

# ICMA European Repo and Collateral Council General Meeting

17 October 2018, London





# **Welcome remarks by the ERCC Chair**

**Godfried De Vidts, Director of European Affairs, NEX**





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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<sup>1</sup> in transferable securities, money-market instruments, units in collective investment undertakings, and emissions allowances,<sup>2</sup> which are admitted to trading or traded on a trading venue or cleared by a CCP.<sup>3</sup>
- 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.<sup>4</sup>
- SFTs with terms  $\geq 30$  business days are in scope of mandatory buy-ins.<sup>5</sup>

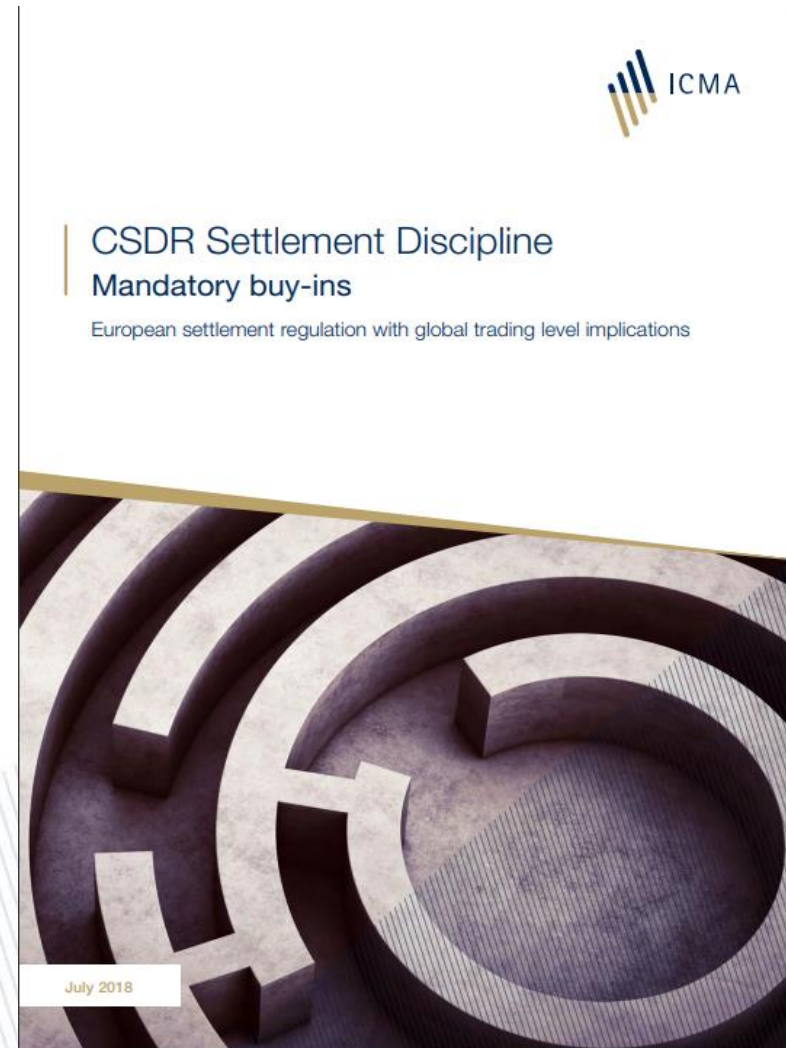
<sup>1</sup> Articles 1(1) and 1(2)

<sup>2</sup> Article 5(1)

<sup>3</sup> Article 7(10)

<sup>4</sup> Article 7(4)(b)

<sup>5</sup> RTS: Article 22(2)



## Challenges of applying mandatory buy-ins to SFTs

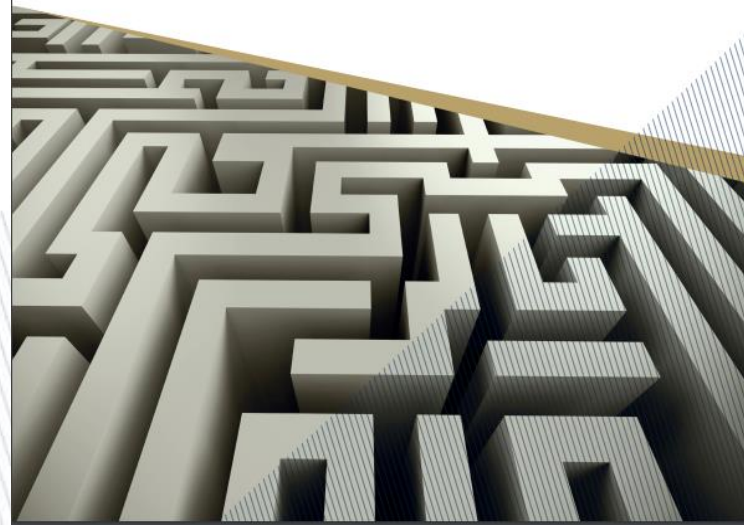
- If you buy-in against the start-leg, does the end-leg remain valid?
- If a buy-in against the start-leg results in cash compensation, what happens to the end leg? Does that remain valid?
- How is the settlement of the buy-in/cash compensation determined? Is this based on the price assigned to the start-leg?
- 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?



## CSDR mandatory buy-ins and securities financing transactions

A discussion paper by the ICMA European Repo and Collateral Council's (ERCC) Committee and the Secondary Market Practices Committee (SMPC)

October 2018



## 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/csd- settlement-discipline/>

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# **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 (35<sup>th</sup> 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,...)

### 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



### A Guide to Best Practice in the European Repo Market

ICMA European Repo and Collateral Council  
December 2017



Click on the picture to download

### 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

## 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

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



### 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



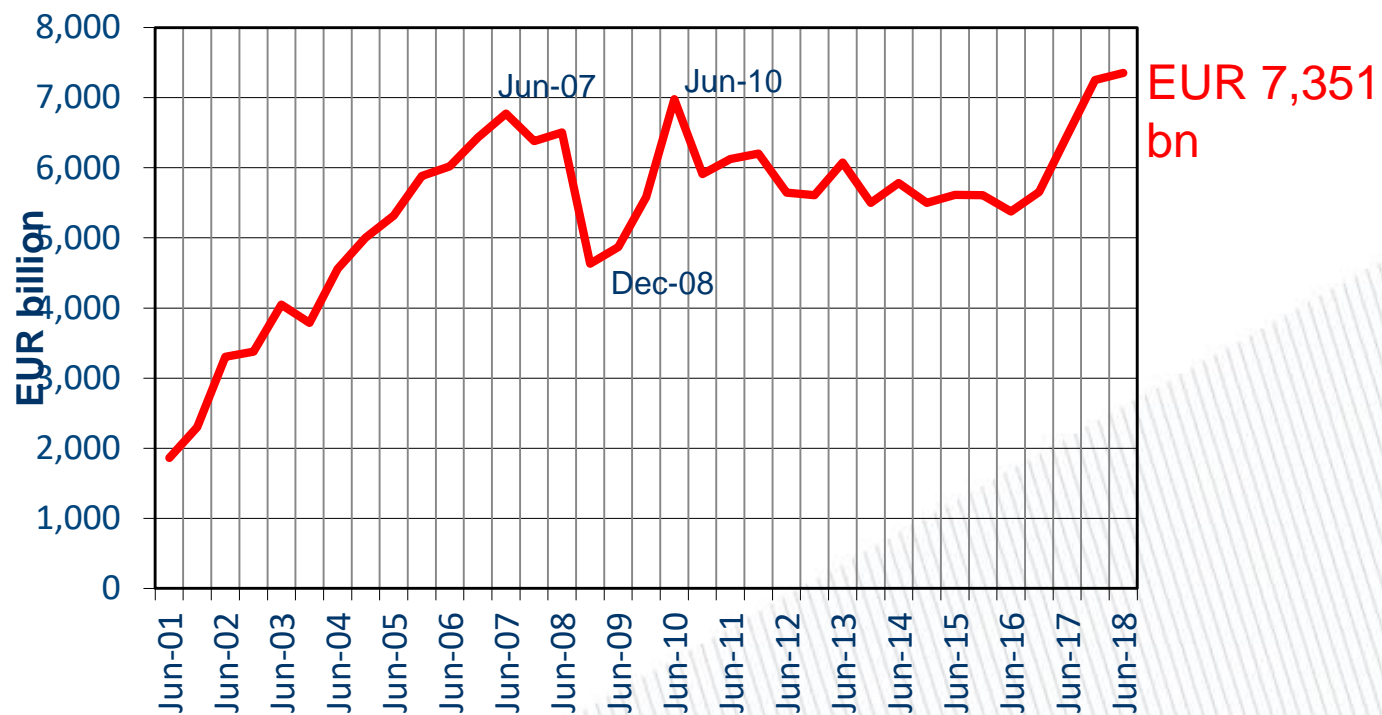


# **Results of the 35th semi-annual repo survey**

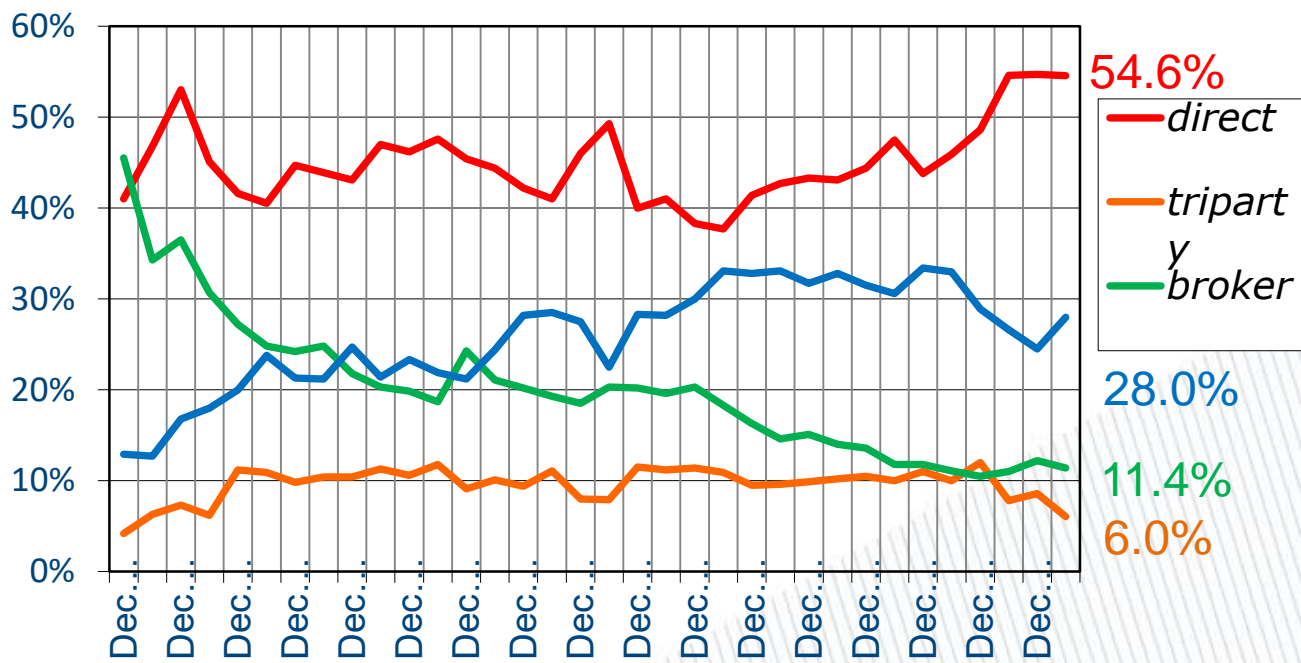
**Richard Comotto, ICMA Centre at Reading University**



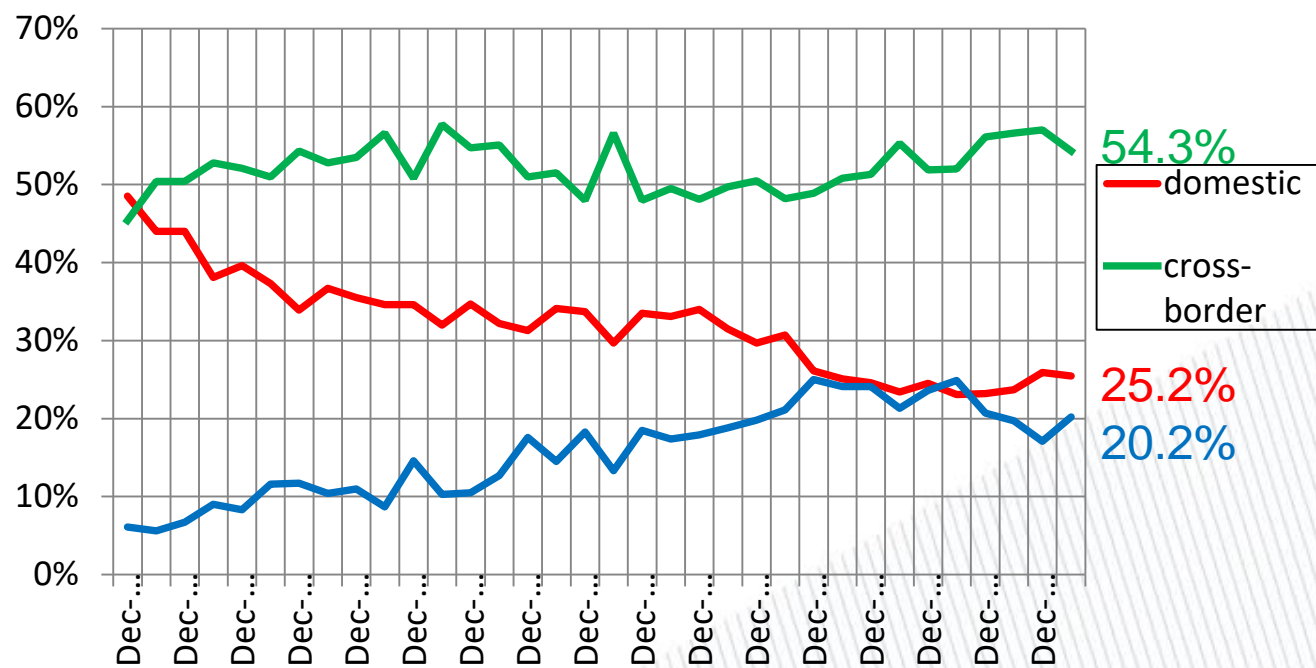
## Headline numbers



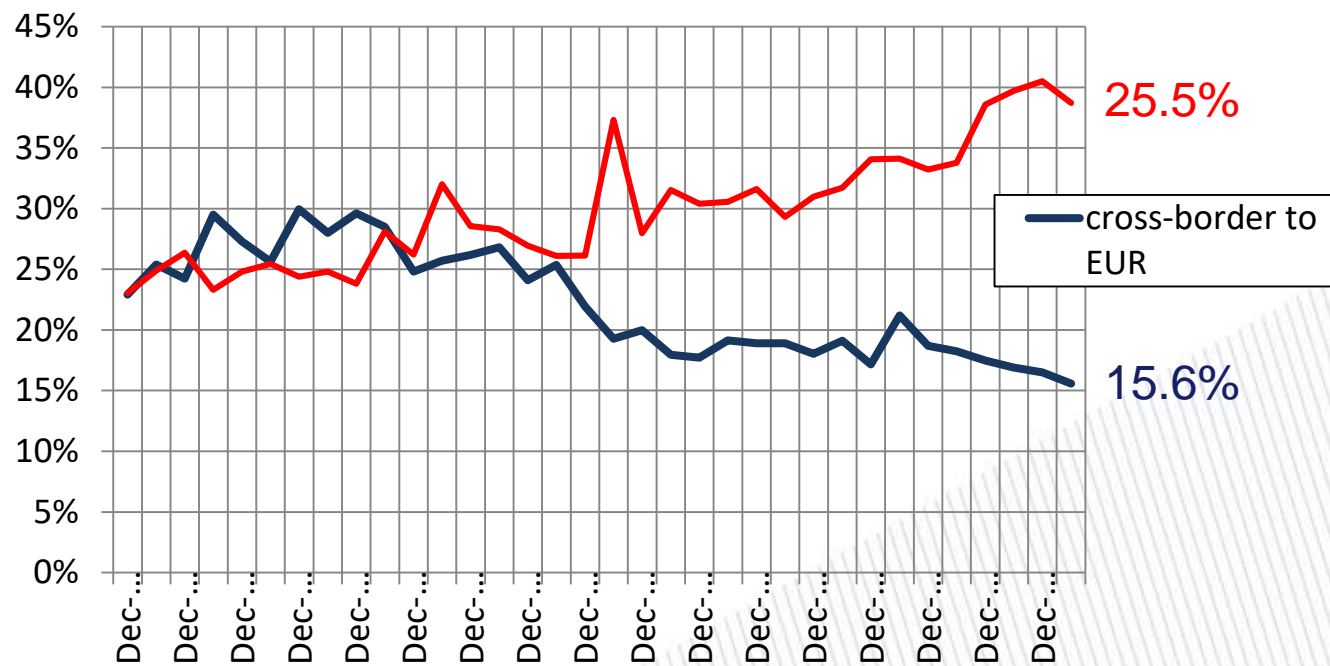
## Trading Analysis



## Geographical Analysis

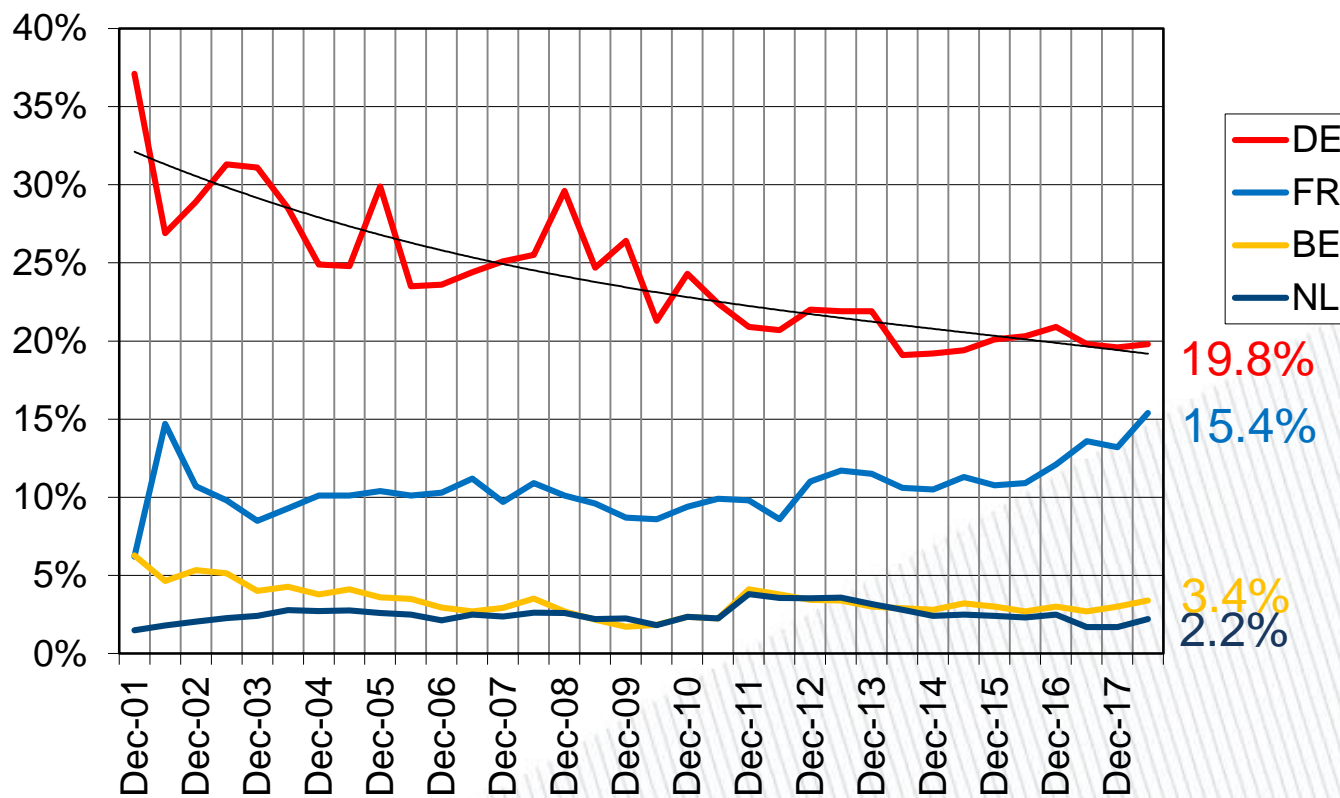


## Geographical Analysis

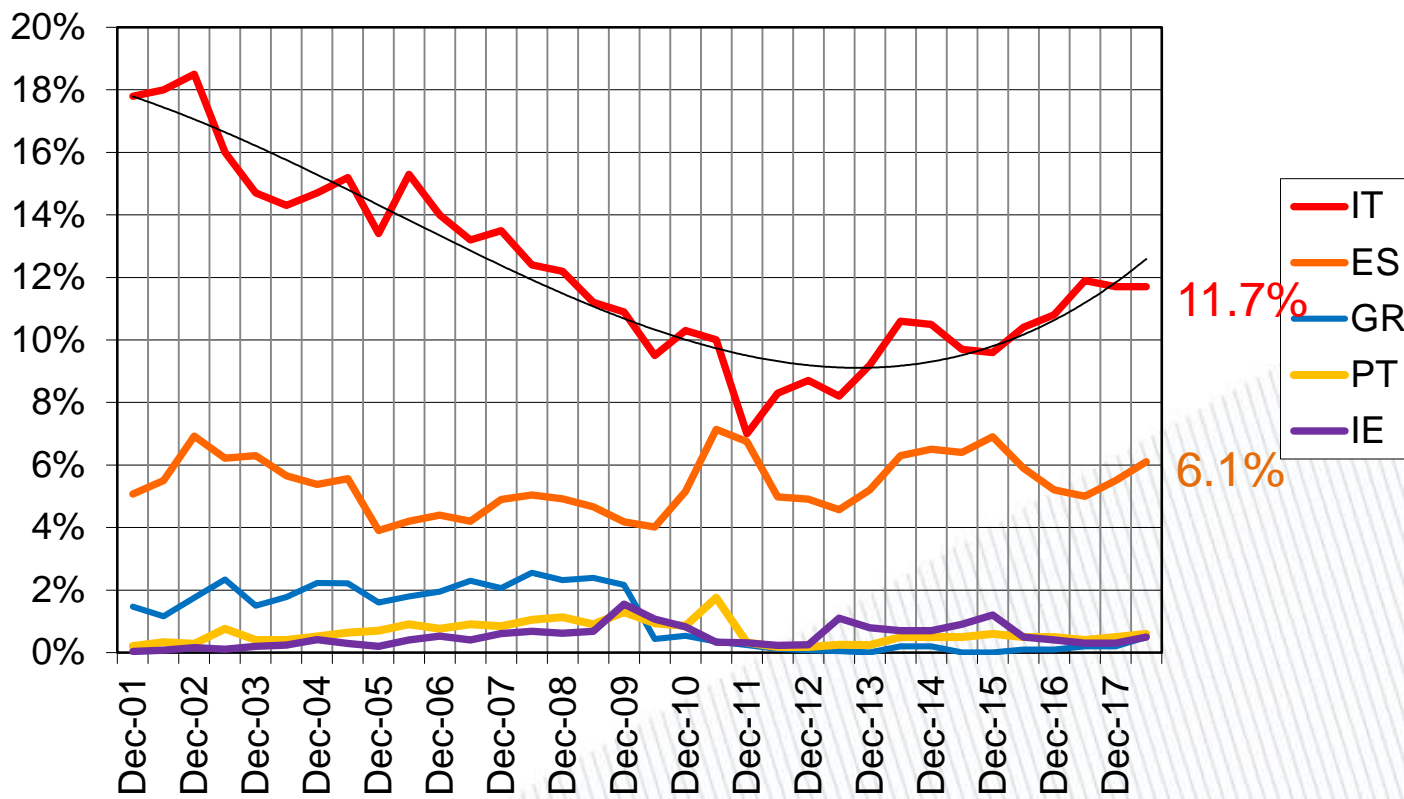




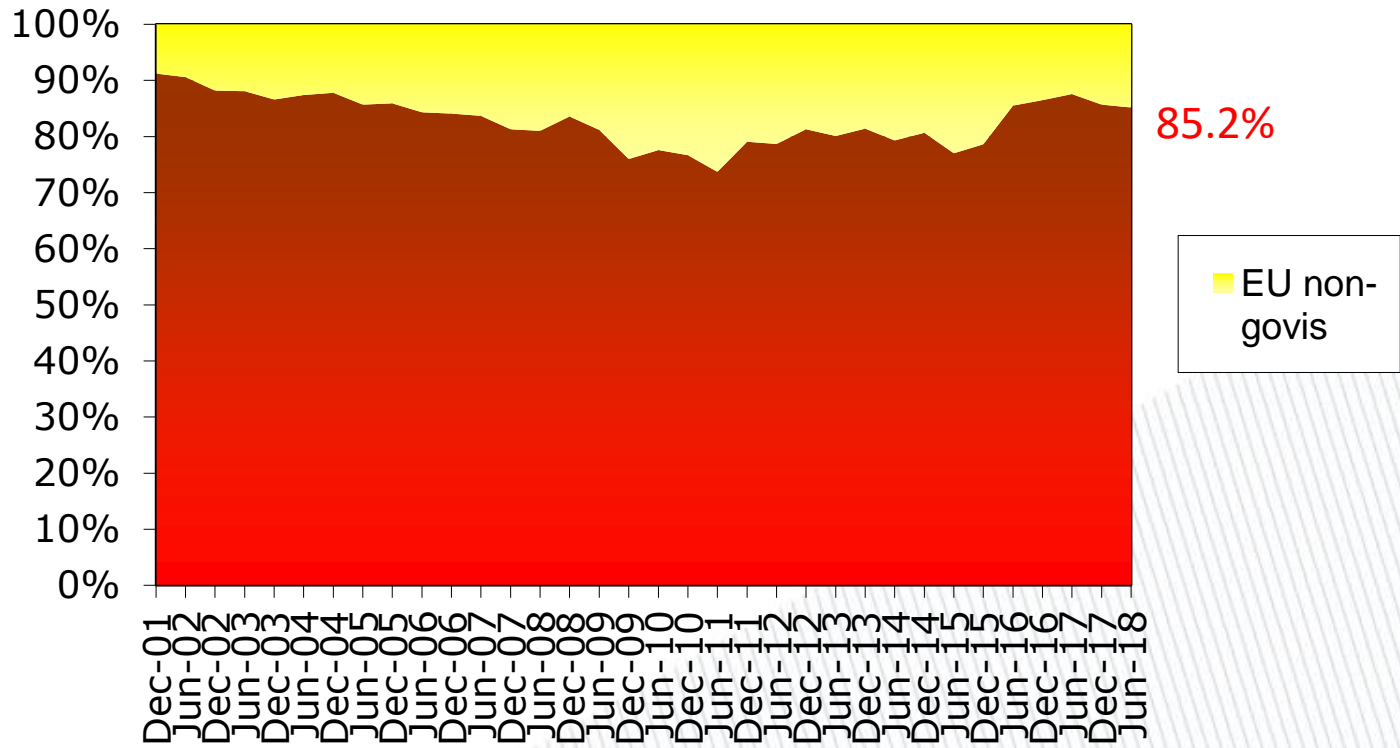
### Collateral Analysis --- Core Eurozone



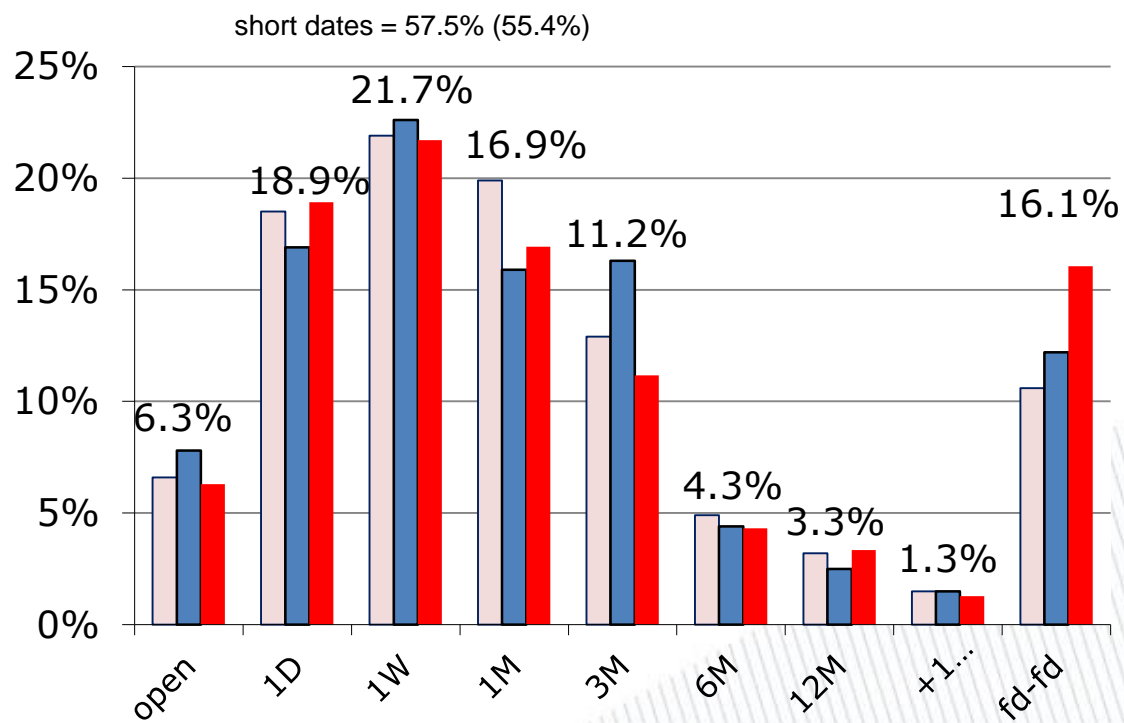
## Collateral Analysis --- Peripheral Eurozone



## Collateral Analysis



## Maturity Analysis





# Panel discussion on SFTR implementation

Moderator:

**Richard Comotto**, ICMA Centre at Reading University

Panellists:

**Nikolay Arnaudov**, Senior Policy Officer, ESMA

**Craig Laird**, Vice President, Regulatory Operations, Morgan Stanley

**Dawd Haque**, Global lead Market Initiatives, Regulatory Transformation & Strategy,  
Deutsche Bank

**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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International Capital Market Association

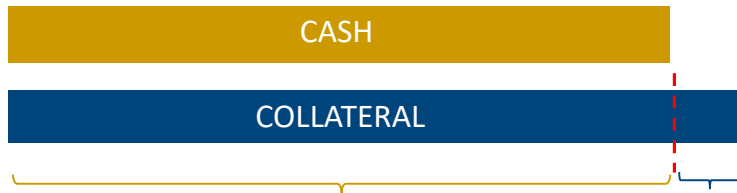
# Coverage of GMRA 1995

- 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.

- 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.



# ERCC Initial Margin pledge project



Par repo under GMRA

Initial Margin

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

**Current treatment for standard GMRA transaction:**

EAD = 105MM - 100MM + 2.9694MM  
 EAD = 7.969MM  
 RWA (@100%) = 7.969MM  
 Capital (@10%) = 0.797MM

Regulatory risk adjustment of 2.828 % of Exposure (105MM).

**Treatment for IM Pledge Structure:**

The IM of 5MM would attract **zero exposure** on that basis that the IM is segregated in a pledge account.

EAD = 100MM – 100MM + 2.828MM  
 EAD = 2.828MM  
 RWA (@100%) = 2.828MM  
 Capital (@10%) = 0.283MM

Regulatory risk adjustment of 2.828% of Exposure (100MM).

**Saving using IM Pledge Structure:**

EAD = 5.141MM  
 RWA = 5.141MM  
 Capital = 0.514MM

*The numbers in this example are for illustrative purposes only.*

- 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



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# 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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EUROSYSTEM

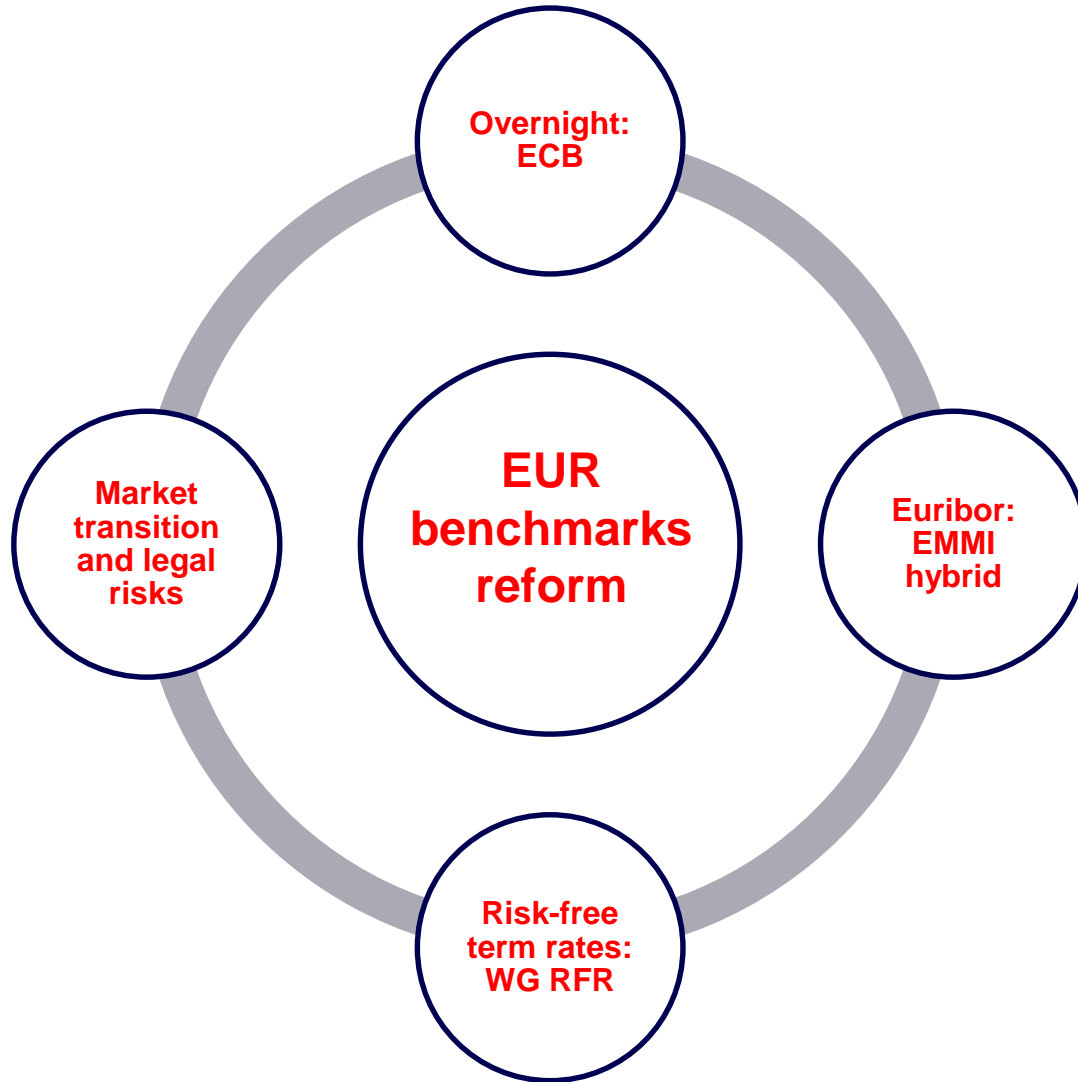
**Pascal Nicoloso**  
ECB  
DG Markets  
Money Market and Liquidity Division

# **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

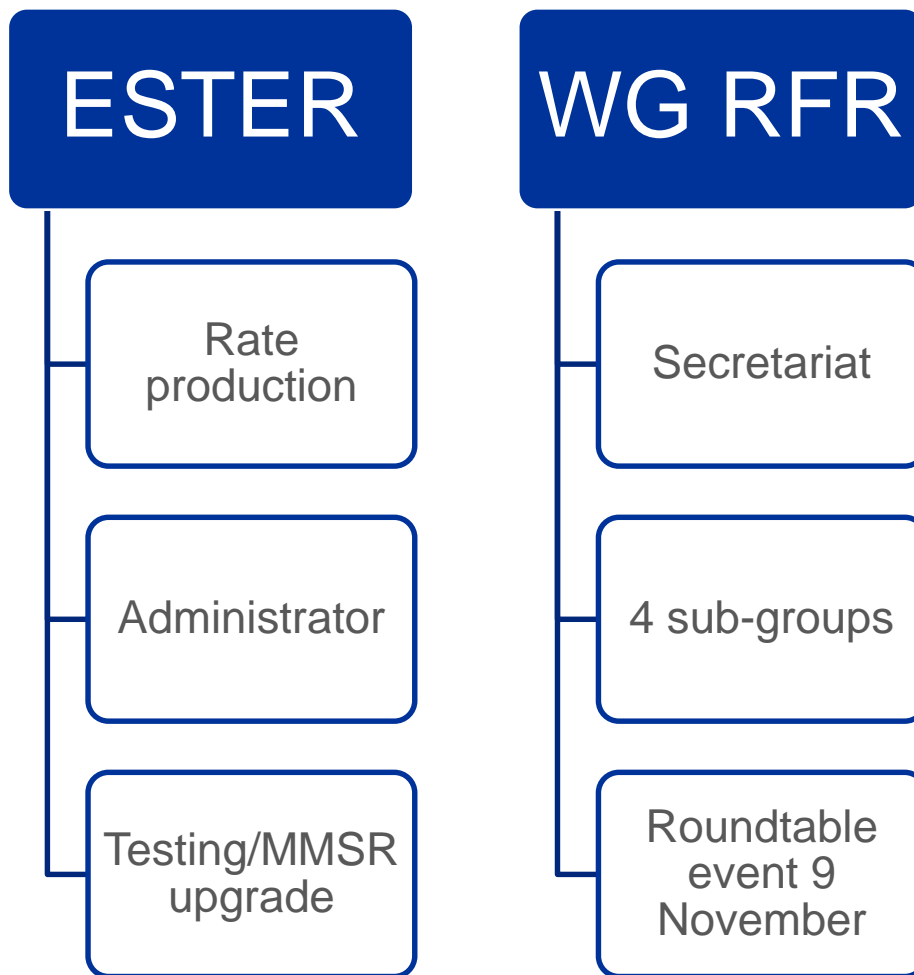
Challenges ahead

## 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



**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](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

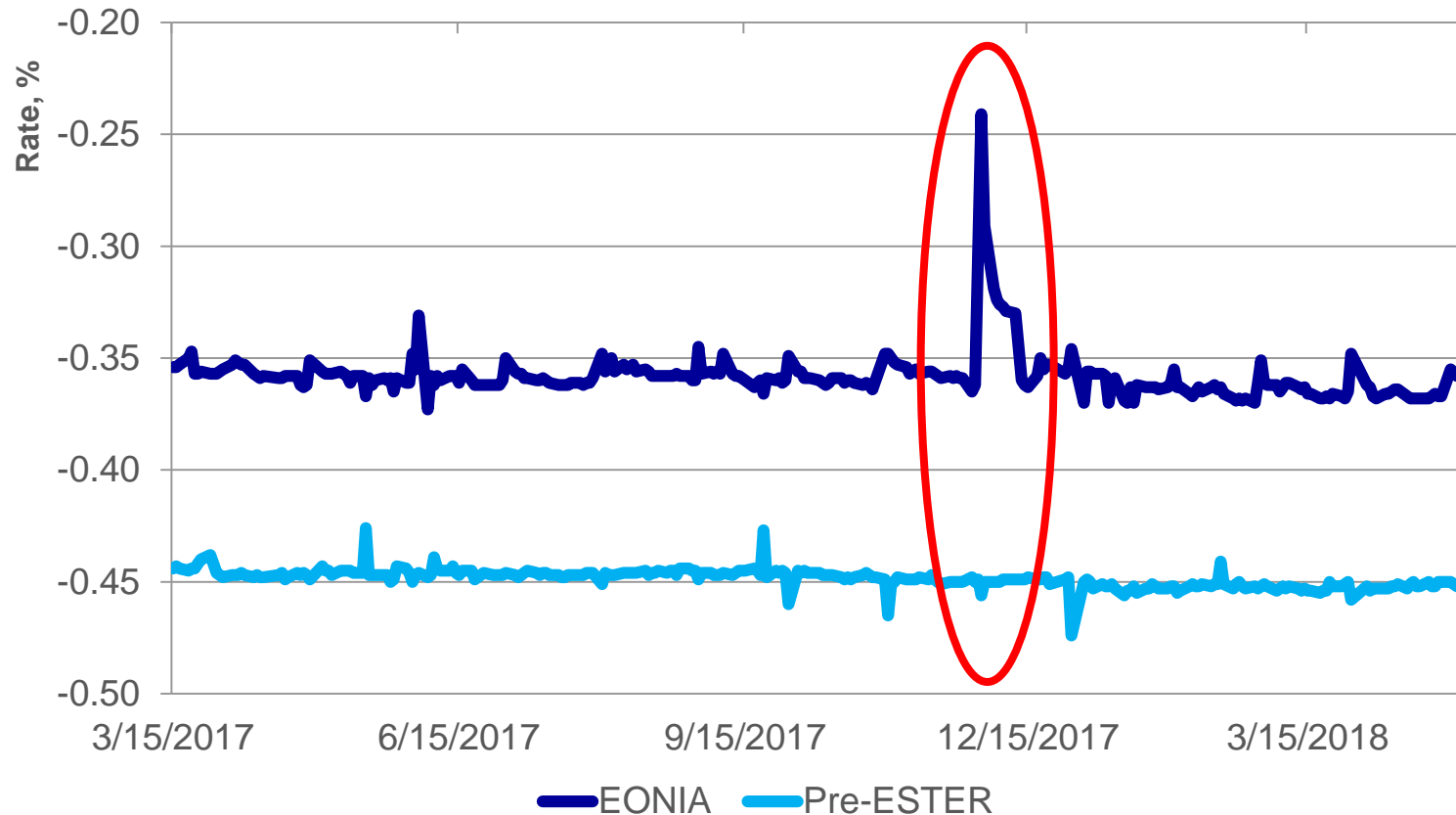
Publication policy and transparency on errors

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/share\\_d/pdf/ecb.ESTER\\_methodology\\_and\\_policies.en.pdf](https://www.ecb.europa.eu/paym/initiatives/interest_rate_benchmarks/share_d/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)

## A new rate is born

August 2018

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

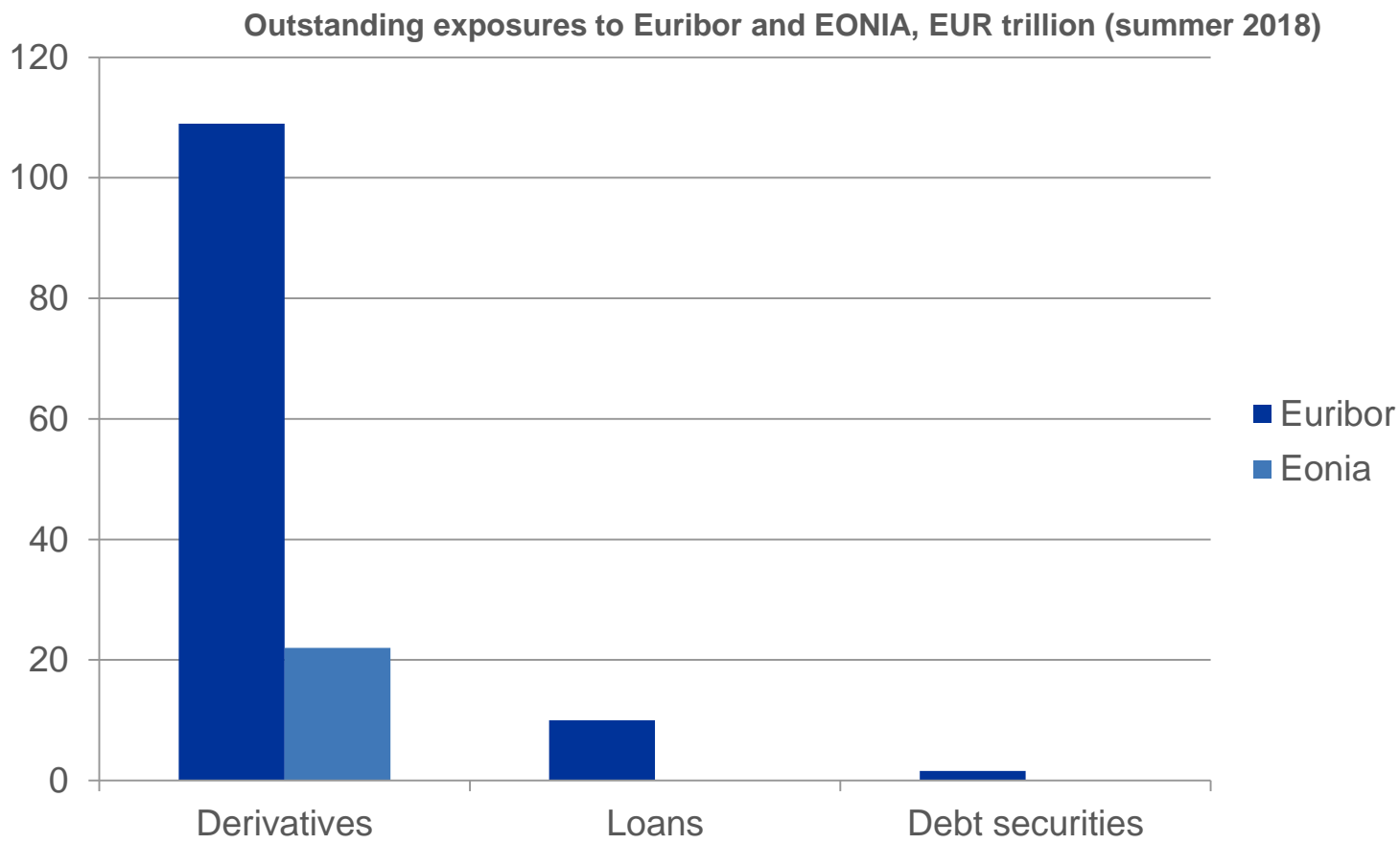
13 September  
2018

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?

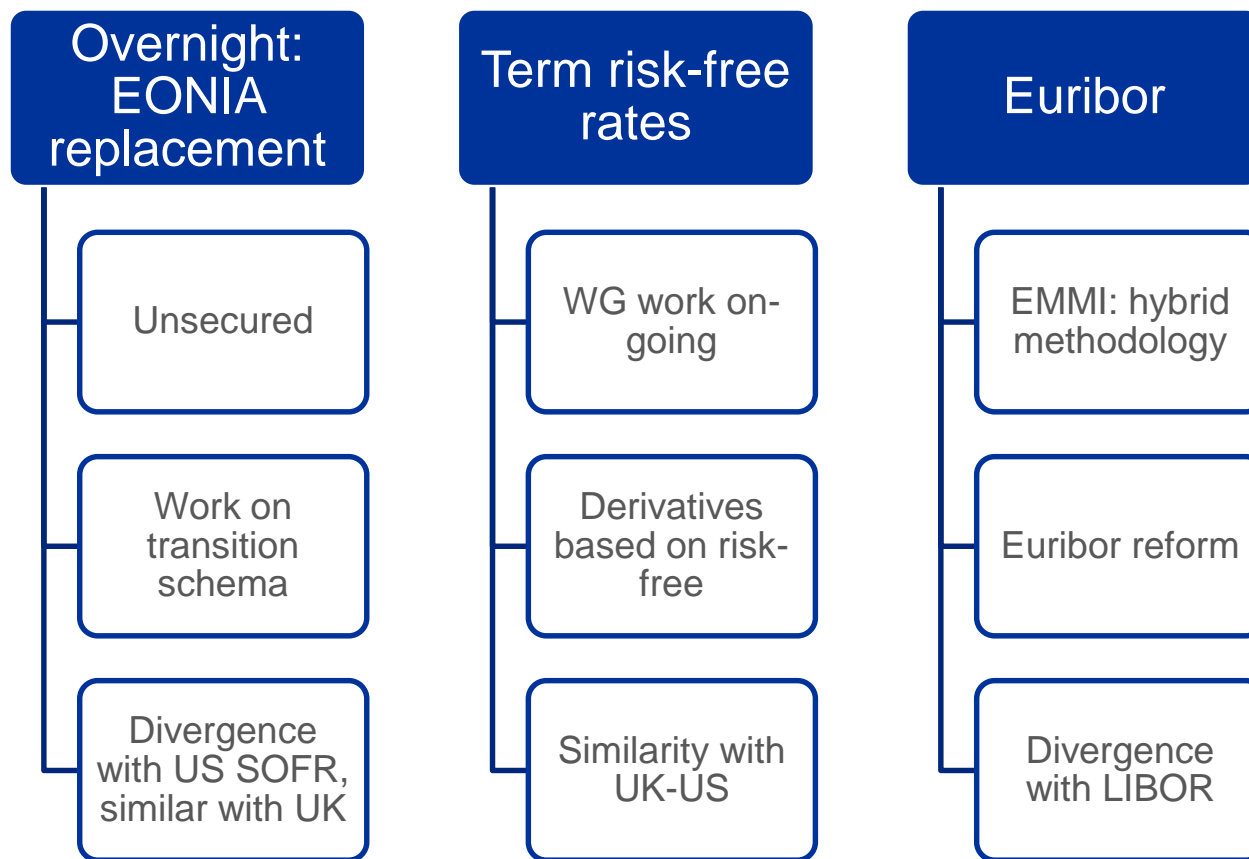
# Wholesale versus retail



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



**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



## ERCC Annual General Meeting 2019

- **Thursday 31 January 2019, 10:00 – 13:00 (CET)**
- Hosted by **Clearstream** in Luxembourg (in the margins of the Annual GFF Summit)

Please join us  
for a networking  
drinks reception

