

Minutes of the ERCC Committee meeting held on 26 October, 2016 in Frankfurt

Present:	Mr. Godfried De Vidts	ICAP (ERCC Chairman)
	Mr. Grigorios Markouizos	Citigroup (ERCC Vice Chair)
	Mr. Dan Bremer	BAML
	Mr. Michael Manna	Barclays
	Mr. Peter Schmidt	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. Sylvain Bojic	Société Générale
	Mr. Richard Hochreutiner	Swiss Reinsurance
	Mr. Gareth Allen	UBS Limited
	Mr. Harald Bäensch	UniCredit Bank
On the phone:	Ms. Lisa Cleary	ICMA
Also Present:	Mr. David Hiscock	ICMA
	Ms. Lalitha Colaco Henry	ICMA (ERCC Secretary)
Apologies:	Mr. Eugene McGrory	BNP Paribas
	Mr. Andreas Biewald	Commerzbank
	Mr. Andrea Masciovecchio	Intesa SanPaolo
	Ms. Amanda Brilliant	Nomura
	Mr. Eduard Cia	UniCredit Bank (ERCC Vice Chair)
	Mr. Ed Donald	Standard Chartered (ASIFMA)

Welcome

The Chairman welcomed those in the room and on the phone and thanked ICAP for hosting the meeting.

1. Minutes from the last meeting

It was agreed to postpone approval of the minutes of the last ERCC Committee meeting, which took place on 30 September 2016 in Munich.

2. ERCC meeting with the ECB

The Chairman said that Mr. Manna, Mr. Markouizos, Mr. Cia, Mr. Danese and himself had participated in a two-day ECB-IMF workshop from 24 – 25 October to discuss money markets, monetary policy implementation and market infrastructures. The agenda and some of the papers that were presented at the workshop are publicly [available](#).¹ It was clear at the workshop that the approach hitherto taken by some authorities regarding financial stability is starting to change. Some are acknowledging that the regulatory response to the financial crisis perhaps went too far and that the impacts of certain regulations, such as the leverage ratio, were underestimated, especially in relation to market making. Possibly one reason for this shift is that some regulators are now realising that the new regulatory regime has negatively impacted liquidity in the German bund market. However, regulators are still of the view that while certain effects may have been unintended and undesirable they can only be rectified as long as the safety and soundness of the financial system is not impacted; and that increased risks are not introduced into the system.

The Committee noted that it would be worthwhile to work more closely with academics and try to assist them with understanding the market and provide them with data where possible. Such data could also be shared with regulators as part of the ERCC's on-going educational efforts. The Chairman drew the Committee's attention to a qualitative survey being conducted by the Committee on the Global Financial System (CGFS). The CGFS is seeking to evaluate possible changes in the structure, activity and liquidity of repo markets collateralised by government securities. It aims to investigate potential factors behind these changes and to assess the extent to which they may affect the ability of these markets to support the financial system in the medium to long term, both in normal and stressed market conditions. It was agreed that firms should be encouraged provide responses, on a best efforts basis, directly to the CGFS; but should be requested also to confidentially copy their responses to Mr. Comotto so that he can analyse the aggregated ERCC member response.

For the Committee meeting with the ECB it was agreed that Committee members would discuss general market conditions, the ECB's asset purchase programme and the lack of harmonisation regarding the way the participating National Central Banks (NCBs) are managing their securities lending facilities. It was noted that this topic has been raised with the ECB in the past and that the current arrangements are a result of a political compromise which the ECB can do little to change. It was also agreed that the Committee should raise its concerns about the lack of a standardised legal agreement for use with the NCBs. The Committee also agreed that the conclusions reached in Mr. Burke's [report on CCP trade registration models](#)² should be raised at the meeting. The issues regarding intraday liquidity and the need for more efficient clearing and settlement would also be discussed, though it was noted that some within the ECB believe that T2S is working well towards solving these issues. The Committee agreed that the scope of T2S is too limited for it to solve all these issues, as it only deals with central bank money (CeBM) settlement, for participating CSDs in Europe. Ideally the market needs some form of "global T2S" that would work globally for both CeBM and commercial bank money (CoBM) settlement. The Committee also agreed to raise the question of the ECB's role in the development of a European secured benchmark.

¹ Alternatively, see:

https://www.ecb.europa.eu/pub/conferences/html/20161024_joint_ECB_IMF_workshop_money_markets_implementation_infrastructure.en.html

² Alternatively, see: <http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/repo-and-collateral-markets/ercc-publications/icma-ercc-reports/icma-ercc-report-on-the-trade-registration-models-used-by-european-ccps-for-repo-transactions/>

3. Netting of cash in a T2S or CSDR environment

It was agreed that this item would be postponed.

4. ESMA's report on haircuts

Mr. Hiscock said that ESMA had published its [report on securities financing transactions and leverage in the EU](#) on 4 October. There are four key points from the Executive Summary worth highlighting. First, ESMA recommends that the FSBs qualitative standards on the methodology used to calculate haircuts in non-centrally cleared SFTs should be introduced as a first step to improve the transparency and stability of haircuts, and the resilience of financial institutions. Second, ESMA goes on to say that the procyclicality of collateral haircuts used by CCPs should be addressed in the context of the EMIR review. Third, numerical haircut floors for non-centrally cleared transactions, such as those set out by the FSB, should only be introduced and calibrated following a thorough analysis using granular SFT data (which will only be available after the full implementation of SFTR), and following careful assessment of the scope, considering in particular the size and relevance of EU government bond markets. This means that any proposals for mandatory haircuts would be postponed until some considerable time after SFTR implementation. Finally, ESMA recommends that other macroprudential instruments, including counter-cyclical instruments, should first be agreed at an international level and only be introduced if it is found after a careful assessment that measures already introduced (such as capital requirements and bilateral margins) are insufficient to limit the leverage in the system. Only subject to these two conditions would ESMA consider whether further macro-prudential instruments are warranted. The report is a very positive development. It will be considered by the Commission when determining how best to proceed. The Committee noted that there could be merit in repeating its haircut data exercise, possibly on a periodic basis.

It was noted that a paper by Mr. Markus Brunnermeier et al³ has been receiving some attention. The paper suggests that the ECB or a similar entity could issue safe bonds using, as collateral, the euro zone government debt that the ECB has accumulated as a result of its quantitative easing programme. Such a securitised bond issue could be one way for the ECB to start unwinding or reversing its quantitative easing programme and would also introduce more HQLA into the market. The new instrument could comprise a senior bond that might be sold to insurance and pension schemes and a riskier junior bond to be sold to hedge funds.

The ECB has set up a task force, chaired by Bank of Ireland governor Mr. Philip Lane, to consider the idea further. One of the questions being considered by the task force is whether the issuer of the bonds should be a public or a private entity. The establishment of the task force is regarded by some to mean that the proposal is being given serious consideration by the ECB. The danger for the ECB is that if there is insufficient demand for the junior tranche then the ECB would be left owning the riskiest debt. However, one way to address this might be for a special purpose vehicle (SPV) to be set up to purchase the ECB's debt stock and then for it to issue the safe bonds.

³ See: <http://www.centreformacroeconomics.ac.uk/Discussion-Papers/2016/CFMDP2016-27-Paper.pdf> and <http://uk.reuters.com/article/eurozone-bonds-securitisation-idUKL5N1C94DK>

5. MiFID II best execution and SFTs

Mr. Bouillet said that SFTs are exempt from trade reporting under MiFID because of the provisions set out in SFTR⁴. However, the position of SFTs in relation to best execution requirements under [Regulatory Technical Standard \(RTS\) 27](#)⁵ of MiFID II is less clear. MiFID II firms are required to take “all sufficient steps” to achieve the best possible results for their clients with respect to orders for both equity and non-equity transactions. Importantly, trading venues (exchanges, MTFs and OTFs), systematic internalisers (SIs), market makers and other liquidity providers are required to make data available to the public, on a regular basis and at no cost, on the quality of transaction execution. Investment firms are also required to publish annually information on the quality of execution obtained on their top five trading venues based on volumes (by class of instrument).

RTS 27 does not specifically mention SFTs or specifically exclude them. It is unclear what is meant by the term “market maker” and “liquidity provider” in the context of SFTs and whether they would fall under the definition of “execution venue”. A best-case scenario is that SFTs would fall outside the scope of RTS 27. A worst case scenario is that they would fall within the scope of RTS 27 and accordingly firms that quote SFTs would have to comply with the best execution requirements. It was agreed that the position needs to be clarified with the Commission as soon as possible and that a suitable letter should be prepared as soon as possible. It was also agreed that this letter should make clear why best execution principles developed for cash securities activities do not make sense in the context of SFTs.

6. Large exposure rules

Prompted by a query from Deka Bank, the Committee discussed a question regarding the April 2014 BCBS standards for measuring and controlling large exposures (BCBS 283). It was noted that the exposure value for SFTs is explicitly covered by paragraph 34 of BCBS 238. It was generally felt that the provisions regarding credit risk mitigation (CRM) techniques in paragraphs 36-43 of BCBS 238 should not be seen to concern the case of GMRA repos, rather seeming to relate to transactions such as secured loans, but it was recognised that there is a degree of ambiguity in interpreting this BCBS text. It was suggested that Deka Bank (and any others concerned by this topic) should seek further regulatory expert guidance to support such an interpretation of the text, which ought then to alleviate the concern regarding large exposure measurement which had been flagged.

7. ERCC Operations Group update

It was agreed that this item would be postponed.

8. Bank of England Sterling Monetary Framework Collateral Pool Account

Mr. Allan said that he had been looking at the leverage ratio framework and came across the counterparty credit risk (CCR) add-ons. The Bank of England changed its rules regarding its single pool collateral account in 2014. Since then, use of the Bank’s single pool collateral account to pre-
position collateral means that you are using a full title transfer collateral agreement structure

⁴ Except in relation to repos where the counterparty is a central bank in the European System of Central Banks (ESCB). This is because the reporting exclusion in SFTR for SFTs transacted with central banks in the ESCB means that such transactions are still seen to be within scope of the transaction reporting requirements of MiFID.

⁵ Alternatively, see: http://ec.europa.eu/finance/securities/docs/isd/mifid/rts/160608-rts-27_en.pdf

instead of a pledge structure. With most central banks, when you put your collateral in it is still your collateral. Given the rule change, when you put your collateral into the single pool collateral account you are essentially giving the bank an unsecured loan of your collateral. This, in turn has implications for calculating your CCR add-on under the leverage ratio and would result in double-counting.

Firms are advised to look at this issue and speak with their regulator to determine if this is a problem for them and should flag any concerns to the Bank.

9. Legal update

Ms. Cleary asked Committee members to contact her if they would like any additional jurisdictions to be included as part of the 2017 legal opinion exercise. She also noted that the latest draft of the buy-side annex had been circulated to the working group. ICMA will look to start a road show of the document shortly to interested parties.

10. Administrative matters

It was agreed that AXA Investment Managers GS should be admitted to the European Repo and Collateral Council.

Ms. Colaco-Henry said that following on from the discussion at the 30 September Committee meeting about buy-side engagement she had circulated a paper regarding possible ways to increase buy-side involvement in the ERCC. It was agreed that it would be better to hold conference calls with ERCC members rather than sending more emails as people are already bombarded with too many emails. Conference calls would also provide better, more immediate feedback about whether calls are useful to ERCC firms. However, it was noted that conference calls would have to be managed carefully.

It was noted that the basis of the ERCC and the Committee are set out in ICMA's by-laws and this is unique amongst all of ICMA's councils and committees. As a result, there is a certain rigidity about the membership of the ERCC and the Committee which does not easily allow for changes to be made to the composition of either the Council or the Committee. At issue is the extent to which the Committee is reflective of the changing face of the repo market as a whole. Currently there is nothing to prevent buy-side firms from becoming ERCC members; and ICMA's buy-side members are being encouraged to become ERCC members – which may in turn lead to evolution in the Committee's composition.

11. AOB and further dates

Further **ERCC Committee meetings** are scheduled as follows:

1. **14 November 11:00 – 13:15 CET** - ERCC Committee meeting in the margins of the Euroclear Collateral Conference in Brussels;

2. **25 January 14:00 – 17:00 CET** - ERCC Committee meeting in the margins of the Clearstream Global Securities Financing Summit in Luxembourg. The meeting will be held at Clearstream's offices at The Square, Room KB.01.C50, 42 Avenue JF Kennedy, L-1855 Luxembourg.

The ERCC Chairman:

The ERCC Secretary:

Godfried De Vidts
14 November 2016

Lalitha Colaco-Henry