International
Capital
Market
Association

Minutes of the ERCC Committee meeting held on 14 November in Brussels
Hosted by Euroclear

Present:	Mr. Michel Semaan	Crédit Agricole (ERCC Chair)
	Mr. Grigorios Markouizos	Citi (ERCC Vice Chair)
	Mr. Richard Hochreutiner	Swiss Reinsurance (ERCC Vice Chair)
	Mr. Charlie Badran	AXA IM
	Mr. Dan Bremer	BAML
	Mr. Nick Dent	Barclays
	Ms. Emma Cooper	Blackrock
	Mr. Jean-Robert Wilkin	Clearstream
	Mr. Peter Schmidt	Commerzbank
	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. Nicholas Hamilton	J.P. Morgan (ERCC Ops Chair)
	Mr. Godfried De Vidts	ICMA ERCC Special Advisor
	Ms. Lisa Cleary	ICMA
	Mr. Richard Comotto	ICMA Centre
	Mr. Andy Hill	ICMA
	Mr. Alexander Westphal	ICMA (ERCC Secretary)
Guest:	Mr. Hervé Foyan Djoudom	Euroclear
On the phone:	Mr. Eugene McGrory	BNP Paribas
	Mr. Romain Dumas	Credit Suisse
	Mr. Jean-Michel Meyer	HSBC
	Mr. Gareth Allen	UBS Limited
	Mr. Harald Bänsch	UniCredit Bank
Guest (phone):	Mr. Frank Odendall	Eurex Clearing
Apology:	Mr. Andreas Biewald	Commerzbank

<u>Welcome</u>

Meeting host Hervé Foyan Djoudom (Euroclear) opened the session welcoming Committee members to Euroclear's offices and inviting everyone to join Euroclear's Collateral Conference directly following the meeting. Michel Semaan, ERCC Chairman, thanked Euroclear for the hospitality and added some introductory remarks. In particular, Mr. Semaan informed members that he will be leaving Credit Agricole in a few months and will therefore step down as ERCC Chairman and also as a member of the ICMA Board. He thanked all Committee members for the valuable discussions over the past years and the overall very positive experience.

Mr. Semaan then handed over to Godfried De Vidts (ICMA) to introduce the agenda.

1) Minutes from previous meetings

Members approved the minutes of the last ERCC Committee meeting held on 25 September in London without further comments.

2) Repo Market conditions

Godfried De Vidts invited members to share their views on current repo market conditions, noting the current focus on repo in the media and the official sector following the stress in the US repo market observed in September. In this context, many of the old misconceptions about repo seem to resurface. Greg Markouizos agreed that the current level of attention paid to repo, including from senior management within the banks, is very high. The market itself remains calm but with a noticeable degree of nervousness in light of the September volatility in the US and the upcoming year-end. While current pricing points to a relatively quiet turn of the year, some risks remain, in particular related to banks managing their year-end G-SIB ratios. Members briefly discussed the underlying causes for the recent events in the US. Mr. Markouizos pointed to fundamental changes in the US market structure as one of the key contributing factors to the recent volatility. Most of the volatility seems to have been focused on the cleared repo market, which has been expanding in recent years, while bilateral relationships remained relatively stable. One likely reason is that these lines are easier for banks to scale down in stressed market conditions. In conjunction with the persisting regulatory pressures on banks, this would indicate that recent events were probably not isolated but have to be seen as the new normal, with similar pockets of instability becoming more frequent and pronounced. On the upside, members noted that the recent focus on repo means that regulators seem more alert to the underlying factors and the health of the repo market more generally.

Looking at the euro market, Mr. De Vidts noted the current focus on the role of the ECB. For one, this is due to the ECB's decision to introduce a tiered model of compensating bank reserves which has continued to stir discussion, but also to a number of important personnel changes in the senior management at the ECB, including of course the presidency but also the reshuffle at the director level.

Frank Odendall joined the meeting by phone to provide a brief update on recent developments at Eurex Clearing:

- In October, Eurex Clearing changed its approach to haircuts, switching from ECB haircuts to the use of their own haircuts, which continue to be applied on an individual ISIN basis.
- A new GC Pooling basket was introduced in August
- An updated SFTR solution will be available as of November and ready for testing by clients

- Their repo partnership programme has had a good uptake so far and has led to a significant increase in their repo volumes
- In terms of Brexit preparations, they are facilitating EU members to make any necessary adjustments to their technical setup and also coordinate with UK authorities to make sure that they can continue to offer services to UK-based clients
- Buy-side offering continues to expand with a small number of real-money investors already live
- The ECB's tiering decision has had a major impact and has led to a dramatic increase in GC volumes and related spreads (extended basket vs ECB basket)

On a related topic, Mr. Wilkin informed members of a new initiative launched by Deutsche Boerse to allow balance sheet netting across GC Pooling activity and ICSD settlement, using the ICSD account as single cash account (in commercial bank money). The solution is currently being tested with a few pilot clients but will be extended soon to all interested clients.

3) Legal updates

Lisa Cleary updated members on the latest legal developments discussed by the ERCC's Legal Working Group. Ms. Cleary highlighted a recent letter sent by the ECB (Single Supervisory Mechanism) to all directly supervised institutions which introduces a new notification requirement regarding the recognition of netting agreements as risk reducing, to come into effect in early November 2019. ICMA and other relevant industry associations jointly replied to the ECB asking for clarification on scope and application issues and requesting a longer period before implementation. In response, the ECB agreed to delay the application to January 2020 and is working in the interim on a Q&A document to provide further guidance.

As the substantive work on the Repo Pledge project is about to kick off, Ms. Cleary asked members to confirm whether the previously agreed approach still reflects market needs. The plan so far has been to focus initially on the development of pledge documentation only for initial margin and to decide subsequently if there is also a need for a security interest agreement. Based on the latest market developments, members expressed a preference to reverse the approach, i.e. to prioritise the security interest agreement, given that this would seem to provide more immediate benefits to the industry. Members also briefly discussed whether there was still a need to develop IM pledge documentation at all (i.e. in a second step), considering the likely operational challenges with such a product. This question will be further explored.

As regards the GMRA opinions, Ms. Cleary informed members that the schedule for the 2020 updates will return to normal for all jurisdictions (i.e. publication scheduled for April). The pending 2019 opinion updates for EU jurisdictions, which were delayed due to Brexit, have now all been published, except for the UK, which is due to be released shortly.

ICMA received a few requests regarding dedicated opinions for International Financial Institutions (IFIs), following the decision by ISDA to publish IFI opinions. Members are asked to enquire internally if there is a need for such opinions in the repo space and to feed back to ICMA.

4) Basel III implementation

On 11 October the European Commission released a public consultation on the implementation of the finalised Basel III standards in the EU. Andy Hill briefed members on the content of the consultation paper and asked for initial feedback. The consultation includes a section specifically on SFTs, covering minimum haircut floors and the calculation of counterparty credit risk exposures stemming from SFTs. Mr. Hill noted that the joint ICMA-GFMA Repo Market Study published in December 2018 contains a number of important messages which could be reiterated as part of the ERCC's consultation response. He also reminded members that the EBA already published in July 2019 some helpful advice on the Basel III implementation in relation to SFTs, recommending among other things to delay the implementation of the numerical haircut floor framework until further quantitative information is available post-SFTR. Members briefly reviewed the SFT-specific questions of the Commission questionnaire and agreed that the ERCC should respond to the consultation. The deadline for responses is 3 January 2020.

Andy Hill also reported back briefly from a related public conference organised by the Commission on 12 November in Brussels to discuss the potential implications from Basel III implementation in Europe. He noted that the key take-away from the conference was that in the EU, in contrast to other major jurisdictions, there seems to be very little appetite to diverge from the global framework.

5) EMIR and pension funds

In the context of the ongoing discussion in relation to the exemption for pension funds from the EMIR clearing obligation, the Commission has set up a High-Level Expert Group which meets twice a year to assess the issue and discuss potential solutions. Andy Hill and Godfried De Vidts were invited to the latest meeting of the expert group on 30 October to give a presentation on repo market conditions and vulnerabilities, as it has been argued that the repo market does not provide a sufficiently reliable access to liquidity for pension funds in a stressed market where they could be required to meet very significant margin calls. A recent ECB study has tried to quantify the potential scale of the issue and found that a 100bp shift in Euribor is expected to lead to (variation) margin calls on European pension funds in the region of €250 billion. From a pension fund perspective, Paul van de Moosdijk explained their concerns and noted that the two possible solutions would be either to grant pension funds direct access to ECB liquidity as a backstop or to put in place a workable sponsored clearing model. He also noted that the latter introduces additional complexities that would need to be resolved, e.g. some clearing sponsors have argued that the size of the pension funds would be challenging for a single institution to accommodate. Other members agreed that direct access to ECB liquidity would be one option, however also noting the considerable reluctance in the central bank community to agree to such a solution. The alternative would be to allow banks to step in and provide the required liquidity backstop for pension funds. However, for this to work regulators would need to permanently exempt banks from the related capital charges, which again seems unlikely. Mr. Hill and Mr. De Vidts have been invited to join the Expert Group as permanent members and will continue to report back to the Committee.

6) <u>Update from the ERCC Operations Group</u>

ERCC Ops Chair Nicholas Hamilton (JP Morgan) updated members on the latest initiatives and discussions of the group. He noted that James Upton (LCH) has been appointed as new co-chair of the group, alongside himself. Mr. Upton has already been actively contributing to the ERCC Ops work over the past months, adding an important new perspective to the discussions. In terms of priorities, the ERCC Ops work over the past months focused on two areas, namely: (i) following up on previous discussions in relation to intraday liquidity management and (ii) the work with the ECB on collateral management harmonisation.

Intraday liquidity has been on the ERCC Ops agenda for a couple of years. A significant focus over the past months was to further develop and refine the existing analysis on intraday liquidity use cases and to tie the work back to best practices, in particular in relation to shaping and partialling, both considered important tools in this context. This work will continue into 2020 with a view to develop concrete findings and recommendations.

Several ERCC Ops members continue to be actively involved in the work of the ECB's collateral management harmonisation Task Force (CMH-TF). In this context the ERCC was asked to undertake a survey among members on settlement cut-off times. This was done jointly with ISLA over summer. The findings from the survey, based on over 40 responses, were generally encouraging, indicating significant infrastructure improvements over the past years across the 6 markets covered by the survey (a similar survey had already been undertaken by the ERCC in 2014). Mr. Hamilton also noted the important overlaps with the work on intraday liquidity which brings to light further frictions beyond cut-off times.

More generally, the focus of the CMH-TF has been to develop detailed harmonisation standards in different areas of collateral management, including tri-party and asset servicing, which have now been finalised. The areas covered so far are considered as core requirements for the development of the Eurosystem Collateral Management System (ECMS) which is due to go live in November 2022, introducing a new harmonised framework for managing collateral for Eurosystem credit operations. Commenting on the scope and importance of the ECMS, Mr. Hamilton noted that the project will be a significant development that will be most impactful for firms' treasury management. Another important focus of the CMH-TF work has been on messaging standards and the transition path to ISO20022. The ICSDs commented on the work undertaken and noted in this context the drive to more interoperability between central bank and commercial bank money settlement, which also includes the project to integrate Eurobonds into T2S.

On a final note, Mr. Hamilton commented on the evolution of settlement volumes in T2S which have seen a significant uptick with the migration of repo activity from LCH Ltd to LCH SA in March, but also noted that many firms are still in the process of adjusting their operating model to T2S and this is expected to be an very gradual process.

7) <u>CDM update</u>

Andy Hill provided a brief update on ICMA's joint work with ISDA to extend the Common Domain Model (CDM) to SFTs. As a first concrete step in this journey, it has been decided to map a vanilla fixed-term fixed-rate repo into the CDM. In terms of next steps, Mr Hill suggested that ICMA jointly with ISDA and REGnosys (the firm in charge of the technical CDM development) is planning to set up a series of CDM workshops with interested members to develop concrete use cases in the CDM. For example, a good starting point could be to focus initially on an open repo with relevant lifecycle events (e.g. a re-rate). Mr. Hill noted that active member engagement remains the pre-requisite to make any progress in relation to the CDM. For the workshops, we would ideally need input from all the relevant business areas, including trading, middle and back-office, as well as technology experts to fully understand all the challenges throughout the repo lifecycle that need to be addressed. A number of firms expressed interest in the proposed workshops. ICMA will approach firms individually and will look to schedule a first workshop in early 2020.

8) <u>Best Practice</u>

a) <u>Transition from EONIA to €STR</u>

Godfried De Vidts noted the very positive feedback received from the ECB on the successful transition from EONIA to €STR and the efficient coordination by the ERCC through the related best practices (an updated version of which was published on 27 September). Members briefly discussed feedback from the transition and the operational impacts, noting that these have been relatively muted given that (i) the interbank market has now fully moved to fixed-term repo (in line with the recommendations) and that (ii) the recommended net claims threshold of 500€ (per counterparty, per day) has only very occasionally been surpassed. As anticipated, a number of buy-side clients continue to rely on floating rate repo, although this number has also decreased.

b) Update from the ERCC Guide Working Group

The latest meeting of the Guide Working Group was held on 3 October. Sylvain Bojic, chair of the WG, reported back from the meeting and briefly introduced the latest set of proposed amendments to the Guide. In particular, it is proposed to reinforce some of the behavioural recommendations in the Guide, e.g. in relation to the timing of the margining process (and the resolution of related disputes) or notifications for re-rates or terminations. Another important but controversial issue that is still being discussed is the process for interest claims in the context of negative rates negative, as views differ as to what the appropriate basis should be for such claims.

Final amendment proposals agreed by the working group will be circulated to the ERCC Committee ahead of the next meeting for final review and approval.

9) Regulation

a) CSDR

Andy Hill updated members on the latest developments in relation to CSDR mandatory buy-in provisions. On 23 October ICMA had the latest call with the Commission and ESMA to discuss some of the many open issues in relation to the implementation of buy-ins. The focus of the call was on two important pending issues. One priority is to solve for the inherent asymmetry in the payments related to buy-in price differentials and cash compensation. ESMA and the Commission seem to be generally on board with the proposed contractual solution to allow for symmetric payments, although some concerns seem to remain in relation to cash compensation. Another topic that was discussed is the treatment of open SFTs. ICMA has asked authorities to clarify that these are out of scope for mandatory buy-ins (i.e. that the exemption for short-dated SFTs should also apply to open SFTs). ESMA and the Commission asked for further evidence to support the suggestion, in particular to provide more details on the treatment of open repos in accounting terms as well as from a regulatory capital perspective. ICMA is currently compiling the requested inputs and will reach out to members for feedback.

b) SFTR

Alex Westphal provided a brief update on the latest work with members in relation to SFTR implementation. The work continues at a high pace, with a very good and active engagement by members, which is expected to increase even further over the next months as we are approaching the reporting go-live in April. The implementation timeline is proving increasingly challenging as the important level 3 guidance from ESMA is still pending. It is currently expected that ESMA will publish the documents, including the detailed Reporting Guidelines by the end of the year. While waiting for the ESMA guidance, ICMA continues to work with members to further develop its detailed best practice recommendations in relation to reporting which aim to complement the regulatory framework. The ICMA SFTR Guide, the most important among the documents that are being developed, continues to grow and now covers well over 70 issues. While the Guide is still an internal draft it is planned to publish the document once the final ESMA Guidelines are available and have been incorporated into our own recommendations. Besides maintaining a regular dialogue with ESMA, ICMA is also reaching out to national competent authorities, including the FCA, which will be responsible for the SFTR implementation in the UK post-Brexit.

c) Other regulatory updates

In terms of other relevant regulatory developments, Andy Hill mentioned that EU Council and Parliament recently published another compromise text on the CCP Recovery and Resolution Regulation. While ISDA is in the lead on this file, the ERCC is monitoring the developments mainly to make sure that VM gains haircutting continues to apply only to gains and exempts SFTs, which continues to be the case.

10) AOB and further dates:

Members approved an application of the EIB to become a full member of the ERCC.

Alex Westphal briefly mentioned the upcoming ERCC elections. As usual, the process will be launched in early December with the call for nominations. Voting itself will open in late January, so the election should be concluded in early February.

Greg Markouizos informed members that after 18 years on the Committee, he will not stand again in the upcoming elections, due to increased internal responsibilities. He thanked everyone involved in the ERCC, current and past members, for the very fruitful and intellectually stimulating discussions over the past years.

Upcoming ERCC meetings:

- **15 November, 13:00 – 16:00 CET:** ERCC General Meeting in Brussels, hosted by Euroclear (as part of their Collateral Conference)
- **End of February (following the conclusion of the ERCC elections):** first meeting of the new ERCC Committee in London (date tbc)