the press, this seems to have had a major positive impact in terms of balance sheet for a number of banks. The issue had already been briefly mentioned at the September Committee meeting, however, without further consideration of the implications for repo. Members commented that this initiative seems to be less relevant for repo for several reasons. Most importantly, potential future exposures in the context of repos are significantly lower than for derivatives given their much shorter duration; and hence the potential benefits in terms of the relevant LR-add-on are more limited. Furthermore, the daily settlement of open repo trades would be very difficult to achieve operationally. It was also mentioned that firms already have the possibility to reprice repos where the exposure becomes excessive. Members also briefly commented on a similar initiative by LCH a few years back called "repo bundles", which aimed to unbundle term trades into a stream of one-day repos. While this initiative also had other merits beyond capital treatment, members didn't feel that the fundamental assessment at the time has

changed and that there is likely no desire from market participants but importantly also not from regulators to revive this initiative.

5) Legal update

Ms. Cleary updated members on recent legal developments.

As regards the proposed **discontinuation of GMRA 1995 coverage** in the annual updates of the ICMA GMRA legal opinions from 2019, Ms. Cleary noted that no further written objections have been received and asked members to approve the proposal. Committee members unanimously agreed with the proposal. Ms. Cleary will thus prepare a formal notification of the change which will be circulated widely among ERCC members and which will also be published on the ICMA website. The change will be formally announced at the next ERCC AGM.

As requested by the ICMA Board in its discussion on the **Repo Pledge initiative** in September, ICMA has continued negotiations with the relevant law firm and agreed a fee cap for the work to be undertaken. The actual work on the documents will start in late January/ early February. A small focused working group will be established under the ERCC Legal Working Group to support the work.

ICMA recently received some indications of interest from the market to extend the **coverage of GMRA legal opinions** to Kuwait and Saudi Arabia. A previous legal opinion for Kuwait has been on hold for a while due to a pending court case. In the case of Saudi Arabia, a previous legal opinion from 2010 was of exploratory nature only as Saudi Arabia was not considered to be a legally robust jurisdiction for netting purposes. It was indicated that this might have changed since then. Members expressed interest in a renewed legal opinion for Saudi Arabia. Ms. Cleary will follow up with ICMA's local counsel and will update members accordingly.

Following up on a request from the ICMA management to consider potential legal implications from **Distributed Ledger Technology (DLT)**, Ms. Cleary encouraged members with a specific interest or knowledge on this topic to reach out to her. Members supported the idea to look into this topic and mentioned a number of relevant initiatives that are under way in this area.

6) MiFID II/R implementation – impacts on repo

Ahead of the January 2018 implementation date, members exchanged views on the state of preparations and any outstanding issues in relation to repo. Mr. Hiscock recapped the main relevant MiFID II/R provisions and how they apply to repo, including best execution, order record-keeping and costs and charges provisions (see [ICMA FAQs on MiFID II/R and SFTs](#)). Members discussed some of the practical challenges in complying with the order record-keeping requirements, commenting that this will likely require firms to use a centralised workflow tool to capture all orders coming in from different sources that are not yet electronically captured. Members commented that this will

make the front office task more work intensive as it requires traders to manually input the orders into such tool.

7) Regulation

Mr. Hiscock provided updates on other recent regulatory developments, including:

a) CCP Recovery and Resolution/ location policy

The legislative debate on the proposed EU Regulation on CCP Recovery and Resolution continues. From an ERCC perspective, the main concern with the proposal continues to be around the potential haircutting of variation margin a concern that is also being shared by ISDA. Mr. Hiscock noted that the discussion on this particular issue seems to be moving in the right direction as co-legislators have acknowledged the related problems. Another point that was recently flagged to us by ISDA is a proposal to allow initial margin to be used temporarily in a resolution scenario to meet liquidity needs. While this seems to be less concerning from a derivatives perspective, in a repo context this seems to be a very problematic proposal. Mr. Hiscock encouraged members to further assess the issue, provide feedback and also more broadly to reach out to the relevant colleagues internally who are active within the relevant ISDA working groups to coordinate views on this file.

In the context of proposals on CCP location policy put forward as part of the EMIR review, members noted that the expected move of the repo market from LCH Ltd to LCH SA has not yet happened at a significant scale. The main barrier currently seems to be linked to the remaining uncertainty around balance sheet netting opportunities (see item 3).

b) BRRD - Proposed revision of moratorium powers

In relation to the ongoing BRRD review, Mr. Hiscock recalled that the ERCC had sent a letter to policy makers in July 2017 to raise concerns with the proposed new moratorium powers. A follow-up call with the European Commission was held in September to discuss more in detail. Other trade associations have also picked up these concerns in their own advocacy efforts. Ms. Cleary added that these efforts on the side of industry have also been supported by several Member States who have raised similar concerns in the context of the ongoing legislative discussions. While a few relevant improvements to the text have already been made, especially in relation to the timeline of the proposed moratorium powers, the main issue remains unresolved and ICMA is currently coordinating with other associations to decide on next steps.

c) CRD IV review, including large exposures and NSFR

Mr. Hiscock updated members on the latest developments in relation to the different proposals that are being discussed in the context of the ongoing CRD IV review.

Regarding proposals in relation to large exposures, he noted that the particular requirement that had been discussed at the previous Committee meeting seems to have been addressed now.

In relation to NSFR, Mr. Hiscock recalled that the Commission proposals already helpfully diverge from the Basel agreements in that they reduce the asymmetry in the treatment of repo. The proposals are now being discussed and amended by both European Parliament and Council as part of the regular legislative process. In the Parliament, on 22 November the relevant rapporteur for the file published his draft report with proposed amendments to the Commission text. Importantly, this includes an amendment which appears to allow for a much broader netting set for repo trades as it defines the relevant settlement date as the only condition for netting. While this would seem to be a very helpful development, Mr. Hiscock also cautioned that the draft report is only the first step in a longer legislative process which also involves the Council. In terms of implementation timeline, Mr. Hiscock explained that once both institutions have agreed their respective positions they will start discussions on a final compromise text which could be adopted by end 2018 or early 2019. This would then probably be followed by a two-year transition period before the requirements apply (i.e. probably 2021). While there is still some time to go, the discussions in the next weeks will be crucial and any important points would need to be raised at this stage. The ERCC will thus continue to monitor closely any developments. At the same time, we are coordinating closely with other associations, in particular AFME, who have also been looking at the treatment of repo under NSFR in context of its overall work on this file under its prudential regulation division and created a dedicated working group to focus on this particular issue. While Mr. Hiscock himself has been part of these discussions, he also encouraged members to reach out internally to the relevant colleagues involved in the AFME work to make sure that views across the different constituencies are fully aligned.

Mr. Hiscock reported that the BCBS endorsed on 7 December a set of outstanding Basel III post-crisis regulatory reforms, including, among other measures, the final Leverage Ratio (LR) framework. The latter incorporates recent Q&As on LR issued by the BCBS but does not otherwise include any major changes as compared to the previous LR framework published in 2014. The BCBS also recognises the need for a continued close monitoring of any developments in relation to SFTs, thus following the conclusions reached by the April 2017 CGFS report on repo market functioning. In this context, Mr. Hiscock also noted the publication on 7 December of a BCBS discussion paper on the regulatory treatment of sovereign risk exposures. Members agreed that there is no need for the ERCC to submit a response to this consultation but that we should coordinate with other associations that are likely to respond, including AFME.

The Chairman reported that the EU Council recently adopted its position on EMIR REFIT. Importantly, the final Council text includes a recognition of certain post-trade risk reduction services, which could help reduce global collateral demands and increase collateral fluidity.

8) Benchmark reform

(i) Switzerland: Mr. Ernst Lienhard, SwissRe and member of the [National working group on Swiss franc reference rates](#), dialled in to give an update on the ongoing benchmark reform process in Switzerland. The Swiss reference rates working group, which includes the SNB as well as the main private sector firms, has worked since spring 2016 to manage the transition from the unsecured TOIS rate to SARON, a secured benchmark. The latter has been in existence in Switzerland since 2009 already thanks to the centralised and electronic nature of the Swiss Repo market which is concentrated on the SIX platform. Ahead of the transition to SARON, legacy positions in interest rate swaps that directly referenced TOIS were identified as the biggest issue. However, in the specific Swiss case both number and notional of the impacted contracts were relatively limited which was a major facilitating factor. In addition, the initial impact analysis showed that most banks with outstanding positions referenced to TOIS had hedged these positions with positions that were equally referenced directly to TOIS. As a result, although both rates differed, the transition to SARON hardly had any impact on the NPVs of the impacted positions, which allowed them to go for a transition without any compensatory payments. As the approach was largely consensual, potential litigation was moreover not a major concern, also facilitated by the limited number of involved parties. Following the successful transition from TOIS, the focus of the WG has now shifted to issues linked to the transition from LIBOR.

(ii) United Kingdom: With regards to the UK, Mr. Hiscock updated members on the recent developments following on from the authorities' announcement in November that they will not continue to oblige panel banks to make LIBOR submissions after 2021. As discussed previously, in April 2017 SONIA had been chosen as the new (unsecured) near risk-free rate by the relevant UK working group on sterling risk-free rates. While the discussions so far have focused heavily on derivatives, on 29 November 2017 the Bank of England [announced](#) the launch of the next phase of sterling LIBOR transition work which will include establishing two new sub-groups to focus on loan and cash bond markets. The cash bond sub-group will be chaired by Mr. Paul Richards, ICMA's Head of Market Practice and Regulatory Policy.

(iii) Euro Area: The Chairman introduced a discussion on the latest developments related to euro area benchmarks. Mr. Evenepoel reported back from the latest meeting of the ECB's Money Markets Contact Group (MMCG) where benchmark reform was discussed at some length. There was broad support in the group for the ECB's initiative announced in September 2017 to develop a new overnight unsecured rate based on MMSR data. A first public consultation on the new unsecured rate was published on 28 November (deadline for responses: 12 January 2018). However, MMCG members also called on the ECB to develop a clear roadmap for the transition to the new rate. In this context, the Chairman noted the recent [call for expressions of interest](#) to join a new working group on Euro Risk-Free Rates published jointly by the ECB, ESMA, European Commission and FSMA on 29 November 2017 (deadline to apply: 12 January 2018). Mr. Hiscock said that ICMA is planning to apply as an observer, alongside ISDA and EMMI who have already been awarded this status. Overall the expectation is that the group should be principally composed of panel banks.

As regards the question of secured versus unsecured reference rates more generally, members felt that discussions in Europe are likely to follow the UK precedent, recommending an unsecured rate as near risk-free rate. There seems to be an inherent bias in favour of unsecured rates, despite the robustness of repo-based rates which can rely on far greater trading volumes. This seems to be partly rooted in a broader resistance to change by the key stakeholders, as many of the arguments put forward against secured rates often apply in a similar way to the unsecured alternatives, e.g. the need to construct term rates from actual O/N volumes. Members remarked that some momentum for repo-based secured rates might come from the US, where a new secured index is being developed and has been chosen as the USD risk-free rate. However, members also cautioned that in Europe the US is often not considered as a viable reference model given the more homogenous market structure (in terms of collateral as well as market infrastructure). Another key difference is the active involvement in the US by the Fed which is actively pushing towards a secured rate, while the ECB in Europe has been largely passive. In conclusion, members reiterated the ERCC's support for the work undertaken by EMMI to develop a robust secured benchmark in Europe. It was also remarked that there is no reason in principal why both a secured and an unsecured risk-free rate could not usefully co-exist in the market. As regards the ongoing ECB consultation on developing a euro unsecured overnight interest rate mentioned above, members agreed that there is no need for the ERCC to submit a response.

9) ERCC Operations Group update

Mr. Nicholas Hamilton, Co-chair of the ERCC Operations Group updated members on the latest ERCC Ops Group initiatives, focusing on the work that is being undertaken in the context of the ECB's AMI-SeCo and its sub-groups. The AMI-SeCo last met on 6-7 December in Frankfurt. Mr. Hamilton attended the meeting as ERCC Ops Co-Chair. One important initiative under way in this context is related to the ECB's request to the ICSDs to develop a solution to make euro-denominated Eurobonds available for settlement in T2S. The ICSDs have been working jointly on the technical proposal which they presented at the latest AMI-SeCo meeting. The solution would centre around Euroclear France and CBF, the German CSD, as technical issuer CSDs for Eurobonds which would thus serve as hubs to access these instruments in T2S. One of the challenges is that this solution will require a high level of interconnectivity with the other domestic CSDs in T2S to allow for cross-CSD settlement. These discussions are ongoing. Mr. Hamilton encouraged members to carefully review the ICSD proposal and to discuss with relevant colleagues internally. He would be keen to relay any feedback from members to the AMI-SeCo. Members briefly discussed the benefits and risks of the initiative and some broader issues related to T2S, expressing some frustration that the common platform has not yet delivered the expected efficiencies which would ultimately allow firms to consolidate all their collateral in one place within T2S, i.e. allowing for settlement in central bank money. Members agreed that the ICSDs should be invited to the next meeting of the Committee to allow for a more in-depth discussion.

A second important ongoing work stream under the AMI-SeCo umbrella is the development of the Eurosystem Collateral Management System (ECMS) which is due to replace the fragmented national

framework for collateral management for Eurosystem credit operations under the current CCBM system. This work is supported by an extensive agenda to harmonise collateral management frameworks and market practices. The ERCC Ops is actively involved in this work through several of its members, also closely collaborating with ISLA. One of the key objectives of the work is to establish an efficient tri-party collateral product in T2S, but it is also expected to achieve a more consistent collateral product definition more broadly with a particular focus on collateral messaging. Mr. Biewald asked whether this work also aims to address issues around intraday liquidity management which had been discussed previously in an ERCC context and which were also highlighted in the recent EPTF report. As this has not yet been covered explicitly, he and a few other members reiterated the importance of this issue and suggested that this should be raised with AMI-SeCo. The ERCC Ops will pick up the issue and suggest appropriate follow-up actions.

10) AOB and further dates:

Meetings:

- **21 February 2018, 13:00 – 16:00 (UK time):** First meeting of the new ERCC Committee, hosted by ICMA in London
- **14 March 2018, 12:00 – 18:30 (UK time):** ERCC Annual General Meeting, hosted by BNY Mellon in London

ERCC elections 2018 – timeline:

- **14 December 2017:** Call for nominations for candidates to the ERCC elections 2018
- **11 January 2018:** Deadline for member firms to put forward their candidate for the elections
- **26 January – 9 February 2018:** Electronic voting open (2 weeks)
- **12 February 2018:** Announcement of results (and opening of second ballot, if necessary)