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Minutes of the general meeting of the European Repo Council held on October 16, 2013 in London

Location: **J.P. Morgan, 25 Bank Street, London E14 5JP**

Time: **10:00 – 12 :30**

1. Opening of the meeting by the Chairman of the European Repo Committee, Mr Godfried De Vidts

Mr De Vidts welcomes everyone to the General Meeting of the ICMA European Repo Council and thanks J.P. Morgan for hosting. Mr De Vidts explains that Mr Martin Scheck, Chief Executive of ICMA, is unable to attend the meeting and so Mr De Vidts will say a few words on Mr Scheck's behalf.

Mr De Vidts describes ICMA's annual general meeting in Copenhagen as proof of the sound work of ICMA. The chairpersons of the main ICMA committees each provided a brief update of their activities and each of them chaired a panel with experts in their field during the conference. Alongside the repo work which is the focus of today's meeting, work in the primary debt capital markets, secondary markets, and the asset management and investor council creates value for the ICMA membership. Mr De Vidts recommends to the meeting that they read the ICMA quarterly report, the latest edition of which was published on October 8, 2013. Mr De Vidts explains that the ICMA quarterly report provides all the necessary information needed to stay abreast of the various workstreams and regulatory initiatives of which attendees at the meeting need to be aware, and only when one engages in today's debates can ICMA help its members to innovate, adapt and, as a result, perform better in their day job.

Mr De Vidts explains that he has recently accepted a nomination as a Board member of ICMA. Mr De Vidts states that this should assist in securing even more commitment from the ICMA Board for the essential work needed to support the repo community, and notes that Mr Scheck often mentions the valuable work of the ICMA European Repo Council and Committee. Mr De Vidts explains that the work of the ICMA European Repo Council and Committee is not a one-man show: it is the repo community at large that influences the debate around repo. And, despite Patrick Pearson's comment at the repo academic event held in June 2013 that the European Repo Council should widen its work to those less well-informed, Mr De Vidts is glad that the voice of the European Repo Council has been heard in the past, and is confident that it will continue to be listened to in the immediate future.

Mr De Vidts explains that the agenda for the meeting is full and so his opening remarks will be brief and will cover three items: (1) the triparty settlement interoperability memorandum of understanding ("TSI MoU") and further work on market infrastructures; (2) the secured benchmark issue; and (3) a new study to be published.

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In relation to the TSI MoU and further work on market infrastructures, Mr De Vidts highlights that at this year's annual SIBOS event organised by SWIFT (which was held in Dubai and brought together some 6000 participants mainly involved in the post-trade business), there were interesting conferences held in the margins of the event. Mr De Vidts explains that he attended two days of workshops along with many bilateral meetings. The Eurosystem has previously been present for a number of years with a stand, highlighting the ongoing work around T2S. Through the European Repo Council's involvement with COGESI, other forums like CESAME previously hosted by the European Commission, and the EPTG group (bringing together the European Central Bank, the European Commission, ESMA and the industry), the European Repo Council has focused on creating a better framework than the legacy national settlement systems that make repo less efficient than it should be. In short, the Eurozone lacks a true European capital market. However, a lot of progress has been made, with T2S as a catalyst. The interest of legislators and regulators around these topics are now clearly visible through the huge amount of regulatory initiatives being discussed in Brussels as a direct result of the G20 agenda, but also the need for Europe to get its house in order. The repo market is in the middle of all this work, as the raw material it uses, collateral, is channelled through its product. The meeting will discuss regulatory initiatives further later this morning.

Mr De Vidts explains that a short film was played at the SIBOS event ahead of a session introduced by Mr Benoit Coeure, Member of the Executive Board of the ECB, called "Key challenges and opportunities for the integration of European financial market infrastructures". The film is shown to the meeting[1]. The film shows that the TSI MoU was signed on July 15, 2013 at a signing ceremony hosted by the ECB and attended by the European Commission. Mr De Vidts states that all the signatories to the TSI MoU have now committed to this major project. Mr De Vidts, as chairman of the ERC, has been asked by all parties to continue to chair meetings if and when necessary to make sure the project does not derail. The ECB and the European Commission are also tracking the progress of this project. All parties appear to be committed, with numerous meetings currently taking place between them. A progress report and expected timeline for delivery of the project will be delivered at the COGESI meeting at the end of November. Mr De Vidts continues to be involved in a number of working groups to progress the project, and is assisted by the ERC Operations Group.

Mr De Vidts reports that one workstream is the preparation of a report entitled "Report on efficient functioning of the repo market: Improvements to support end-of-day liquidity management and triparty settlement interoperability". A meeting took place on October 7, 2013 and a specific ad hoc group chaired by the EBF/ERC with the ECB as secretariat is looking at the commercial bank money flows that eventually end up linking into central bank money. The ERC has demanded (not requested) to be able to trade repo with all market participants in the Euro currency without any barrier up to 4 p.m. CET, and to create the possibility to square treasury positions in DVP repo between interbank participants involved in this area even later in the day, possibly close to TARGET2 cash close of day. In due course the results of this workstream (which is due to be finalised by year end) will be published.

In relation to the secured benchmark issue, Mr De Vidts explains that Eurepo was created in co-operation of the ERC with the EBF, with the ECB as observer. There have been some demands for Eurepo to be reformed, and as a result the EBF issued a questionnaire on the use of the Eurepo benchmark. The results of that questionnaire show that there is limited activity linked to the Eurepo fixing and even though most agreed that the Eurepo fixing could be discontinued, they also said that it should be maintained until a reliable alternative, representing the entire curve and reflecting the 'European' market, is in place. In terms of

[1] The film is available here: http://www.youtube.com/watch?v=mVcgRLqBOsM

considering the ideal repo benchmark, a joint meeting of a working group of the ERC and the Eurepo steering committee will be held in November 2013, jointly chaired by Euribor-EBF Chief Executive Guido Ravoet and Mr De Vidts as Chairman of the ERC. The ECB will also be invited as an observer.

In relation to the new study to be published, Mr De Vidts updates the meeting on a paper that ICMA is preparing on the impact of current and forthcoming regulatory changes on the ability of European fixed income and repo markets to fulfil their essential economic role of helping to lubricate and sustain economic recovery and growth. The paper will aim to identify specific examples where the market is concerned that aspects of the reform of regulation give rise to inconsistencies, conflicts, overlaps, and unintended consequences which may undermine core aspects of these markets and the economic functions they perform, and so put at risk the shared policy objectives of regulatory reform. There is widespread concern that some of these problems, and their cumulative impact, are in danger of doing serious harm to European fixed income markets and the real economy which they service. The paper will highlight the need to agree practical, consistent, and directed ways of resolving these problems so that the authorities and markets can, together, achieve the aims of regulatory reform, financial stability and renewed growth.

Mr De Vidts also updates the meeting on the recent topical issue of fire sales of collateral, noting that a recent Federal Reserve Bank workshop generated headlines and reports using the phrases 'run on repo' and 'fire sales' as headline grabbers. Mr De Vidts notes that it is important to recognise (and explain to outside observers) that the workshop was focused on the special problems of the US triparty repo market. US triparty is very different in terms of operational structure, risk exposures, investor concentration, collateral and term to the European repo market. Just because the US and European markets share the labels 'repo' and 'triparty' does not mean they are the same in all key details. It is too easy to assume that both markets have identical priorities and need the same solutions, and it is important that the FSB recognises regional and national differences and the market (through the ERC) addresses these misunderstandings.

2. Approval of the minutes of the ERC Annual General Meeting held on March 11, 2013 in Paris

The ERC unanimously approves the minutes of the ERC annual general meeting held on March 11, 2013.

3. ERC Repo Survey

3.1 Introduction and note on fire sales of collateral

Mr De Vidts introduces Mr Richard Comotto of ICMA Centre, and explains that Mr Comotto will discuss the fire sales of collateral topic that Mr De Vidts just touched upon, the results of the most recent ICMA semi-annual repo survey and the proposed ICMA European Repo Council Guide to Best Practice in the International Repo Market.

Mr Comotto notes that the issue of fire sales of collateral has grabbed the media attention recently, and that it has been a concern for some time. Mr Comotto stresses that, although risk of fire sales is not irrelevant in Europe, the primary source of the current debate is the US triparty repo market. This is very different to the European triparty market and care should be taken not to uncritically read the issues across from the US to Europe. He outlines the differences between the US and European triparty repo markets, including (among other things) that as much 60 per cent. of the US repo market may be transacted on triparty basis, compared with 10% of the European repo market and that the daily unwind and rewind of positions in the US, which gives rise to a long intra-day gap and interim exposure (albeit being reduced by reforms being pushed by the Fed) is a key problem in the US which does not occur in Europe. In addition, the vast majority of the repo market in the US is transacted on an overnight or open basis, which is not the same in Europe. Given the different market practices and structures in the European and US markets, fire sales are a far more serious concern in the US than in Europe. The likely outcome in the US will be a repo resolution mechanism or process. Although not faced with the same problems, there is a risk that European regulators will want the same solution.

3.2 25th Semi-annual ICMA repo survey

Mr Comotto reports that the ERC has released the results of its 25th semi-annual survey of the European repo market. The survey, which computes the amount of repo business outstanding on June 12, 2013, compiles the results of 65 responses from 61 groups and reveals a headline figure for the market size of EUR 6,076 billion. This represents an increase of 8.6% in the size of the market since the last survey in December 2012 (measured using a constant sample of survey respondents). The survey also revealed a contraction in the US repo market. The revival in repo activity in Europe appears to be driven by banks in the eurozone returning to the market for funding as they start to repay the exceptional assistance of over EUR 1,000 billion euros, provided to the market via the ECB through the Long Term Refinancing Operations (LTROs). The LTRO repayments have contributed to tighter market conditions and a steepening money market yield curve. The higher rates and greater market confidence have attracted lenders away from the ECB deposit facility (which pays zero per cent.) and back into the market.

Mr Comotto discusses the results of the survey's trading analysis, noting that bilaterally-settled trades arranged by a voice-broker account for 14.6 per cent. of total trades, although the survey numbers are given in terms of volumes outstanding rather than turnover, so it may understate short-term and overnight trades. In addition, the data shows that triparty trades trend at 10 per cent. of all trades, and the value of electronic trading has reached a new high.

In terms of the geographical analysis, the survey shows a decline in domestic trading and then a flattening in the crisis, although it is queried whether this is a trend that will continue. The business cleared across CCPs jumped during the sovereign debt crisis and again after the introduction of the LTROs.

The results of the currency analysis are not surprising, with EUR and USD trades representing the largest parts of the market. The collateral analysis shows a decline in use of Greek and Italian collateral, and the effect of ratings downgrades can be seen in the data.

The data relating to maturity shows there is a high proportion of open and forward repo, and there has been an increase in the volume of open repo since the previous survey. Mr Comotto believes this may be evergreen repo, which has been driven by regulation. In terms of the levels of ATS and voice-broker transactions at different maturities, ATS dominates the short-end of the maturity range and vice versa.

In terms of the levels of securities lending compared with repo, securities lending accounted for more than 20 per cent. of the market before the crisis, but that level has declined since the crisis and remains low at 10.4 per cent.

The concentration analysis shows that market concentration is continuing to decline, which may reflect continued regulatory pressure on banks to reduce deleverage. This is likely to affect larger banks more.

Mr Comotto reminds the meeting that the deadline for responses for the next semi-annual repo survey is December 11, 2013 and encourages participation from all ERC member firms. Mr De Vidts thanks Mr Comotto for his work on the semi-annual repo survey.

4. <u>ERC Guide to Best Practice in the International Repo Market</u>

Mr De Vidts notes that the repo market takes self-regulation of its market very seriously. In line with this, the ERC has been working with Mr Comotto to prepare a Guide to Best Practice in the International Repo Market (the Guide). Mr De Vidts notes that this project has taken a long time, and is not yet finalised.

Mr Comotto introduces his discussion of the Guide by emphasising that the Guide is intended to be a guide to *best* practice, and not an assessment of *market* practice. It is not the same as the GMRA, which is a legal document. It consolidates disparate pieces of ICMA and ERC guidance and incorporates updates. The aims of the Guide are (i) to promote an orderly, safe and efficient market by harmonising practice at the highest standard and reducing scope for uncertainty or disagreement, (ii) to provide guidance on specific issues beyond the scope of the GMRA and (iii) to provide a focus for future discussion on best practice. Mr Comotto also notes that the Guide will be a living document and so will change over time, so it will be important that market participants check the date of the version they use.

Mr Comotto notes that the Guide is not a “code of conduct” and it doesn’t have a prudential function, but it should complement Codes of Conduct that are also available. Parties are free to agree other terms and not follow the Guide, but they will need to recognise the risks to which they may expose themselves as a result. In terms of the focus of the Guide, the market focus is trading and post-trade conventions in the international (cross-border) repo market. The primary geographical focus is Europe, but it should be applicable globally hence it being called “Guide to Best Practice in the *International* Repo Market”. The primary counterparty focus is ICMA members but others are encouraged to apply the Guide.

Mr Comotto describes the existing guidance available. In terms of existing ICMA ERC guidance, the Best Practice Guide to Repo Margining published in 2012 and Repo FAQs will be annexed to the Guide. Various other ICMA recommendations will be consolidated in the Guide. Mr Comotto also notes the Gilt Repo Code of Guidance of May 2008 and the Equity Repo Code of Guidance published by the Bank of England, which market practitioners will need to consult while they are still current. Mr Comotto goes on to describe the various sections of the Guide, namely best practice in initiating a repo transaction, best practice in managing the life cycle of a repo and the various annexes; noting that most of the content is either part of previous guidance or has been included as a result of commonly asked questions posed to ICMA.

The Guide will be made available on the website of the ICMA. The ERC will depend on its members to suggest improvements for the Guide and highlight new issues. The ICMA Legal & Regulatory Helpdesk will be available to answer queries and, in due course, there may be a course with an exam or certificate.

Mr Comotto concludes by encouraging ERC members to voice any issues or comments on the Guide, noting that the market needs to take ownership of this document in order for it to be as useful as possible for market participants.

Mr De Vidts thanks Mr Comotto for his hard work on the Guide.

5. Keynote Speech

Mr Rule introduces himself as speaking in his capacity as Chair of the FSB's WS5 on shadow banking risks in securities lending and repos. Mr Rule outlines the background to the FSB's focus on shadow banking, namely (i) shadow banking is seen as a significant factor in the crisis, and (ii) tighter regulation of banking may encourage shadow banking in future. Regulators are looking at entities that undertake some of the functions of a bank but operate outside the banking sector. Mr Rule describes the timeline for the FSB's work on securities financing markets, starting in September 2011, including the publication of revised policy recommendations (including specific proposals on minimum haircut standards for consultation) in August 2013 and finalising the recommendations on minimum haircut standards in the second quarter of 2014. Mr Rule notes that the consultation on minimum haircut standards is open until November 28, 2013 and that the FSB is keen to hear market participants' views on this topic.

Mr Rule notes the three aspects of the FSB's August 2013 policy document, namely improvement in transparency, regulation of securities lending and repo and structural aspects of the securities financing market, and describes how the policy recommendations address fire sales of collateral, procyclicality of leverage, rehypothecation, reinvestment of cash collateral in securities lending and risk management standards.

In terms of improvement in transparency, the recommendations include improving data collection through counterparties reporting exposures; and a new data experts group has begun looking at technical questions relating to data collection and aggregation. Data will typically be collected at a regional/national level and questions of implementation now need to be considered. In terms of regulation of securities lending and repos, the minimum standards for cash collateral reinvestment by securities lenders will be taken forward by regulators.

Moving on to the new consultation, in Annex 2 of the FSB's August paper, Mr Rule explains that one aim is to target procyclicality of haircuts. The primary intention is to regulate the terms on which non-banks borrow from banks against non-government collateral. If non-banks were to finance each other in the future on a material scale then this will need to be considered. There is an exemption for securities lending against cash where it is not undertaken for financing purposes. In addition, the FSB aims to include anti-avoidance measures in the recommendations. Mr Rule emphasises that the recommendations do not include recommended levels for haircuts, but rather recommended floors for haircuts.

Mr Rule summarises the first phase of the FSB's quantitative impact study, known as QIS1, which consisted of a data request to 17 large financial intermediaries in 12 FSB member jurisdictions. The questions covered three historical periods: 2006, 2008 and 2012. Of the transactions reported in the 2012 period, less than ten per cent were within the scope of the FSB proposals and over half were undertaken with zero haircuts (although Mr Rule queries whether there may have been some mis-reporting in this regard).

Mr Rule explains that the second phase of the FSB's quantitative impact study (QIS2) will be conducted in the autumn with a broader sample of participating institutions. The study will aim to collect data on transactions with zero haircuts and additional collateral required under the proposed numerical haircut floors; and ask a set of qualitative questions on the potential impact of proposed numerical haircut floors, with the aim of understanding the extent to which market participants are already complying with the FSB proposals.

Mr De Vidts thanks Mr Rule for his presentation and asks whether there are any questions for Mr Rule.

Mr Rajen Patel of Morgan Stanley asks Mr Rule whether the FSB is concerned by the migration of repo transactions away from CCPs. Mr Rule states that it is a concern, particularly in the inter-dealer market. FSB members would be concerned if market participants were to avoid using CCPs due to margin requirements. Mr Rule re-iterates that FSB members are monitoring this area.

Mr David Hiscock of ICMA notes the degree of scepticism expressed by the FSB in relation to transactions with zero haircuts and asks Mr Rule whether the FSB expects to see haircuts on all transactions or whether the FSB may consider it to be reasonable to have certain transactions with no haircut. Mr Rule notes that the FSB is aware that enforcing haircuts in the interbank market would mean that banks are forced to take some exposure to each other as for every bank taking a haircut there will be a bank giving a haircut. The proposed haircut floors are specifically proposed on a basis which focuses on transactions with non-banks.

Mr Michael Manna of Barclays welcomes the qualitative element of the data collected by the FSB. He moves on to ask Mr Rule whether he can describe a “non bank”. Mr Rule explains that the FSB sees a “non bank” as any entity not subject to prudential regulation of capital and liquidity and not in the definition of a “bank”. Mr Rule notes the issue of securities dealers (broker-dealers or investment banks), which should be seen as within the definition of “banks” for this purpose. He states that the FSB’s intention is for “non-banks” to capture other financial entities such as hedge funds, pension funds and insurers.

Mr De Vidts thanks Mr Rule for his presentation.

6 <u>Legal Update</u>

Mr De Vidts notes that ICMA is focused on ensuring a robust legal framework for the repo market, and is currently encouraging the move from the GMRA 1995 and GMRA 2000 to the GMRA 2011. Mr De Vidts hands over to Ms Lisa Cleary of ICMA to provide an update on recent legal developments.

Ms Cleary reports that ICMA is delighted to confirm the adherence of the first party to the GMRA 2011 Protocol which provides parties with the ability to upgrade certain provisions of their existing GMRA documentation on a multilateral basis with other adhering parties. The market is regularly reminded about the importance of keeping documentation up to date, especially following reviews prompted by market events. ICMA is delighted to see the first ERC member adhere to the GMRA 2011 Protocol and wishes to assist others in doing the same. It is important that efforts to make repo documentation even more robust are supported by the market participants who have helped to develop it.

Ms Cleary reports that another area in which the GMRA working group has been developing the documentation is with respect to FATCA. The group has developed standard language for use with the GMRA which is broadly based on existing market standard FATCA wording. The wording places the risk of non-compliance on the payee, the recipient being the party burdened with the FATCA withholding tax if it chooses to not comply. The GMRA wording is in the process of being finalised and will be published shortly.

Ms Cleary provides a quick update on the GMRA legal opinion exercise, explaining that the annual process has commenced to update the opinions for publication in Spring 2014, with the addition of Lichtenstein as a new jurisdiction. This brings the total number of jurisdictions covered to 64. In an effort to support and encourage the use of up-to-date market documentation, it has been discussed when it would be appropriate to discontinue coverage of the GMRA 1995 within the opinions. This will not be done in the short-term but it should focus market participants' minds in terms of documentation for the medium-term.

Finally, Ms Cleary reports that to the extent that ICMA is made aware of regulatory or legislative amendments which prompt changes to the conclusions drawn in the GMRA legal opinions, it will publish interim opinions or update memos on its website. ICMA has been made aware of a number of issues which may require such action and are liaising with counsel in the Netherlands (noting a recent call of the ERC on the Dutch Intervention Act) as well as in Cyprus (where ICMA published an updated opinion on October 15, 2013) and Belgium (where ICMA is seeking further clarifications in the 2014 legal opinion).

Mr De Vidts thanks Ms Cleary for her continued work in this area.

7 ERC Operations Group update

Mr De Vidts explains that front office repo teams and repo operations teams need to work together to ensure efficiency, which is why the Chairmen of the ERC Committee and the ERC Operations Group attend each other's meetings. Mr De Vidts notes that Mr Tony Platt was the first Chairman of the ERC Operations Group, and has now been replaced by Mr Nicholas Hamilton, the current Chairman of the ERC Operations Group.

Mr Hamilton reports that the ERC Operations Group has two working groups, one in post-trade affirmation and matching and another deployed on the growing analysis of the data repository activity for repo. There are also focus groups for TARGET2 securities, margins and on the large number of ad hoc demands that have required some rapid engagements to support practitioner views on regulation, product and processing.

Mr Hamilton explains that Ms Camille McKelvey of Citi leads the post-trade affirmation and matching sub-group, with ten other firms represented. The sub-group is intended to be a permanent group as this element is seen as key to the efficiency and control of post-trade processes now and going forward. There are clear challenges in this area in consistency of definition, direction, platform growth, identification of common denominators and low automation in a growing product flow. This is more sensitive as term begins to return to the market, as longer-dated risk needs increased operational risk management. The sub-group has reviewed definitions to clarify context of the post-trade processes and is sending a renewed request for information to market vendors.

Mr Hamilton goes on to note that Mr Jonathan Lee of J.P. Morgan is leading a working group on the data repository workstream. A paper entitled "Enhancing the transparency of the European repo market" is due to be published which considers and gives the ERC's views on the challenges and feasibility of outputs to regulators of repo information. In preparing this paper, the working group set about identifying the key objectives, product scope and data requirements of regulatory bodies including the European Systemic Risk Board (ESRB), European Securities and Markets Authority (ESMA), Financial Stability Board (FSB), European Central Bank (ECB) and International Organisation of Securities Commissions (IOSCO). The papers produced by these organisations have many common elements but none of them has yet proposed a clear and practicable framework for enhancing transparency of the European repo market. It became apparent that while a number of papers commented on the desirability of receiving trade level data (in some cases in addition to position level and aggregated data), it was not clear how this data would be sustainably managed and that the sheer volume of data has a lot of scope to confuse recipients and exacerbate costs. Therefore, there appears to be solid case to recommend a position-level survey-based programme in Europe that will meet the overriding macro and micro prudential demands of regulators in the short to medium term without the cost, level of development or disruption of implementing a trade-level repository. Standardisation of terms and reporting consistency should also help to provide a solid benchmark for rolling out this agenda across other regions, ultimately enabling the data to be aggregated globally (again in line with regulator aspirations). In the longer term, trade-level information, which is validated, timely and complete, could also be produced but the regulators and the market must take note of experience in the derivatives space and manage scope and timetable closely. The Russian market experience has offered new perspectives which should be acknowledged too in multi-asset class, matched models from multiple service providers. This debate has evolved rapidly this year and practitioner input will help shape a better outcome in post trade transparency framework. In summary, the paper has a strong foundation to it in the reviews of consultations and regulators' outputs of the past 12 months and more contemporary feedback in the Financial Stability Board request for information on transparency and haircuts. Mr Hamilton hopes that the paper will allow discussions to be furthered in this area.

Mr Hamilton reports further that the TARGET2 securities focus group led by Mr Mason has run a successful introductory session to T2S timetabling with some key functional clarification in the earmarking, tagging and blocking processes. Mr Hamilton states that the process of establishing views and entry points in advance of the first wave in 2015 is well underway and the ERC Operations Group will continue to advocate market discussion and debate as the timing and functional elements become more tangible, dependant on firms' entry points.

Mr Hamilton also reports that the margins team, led by Mr Adam Bates of Morgan Stanley, has worked with Mr Comotto to collate a useful set of guidelines on margin processing. Calculation definitions, timings and many of the technical nuances are represented in this document. Mr Hamilton stresses the importance of market engagement in these discussions, noting that consensus views allowed the ERC to create a number of very useful documents for firms' reference in the markets and operational areas. In particular, the FAQs and Guidelines documents that Mr Comotto and the ICMA have collated, validated and published should help to reduce ambiguity in market process and also stimulate further discussion on what future market practice should be.

As well as this exciting work around securities settlement, a joint ERC-EBF-ECF group is working on identification and implementation of enhancements to security settlement related transactions in commercial bank money. This group is currently determining an approach to identify and model the interdependency of individual processes for cash settlement across banks, custodians, CSDs and ICSDs and pulling together this information in the context of current timings and cut-offs on a product and market basis. This model should eventually expose key opportunities for reducing processing cycles and determining the most efficient cut-off times for sending instructions for settlement. There are challenges to creating this deep view of what is a complex and multi-layered process, and to truly identify what are hard restrictions and what are simply accepted norms in a landscape that has evolved with the technology to meet needs but without an initial market-wide vision. Challenging the status quo and providing the best analysis will require support and consensus, not only across market participants but also within institutions themselves where cash processes across departments and functions have likely also remained unchallenged and perceived as firm processes due to external market cut-offs – cut-offs that are now being questioned and revised.

Mr Hamilton notes that Mr John Serocold of ICMA will highlight in more detail the work of ICMA in response to the Level 1 texts for the CSD Regulation. Article 7 of the CSD Regulation is of concern to the industry as un-calibrated mandatory buy-ins with inconsistent application across venues may materially impact liquidity. It is important that the market continues to present the detail, areas of concerns and mechanical flows affected by the proposed regulation as a group. Operational perspectives are providing useful objectivity as the trilogue of this regulation evolves.

Mr Hamilton also reports that the ERC Operations Group is looking forward to working with its partners Eurex, Euroclear and Clearstream to progress work in relation to triparty interoperability further to the signing of the memorandum of understanding. It is hoped that this will improve the efficiency of movement and increase the size of the collateral pool in Europe.

Finally, Mr Hamilton notes that the continued partnership of the ERC with other industry fora, in particular AFME, ISLA and the EBF is essential going forward. This allows ERC to focus resources and thinking in areas where it has the appropriate experts and networks to deliver objective and well-founded views as the repo industry landscape continues to evolve.

Separately, Mr Hamilton thanks the previous Chairman of the ERC Operations Group, Mr Platt, who recently stepped down and who has been a great thought leader, advocate and agent of change over the past three years. Significant steps in triparty interoperability planning and standardisation of market practice in margin guidelines were made over the past three years, including numerous responses to regulatory consultations and excellent work in cross-border harmonisation discussions and developments. Mr Platt also invested much time in education and active mentoring of his peers.

Mr Hamilton and Mr De Vidts present Mr Platt with a gift in recognition of and thanks for his achievements as Chairman of the ERC Operations Group.

8 Regulatory Update

Mr De Vidts introduces the regulatory update by noting how important it is that the market makes its views and concerns known before regulation is finalised, as it is too late once regulation has been finalised. Mr De Vidts encourages the ERC to involve their clients in regulatory discussions, as corporates and not just banks will be affected by the proposed changes in regulation.

Mr Hiscock begins by explaining that repo is an essential component at the heart of the financial system; and that it is central to the provision of liquidity and the flow of collateral. ICMA has been working hard to deal with the tsunami of regulation, including bank regulation, liquidity and capitalisation rules, derivative regulations, margining requirements and shadow banking proposals. In relation to shadow banking proposals, Mr Hiscock emphasised the efforts that ICMA and the ERC are making to engage in this discussion, with a joint ICMA/ISLA response to the latest FSB consultation already under discussion. ICMA is also considering the European Commission's roadmap document on shadow banking which is still quite high level. ICMA is continuing to work diligently to shape the measures in order to sustain an efficient and fluid market.

Mr Hiscock reports that a BCBS consultation on the revised Basel III leverage ratio framework was launched on June 26, 2013, with the intention of building the capital strength of the banks. The leverage ratio is seen as a backstop to risk based capital, as there are concerns that the complexities of risk based capital can lead to wrong results. However, there can be perverse consequences of the leverage ratio proposals not taking an asset's risk into account, as it can make it relatively expensive to hold less risky assets. The proposals' focus on gross, rather than net, securities financing exposures also makes repo expensive from a balance sheet perspective. ICMA has responded to the consultation highlighting these issues, and this is an area the market will need to watch. Further, the market needs to do more to quantify the impact of the proposals.

In relation to the proposed financial transaction tax (FTT), this an ongoing file on which ICMA published two very important papers earlier this year outlining concerns with the FTT proposals and explaining why repo and collateral are linked. A host of other market players have also raised concerns with the proposals. There have also been legal challenges (including from the UK and the European Council's own legal services) suggesting that some elements of the proposal, in particular the concept of deemed residence, are illegal. The debate on this topic seems to have moved to look at alternatives to the current proposals, and so it is important to remain vigilant in this area in relation to any new proposals that may emerge.

Mr Hiscock reports further that the ERC has engaged in the debate on asset encumbrance as it is important to consider the impact of these proposals on the repo market. The IMF's October 2013 Global Financial Stability Review reports on changing bank funding patterns and makes a clear statement that limits on asset encumbrance may be needed going forward. If this signal of policy direction does lead to limit proposals, this would be very significant for the repo market as a limit on asset encumbrance would almost certainly be proposed in such a way that would be a limit on repo.

Mr Hiscock hands over to Mr Serocold, who introduces two pieces of regulation on which ICMA has been actively involved from a secondary market perspective. Both of these incoming regulations potentially impact repo markets in a number of ways. Turning first to the MiFID II package, this consists of a recast directive, repealing the MiFID I Directive, and secondly a new regulation. The regulation element satisfies the desire for a single European legislative text, seeking to deal with a number of issues not covered in MiFID I. Subsequently MiFID II aims to improve European markets and enhances investor protection. Importantly, the package allows large European countries to deliver on its G20 Commitments as outlined in the Pittsburgh summit in 2009.

The content of the regulation and directive together cover how markets function, how interactions between market participants should be conducted, as well as rules for internal organisation and authorised activities. It is worth nothing that the functioning of markets and interaction between participants will cause change in the repo markets where the issues of pre- and post-trade transparency will provide a framework for fixed income securities for the first time. There will also be trends towards more automation, rules for HFT, as well as providing access between market infrastructures. The key issue arising from post-trade transparency is how repos will be affected in the form of calibration being developed for fixed income markets. Repo has not been exempted from the regulation, as the texts states that criteria can be put in place for transactions involving collateral and lending. Furthermore, post-trade reporting will apply to all financial transactions, and repo transactions would most likely be reported to a trade repository. ICMA will watch closely the fine details as to reporting and publication required under each of the market structures arising from the package.

ESMA will be heavily engaged in this work stream since they will be providing advice, developing proposals and creating binding regulatory standards in respect of these issues. In terms of timetable and next steps, MiFID II will be competing alongside other major pieces of regulation in the European Council and Parliament before the elections in May 2014. Although trilogues have started and are due to finish next year, a Level 1 text is expected in February 2014 before Parliament dissolves. Following this, it would take some months for official language translations to be completed before the package is published in the Official Journal, which is expected between June and August 2014 under the revolving Presidency. It is expected that ESMA will write a very detailed discussion paper after the text is agreed. There will be a short window for a consultation, where market participants will be invited to voice their concerns.

In relation to the CSD Regulation, where the proposal’s aim is to harmonise post-trade infrastructure in the single market and integrate the CSD network in Europe, there are a number of changes that will affect fixed income markets and repo in particular. As was announced on March 7, 2012, the trade cycle will account for 2 days instead of 3, coming into effect in 2015. Furthermore there will be a CSD authorisation process involving prudential rules and capital requirements. This will create a new landscape of CSDs, changing the way they think about their ancillary and core services. As mentioned in the MiFID II package, there will also be requirements for access provisions to be put in place between vertically linked CCPs and trading venues to open up the flow of clearing. The ECON Committee within the European Parliament finalised their text in February 2013, while the Council agreed their General Approach in September 2013. Trilogues are expected very shortly as the institutional working groups gather common positions and finalise areas for political and technical work. There has been much focus on Article 7 concerning the mandatory buy-ins for cash bonds, which also applies for repo markets. ICMA believes that this threat has been staved off in the recent months, but it is still an area that needs to be closely monitored. The issue of core and ancillary services which would affect the ICSDs and their ability to settle in commercial bank money has implications for the efficiencies that DVP currently offers. In summary, ICMA will be engaging with regulators and working groups where necessary to promote the infrastructure necessary to achieve effective functioning of the repo markets.

9 Any other business and next meetings

Mr De Vidts thanks all those who have contributed to and participated in the meeting, including J.P. Morgan for hosting and the ICMA for organising the meeting.

The next ERC Annual General Meeting will be held on January 22, 2014 in Luxembourg, hosted by Clearstream.

The Chairman: The acting Secretary:

Godfried De Vidts Charlotte Bellamy

Annex 1

List of presenters and represented firms in attendance

Presenting:

Godfried De Vidts *(Chairman), ICAP Securities plc*
Richard Comotto, *ICMA Centre*
David Rule, *Financial Stability Board*
Lisa Cleary, *ICMA Limited*
Nicholas Hamilton, *J.P. Morgan*
David Hiscock, *ICMA Limited*
John Serocold, *ICMA Limited*

The following member firms were represented at the meeting:

Banca IMI S.p.A., Milan
Banco Bilbao Vizcaya Argentaria, S.A., Madrid
Banco de Sabadell SA
Banco Santander, S.A., Madrid
BANKIA, S.A., Valencia
Barclays Capital Securities Limited, London
Bayerische Landesbank, Munich
Belfius Bank & Insurance, Brussels
BNP Paribas, Paris
BNP Paribas Fortis, Brussels
CAIXABANK, S.A., Barcelona
Citigroup Global Markets Limited, London
Commerzbank Aktiengesellschaft, Frankfurt
Credit Suisse Securities (Europe) Limited, London
Daiwa Capital Markets Europe Limited, London
Deutsche Bank AG, Frankfurt
DZ Bank AG Deutsche Zentral-Genossenschaftsbank, Frankfurt
Eurex Repo GmbH, Frankfurt
EuroMTS Limited, London
HSBC Bank plc, London
HSBC France, Paris
ICAP Securities Limited, London
ING Bank N.V., Amsterdam
ING Belgium SA/NV, Brussels
J.P. Morgan Securities plc, London
Jefferies International Limited, London
KBC Bank N.V., Brussels
KBL European Private Bankers S.A., Luxembourg
LCH.Clearnet Limited, London
Lloyds TSB Bank plc, London
Merrill Lynch International (trading as Bank of America Merrill Lynch), London
Mitsubishi UFJ Securities International plc, London
Morgan Stanley & Co. International PLC, London

NATIXIS, Paris
Nomura International plc, London
Nordea Bank Danmark A/S, Copenhagen
RBC Europe Limited, London
Société Générale S.A., Paris
The Royal Bank of Scotland plc, London
UBS AG, Zurich