International
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ICMA

EUROPEAN REPO AND COLLATERAL COUNCIL

Minutes of the General Meeting of the ICMA European Repo and Collateral Council (ERCC) held on 17 October 2018, in London

Host: Bloomberg

Location: 3 Queen Victoria Street
London EC4N 4TQ

Time: 14:00 - 17:00 (London time)

Presentation slides: Please see Annex A

1. **Welcome remarks by the ICMA ERCC Chairman**

- Mr. Godfried De Vidts, Chairman of the ICMA ERCC, welcomed delegates in the room and thanked Bloomberg for hosting the event.

2. **CSDR mandatory buy-ins and SFTs**

- Mr. Andy Hill, Senior Director, ICMA (see slides on page 1 of Annex A)

3. **SFTR in Focus** (see slides on page 5 of Annex A)

(a) ESMA update

- Mr. Nikolay Arnaudov, Senior Policy Officer, ESMA

(b) Industry implementation work

- Mr. Alexander Westphal, Director, ICMA
- Mr. Andy Dyson, Chief Executive Officer, ISLA

(c) Panel discussion on SFTR implementation

Moderator:
Mr. Richard Comotto, Senior Fellow, ICMA Centre

Panellists:
Mr. Nikolay Arnaudov, Senior Policy Officer, ESMA
Mr. Craig Laird, Vice President, Regulatory Operations, Morgan Stanley
Mr. Dawd Haque, Global lead Market Initiatives, Regulatory Transformation & Strategy, Deutsche Bank
Mr. Tony Holland, Front office solutions, MUFG Securities
Mr. Sander Baauw, Product Management Securities Lending & Collateral Management, Euroclear

4. Legal update

Ms. Lisa Cleary, Senior Director, ICMA (see slides on page 14 of Annex A)

5. Benchmark reform: Update on ongoing work in the euro area

Mr. Pascal Nicoloso, Principal Market Operations Expert, ECB (see slides on page 17 of Annex A)

6. Presentation: Joint ICMA ERCC- GFMA Repo Market Report

Mr. David Hiscock, Senior Director, ICMA and Mr. Jouni Aaltonen, Director, Prudential Regulation, AFME (see slides on page 23 of Annex A)

7. Any other business and next meetings

The next **ERCC General Meeting** will be held on 31 January 2019, 10:00 – 13:00 (UK time), in Luxembourg, kindly hosted by Clearstream in the framework of Deutsche Boerse's annual GFF Summit.

Annex A

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CSDR Mandatory Buy-ins & SFTs

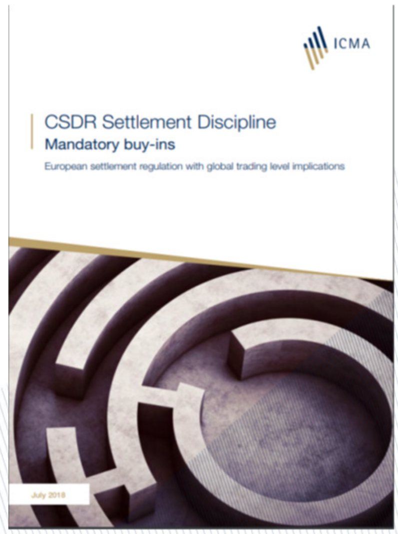
ICMA ERCC General Meeting
London, October 17 2018

Andy Hill, Senior Director, ICMA

- Part of CSD Regulation Settlement Discipline package
- Regulatory technical standards published in EU Official Journal in September 2018
- Will apply from September 14 2020

What is the scope of CSDR Settlement Discipline?

- Settlement Discipline will apply to all transactions intended to settle on an EU CSD[1] in transferable securities, money-market instruments, units in collective investment undertakings, and emissions allowances,[2] which are admitted to trading or traded on a trading venue or cleared by a CCP.[3]
- This will apply to all **trading level entities regardless of their domicile**, that enter into such transactions that settle on an EU CSD, whether directly as CSD members, or indirectly via a settlement or clearing agent (a "CSD participant"). .
- Securities financing transactions (SFTs) are in scope of settlement discipline. [4]
- SFTs with terms ≥ 30 business days are in scope of mandatory buy-ins. [5]

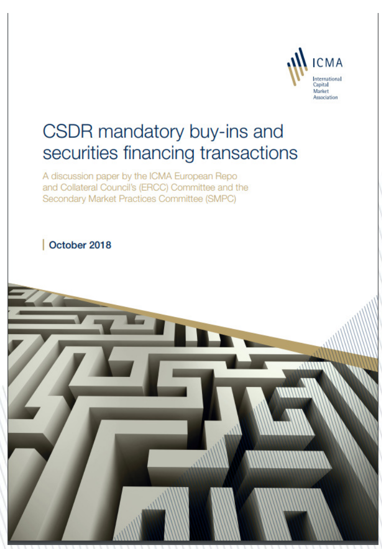


[1] Articles 1(1) and 1(2)
[2] Article 5(1)
[3] Article 7(10)
[4] Article 7(4)(b)
[5] RTS: Article 22(2)

CSDR mandatory buy-ins & SFTs

Challenges of applying mandatory buy-ins to SFTs

- If you buy-in against the start-leg, does the end-leg remain valid?
- If a buy-in against the start-leg results in cash compensation, what happens to the end leg? Does that remain valid?
- How is the settlement of the buy-in/cash compensation determined? Is this based on the price assigned to the start-leg?
- How do you apply the asymmetry to buy-ins against SFTs?
- How do you account for haircuts in determining the appropriate buy-in/cash compensation differential payment? Does the asymmetry still apply in the case of haircuts?
- What happens to open trades if they reach 30 business days?
- Will CCPs require separate netting pools for in- and out-of-scope SFTs?
- How do you manage the buy-in risk in a matched-book with both in- and out-of-scope SFTs?



Addressing the CSDR asymmetry

- ICMA is exploring the possibility of updating its Buy-in Rules (or a version of its Buy-in Rules) to align with the regulatory provisions of CSDR.
- The exception would be that the ICMA Buy-in Rules would allow for a contractual agreement between members or users of the Rules to settle the buy-in (or cash compensation) differential symmetrically.
- This would help to address a number of the more problematic risks arising as a result of the CSDR asymmetry, including:
  - Additional risks to liquidity providers
  - The inability to use pass-ons to settle transaction chains
  - Additional risks to lenders of securities
  - The unlikelihood that non-EU firms will contractually agree to asymmetric buy-ins

Going forward

- ICMA will continue to raise awareness of scope and provisions of the regulation (globally)
- ICMA will continue to engage with members, other TAs, and ESMA to establish best practice and practical solutions to support implementation, both for bond and SFT markets
- ICMA will continue to convey members' concerns to regulators and policy makers with respect to potential adverse market impacts

Regulatory texts:

CSD- Regulation (EU) No 909/2014 ["Level 1"]

Delegated Regulation ("Level 2") 25.5.2018 [RTS for mandatory buy-ins]

CSDR Frequently Asked Questions (September 2014)

ICMA resources:

CSDR mandatory buy-ins and SFTs
October 2018 (Discussion Paper)

CSDR Settlement Discipline: mandatory buy-ins
July 2018 (Information Brochure)

How to survive in a Mandatory Buy-in World
June 2018 (Discussion Paper)

More information and resources can be found on the dedicated CSDR-SD page on the ICMA website:
https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Secondary-Markets/secondary-markets-regulation/csdr-settlement-discipline/

CSDR mandatory buy-ins & SFTs

Industry implementation work

Alexander Westphal, Director, ICMA

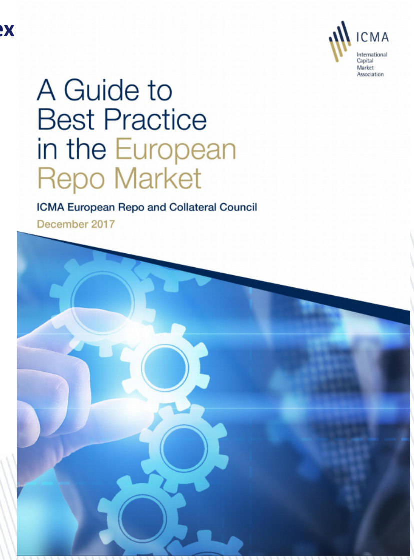
ICMA ERCC work on SFTR – an evolving agenda

- **Repo market transparency among the cornerstones of the ERCC's work**
  - Bi-annual European Repo Market survey compiled since 2001 (35th edition just published)
  - ERCC Ops involved from the start in the global discussions on repo market transparency
  - ERCC White Paper on Enhancing the transparency of the European repo market (October 2013)
- **ICMA ERCC SFTR Task Force** formally established in 2015 to respond to ESMA's consultations on SFTR technical standards
  - Chair: Craig Laird (Morgan Stanley) (since June 2018), vice-chair: Darryl Hockings (SocGen)
  - Membership covers broad range of market participants (sell-side & buy-side) & continues to grow
  - In late 2017, membership of the TF was extended to include relevant service providers (vendors and TRs)
  - Main aim of the group is to facilitate implementation by providing common definitions and market best practices
  - Close collaboration across SFT industry is key, including with other relevant associations (ISLA, AFME,…)

ICMA ERCC work on SFTR

The ERCC Guide to Best Practice - SFTR Annex

- Guide initially published in March 2014 and reviewed on an ongoing basis
- Sets out detailed standards for the orderly trading and settlement of repo
- Dedicated SFTR Annex with reporting best practices being developed by the SFTR TF – rapidly growing
- Ongoing engagement with ESMA to seek guidance on open questions and validation of any SFTR market practice recommendations



Click on the picture to download

ICMA ERCC work on SFTR

Some issues that we are looking at…

- **Reporting of buy/sell-backs**
  - Around 14% of outstanding repos (ERCC survey Dec 2017)
  - Vast majority documented under GMRA, but SFTR (Level 1) definition restricts buy/sell-backs to undocumented trades
- **UTI generation and distribution**
  - ESMA decision tree for UTI generation generally workable, but some questions remain, e.g. generation of UTIs for CCP-cleared trades during the transition period
  - Sharing of UTIs (OTC) – industry agreement needed?
- **Variation margining**
  - Separate margin report defined by ESMA – but only applicable to CCP-cleared trades
  - For bilateral trades: Initial margin/haircut reported as part of the trade report, but no express provision in the draft RTS for variation margining
  - Recommendation to report as (daily) collateral update – but needs to be on a position/net exposure basis

ICMA ERCC work on SFTR

Some issues that we are looking at…

- **Backloading**
  - SFTR requires backloading of trades executed prior to reporting go-live, as follows:
    - Fixed term repo, if remaining maturity on go-live > 180 days
    - Open repo, if still outstanding 180 days after go-live
    - Report in both cases required between 180 – 190 days after go-live
  - A number of practical problems - common industry approach needed given that reports need to match
- **Reporting of collateral reuse**
  - Daily reporting at ISIN level but only on S+1
  - Reuse estimate to be calculated based on the FSB's "approximate measure"
  - Ongoing discussions on the components of the formula

$$collateral_{ij}^{reused} = \left(\frac{collateral_{ij}^{received,eligible\_for\_reuse}}{collateral_{ij}^{received,eligible\_for\_reuse} + assets_{ij}^{own}}\right) \times \left(collateral_{ij}^{posted}\right)$$

ICMA ERCC work on SFTR

Beyond the SFTR Annex…

- **Field-by-field analysis & ESMA validation logic**
  - ESMA shared a first draft of the SFTR validation rules in Oct 2017 – ERCC comments submitted
  - Additional questions/issues highlighted by ICMA's bilateral reconciliation exercise and further analysis
  - Further focus sessions with TF members to go through the reporting tables, field-by-field and validate field contents and validation logic
  - Important complement to the work on the SFTR Annex
- **Template reports**
  - More than 10 trade scenarios covered so far
  - Number of required fields ranging between 45 – 60 for each new trade
  - Covers new transactions, but also subsequent lifecycle reports (substitution, early termination etc.)

Template reports

Reporting scenario (new transaction report)	# fields required
OTC buy/sell-back (documented)	46
OTC buy/sell-back (undocumented)	43
OTC Repo (fixed term, fixed rate)	50
OTC Repo (fixed term, floating rate)	58
OTC Repo (forward)	50
OTC Repo (open, fixed rate)	48
OTC Tri-party Repo (open, fixed rate) (+subsequent collateral update)	37 (+22)
Voice-brokered Repo (fixed term, fixed rate)	51
CCP-cleared Repo (fixed term, fixed rate)	55

Industry implementation work

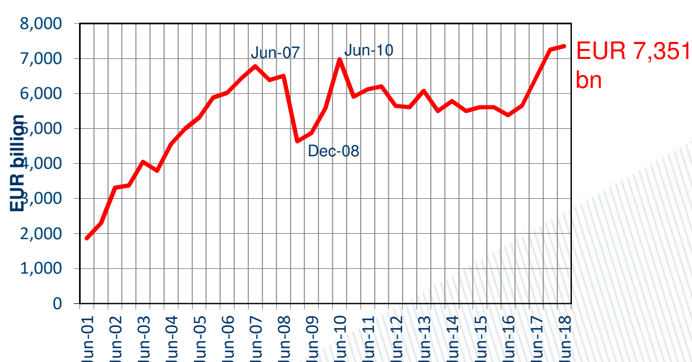
Andy Dyson, Chief Executive Officer, ISLA

Results of the 35th semi-annual repo survey

Richard Comotto, ICMA Centre at Reading University

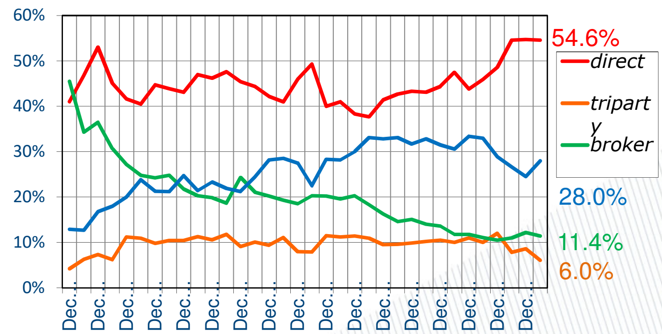
35th European repo market survey conducted in June 2018

Headline numbers



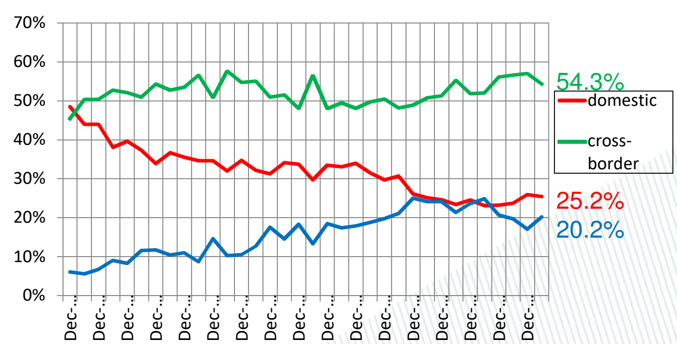
35th European repo market survey conducted in June 2018

Trading Analysis



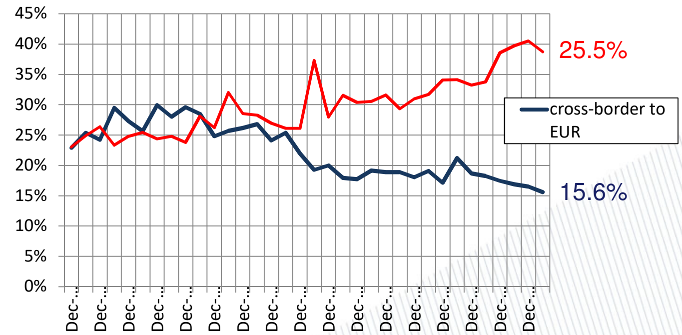
35th European repo market survey conducted in June 2018

Geographical Analysis



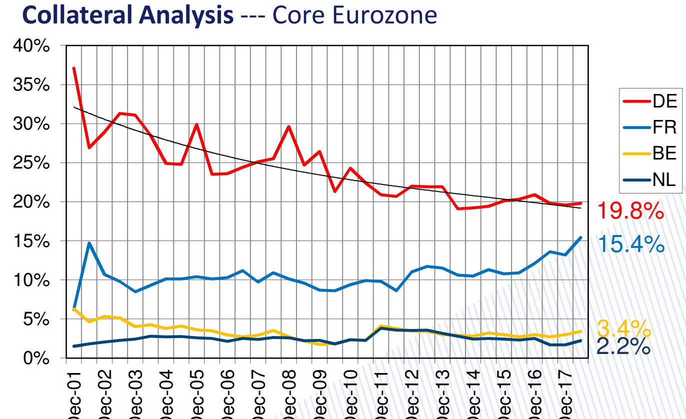
35th European repo market survey conducted in June 2018

Geographical Analysis



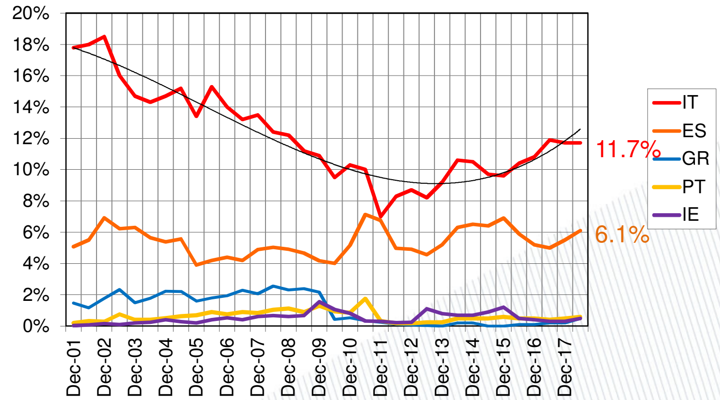
35th European repo market survey conducted in June 2018

Collateral Analysis --- Core Eurozone



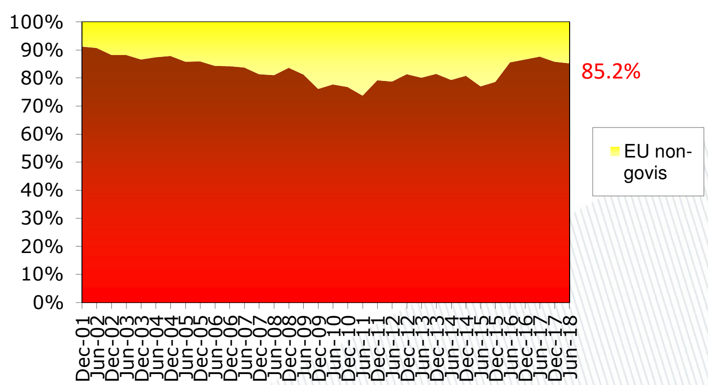
35th European repo market survey conducted in June 2018

Collateral Analysis --- Peripheral Eurozone



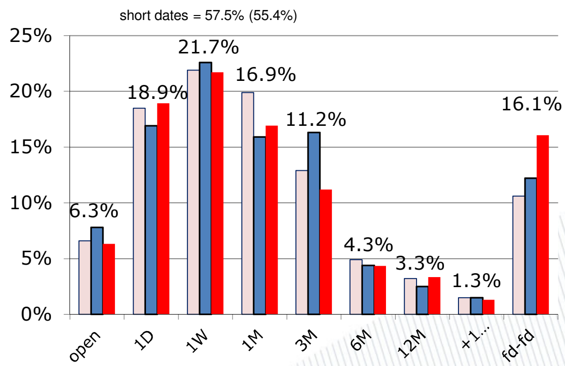
35th European repo market survey conducted in June 2018

Collateral Analysis



35th European repo market survey conducted in June 2018

Maturity Analysis



Panel discussion on SFTR implementation

Moderator:
Richard Comotto, ICMA Centre at Reading University

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Tony Holland, Front office solutions, MUFG Securities
Sander Baauw, Product Management Securities Lending & Collateral Management, Euroclear

Legal Update

Lisa Cleary, Senior Director, Associate Counsel, ICMA

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Coverage of GMRA 1995

- The ERCC committee have taken the decision to discontinue coverage of the GMRA 1995 in the GMRA legal opinions from 2019 onwards.
- The GMRA legal opinions will continue to cover:
  - GMRA 1995 as amended by the Amendment Agreement; and
  - GMRA 1995 as amended by the 2011 GMRA Protocol (subject to certain elections)
- The opinions will not cover annexes to the GMRA 1995 or changes to the core provisions of the GMRA 1995.

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ERCC Initial Margin pledge project

- ERCC sponsored project:
  - Developing a ‘Initial Margin Pledge Structure’ whereby the ‘haircut’ or initial margin (IM) in a repo transaction is secured on a pledge basis. Ideally this would be documented separately from the GMRA so as to protect the title transfer characteristics of the master agreement but there would need to be a robust linkage between the GMRA and the pledge document to ensure they were executed simultaneously and for the purposes of netting.
  - Developing a ‘Secured Loan Agreement’ which would provide for raising cash against pledged securities.

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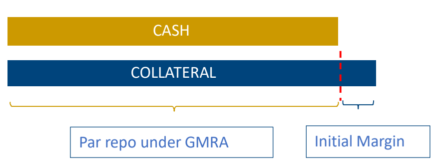
ERCC Initial Margin pledge project



Glossary

GMRA	Global Master Repurchase Agreement
RWA	Risk Weighted Asset
E	Exposure
C	Collateral
RA	Risk adjustment
EAD	Exposure at default for regulatory purposes

Current treatment for standard GMRA transaction:	**Treatment for IM Pledge Structure:**	**Saving using IM Pledge Structure:**
	The IM of 5MM would attract **zero exposure** on that basis that the IM is segregated in a pledge account.	
EAD = 105MM -100MM + 2.9694MM EAD = 7.969MM RWA (@100%) = 7.969MM Capital (@10%) = 0.797MM	EAD = 100MM – 100MM + 2.828MM EAD = 2.828MM RWA (@100%) = 2.828MM Capital (@10%) = 0.283MM	EAD = 5.141MM RWA = 5.141MM Capital = 0.514MM
Regulatory risk adjustment of 2.828 % of Exposure (105MM).	Regulatory risk adjustment of 2.828% of Exposure (100MM).	

The numbers in this example are for illustrative purposes only.

ERCC Initial Margin pledge project

- ERCC legal working group action item
- Phase I
  - Development of IM Pledge Structure and outline triparty control agreement
  - Discussions with triparty service providers to customise control agreements
  - Preparation of legal opinions to support use of IM Pledge Structure
  - Preparation of associated guidance notes
- Phase II
  - Development of Secured Loan Agreement

GMRA and Brexit

- ICMA work
- Governing law of the GMRA
- FAQ on GMRA & Brexit
- Legal opinion scheduling

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Contact

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ECB-PUBLIC

EUROPEAN CENTRAL BANK
EUROSYSTEM

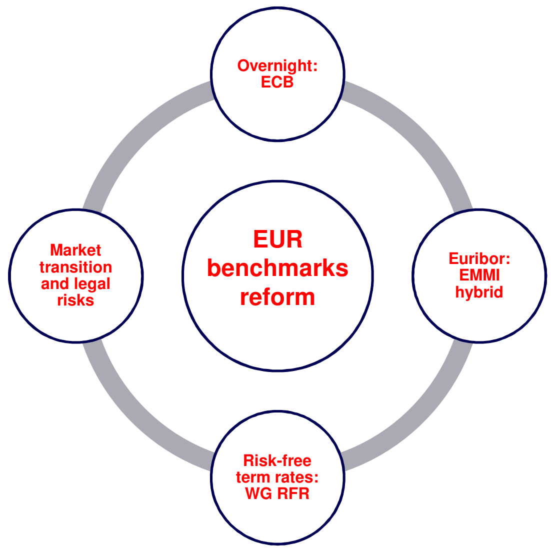
Pascal Nicoloso
ECB
DG Markets
Money Market and Liquidity Division

Benchmark reform – Update on ongoing work in the euro area

Presentation to the ERCC
London, 17 October 2018

Foreword

Benchmark reform: multiple dimensions and actors



Foreword

- Why involve ECB?
- How does ESTER work
- Transition is on its way
- Challenges ahead

EONIA reform efforts at risk, ECB stepped in

- EONIA **low underlying volumes, high panel concentration: not compliant with the Benchmark Regulation**
- Banks leaving the panel
- EMMI and the panel banks announced the end of reform efforts early 2018: EONIA cannot be used in new contracts as of 1/1/2020
- Given the systemic importance of benchmark rates reform, ECB announced in September 2017:
  - The production of an overnight unsecured rate by October 2019
  - The setup of the Working Group on risk-Free Rates (WG RFR) led by ING, with ECB in charge of Secretariat

New tasks for ECB

- **ESTER**
  - Rate production
  - Administrator
  - Testing/MMSR upgrade
- **WG RFR**
  - Secretariat
  - 4 sub-groups
  - Roundtable event 9 November

Do you want to know more?

ECB webpage on Interest rate benchmarks
https://www.ecb.europa.eu/paym/initiatives/interest_rate_benchmarks/html/index.en.html

Main features of the rate

Scope: unsecured overnight deposits to measure borrowing costs

Calculation: weighted average, trimming 25%

Data sufficiency policy: contingency triggers (20 banks, 75% top 5 banks' concentration ratio)

Governance and processes: ESTER published by 9:00 am Frankfurt time

Publication policy and transparency on errors

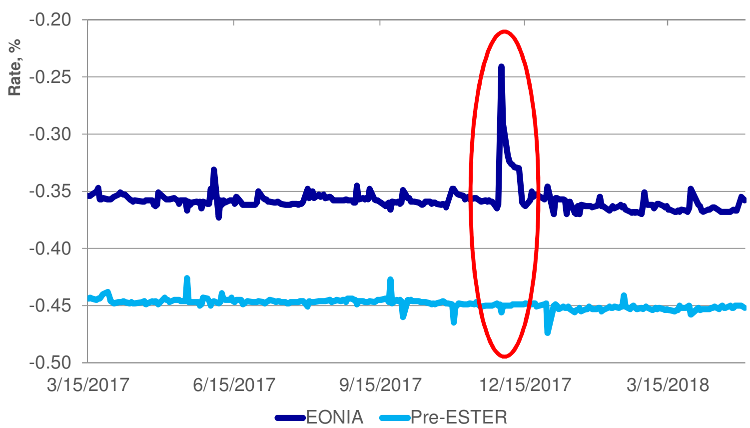
Rate published daily by October 2019

Pre-ESTER publications since 28 June

Do you want to know more?

Parameters more detailed in the statement of methodology
https://www.ecb.europa.eu/paym/initiatives/interest_rate_benchmarks/shared/pdf/ecb.ESTER_methodology_and_policies.en.pdf

ESTER is quite stable



Source: ECB pre-ESTER publication

In sum:
- **Rate reacts to market factors (Excess Liquidity, rate falls at quarter-ends)**
- **While being less vulnerable to outliers**
- **Pre-ESTER (post corrections) very similar to ESTER (based on 7:00 data)**

 ECB-PUBLIC

A new rate is born

August 2018

Public consultation: 88% of respondents in favour of ESTER versus GC Pooling-Repo Funds

13 September 2018

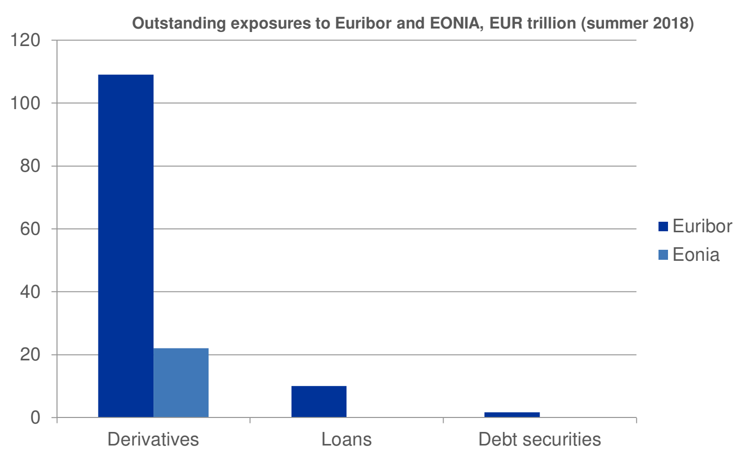
ESTER selected by WG RFR as EONIA replacement

PR 13 September: ESTER […] will be produced by ECB at the latest as of October 2019

Why not a secured rate comparable to SOFR: is volume everything?

 ECB-PUBLIC

Wholesale versus retail



Sources: ESMA, ECB.

Disclaimer: trade repository (TR) data reported under EMIR may be subject to future revisions, reflecting possible data quality issues and reporting completeness. The figures are only intended to provide a broad overview of EU derivatives markets for internal discussion background and should not be used for policy decisions.

Europe transition: divergences and similarities with UK and US

- **Overnight: EONIA replacement**
  - Unsecured
  - Work on transition schema
  - Divergence with US SOFR, similar with UK
- **Term risk-free rates**
  - WG work on-going
  - Derivatives based on risk-free
  - Similarity with UK-US
- **Euribor**
  - EMMI: hybrid methodology
  - Euribor reform
  - Divergence with LIBOR

BMR PROLONGATION BY 2 YEARS REQUESTED BY THE WG RFR

Legal options to ensure smooth EONIA transition and Euribor reform

- Bilateral agreements
- Multilateral agreements (protocols, standards etc)
- Regulatory amendments involving European or National law
- Public authorities' support (statements, speeches)

=> No easy or mutually exclusive options

Joint ICMA ERCC-GFMA Repo Market Report

Jouni Aaltonen, Director, AFME

David Hiscock, Senior Director, ICMA

Joint ICMA ERCC-GFMA Repo Market Report

- Why is this study being produced at this time?
  - Following a decade of financial regulatory reform
    - Work is still continuing to implement various elements of the reform programme
    - Additional elements of the reform programme continue to be worked on
    - Official efforts are being made in Europe and by the global bodies to assess the coherence and calibration of reforms
  - So now is the time to take stock and contribute to the debate
    - In this context a new global repo market study is being produced
    - Based on joint input from the ICMA ERCC and the GFMA
    - Publication is anticipated in the coming weeks

Joint ICMA ERCC-GFMA Repo Market Report

- What will be the content of the study?
  - The study's executive summary, conclusions and recommendations will be supported by detailed material outlining:
    - Why the repo market is important
    - How the repo market performed during the crisis and what was driving the behaviour
    - What initial assessment was made of this performance and behaviour
    - Whether the risks identified have been addressed by the implemented post-crisis reforms
    - If the post-crisis regulatory framework is commensurate to the risks in repo markets
    - How the repo market has changed subsequent to the crisis

Joint ICMA ERCC-GFMA Repo Market Report

- How has the study been performed?
  - Detailed review and synthesis of official and market participant research papers
  - Supporting qualitative market survey
  - Detailed QIS to assess further proposals regarding haircut requirements

Joint ICMA ERCC-GFMA Repo Market Report

- What is the study expected to show?
  - The repo market is a cornerstone of financial markets – vital to both public & private sectors
  - Repos' role in the financial crisis was quite significantly overstated
  - Reforms based on inaccurate analysis were over-calibrated
  - Much good reform has been done, but repo markets have been overly impacted
  - Repo markets are adapting, but there is clear evidence of the stresses they face
  - Careful reappraisal at this stage should inform the process of finalising reforms
  - Some steps already taken should be recalibrated in light of impact assessments

Closing remarks

Godfried De Vidts, Director of European Affairs, NEX