International
Capital
Market
Association

Minutes of the ERCC Committee meeting held on 7 May in Frankfurt
Hosted by Commerzbank

Present:	Mr. Grigorios Markouizos	Citi (ERCC Vice Chair)
	Mr. Charlie Badran	AXA IM
	Mr. Dan Bremer	BAML
	Mr. Nick Dent	Barclays
	Mr. Jean-Robert Wilkin	Clearstream
	Mr. Andreas Biewald	Commerzbank
	Mr. Romain Dumas	Credit Suisse
	Mr. David Joughin	Deutsche Bank
	Mr. Nicola Danese	J.P. Morgan
	Mr. Antony Baldwin	LCH Limited
	Mr. Paul Van De Moosdijk	PGGM
	Mr. Sylvain Bojic	Société Générale
	Mr. Gareth Allen	UBS Limited
	Mr. Harald Bänsch	UniCredit Bank
	Mr. Nicholas Hamilton	J.P. Morgan (ERCC Ops Chair)
	Mr. Godfried De Vidts	ICMA (ERCC Senior Advisor)
	Mr. Andy Hill	ICMA
	Mr. Alexander Westphal	ICMA (ERCC Secretary)
On the phone:	Mr. Richard Hochreutiner	Swiss Reinsurance (ERCC Vice Chair)
	Ms. Emma Cooper	Blackrock
	Mr. Eugene McGrory	BNP Paribas
	Ms. Lisa Cleary	ICMA
Apology:	Mr. Michel Semaan	Crédit Agricole (ERCC Chair)
	Mr. Jean-Michel Meyer	HSBC

Welcome

On behalf of the ERCC Chair, Godfried De Vidts (ICMA) welcomed members and thanked Commerzbank for hosting this second meeting of the new Committee.

1) Minutes from previous meetings

Members approved the minutes of the previous ERCC Committee meeting, held on 13 March 2019 in London without further comments.

2) Preparatory discussion for the meetings with the ECB

An important objective of the meeting was for ERCC Committee members to prepare their subsequent visit to the ECB, consisting of two separate 1-hour meetings: first a session with senior officials from DG Market Infrastructure, followed by a meeting with DG Market Operations. On 29 April, members had held a first preparatory discussion to agree a tentative agenda for both these meetings.

a) **Meeting with ECB's DG Market Infrastructure and Payments**

Members recapped the proposed agenda for the meeting with Marc Bayle and colleagues from the Directorate General (DG) Market Infrastructure.

(i) Progress with T2S: Nicholas Hamilton, ERCC Ops Chair and ERCC representative in AMI-SeCo, introduced the discussion. He suggested that a key focus of the meeting with the ECB should be the lack of progress in relation to T2S and factors that still prevent banks from making significant operational adjustments to take full advantage of the new harmonised settlement platform. Members discussed the various obstacles that are relevant in this context. While T2S has clearly been a success from a technical perspective, it is clear that a broader adoption is still hampered by different external factors. A full investor CSD model in T2S, which has been at the core of the project, is still not available to firms, as CSDs are still putting in place the required functionalities and connections. In this context, members pointed particularly to the lack of progress in certain markets, including Italy and Spain, which are both expected to become fully accessible for investor CSDs in 2020 at the earliest. While this was considered an important constraint, members also agreed that firm-specific factors will matter and strategies differ across firms. Instead of choosing an investor CSD model, some firms may find it more attractive to consolidate only their cash side into a single DCA and to keep several CSD accounts, which should allow for balance sheet netting. A third model could be for firms to consolidate their settlement activity in a first step in one of the ICSDs (which allows for netting) before a full transition to T2S becomes achievable and attractive.

Apart from the CSD infrastructure and connectivity, members also highlighted a number of other important factors that are constraining the success of T2S. One obstacle remains balance sheet netting in T2S, as a positive conclusion on this question is still pending. Finally, there is a range of other important factors at play which would require a political solution. This includes constraints due to tax issues or other national barriers that still restrict a more integrated post-trade environment in Europe, despite having been well known and on the agenda of policy makers for many years. In terms of priorities for the ECB, members remarked that on most of the factors listed the ECB itself only has limited direct influence. However, they would still be a powerful ally particularly as regards barriers that need to be addressed by policymakers given the ECB's clout with the relevant (mostly national) stakeholders.

(ii) Intraday liquidity, shaping and partialling: Members followed up on previous discussions in the ERCC Committee and ERCC Ops on intraday liquidity management and specifically shaping and partialling, and discussed which points should be raised with the ECB. Mr. Hamilton updated members on the outcome of the latest ERCC Ops check point on the topic which was held on 15 April. One of the follow-up actions is to gather relevant data to better understand the extent to which shaping is already applied in the markets today. It is hoped that the ICSDs can provide some relevant data points to help with this assessment. Members remarked that only (auto-)partialling is in the direct control of the ECB, given that this is a (currently optional) functionality in T2S. In order to promote a broad use of shaping, on the other hand, market consensus would be required.

Members recapped the benefits and costs of both tools. In particular, there was a discussion on the need for shaping in an environment where auto-partialling is working efficiently. Some members were of the view that the costs for implementing shaping across the market might be quite substantial and also pointed to the likely opposition to a broader introduction of shaping by certain market participants, including the prime brokerage/ hedge fund community. Other members insisted on the positive complementary benefits of shaping, in particular in relation to intraday liquidity management, which cannot be achieved through partialling. Overall, it was agreed that the Committee should remain broadly supportive of both tools, but also take into account the related costs and client challenges. While further analysis and cross-industry consultation will be needed to better understand the latter, the Committee should continue to actively drive this discussion.

b) Meeting with ECB's DG Market Operations

Members briefly recapped the proposed agenda for the meeting with Ulrich Bindseil and colleagues from the DG Market Operations. This meeting was focused on the general repo market conditions, starting off from the recent findings of the European Repo Survey and complementary views from members. In addition, Committee members also agreed that some of the important issues recently discussed with the BCBS, should also be raised with the ECB, including the concerns in relation to the proposals on minimum haircut floors (see item 5a).

3) Technology

Andy Hill updated members on the latest developments in relation to ISDA's Common Domain Model (CDM) project and the initiative to extend this to other asset classes, in particular SFTs. An ICMA draft note was circulated to members ahead of the meeting which tries to explain the fundamentals of the CDM and the implications for repo. Mr. Hill noted that ICMA staff level discussions with ISDA and REGnosys are progressing well and that some basic aspects of Repo are already being incorporated into the CDM as a test case. He commented that ICMA remains very supportive of the initiative. There is a view that the extension to other asset classes is a natural development which will very likely happen with or without ICMA involvement. It is therefore considered important for the ERCC to stay closely involved in order to make sure that this is done properly. In terms of next steps, ICMA will continue discussions with ISDA and has also invited ISDA to present to the Committee directly at one of the next meetings. Separately, members are strongly encouraged to connect with their peers on the derivatives side who are already involved in the ISDA project. Members reiterated their broadly supportive stance on the initiative and suggested to also involve technology experts in the discussion. ICMA will aim to set up a small subgroup of interested member firms to drive forward the discussion, involving traders, Ops and technology experts.

Mr. Hill informed members of the upcoming *ICMA FinTech Forum: How is technology shaping international fixed income markets?*, which will be held on 25 June in London hosted by UBS.

4) Legal updates

Item postponed. A written update with the latest legal developments will be circulated after the meeting.

5) Regulation

a) Minimum haircut floors

On 5 April 2019, a GFMA/ICMA delegation went to Basel to meet representatives of the FSB/BCBS and BIS (CGFS) and discuss the December 2018 GFMA/ICMA Repo Study and the follow-up QIS work related to minimum haircuts. Gareth Allen (UBS) reported back from the meeting. Key topics discussed included balance sheet averaging, as proposed by the FSB, which participants generally supported as it is hoped to ease volatility around reporting dates, although further analysis of the potential impacts on overall intermediation capacity was encouraged. Other important topics included the restrictions in relation to balance sheet netting in T2S, as well as the important role of broker/dealers as shock absorbers in a stressed market and the fact that they are increasingly unable to play this role, especially around reporting dates, due to leverage constraints. Participants also discussed at some length the FSB proposals in relation to minimum haircut floors. The proposed rules are a major concern, particularly for securities lending which is generally not done for the purpose of leverage (most lenders do not need leverage), but to earn incremental income from securities holdings. The delegation reiterated the need to refine the FSB guidance to provide an adequate carve-out for securities borrowing transactions, in particular where the transaction is collateralised with securities rather than cash. In this context, the delegation also briefly raised the scenario of lending under ISLA's new collateral pledge structures, where the collateral cannot be re-used (and so cannot be used to generate leverage). The FSB/BCBS were interested to learn more. Members agreed that these issues should be raised in the subsequent ECB meeting with the DG Markets Operations team.

b) CSDR

Andy Hill (ICMA) briefly updated members on recent discussions in relation to the upcoming implementation of CSDR mandatory buy-ins, covering two relevant points. On 29 March, ICMA submitted a proposal to ESMA to ensure that GMRA contractual means can be used as a way to avoid CSDR mandatory buy-ins to be applied to repo. A response from ESMA on this question is still pending. A second question that has been discussed with ESMA is ICMA's proposal to exclude open repos from the scope of mandatory buy-ins. In response, ESMA has raised some concerns regarding the role of the CSD and how they would be able to monitor the process. Having subsequently discussed with CSDs, they have pointed out that their role under the CSDR does not include any policing powers in relation to buy-ins. The issue will be discussed again with ESMA.

c) SFTR

Alex Westphal (ICMA) provided a brief update on the latest discussions on SFTR and the work of the ERCC SFTR Task Force. In terms of process, the main news since the previous Committee meeting has been the publication of the final Regulatory and Implementing Technical Standards (RTS and ITS) in the EU's Official Journal on 22 March and their subsequent entry into force on 11 April. The publication of the technical standards finally provides certainty in relation to the implementation timeline of the reporting requirements. The relevant reporting go-live dates will be as follows (or next business day where the legal go-live date is on a weekend):

- 11 April 2020: banks and other investment firms
- 11 July 2020: CCPs and CSDs
- 11 October 2020: Most buy-side firms
- 11 January 2021: Non-financial counterparties

In terms of next steps, the industry is now waiting for ESMA to kick off the so-called Level 3 process, during which they will provide additional implementation guidance beyond the technical standards. Most imminently, ESMA is expected to publish some detailed draft Reporting Guidelines which should be issued by end of May for public consultation. The draft Guidelines are hoped to clarify a number of the outstanding questions and issues that have already been raised with ESMA over the past months.

In parallel, the discussions within the ERCC SFTR Task Force have continued and the work on the various best practice documents is making good progress. In particular, the SFTR Annex to the Repo Guide to Best Practice continues to grow, already covering around 60 different implementation issues. In addition to the Annex, the group is also working on a list of sample reports (covering close to 30 repo scenarios) and has more recently focused on the reporting of repo lifecycle events. Over the past weeks, ICMA has also stepped up efforts to publicise the extensive work of the Task Force, including through a revamped SFTR webpage, as well as regular SFTR Task Force updates that are being sent to the wider membership.

d) <u>EMIR Refit</u>

Following up from the discussion at the previous meeting, members were invited to provide updates in relation to the discussions on EMIR Refit. No significant new developments were reported. The ICMA ERCC and the relevant member firms will continue to closely follow the discussion and contribute where needed.

e) <u>Benchmark reform</u>

Members discussed recent developments in relation to benchmark reform, focusing specifically on the upcoming transition from EONIA to €STR. Eugene McGrory (BNPP) introduced the topic, suggesting that this transition seems to present a good opportunity for the French market to move away from floating-rates to a fixed-rate repo market. He argued that the current reliance on floating-rate repo in France is out of line with other markets and seems to be largely the result of legacy. Members discussed the proposal. While generally in agreement that a move away from floating-rate repo would make sense and avoid the related practical problems, other members also voiced concerns that some French institutional investors could be opposed to such a step and felt that the ERCC Committee should not take an unnecessarily strong view on a question that concerns investment strategies of institutional clients.

Members moved on to discuss more concretely the practical challenges with the transition from EONIA to €STR. Given that €STR, unlike EONIA, will be published on T+1 only (publication at 9am, with amendments possible until 11am), this creates some practical challenges for the settlement of repo end legs. Four different options have been put forward:

1) Apply the historic (T-1) €STR rate published on the current business day, plus subsequent settlement of any difference (as a 'delta payment') on the day following end-leg settlement.
2) Delaying the instruction of the end-leg until the publication of €STR.
3) Settling the trade (DVP) against the (known) principal value only, then settling the repo interest (FOP) later that day.
4) Crystalize the interest based on the historic rate (T-1), with no adjustment.

Members discussed the proposal to delay settlement (option 2), cautioning that this would lead to a shift of settlement activity from the night-time batch cycle into day-time RTGS settlement which is not desirable from an operational perspective and very costly in terms of intraday liquidity. It is also unlikely to be welcomed by authorities, including the ECB, which is keen to promote settlement efficiency and over-night settlement. The alternative approaches were considered preferable, even if members also commented that neither of them was ideal and free of operational complexities. Irrespective of the approach chosen, members stressed that it will be important to agree a common approach across markets. In particular, ICMA should approach ISDA on this question to find out which approach they are advocating in relation to interest rate swaps and to try and ensure alignment.

f) Other regulatory updates

In terms of other regulatory developments, Andy Hill (ICMA) informed members of a recent EBA consultation published on 2 May on draft technical standards on the standardised approach for counterparty credit risk under the CRR. The ERCC is currently not planning to respond to the consultation (deadline for responses is 2 August).

6) AOB

Andy Hill informed members that ICMA is currently working on the 3rd Study into the State and Evolution of the Corporate Bond Market. In this context, he will be conducting interviews and would be keen to get input from credit repo traders.

The ERCC Committee, including the two members of the IRCC Committee, approved applications received from Wells Fargo Bank and Union Investment Privatfonds GmbH to become ERCC member, taking the total number of members to 102.

7) Further dates:

- **18 June, 12:00 – 15:00 CET:** ERCC Committee meeting in Madrid, in the margins of ISLA's Annual conference
- **15 November, 13:00 – 16:00 CET:** ERCC General Meeting in Brussels, hosted by Euroclear (as part of their Collateral Conference)