

# **Minutes of the European Repo Council General Meeting held on May the 14, 2002 in Vienna**

**Location:** Bank Austria  
"Oktogon" 1 Floor  
Schottengasse 6  
1010 Wien

**Time:** 14:00hrs- 16:00hrs

**Date:** Tuesday 14 May 2002

## **1. Welcome by the Chairman of the ERC**

### 1.1 Welcome words

The chairman welcomed all members of the ERC, ISMA, ACI, observers especially those from TBMA) as well Mr Günter Toifl who is ISMA's regional chairman for Austria, Eastern and South Eastern Europe.

The ERC meetings are held three times a year, and by moving to different cities in Europe the ERC aims to generate interest from the local banks. The chairman extended his thanks to our host Bank Austria for sponsoring the event.

### 1.2 Announcements

Before starting the points on the agenda the following announcements were made :

The financial markets never stop, changes happen all the time. As a consequence, careers change all the time in our industry. It was announced with regret that some members of the steering committee left our group and have redirected their career.

Thanks especially to Ray Kuramoto from CSFB for all his devotion to the ERC. He has been replaced by Jean-Marie Begonin.

Thanks also to David Wishnow from UBS who has been replaced by Rizvi Ashraf and Geraldine Glise from Soc Gen who has been replaced by Nicolas Truong.

The chairman looks forward to employing the same commitment from the new members to the steering committee, similar to the commitment he had from the outgoing members whom are thanked by the chairman for their contributions.

### 1.3 Approval of previous minutes

The minutes of the meeting held in Madrid on the 14<sup>th</sup> of January 2002 and dated January 31, 2002 were unanimously approved and no remarks were made (the minutes were already approved at the ERSC meeting).

### 1.4 Update on events and information

The chairman provided the assembly with a brief update on developments in the repo world in Europe:

After the elections in Madrid, the official posts were chosen amongst the steering committee members. Ulf Bacher as vice-chairman and Godfried De Vidts as chairman have been re-elected. Unfortunately, as there is no permanent secretary, the decision was taken between the members to rotate the job. As a consequence, Mr. M. Murray from Ceca Madrid was appointed secretary for this meeting.

The next repo survey will be conducted as of June 12<sup>th</sup> 2002. If your bank has not participated in the past please come forward.

It is important that as many banks as possible participate. Not only for the repo survey itself, but for the benefit of the industry. Firstly, it gives you a very good idea as to where the product is moving too and helps the central banks to judge the importance of the repo market. Secondly, it will show your direct superiors that your job is worth every single penny of investment.

The data submitted by your firm will be handled in the strictest confidence. A pledge of confidentiality may be found on the survey form. The data will only be seen by one person at the ISMA centre, the person conducting the survey on behalf of ISMA and the ERC.

The survey form can be downloaded from [www.isma.org](http://www.isma.org) by going to the "surveys and reports" section and by choosing repo market surveys link. Alternatively, you can email the chairman and he will forward the document to you as soon as possible.

Recently there was a call for contributions from interested parties on the joint work of the ESCB and the Committee of European Securities Regulators in the field of Clearing and Settlement. This document can be found on the ECB's website. It would be very useful if all of your institutions could contribute to this important initiative. The chairman expressed the opinion that Europe is finally getting ready to tackle our securities infrastructure.

The following activities are taking place in this field:

The European Commission will issue a communication on the subject of clearing and settlement at the end of May.

The Giovannini group has started work on the second report and a meeting will take place at the beginning of June. This report should be available by mid summer.

The European Banking Federations have created a permanent working group called ESI, the European Securities Infrastructure Working Group bringing together a group with a European bank practitioner's perspective to address the authorities.

Furthermore, the ECB had a meeting on collateral issues on January 21, 2002 specifically on collateral issues.

CCP Update this name has now been adopted rather than CCCP; CCP stands for cash and collateral pool.

Work on this project is currently in progress and is being carried out by a working group of the New York Federal Payments Risk Committee. There are currently the following three separate strands or models under consideration:

- Cash based
- Collateral based
- Guarantee based

The working group will present and report a review of the work to date to members of the Payment Risk Committee and to attendees from a group of central banks who have shown interest in the proposals. A full draft report is expected by Q2-Q3 this year.

#### Education

Moving on, and a small remark on education. Part of the task of the ERC is to educate our members on the development of the market. We have identified a real need for education. The group is aware that there are many seminars available, many of which are commercially organised events and therefore relatively expensive.

The chairman has requested ISMA to ascertain whether an educational seminar could be organised for the members of ISMA and ACI, whereby the steering committee - amongst other speakers - would go step by step into the topic of repo transactions. Currently, the target date is late November 2002. The first, but if successful not the last seminar will be held in Brussels. Details will be provided via email and will also be available on ISMA's website.

#### Local repo workgroups

The chairman attended Germany's ACI repo steering group and their general meeting. He expressed the usefulness of having local meetings in some other large countries with local banks when ACI meet. The local topics can then be raised to a European wide level. Mr. Murray has already started such an initiative in Spain as well. The repo community can benefit from each other's work and will without a doubt help to further unify the markets. The ERC has been created to make the repo market more liquid and efficient. The steering committee welcomes contributions from all members but needs to know the worries and suggestions from its members.

## **2. Spanish legal opinion: update & future developments (ISMA Zurich – Dexter Morse)**

As an interim solution to the problems faced in relation to this subject, ISMA issued a circular date 02/03/2002, by which they provided a short side letter modifying the GMRA and enabling market participants to use the TBMA/ISMA GMRA in Spain.

This initiative was undertaken due to the delays encountered in drafting the Spanish Financial Law and should simply serve as a provisional vehicle until the law is finally passed.

With respect to this new financial law, Mr. Morse pointed out that if the Parliament approves the law as outlined in the latest draft issued by the relevant Spanish Authorities, then a clear legal opinion may be obtained for Spain.

Some questions were made in relation to this side letter and whether it would still be necessary when the draft financial law is enacted. Mr. Morse informed that ISMA together with Freshfields would review the amendments to the draft financial law and would keep members closely informed of developments. The Chairman clearly pointed out that ISMA in this sense is working on the legal framework, and not the operational one.

## **3. Japan tax issue: thin capitalisation rule (S. Bellani)**

Mr. Bellani reported on the Japanese withholding tax developments in cross border transactions, and in particular to the very thin capitalisation rule. The exemption criteria apply only between licensed institutions involved in transactions of maturity 6 months or less and on JGB's and government guaranteed bonds issued in OECD countries. Corporates are excluded.

The Japanese Financial Authorities to date, do not seem very keen on easing the current 3 to 1 rule to the proposed 20 to 1 for broker dealers. However, Mr. Bellani informs the assembly that the industry is lobbying this issue heavily.

## **4. Legal documentation for Greece: what is the issue (E. Cia)**

In the same manner as in the Spanish case the ERC has been working very intensely on the legal documentation required for the treatment of repos in Greece.

The speaker informs the assembly that Greek repos are very similar to the traditional repos; however, some differences do exist. The local repo is regulated by the Bank of Greece and its format is similar to that of a collateralised deposit, whereby the underlying collateral is blocked and no transfer of title takes place. In this sense, he appeals to the lawyers at the banks to look very carefully at the implications of such differences.

Mr. Cia suggests that we should not look to change or strive to substitute this local product, as it would have a profound effect on Greek banks and their customers due to the associated fiscal issues.

In relation to traditional repos with Greek banks, there should be no inherent problems. However, some problems may arise with local securities due to a possible re-characterisation risk. Looking forward, we expect some changes which will enable a legal opinion for the Greek market to be obtained; nevertheless, a similar side letter to that proposed for the Spanish case may permit a provisional solution to the problem mentioned above.

Some questions were raised with reference to the possible side letter and to whether it actually solved issues relating to netting procedures, finally concluding that this should not pose any difficulties as there is no specific case law on this matter.

#### **5. Eurepo: reflection on the reference rate (M. Painting)**

Mr. Painting gave a brief update on the developments of this new index and went on to comment on the behaviour of the index, particularly in comparison to that of the old BBA fixing

The graph depicts the evolution of Euribor, BBA/Eurepo and their corresponding spread over time. The graph clearly indicates that spreads are wider using the old methodology and that this can be easily explained by the fact that there is a broader number of panel banks in the new index.

The speaker sends out a message of encouragement to the market and to those present to ensure the success of this index; in his own words: "Eurepo belongs to us all and it is in our own interest to promote it".

The chairman asked the speaker if he had observed any new business arising from this initiative, to which he replied that he had seen very little and that more efforts should be made in line with the original idea to convince customers that this index *is* indeed the market benchmark.

#### **6. Clearstream /Euroclear bridge (C. Fitzmaurice)**

Ms. Fitzmaurice reported that there has been much debate on this topic at the European Repo Steering committee meetings as to which is the best way to approach the issue, since it is clearly affecting market liquidity.

We are aware of some advanced discussions between both providers striving for a daytime bridge and that all interested parties (Bank of Belgium, Bundesbank, ECB ) were present at these meetings.

From these discussions there are reports that Euroclear is working on an initiative that will presumably alleviate the actual situation within a month. Nevertheless, it is clear that the ERC needs to talk to both providers with the aim of making them sensitive to this issue and bring the debate forward to a satisfactory solution.

#### **7. Tier 1 & 2 : position of ERSC (U. Bacher)**

Mr. Bacher informs the assembly that the use of collateral in recent times is very efficient; indeed, more so than ever. This has brought to light some imperfections

or differences within markets in the Euro area in so far as the movement of collateral is concerned. The national banks seem to have differing collateral policies as regard to Tier 2.

The speaker raises the question, whether our objective should be to harmonise markets or ask the ECB to eliminate the Tier 1 / Tier 2 concept. It is quiet clear to the speaker that if we wish to have a level playing field for all banks, markets should be harmonised and central bank collateral policies should be similar.

#### **8. Basle II – update (R. Ashraf)**

Mr. Ashraf provided a brief update as to the status of Basle 2, pointing out that due to the intense market response and feedback to the drafts throughout the consultation process the target date continues to suffer delays. However, having reached this point it seems that the industry is generally supportive and strives to end this process. Some issues, including the W factor treatment of Haircuts etc. still remain under debate.

As part of the effort by the ERSC to update its members, service providers can from time to time address the audience on topics that impact upon the repo business. The presentation can be obtained by contacting the organisations directly. For information purposes only a summary of the presentations follows:

#### **A. Euro-MTS – update on product developments (G. Garbi)**

Mr. Garbi informed the assembly by means of an electronic presentation on recent developments in relation to their trading system (Blind Brokerage) and on the creation of the Italian CCP, pointing out that in order to use this product one can either access via CC&G, Clearnet or by becoming a General Clearing member.

The system will permit banks to submit their orders and specify whether they wish execution through the CCP, Bilaterally or either.

Some questions were posed by the attendees in relation to the costs of trading repos. Mr. Garbi at the time was not able to give a concrete response; however, he did mention that rebates would be applied similar to those offered on the cash market.

#### **B. BrokerTec Europe – update on product developments (G. Jones)**

Mr. Jones provided an update on the recent developments of their products focusing on the cost structure of trading and emphasising that in his opinion brokerage was not going to get any cheaper. He pointed out that if the costs needed to be minimised, one would have to look more closely at internal STP in order to increase efficiency and consequently reduce costs.

#### **C. Electronic Repo Market : An analysis of the Electronic Repo Market in the Euro-Zone by kpmg Consulting AG (I. Lengensdorf)**

Mr. Lengersdorf outlined briefly the most important aspects of the study which will be ready for publication in June 2002 and will be available free of charge. The study is based on the information provided by 20 market players and highlights important issues such as the development of ATS's amongst others.

Next Meeting : ERC General Meeting: September 18<sup>th</sup> 2002, Luxembourg

June 11, 2002

The chairman  
G. De Vidts