

ICMA quarterly report

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and Regulatory Policy

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ICMA

International Capital Market Association

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The past year in the market and the year ahead

Foreword by David Marks

The close of the year is the natural point at which we reflect on the past year and the challenges it has posed for our industry and our firms – and of course the prospects for the year ahead. Indeed, 2012 has been a year of remarkable recovery for the international capital markets as well as continued transformation of our industry and many of our member firms.

Picking up on Martin Scheck's observations in the previous review, reputational issues continue to cast a long, if not darkening, shadow. At the same time the quarter has seen leading firms announce bold restructurings in their fixed income businesses, while all firms have had to look hard at their cost bases.

Yet, for active participants in the market we close a remarkable quarter of primary market activity that has also reinvigorated the secondary market. The conditions that have helped create this are familiar to all: renewed confidence around the euro area, continued accommodative policy by monetary authorities, low absolute rates, favourable asset allocation decisions etc. Critically, many of these circumstances look set to prevail well into 2013. Indeed, we can look forward to next year with confidence (albeit cautious) for the high-grade bond market – the market at the heart of our Association. So while the US "fiscal cliff" and anaemic European growth have remained major concerns, the biggest challenge we hear mentioned by most credit investors is the near impossible one of repeating 2012's performance. I may live to regret writing these words, but we are in a very different place from the edge of abyss that we faced at the close of 2011 and before the decisive LTRO intervention. Indeed, a growing number of economists expect euro-area growth to resume from the end of first quarter 2013 driven by easier financial conditions and a mild degree of fiscal forbearance.

This change in sentiment is perhaps most evident when one considers banks themselves. Of ICMA's increasing membership, which at the end of 2012 totalled 434 members, 271 are banks – and they dominate the highest tiers of membership. Their role as intermediaries is clear, but they also act as a key part of our investor base (be they universal, investment or private banks).

With the improvement in market conditions, they have thankfully also returned as high-volume issuers. This rehabilitation has been most dramatic with banks from the periphery, and has successfully extended over the past quarter to banks from the programme countries, even on a subordinated basis. Clearly the health of banks, and their ability to participate in the capital markets, is a central issue for us all.

So what can we expect for 2013? Clearly not the returns we had in 2012 given our starting point of tighter spreads and lower yields relative to 2012. But the factors above do give confidence. Interest rates will remain a powerful influence on credit strategy – likely favouring high-yield over investment-grade activity and those sectors less correlated with interest rates (such as insurance). We may well see in 2013 high-grade portfolio managers deploying interest-rate hedges in an effort to protect positive credit returns.

And what will be the implication of lower returns? The currently strong market technicals will certainly suffer. However, high-grade investors appear to remain defensively positioned, so any outflows could take some time to affect the current buoyant conditions.

So the progress made, and the prospects for the next quarter, have rarely been so great. The role of ICMA in helping to ensure the smooth functioning of the international capital markets and in helping to guide members through the regulatory tsunami that continues has never been so relevant.

David Marks
Chairman, FIG Debt Capital Markets, J.P. Morgan
Deputy Chairman, ICMA



Message from the Chief Executive

I want to use the introduction to the first Quarterly Report in 2013 to review briefly some of ICMA's activities in 2012 and outline this year's priorities.

2012 has been an important and exceptionally busy year for ICMA in every area. Our market practice and regulatory policy agenda spans all aspects of the debt capital markets – issuance, primary and secondary trading, institutional investing and wealth management, along with the associated infrastructure. In each of these we have been working with our members both individually and through our committees, councils and working groups to address their concerns over market practices and/or regulation. ICMA founded the Public Sector Issuer Forum in 2012 to address the needs of sovereign, supranational and agency issuers, and this has got off to a good start. We also founded a forum to coordinate the many initiatives being made by ICMA and other associations in the area of collateral, and this has recently issued two important papers.

All of our committees, councils and working groups met regularly in 2012 and the level of interaction with our members – and with policy makers and authorities – has never been higher. Much of the detailed output can be seen on our website (www.icmagroup.org), where we have added new sections (for example on European Banking Union), as major topical issues have arisen. You may have already noticed that we recently posted a compendium of the many new regulations impacting the international debt markets and their status – this has proved a very popular reference document for members.

As every aspect of ICMA's work has intensified in response to regulatory and market practice pressures, we have sought to keep members informed about

new developments through an increased number of briefing calls, conferences and roundtables – all offered free to members. We have extended the range of courses offered by ICMA Executive Education to meet members' needs, and have updated our rules, recommendations, guidelines and standard documentation on an ongoing basis. This is part of our commitment to restoring trust in financial markets through raising standards.

The focus of ICMA and its staff remains providing value and service for members: our expanding membership in difficult times is a measure of success in this area.

Looking at 2013 there are already a number of clear priorities.

From a market practice perspective we will complete the revision of the ICMA Primary Market Handbook which contains the industry-accepted guidelines and recommendations governing primary debt issuance. We will also keep our secondary market rules and recommendations up to date. In the primary market we will continue our initiative to bring together issuers, syndicate managers and investors to discuss primary market practices through a series of meetings in Europe. In the secondary market we expect to hold further seminars on the future of the dealer model in a range of European financial centres.

Repo remains a core priority of ICMA – not merely the annual update of the legal opinions and their expansion to further jurisdictions but the increasing work arising from the current regulatory initiatives, some of which are causing considerable concern.

Regulation in all areas of the markets is continuing apace and we will continue to focus on those aspects which impact the workings of the debt capital markets:

the implementation of the Prospectus Directive review, and the proposed MiFID II/MiFIR, CSDR and MAR to name but a few, are all areas which will require close attention. However other regulatory initiatives are also relevant: for example, the discussions on shadow banking, capital instruments, bail-in, and many others.

We will enhance the level of service to both issuer members and buy-side members. For issuers we will be creating the new ICMA Corporate Issuer Forum, to complement the Financial Institution Issuer Forum and the Public Sector Issuer Forum mentioned earlier, and expect the first meeting in the first quarter of 2013. We will also build on the success of the recent larger scale Asset Management and Investors Council seminar held in London in November with two further such seminars in 2013. We are currently adding to the working groups of this Council to accommodate the work streams defined at the last seminar. 2013 will also see the ICMA Wealth Management Charter of Quality gaining traction throughout Europe following its launch in Luxembourg in October 2012.

Geographically outside our core Europe region we will prioritise our work in Russia, China and the Gulf, strengthening our presence with members, authorities and our partners in these regions, which all have considerable potential to play an increasing role in the global financial markets.

Please note that this year's AGM and Conference will take place in Copenhagen on 22 to 24 May.

Lastly I would like to thank all of you who contributed to our work in 2012 – participating in our committees, councils and roundtables, providing input and ideas, and attending our events. Without your engagement we could not achieve what we have achieved. We encourage you all to participate wherever you are able and look forward to working with you during 2013.

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Quarterly Assessment by Paul Richards

Financing growth in Europe

The international capital market is key to financing the economic recovery from the international financial crisis. While bank finance is currently constrained by the imposition of higher capital and liquidity requirements and by bank deleveraging in response to the crisis, capital market finance – through the issue of debt securities by corporate issuers to investors – is not constrained in the same way, as it involves “disintermediation” of the banking system.

2 This Quarterly Assessment considers the extent to which the authorities’ response to the crisis, particularly in Europe, is encouraging the international capital market to finance economic recovery. It assesses the position as at the end of 2012, and is the sixth in a series of Quarterly Assessments which have charted the course of the euro crisis and the implications for the international capital market in Europe, quarter by quarter.

Recovering from the crisis

3 The European authorities have taken a series of steps intended to encourage recovery from the crisis:

- on the monetary policy side, the ECB has reduced official policy rates to historically very low levels; provided unlimited liquidity to the banking system; and stated that it is willing to intervene in the

secondary market for government debt in unlimited amounts, subject to policy conditions being met; and

- on the fiscal policy side, governments have recapitalised insolvent banks; sought to cut budget deficits to sustainable levels; and proposed a potential way of breaking the “vicious circle” of interdependence between some governments in the euro area and banks.

Monetary policy

4 On the monetary policy side, the underlying problem – particularly on the periphery of the euro area – has related to market concerns about the unsustainable level of government budget deficits and debt, the risk of bank insolvencies, and the interdependence between governments and banks. The ECB cannot solve this problem on its own, but

it can buy time until market confidence is restored – and help to restore confidence – by reducing “redenomination” risk (ie the risk that one or more participating Member States will leave the euro area). Redenomination risk has been fragmenting markets in the euro area along national lines and making the ECB’s monetary transmission mechanism ineffective. The ECB has attempted to address this problem in two main ways:

5 First, the ECB has reduced its official short-term policy rates to historically very low levels and continued to provide short-term liquidity to the banking system. In December 2011 and February 2012, the ECB also provided two Longer-Term Refinancing Operations (LTROs), amounting to over €1 trillion gross, particularly to support banks in need of liquidity but not regarded as sufficiently creditworthy to obtain it from other banks with surplus liquidity; and the ECB has also provided a safe deposit facility for banks with surplus liquidity until confidence is restored. As the ECB lends to banks only against collateral, and collateral is scarce, particularly for banks which cannot borrow without it, the ECB has eased the terms on which it is willing to accept collateral as eligible. The ECB has also engaged in maturity transformation by taking short-term deposits from the banks on the liability side of its balance sheet, and by lending longer-term to the banks through the LTROs on the asset side of its balance sheet for up to three years (though the loans can be repaid early if confidence is restored).

6 Second, following the statement by the ECB President on 26 July 2012 – that “within our

mandate, the ECB is ready to do whatever it takes to preserve the euro and, believe me, it will be enough” – the ECB announced on 6 September that it would be willing to buy government securities in the secondary market under a programme of Outright Monetary Transactions (OMT). The OMT programme differs from the ECB’s previous Securities Market Programme (SMP) in a number of ways:

- the OMT programme is explicitly subject to policy conditions set by euro-area governments as a condition for bail-outs by the European Stability Mechanism;
- it is potentially unlimited in amount;
- it is directed at the short (1-3 year) end of the yield curve (ie close to policy rates); and
- government securities purchased by the ECB under the OMT programme are to be treated *pari passu* with other bondholders, unlike the SMP.

7 Since the announcement of the OMT programme, there has been a substantial reduction in government bond yields, and the yield differential over German bunds, in Spain and Italy; Ireland has been able to return to the sovereign bond market; and the corporate bond market has reopened for issuers in Italy and Spain. Arguably, the announcement of the OMT programme has reduced the market’s perception of redenomination risk by more than a further reduction in short-term interest rates would have done. Having said this, the ECB’s commitment to provide unlimited support through OMTs may yet be tested by the market (eg if the Spanish Government applies for a bail-out).



The ECB cannot solve this problem on its own, but it can buy time until market confidence is restored – and help to restore confidence – by reducing ‘redenomination’ risk, which has been fragmenting markets in the euro area along national lines.

Government bond yields*

% per annum	Yield end-2012	Differential over bunds	Yield change on end-2011
Germany	1.32	-	-0.51
Netherlands	1.50	0.18	-0.71
Finland	1.51	0.19	-0.79
Austria	1.75	0.43	-1.35
France	1.99	0.67	-1.17
Belgium	2.05	0.73	-2.05
Italy	4.53	3.21	-2.49
Spain	5.31	3.99	+0.22
Ireland	4.53	3.21	-3.99
Portugal	7.00	5.68	-6.56
Greece	11.84	10.52	-22.13
Switzerland	0.45	-0.87	-0.24
UK	1.85	0.53	-0.13
US	1.76	0.44	-0.12
Japan	0.79	-0.53	-0.19

Note: *10 years approx. Source: FT, Thomson Reuters

Fiscal policy

8 On the fiscal policy side, the national governments in the euro area have agreed a Fiscal Compact, which is intended to limit their structural budget deficits to a maximum of 0.5% of GDP each year in future, if the agreement can be enforced. But they have also had to bail out governments in Greece (twice), Portugal, Ireland and Spain (for its banks), and are expected to bail out Cyprus. In addition, Greek Government debt to the private sector has been rescheduled, and a further buyback programme has been completed.

9 Official support for these bail-outs was initially provided largely by the European Financial Stability Facility (EFSF). The EFSF, whose role was temporary, has now been replaced by the new European Stability Mechanism (ESM) as a permanent mechanism for bailing out governments in the euro area if necessary in future, provided that they agree to policy conditions. The ESM will be able to purchase government bonds in the primary market (while the ECB is permitted to operate only in the secondary market). It is expected that the ESM will also be able directly to recapitalise banks in future, once a definition of “legacy assets” has been agreed, and once the Single Supervisory Mechanism has been established, with the objective of breaking the “vicious circle” arising from the interdependence between sovereigns and their banks. While the

finance that the ESM itself can provide is limited (to €500 billion), its role is intended to be complementary to the role of the ECB, which is willing to provide unlimited finance under its OMT programme, so long as the debtor government concerned agrees to policy conditions under the ESM first. The ESM and the ECB’s OMT programme are therefore closely linked.

Preventing another crisis

10 Besides taking monetary and fiscal steps intended to restore market confidence and help the economic recovery from the current crisis, the authorities have also been determined to introduce new financial regulations in an attempt to ensure that a crisis on this scale can never happen again.

Regulation

11 The new regulatory initiatives are intended to be both more intrusive in their impact on the financial sector than the “light touch” approach to regulation that prevailed – particularly in some jurisdictions – before the crisis, and they are also designed to be much broader in scope. They cover not just the capital and liquidity required by financial institutions (eg banks through CRD IV/CRR and insurance companies through Solvency II), but they also cover markets, including:

- market issuance (through the revised Prospectus Directive regime);
- market trading (through the proposal for MiFID II/ MiFIR), the prevention of market abuse (through MAR) and securities financing (through a proposal expected under “shadow banking”);
- clearing of standard OTC derivatives in CCPs (through EMIR); and
- settlement (through the proposed CSD Regulation and Securities Law Legislation).

The cost to the industry of complying with these new regulations – some of which have not yet been implemented – is certain to be high, but the cost is seen by the authorities as being outweighed by the potential benefit of avoiding a repetition of the crisis.

12 To help implement the new regulatory framework, the European Supervisory Authorities – ie the EBA, ESMA and EIOPA – have been established at European level with greater powers – eg to impose

a single European rulebook based on detailed regulatory technical standards – than the committees of national regulators which the new authorities have replaced. In addition to regulating individual institutions and markets, central banks and regulators are also concerned to assess their systemic impact – through the ESRB at European level and the FSB at global level.

Supervision

13 Within this new regulatory framework, on 14 December 2012 the European Council endorsed ECOFIN's proposals for supervising banks through the Single Supervisory Mechanism (SSM), subject to agreement with the European Parliament, and without the need for a change in the EU Treaty, at least at this stage. Under the proposals:

- The ECB will become responsible for the overall functioning of the SSM, which will consist of both the ECB and national bank supervisors, and is due to become fully operational from 1 March 2014 (or twelve months after the entry into force of the legislation, if later).
- EU Member States not participating in the euro area will be able to participate in the SSM under arrangements for cooperation. It is currently expected that, in addition to the 17 Member States participating in the euro area, seven of the remaining EU Member States will decide to participate in the SSM, while the UK, Sweden and the Czech Republic are expected not to do so.
- The ECB will be directly responsible for supervising, not only large cross-border banks in the euro area, but also all other euro-area banks with assets above a threshold of €30 billion or more than 20% of national GDP (ie around 150 in total). This is because the crisis has demonstrated that even a

relatively small bank can cause systemic problems. However, the smaller the bank, the greater the supervisory role that will continue to be played by national supervisors. (There are around 6,000 banks in the euro area in total.)

- The ECB will be granted powers: to authorise banks; to ensure that they comply with capital requirements; and to revoke their licences.
- The ECB's supervisory functions are to be clearly separated from its monetary policy functions so as to avoid potential conflicts of interest. A separate Supervisory Board is to be set up in the ECB, with the Supervisory Board's decisions being adopted unless rejected by the ECB Governing Council. The ECB will report to the European Parliament on its supervisory role. EU Member States outside the euro area participating in the SSM will have full and equal voting rights with euro-area members.
- To avoid the ECB having an automatic majority in the EBA, there is to be a "double majority" voting system in the EBA under which EBA decisions have to be approved by a majority of EU Member States not participating in the euro area. However, this is subject to review if the number of non-participating Member States falls below four.

Resolution

14 The SSM is intended to be the first step towards European Banking Union in the euro area. It is due to be followed, as a second step, by a proposal in 2013 from the European Commission to create a Single Resolution Mechanism for winding up insolvent banks, paid for by the financial sector so as to avoid any net cost to taxpayers, with a backstop which is recouped by a levy on the financial sector if taxpayer support is initially required. (The Commission estimates that, between 2008 and 2011, taxpayers



The ECB will be directly responsible for supervising all euro-area banks with assets above a threshold.



Resolution of banks in an orderly way without recourse to the taxpayer is regarded by the authorities as a precondition for avoiding a repetition of the crisis.

in the EU granted banks €4.5 trillion in loans and guarantees.)

15 Resolution of banks in an orderly way without recourse to the taxpayer is regarded by the authorities as a precondition for avoiding a repetition of the crisis, both at European level and at global level. If a G-SIFI fails in future, the UK and US authorities – accounting for the headquarters of 12 of the 28 designated G-SIFIs – have jointly proposed a contingency plan to avoid losses falling on taxpayers. Under the contingency plan, a resolution authority would take control of the parent company of the G-SIFI group if it fails, and allocate losses in an orderly way first to the G-SIFI's shareholders, who would be likely to lose all the remaining value of their investment, and then bail in its unsecured debtholders, with the effect that their claims would be written down (with due respect to their relative ranking) to reflect any losses that shareholders could not cover. A portion of remaining unsecured debt would be converted into equity, where needed, to provide new capital. Senior management would be removed. Loss-making subsidiaries would be restructured or closed. Sound subsidiaries would be kept open and operating in an attempt to limit the risk of contagion across borders.

16 In the euro area, this second step – ie a Single Resolution Mechanism – may eventually be followed by a third step, involving the introduction of a European deposit guarantee scheme in place of national deposit guarantee schemes. The level of guarantees on national deposit schemes has now been set across the EU at €100k. But replacing national schemes with a European scheme is controversial because banks in creditor Member

States would be expected to help pay for the failure of banks in debtor Member States. The question of a European deposit guarantee scheme has therefore been set aside, at least for the time being.

Separation

17 A distinct but related issue is how to prevent banks from failing in the first place. It is clear that good risk management is a precondition for this. But the authorities also consider that it is necessary to separate banks' essential – retail banking and payment – functions from their wholesale functions in one way or another. There are currently at least four broadly similar – but slightly different – proposals to achieve separation: in the UK, the Vickers report, which proposes to ring-fence banks' retail activities; in the EU as a whole, the Liikanen report, which proposes to ring-fence banks' trading activities; in France, a legislative proposal based on Liikanen, but modified; and in the US, the Volcker rule, which bans banks from undertaking proprietary trading.

Impact on growth

Regulatory impact

18 The international financial crisis is estimated – by the Secretary General of IOSCO – to have cost around 15% of global GDP so far. It is very difficult to quantify the cumulative impact of the monetary, fiscal and regulatory measures which the authorities have taken in response to the crisis on economic growth in future, because so much depends on qualitative factors, such as the extent to which they help to restore confidence in the financial system. But the dilemma for the authorities is that, if they are not careful, the regulatory steps which they are taking in an attempt to prevent the next crisis may also have the effect of preventing – or at least slowing down – the economic recovery from the current one. There are a number of questions that need to be addressed:

19 The first question is what the overall impact of these measures on growth will be: whether they will promote growth, because they help to restore market confidence, and because the recapitalisation of the banks will ultimately enable the banks to increase their lending in support of growth in future; or whether the measures will impede growth, because the imposition of austerity as a result of budget cuts



It is very difficult to quantify the impact of measures in response to the crisis on economic growth, as so much depends on qualitative factors, such as the extent to which they help to restore confidence in the financial system.

initially reduces domestic demand, and because new regulations increase costs for the banks, through: higher capital charges; increased margin requirements; and, as a result of the imposition of bail-in, increased costs of funding through unsecured bank debt.

20 Either way, steps to encourage international capital market financing in Europe would represent a complementary way to encourage growth, not just through the financing of very large corporates with high credit ratings, but also of creditworthy smaller companies. Capital market financing in Europe still represents a much smaller proportion of total financing than in the US: at least 75% of corporate debt in Europe is estimated to be financed by banks, compared with around 25% in the US. Even if steps cannot be taken to encourage capital market financing, at least they should not be taken to discourage it:

- There is a risk that this might happen, for example, if regulation were to be unduly extended from bank finance to market finance – eg through the repo market and through the asset management industry – which provides an essential role in financing the economy.
- It might also happen if transparency requirements are not carefully calibrated under MiFID II/MiFIR, with the result that liquidity is damaged in the secondary markets, which would in turn damage conditions in the primary markets.
- In addition, there is considerable scope in Europe for encouraging more retail investment in the corporate bond market (eg as a means of saving for pensions), provided that regulation does not discourage it.

21 The second question is whether the regulatory measures which the authorities have proposed are

all consistent with one another, or whether they have unintended consequences. Consistency is an issue within the EU, where it is sometimes alleged that new regulatory initiatives are introduced in “silos” without consideration always being given to the impact of one measure on another; and in some cases there is also uncertainty in the market about exactly what the authorities intend. Consistency is not just an issue within the EU, but also between the EU (which focuses – broadly speaking – on “mutual recognition”) and the US (where some regulations have extra-territorial effect). And consistency is not just an issue between the EU and US, but also with other countries (eg in Asia), many of whose governments do not consider that similar measures in their countries are necessary, on the grounds that the crisis did not originate with them.

22 The third question is whether the regulatory measures which the authorities have proposed will reduce systemic risk in the financial system or simply reallocate risk from one set of counterparties to another. For example, in shifting from bilateral OTC counterparties to multilateral clearing through CCPs, risk will in future increasingly be concentrated in CCPs, which may as a result become new institutions that are “too important to fail”.

23 The fourth question in Europe is whether closer financial integration in the euro area will affect the integrity of the Single Market across the EU as a whole. There has recently been a debate about the impact of the substantial volume of euro business currently conducted outside the euro area, particularly in London. On one side of the argument, measures to repatriate euro business in London to the euro area would be intended to increase euro-area liquidity and ensure oversight in the euro area of its own currency. On the other side, it is not clear that the volume of euro business in London prevented the

euro-area authorities' response to the crisis in any way. The December European Council notes that "it is important to ensure a level playing field between Member States which take part in the SSM and those which do not".

24 A separate outstanding issue relating to the EU Single Market is whether national regulators in the EU will encourage cross-border banks to set up subsidiaries to ensure that they have sufficient capital in their own jurisdiction instead of relying on branches financed across borders (as originally intended in the EU Single Market), and what approach will be taken within the euro area. Enhanced prudential standards for non-US banks through the use of intermediate holding companies have also been proposed by the Fed in the US.

Wider impact

25 Besides regulatory issues, there are also a number of wider issues arising from the crisis which may have an impact on growth in Europe:

- The first relates to the pace of global economic recovery from the crisis (eg following the debate on the "fiscal cliff" in the US).
- The second relates to the importance for Europe of maintaining its global competitiveness. Within the euro area, there is an additional question whether the bail-outs of debtor sovereigns by creditor sovereigns will reduce imbalances in competitiveness between them; and in particular whether economic adjustment should only be required by debtors or whether creditors should also be expected – even though they cannot be required – to take steps to adjust their economies by strengthening domestic demand (eg by allowing wages to rise in line with productivity).
- The third concerns the change – in response to the crisis – in the relationship between central banks and governments. Before the crisis, many central banks were clearly independent of government in pursuing price stability as their primary or sole objective. But since the crisis began, the relationship between central banks and governments has inevitably become much more closely linked; central bank balance sheets have become much larger; the role of central banks in ensuring financial stability has become increasingly recognised; and the objective of supporting

economic growth has – at least implicitly – become more important.

- Finally, there is the potential political impact, both at national and at European level, of the international financial crisis, which has lasted for over five years and which has led to high unemployment and social change arising from structural reform.

ICMA's role

26 Against this background, what can the industry do to help? Overall regulatory policy is seen by the authorities as a matter solely for them. But the industry can help to implement it by focusing in particular on how best to calibrate new measures to ensure well-functioning markets and on how to prevent unintended market consequences. Within the new regulatory framework, ICMA will help to rebuild trust in the industry by continuing to set standards of good market practice in the international capital market; and it will help to bring the sell side and the buy side of the industry together and to encourage dialogue between the industry as a whole and the authorities.

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In brief

- The international capital market is key to financing the economic recovery from the international financial crisis.
- Besides taking monetary and fiscal steps intended to restore market confidence and help economic recovery from the crisis, the authorities have also been determined to introduce new financial regulations in an attempt to ensure that a crisis on this scale can never happen again.
- The dilemma for the authorities is that, if they are not careful, the regulatory steps which they are taking in an attempt to prevent the next crisis may also have the effect of preventing – or at least slowing down – the economic recovery from the current one.

Recent practical initiatives by ICMA

The purpose of this list is to summarise practical initiatives by ICMA since the previous Quarterly Report. (ICMA responses to consultations by regulators are available on the ICMA website.)

Crisis response

- 1 ICMA has responded to the European Commission consultation on the Liikanen Report on structural reform of the EU banking sector, which proposes to ring-fence banks' trading activities. In the response, we have focused on the implications for international capital markets (eg on proprietary trading, underwriting and bail-in).
- 2 ICMA has responded to the European Commission consultation on non-bank financial resolution and recovery.
- 3 ICMA has made available a webpage linking to sources of information on European Banking Union and bank structural reform.

Short-term markets

- 4 ICMA has responded to the European Commission consultation on benchmarks, taking account of our earlier response to the Wheatley review on the reform of LIBOR, and focusing on continuity of contracts, particularly in the case of FRNs, and on the repo market.
- 5 ICMA has also responded to the BBA on its proposals for the phasing out of certain rate fixings, following the sixth recommendation of the Wheatley review.
- 6 The ERC Committee has participated in a workshop hosted by the ECB, at the ECB's request, on an EU database for repos and securities lending.
- 7 The Collateral Initiatives Coordination Forum (CICF), of which ICMA is a member, has published a paper on *Collateral Fluidity*. Besides ICMA, the paper has been endorsed by nine other trade associations involved in the CICF.
- 8 The CICF has also published a short primer on *Collateral Fundamentals* to guide those interested in, but new to, this important subject.
- 9 Following the implementation of a new regulation in Russia, ICMA will shortly finalise a legal opinion on the GMRA for Russia, a Russian Annex to the GMRA and a Russian translation of the GMRA 2011.

- 10 The latest semi-annual survey of the European repo market took place on 12 December, and the results will be published on 11 March.

Primary markets

- 11 At its meeting in Brussels on 1 October, the Public Sector Issuer Forum held an exchange of views with senior representatives of the European Commission (DGMARKT) on the impact of new regulatory initiatives on the SSA sector.
- 12 The latest in a series of ICMA roundtables for issuers, intermediaries and investors was held at BNP Paribas on 15 November to discuss new issue procedures.
- 13 The Sixth ICMA Primary Market Forum was held at Linklaters on 15 November, focusing in particular on the Prospectus Directive review.
- 14 At its meeting on 28 November, the ICMA Financial Institutions Issuer Forum held an exchange of views with senior representatives of the European Banking Authority on, *inter alia*, the impact of new regulatory initiatives on capital raising by banks.
- 15 The Joint Associations' Committee on Retail Structured Products, of which ICMA is a member, has commented on the publication by the European Commission of a draft regulation on key information documents for investment products under the Commission's Packaged Retail Investment Products (PRIIPs) initiative.
- 16 Work on the review of the ICMA Primary Market Handbook (PMH) is proceeding in the PMH Wider Working Group.

Secondary markets

- 17 ICMA held an event for members in Vienna on 25 October to discuss the potential impact of MiFID II/MIFIR and the future of the dealer model.
- 18 ICMA held a seminar at Allen & Overy on 12 November to discuss the future of the dealer model.
- 19 The ICMA Secondary Market Practices Committee held a meeting in Frankfurt on 13 November to discuss market operations with the European Central Bank.
- 20 ICMA held a lunchtime roundtable on 20 November to discuss the implications of the proposed CSD Regulation for ICMA's Secondary Market Rules & Recommendations.

Asset management

- 21 ICMA held an all-day meeting of the Asset Management and Investors Council (AMIC) at Credit Suisse on 23 November. The main purpose of the meeting was to discuss trends in the asset management industry and to provide feedback to the AMIC Executive Committee on its work programme for the period ahead. The AMIC Executive Committee subsequently met on 18 December.
- 22 Following the launch of the ICMA Private Wealth Management Charter of Quality with the Private Banking Group of the ABBL in Luxembourg on 4 October, the Luxembourg regulator (the CSSF) issued a Circular Letter on 3 December to banks and investment firms in Luxembourg requesting them to inform the CSSF whether they have signed the Charter of Quality.
- 23 ICMA held a roundtable on covered bonds with the Nordic Capital Market Forum in Stockholm on 22 October.
- 24 The AMIC has responded to the European Commission's consultation on UCITS: *Product Rules, Liquidity Management, Depositary, Money Market Funds and Long-Term Investments*.

Meetings with central banks and regulators

- 25 In addition to the other meetings noted above, the Chairs and other key representatives of ICMA's Market Practice and Regulatory Policy Committees held meetings with senior representatives of the ECB in Frankfurt on 28 November, and with the Executive Director, Markets, at the Bank of England on 14 December.
- 26 The Head of Markets and the Head of International Strategy, Markets, at the FSA addressed and answered questions at ICMA's Regulatory Policy Committee meeting on 13 December.

Other initiatives

- 27 ICMA has signed a Memorandum of Understanding with the Emirates Securities and Commodities Authority, which will enhance cooperation between the two organisations on issues relating to the international capital market.

Regulatory Response to the Crisis



by David Hiscock

G20 financial regulatory reforms

IOSCO issued a [media release](#) on 5 October, following a two-day Board meeting on 3 - 4 October. The meeting underscored IOSCO's commitment to tackling emerging risks to investors and securities markets in a proactive and forward-looking way. The Board reconfirmed IOSCO's commitment to meet deadlines on work mandated by the G20 Leaders and the Financial Stability Board (FSB) on regulatory reform; and took a number of key decisions on work in a number of areas. Recommendations on the [Regulation of Money Market Funds](#) and [Oil Price Reporting Agencies](#) were approved, with progress made on recommendations on [Global Developments in Securitization Regulation](#) (subsequently completed and published on 16 November). Agreement was also reached on next steps regarding IOSCO's Report on the Credit Default Swap Market.

The meeting was preceded by a roundtable attended by 18 senior financial services executives drawn from around the world to discuss emerging risks within IOSCO's remit.

The discussions in this meeting with CEOs and CFOs from both developed and emerging markets confirmed the increasing role of securities markets in supporting economic development. IOSCO's recently constituted Board Level Task Force on Financial Market Benchmarks also held its first meeting. The task force drew up a detailed and intensive work plan for developing recommendations on safeguards against abusive practices in benchmark setting by the first quarter of 2013. And, following a meeting of the Board with Michel Prada (Chairman of the Trustees of the IFRS Foundation), a proposal was taken up for IOSCO to play a larger role in global efforts to further the international adoption and implementation of IFRS.

Brief updates given on other global regulatory reform work include:

- development of methodologies to identify Non-Bank SIFIs;
- strong support for IOSCO's involvement in the development of legal entity identifiers (LEIs);
- IOSCO's role in addressing cross-border issues associated with OTC derivatives regulatory reforms in key jurisdictions;

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- IOSCO's role in monitoring implementation of OTC derivatives reforms and the recently approved Principles on FMIs; and
- strong support for IOSCO's ongoing work on protection of client assets in resolution.

In terms of possible new areas of work, the Board considered developing a mandate on the impact of differing regulatory requirements on cross-border activity in securities markets.

At its [10 – 11 October 2012 plenary meeting](#) in Tokyo, the FSB discussed vulnerabilities currently affecting the global financial system and the progress in authorities' ongoing work to strengthen global financial regulation. Members expressed support for the measures being adopted by authorities at the national and EU levels, and look forward to rapid progress in their implementation. More specifically:

- *Addressing SIFIs*: the FSB endorsed for publication the finalised [Framework for Dealing with D-SIBs](#) developed by the BCBS; and discussed the forthcoming annual update of G-SIBs, to be published in November 2012, based on end-2011 data. The FSB also endorsed for publication the IAIS consultation paper that sets out a proposed set of policy measures to apply to global systemically important insurance companies (G-SIIs); and discussed the ongoing FSB peer review, to be finalised in early 2013, to evaluate member jurisdictions' existing resolution regimes and any planned changes to bring them into line with the FSB's *Key Attributes of Effective Resolution Regimes*;
- *Shadow banking*: the FSB discussed a draft set of policy recommendations from the five work streams that have been considering options to strengthen the oversight and regulation of shadow banking; and reviewed the results of its second annual monitoring exercise

of the global shadow banking system. Following the G20 Ministers and Governors meeting in November the FSB expects to publish for consultation an initial integrated set of policy recommendations to strengthen regulation of shadow banking;

- *OTC derivatives reforms*: the FSB reviewed the steps being taken to implement the G20 commitments to OTC derivatives reforms, on which it will shortly issue its fourth progress report; and called on jurisdictions to put in place their legislation and regulation promptly and to act by end-2012 to identify and address conflicts, inconsistencies and gaps in their respective national frameworks, including in the cross-border application of rules;
- *LIBOR and other financial benchmarks*: it was agreed that the FSB should act as a coordinator to ensure that information and knowledge on the various reviews in this area are shared among authorities, and that principles and good practices for benchmark-setting that emerge are widely adopted; and the potential for the official sector to build on these reviews to develop a set of high-level principles applying to benchmark-setting in general was discussed;
- *LEIs*: the FSB welcomed progress in the implementation of the global LEI system; and supported a draft Charter for the LEI Regulatory Oversight Committee for submission to the G20 for final endorsement;
- *Monitoring of Basel III implementation*: the FSB called on all member jurisdictions to take appropriate steps to ensure that national implementation of Basel III is timely and consistent with the internationally agreed standards; and
- *Reducing reliance on CRAs*: FSB members discussed the contents of a roadmap, to be presented to

the G20 in November, to accelerate implementation of its *Principles for Reducing Mechanistic Reliance on CRA Ratings*.

A [communiqué](#) was issued following the 4 - 5 November 2012 meeting in Mexico of the G20 Finance Ministers and Central Bank Governors. From within this, paragraphs #15 - #19 are those which are most directly relevant to the on-going process of financial regulatory reform:

15. "We remain committed to the full, timely and consistent implementation of the financial regulation agenda, and discussed [the latest FSB reports on the progress in implementation of agreed reforms](#). We endorse the conclusions and recommendations of the [fourth progress report on the implementation of the G20 commitments to OTC derivatives reforms and the BCBS report on implementation of Basel III](#). We agree to put in place the legislation and regulation for OTC derivatives reforms promptly and act by end-2012 to identify and address conflicts, inconsistencies and gaps in our respective national frameworks, including in the [cross-border application of rules](#). We agree to take the measures needed to ensure full, timely and effective implementation of Basel II, 2.5 and III and its consistency with the internationally agreed standards. We look forward to receiving for our April meeting the BCBS report on the consistency of measurement of risk-weighted assets. We endorse the [Charter for the Regulatory Oversight Committee](#) which will act as the governance body for the [global Legal Entity Identifier system](#) to be launched in March 2013.

16. We acknowledge progress made in the design and implementation of policy measures to strengthen the resilience of the financial system and reduce systemic risks. In particular, we welcome the [publication by the FSB of an updated list of global systemically important banks](#), the BCBS framework for [dealing with](#)



The G20 remains committed to the full, timely and consistent implementation of the financial regulation agenda.

domestic systemically important banks, and the International Association of Insurance Supervisors (IAIS) consultation paper on policy measures for global systemically important insurance companies. We commit to make the necessary changes to resolution regimes to enable authorities to resolve SIFIs. We welcome the initial integrated set of policy recommendations to strengthen the oversight and regulation of shadow banking together with expanded data monitoring. We call for finalized policy measures by the St. Petersburg Summit for oversight and regulation for shadow banking that can be peer reviewed.

17. We also welcome the recommendations to increase the intensity and effectiveness of SIFI supervision, and the FSB's roadmap to accelerate implementation of the FSB Principles for Reducing Reliance on Credit Rating Agency Ratings. We encourage further work to enhance transparency of and competition among credit rating agencies and ask IOSCO to provide a report on ongoing work at our meeting in April. We support measures to strengthen the transparency of financial institutions and recognize the contribution of the Enhanced Disclosure Task Force. Recognizing the need for adequate statistical resources, we endorse the progress report of the FSB and the IMF on closing information gaps, and in particular look forward to the implementation of the data reporting templates for global systemically important financial institutions. We are concerned about the slow progress achieved toward a single set of high quality accounting standards.

We encourage the International Accounting Standards Board (IASB) and Financial Accounting Standards Board (FASB) to complete work promptly, and report to our next meeting. In relation to LIBOR, EURIBOR and other financial benchmarks, we welcome actions taken and ongoing reviews to identify measures to address weaknesses and restore confidence in benchmark and index setting practices and welcome the coordinator role of the FSB as agreed. We ask IOSCO to provide by our April meeting a report on the next steps on the functioning of credit default swaps markets. We expect the FSB to continue monitoring, analyzing and reporting on the unintended consequences of regulatory reforms on Emerging Market and Developing Economies.

18. We welcome the FSB's progress in implementing the measures endorsed at Los Cabos to strengthen its capacity, resources and governance. We look forward to its establishment as a legal entity by our next meeting and its full implementation by September 2013. We call on the FSB to report back on how it intends to keep under review the structure of its representation.

19. We welcome the observed increase in jurisdictions' adherence to international regulatory and supervisory cooperation and information exchange standards, as stated in the FSB status report, and call for further progress."

In its 18 November 2012 press release the FSB announced the release of a set of three further consultation papers, for comment by 14 January 2013, which

relate to its ongoing work on shadow banking:

- *An Integrated Overview of Policy Recommendations*, which sets out the FSB's overall approach to shadow banking issues and provides an overview of its recommendations across the five specific areas which its shadow banking work streams have been addressing;
- *A Policy Framework for Strengthening Oversight and Regulation of Shadow Banking Entities*, which sets out a high-level policy framework to assess and mitigate bank-like systemic risks posed by shadow banking entities other than MMFs (other shadow banking entities); and
- *A Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos*, which sets out 13 recommendations to enhance transparency, strengthen regulation of securities financing transactions, and improve market structure.

At the same time, the FSB highlights two sets of final shadow banking policy recommendations which have been published by IOSCO, namely:

- *Policy Recommendations for Money Market Funds* (published on 9 October); and
- *Global Developments in Securitisation Regulation* (published on 16 November).

Alongside these policy papers the FSB has also published the *Global Shadow Banking Monitoring Report 2012*. The 2012 report has broadened its coverage to include 25 jurisdictions (all 24 FSB member jurisdictions and Chile), compared with 11 jurisdictions in 2011, and includes analyses on interconnectedness between banks and non-bank financial entities as well as on a specific non-bank financial subsector, namely finance companies.

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The IMF has made available a staff discussion note on *Shadow Banking: Economics and Policy*. This note outlines the basic economics of the shadow banking system, highlights (systemic) risks related to it, and suggests implications for measurement and regulatory approaches. It focuses on two functions of the shadow banking system that are most close economically to those of traditional banks: securitization and collateral intermediation. The paper indicates that policy measures should try to correct market failures and externalities associated with the activities of the shadow banking system. It notes that whilst the right policies are not all obvious yet, one can only aim to further the debate by highlighting a number of priorities for a comprehensive policy response. It is considered that an appropriate set of policies may lead to a smaller shadow banking system, performing its useful economic functions of providing safe claims and credit to borrowers in better ways.

As reported on 20 November 2012, during its Annual Conference on 19 - 21 November, members of IOSCO's Emerging Market Committee (EMC) debated its future within IOSCO, while stressing the importance of building regulatory capacity and developing safe and robust securities markets in emerging economies. The EMC comprises eighty-six members that account for more than 80% of IOSCO's ordinary membership. The EMC members also represent the world's fastest growing economies and include 10 of the G20 members. Emerging economies are expected to represent a growing portion of IOSCO membership as new members continue to join. IOSCO has been allocated an extra seat at the FSB Plenary for the Chairman of the EMC; and the EMC also has a seat on the IFRS Foundation Monitoring Board. After further consultation a position paper on the future of the EMC will be presented to the IOSCO Board in March 2013. A key objective is to establish a mechanism

whereby the emerging markets will be better heard and their needs more efficiently met by IOSCO in the future.

On 14 December 2012, the BCBS issued a statement concerning the progress of its members in implementing the Basel III package of regulatory reforms. The number of BCBS member jurisdictions that have published the final set of Basel III regulations effective from the start date of 1 January 2013 is 11. These comprise Australia, Canada, China, Hong Kong SAR, India, Japan, Mexico, Saudi Arabia, Singapore, South Africa and Switzerland. Seven other jurisdictions – Argentina, Brazil, the European Union, Indonesia, Korea, Russia and the United States – have issued draft regulations, and have indicated they are working towards issuing final versions as quickly as possible. Turkey will issue draft regulations early in 2013. All BCBS members have reiterated their commitment to implement the globally-agreed reforms, and several BCBS members are due to undergo a peer review of the consistency of their final regulations during 2013. At the conclusion of this set of peer reviews, all jurisdictions that are the home regulator for G-SIBs will have been subject to a peer review of their Basel III implementation.

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European financial regulatory reforms

ESMA's 2013 work programme describes the goals and deliverables planned for ESMA in its third year of operation. 2013 will be marked by a major increase of the work of ESMA, given a number of new responsibilities that are in the process or have been given to the organisation by the co-legislators. ESMA's 2013 objectives and priorities are based on three key elements:

- New and revised legislation (MiFID II/MiFIR; MAD II/MAR; CRA III; TD; Regulations on Venture Capital (VC) and Social Entrepreneurship Funds; and CSDR);
- Supervisory Role – CRAs and Trade Repositories; and
- Coordination, monitoring and analysis of financial markets.

In order to enable ESMA to deliver its 2013 work programme, it will need to increase its staffing and budget accordingly. In 2013 staff numbers are expected to grow from 101 to 160 and the budget from €20.2 million to approximately €28 million.

ESMA has structured the different work streams it will undertake according to its key responsibilities and objectives. Hence the planned activities for 2013 are presented under the headings of Single Rulebook; Supervision; Financial Consumer Protection; Contribution to Financial Stability; Convergence; and ESMA as an Organisation.

ESMA's multi-annual work programme 2013-15 describes the goals and deliverables ESMA aims to achieve in the period. 2013-15 will be when ESMA consolidates its position as a key part of the EU's system of financial supervision. In order to meet this objective, ESMA will focus on the following key strategic directions:

- develop the technical standards and guidelines required following the revision of existing, or the introduction of new, legislation;
- implement a new multi-disciplinary supervisory approach, including in-depth reviews, action plans, guidance and enforcement measures;
- develop supervisory manuals and internal guidelines setting out ESMA's supervisory approach and ensure effective pre-screening of supervised entities' business development plans

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in order to facilitate the identification of potential new risk areas;

- further develop tools for financial consumer protection and extend the analysis of consumer risks and trends to respond to potential risks to consumer protection;
- actively monitor developments in financial markets and drive and coordinate appropriate responses;
- achieve greater convergence of national supervisory activity and implementation of EU regulations using ESMA's powers; and
- develop the infrastructure and operational processes required to support new legislative developments, eg major IT projects, when required.

The [EBA](#) has also issued its 2013 work programme; and [so has the EIOPA](#).

On 2 October 2012, the European Commission received the report prepared by the [Liikanen High-level Expert Group](#) on reforming the structure of the EU banking sector. In brief, the Liikanen Group recommends actions in the five following areas:

- mandatory separation of proprietary trading and other high-risk trading activities;
- possible additional separation of activities conditional on the recovery and resolution plan;
- possible amendments to the use of bail-in instruments as a resolution tool;
- a review of capital requirements on trading assets and real estate related loans; and
- a strengthening of the governance and control of banks.

This report feeds the European Commission's reflections on the need for further action. In considering the next steps the Commission will look at the impact of these recommendations both

on growth and on the safety and integrity of financial services; and also in light of the financial reforms that have already been advanced. To add to its reflections, the European Commission formally [opened a related consultation](#). (As the Commission was quite simply asking for comments to be provided on the report's recommendations, no specific consultation paper was produced). This consultation was open until 13 November and [ICMA submitted a response](#). In overall terms, the ICMA considers that the recommendation:

- to separate securities trading activity, possibly isolating it from primary market activity, will have potentially significant adverse impacts on the international capital market; and,
- concerning certain details of how to design bail-in debt, is not the best way to develop this important feature of recovery and resolution regimes.

On 5 October 2012, the European Commission [opened a consultation](#), with a deadline for responses of 28 December, on a possible framework for the recovery and resolution of non-bank financial institutions. This consultation aims to help ensure that, in line with the principles adopted by the G20 and the FSB, all non-bank financial institutions the failure of which could threaten financial stability are capable of being resolved in an orderly manner and with minimal cost to taxpayers. It thus discusses and requests input on: (i) the ways in which the failure of different financial institutions can threaten financial stability and economic welfare in general; and (ii) the possible need for improvements regarding recovery and resolution arrangements. The main non-bank financial institutions covered here, ie financial market infrastructures such as central counterparties and central securities depositaries, and systemically relevant insurance companies. [The ICMA submitted a response](#), drawing attention to its September 2012 responses to the

CPSS/IOSCO joint public consultative report, [Recovery and Resolution of Financial Market Infrastructures](#). These focus specifically on temporary stays and payments moratoria, suggested as resolution powers; and bail-in as a potential resolution tool.

The [European Stability Mechanism \(ESM\)](#) was launched in the margins of a Eurogroup meeting on 8 October 2012, when the ESM Board of Governors held its inaugural meeting. The ESM will be the cornerstone of the European firewall and an integral part of the strategy to ensure financial stability in the euro area.

Conclusions from the 9 October 2012 ECOFIN meeting in Luxembourg are [reported in a press release](#). Items of interest include:

- The Council was informed of developments regarding the possible introduction of a financial transaction tax (FTT), via enhanced cooperation, in a limited number of member states. The Commission indicated that it had received letters from seven Member States requesting a proposal to that effect (Belgium, Germany, Greece, France, Austria, Portugal and Slovenia), and four delegations announced that they would shortly follow suit (Estonia, Spain, Italy and Slovakia).
- The Council was informed by the Presidency of the state of negotiations with the European Parliament on the two proposals in the CRD IV package. The Council confirmed its intention to reach a political agreement on the package before the end of the year.
- The Council was informed by the Presidency of developments with regard to proposals on bank resolution and recovery; and was also briefed by the Presidency on the process for handling proposals on bank supervision.
- The Council (i) was informed by the Commission and the Presidency on the outcome of a G20 finance deputies



The Liikanen Group recommends mandatory separation of proprietary trading and other high-risk trading activities.

meeting held in Mexico City on 23-24 September and on the follow-up to the meeting; (ii) prepared a G20 Finance Ministers' and Central Bank Governors' meeting to be held in Mexico City on 4-5 November; and (c) prepared the annual meeting of the IMF and World Bank Group, to be held in Tokyo on 12-14 October.

As reported in a [23 October press release](#), the Commission has adopted its 2013 Work Programme. Amongst the key policy areas covered by this programme is the achievement of *A Genuine Economic and Monetary Union* – which anticipates additional legislation to enhance stability, transparency and consumer protection in the financial sector, based in particular on the blueprint to a genuine economic and monetary union. Forthcoming initiatives for 2013-2014 which are proposed for this policy area include:

- *Addressing systemic risks related to shadow banking*: following the Green Paper of March 2012 and the international work coordinated by the FSB, the Commission will address the systemic problems related to shadow banking entities and practices eg money market funds, securitisation and activities such as securities lending and repurchase agreements performed by all types of financial entities;
- *Common framework for the production of indices and benchmarks*, in particular their governance and calculation – the overall objective is to enhance the integrity of the production and use

of benchmarks and indices which will enhance market confidence and efficiency and improve investor protection;

- *Review of the European System of Financial Supervision*: the regulations establishing the EFSF (the three European Supervisory Authorities and the Systemic Risk Board) require that the Commission carries out an in-depth review in 2013, in view of making proposals for changes;
- *Providing long-term finance through actions to ensure the effectiveness of financial institutions, markets and instruments*: following the Green Paper to be adopted by the Commission at the end of the year, and the ensuing debate, the Commission will propose policy actions to improve the conditions for long term finance in Europe. Some of the actions may be included in other proposals (like UCITS VI); and
- *Reforming the framework for collective investment funds/UCITS VI* (focus on long-term investments, product rules and depositaries): recent international work on shadow banking has identified certain shortcomings in the field of investment funds that require closer scrutiny (for instance, money market funds and the use of securities lending or sale-and-repurchase arrangements (repos)). This initiative will address a number of concerns relating to systemic risks, the efficiency, competitiveness and integration of the market for UCITS funds in order to preserve the UCITS

attractiveness. This will contribute to preserving financial stability and fostering a culture of long-term investment in Europe, thus underpinning growth and jobs.

Following an extraordinary ECOFIN meeting, on 14 December 2012 the European Council [set out its agreed position](#) on two proposals aimed at establishing a Single Supervisory Mechanism (SSM) for the oversight of credit institutions, stating that this agreement will enable the Presidency to negotiate with the European Parliament with the aim of adopting the legislation before the end of the year (this is described in further detail in the Quarterly Assessment section of this Quarterly Report).

Subsequently [European Council conclusions on completing EMU](#), as adopted on 14 December 2012, were published. From the perspective of financial regulatory reform, paragraphs #6 – #11 are particularly pertinent. In these paragraphs the Council:

- urges rapid agreement on the (i) Single Supervisory Mechanism; (ii) new CRR/CRD rules for banks; (iii) Recovery and Resolution Directive; and (iv) Deposit Guarantee Scheme Directive;
- along with rapid follow up on the Liikanen report; and
- indicates that priority should be given to the proposal of a single resolution mechanism, to be agreed for adoption by the co-legislators within the current parliamentary cycle.

On 17 December 2012, [Ireland's EU Presidency priorities](#) were announced and its [dedicated website](#) went live. In developing its Presidency programme Ireland has listened carefully to the views of partners, the EU institutions, and most importantly, to citizens. The Irish programme reflects the desire across the EU to learn from the economic crisis and to focus on strengthening

competitiveness, fighting unemployment and its causes, and driving forward proposals that will deliver sustainable economic growth and employment. Concerning [economic and financial affairs](#) the Irish Presidency website confirms that the key priorities of the Irish Presidency include:

- promoting stability and economic growth across the EU including through the implementation of the Union's enhanced economic governance measures;
- seeking agreement on the component elements of the Banking Union proposals; and
- seeking agreement on enhanced regulatory financial proposals including the Markets in Financial Instruments Directive and Regulation (MiFID/MiFIR) and progressing other financial services dossiers.

The full programme of the Irish Presidency is being launched in early January 2013.

On 20 December 2012, the EBA published [feedback documents and amended templates](#) following the consultations on Draft Implementing Technical Standards (ITS) on supervisory requirements for (i) liquidity coverage and stable funding; and (ii) leverage ratio. These documents provide the current position of the Authority regarding the supervisory requirements for liquidity and leverage ratio reporting. In the absence of a final text of the Capital Requirements Regulation (CRR), the EBA cannot publish, at this juncture, a final proposal for these draft ITS. However, in order to provide transparency as to the comments received during the public consultations and to facilitate the institutions' timely preparation towards a harmonised liquidity and leverage ratio reporting these drafts have been made available.

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Financial Transaction Tax

On 28 September 2011 the European Commission [adopted a proposal](#) for a Directive on a common system of financial transaction tax (as reported in [Issue 23 of ICMA Quarterly Report](#)). During ECOFIN Council meetings in June and July 2012 it was ascertained that there was not likely to be unanimous support within the Council for a common system of FTT in the EU as a whole, as proposed by the Commission, in the foreseeable future; but it was pointed out that progress could be made on the issue in a more restricted group of Member States in the context of enhanced cooperation between interested Member States.

As from 28 September 2012, the Commission received requests from 11 Member States (Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and Spain) asking it to submit a proposal for a Council Decision to authorise enhanced cooperation; the objectives and scope of which should be based on the European Commission's original FTT proposal. The European Commission's subsequent analysis provided a positive outcome and, accordingly, on 23 October 2012, the [European Commission proposed](#) to the Council to authorise the enhanced cooperation in the area of FTT. The Council will have to decide now that the European Parliament [gave its consent](#) to the latter proposal on 12 December 2012. A subsequent European Commission proposal for a Directive implementing the enhanced cooperation in the area of FTT should follow in due course.

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Macroprudential regulation

Published by the BIS on 3 October 2012, *Managing Systemic Risk from the Perspective of the Financial Network under Macroeconomic Distress*, by Jae Hyun Jo, is the FSI's [Award 2012 Winning Paper](#). This paper proposes an enhanced methodology to assess contagion risk arising from financial connections across financial firms. The methodology addresses the following three questions:

- How does the failure of some financial institutions impact other financial institutions?
- What are the key exposures that create systemic risk?
- How much must inter-financial institution exposures be reduced in order to prevent extensive spillovers and how much additional capital is needed for the same purpose?

On 9 October 2012, Mario Draghi, in his capacity as Chair of the ESRB, [appeared before ECON](#) and discussed the ESRB's activities. Having initially commented briefly on the publication of the first risk dashboard on 20 September 2012 (see [Issue 27 of the ICMA Quarterly Report](#)) he spoke of the perceived status of risks in the banking sector. He then turned to the topic of risks in financial markets, focussing in particular on developments in the fields of CCPs and OTC markets. Before concluding, he also made comments on European Banking Union and the role of the ESRB; and follow-up on ESRB recommendations.

The IMF's full [October 2012 Global Financial Stability Report](#) (GFSR) was made available on 9 October. Chapter 1 of this GFSR, *Global Financial Stability Assessment*, assesses changes in the global financial stability conditions and risks since the last report and discusses policy responses, highlighting that euro area crisis remains the principal risk, emerging markets are most susceptible

to spillovers, while the US and Japan need clear plans for medium-term fiscal adjustment to sustain confidence. Chapter 2, *Restoring Confidence and Containing Global Spillovers*, provides a detailed analysis of the key challenges facing the euro area, US, Japan, and emerging markets, building upon earlier work on European bank deleveraging and exploring the sovereign-banking nexus in Japan as well the stability of US financial markets in the face of short and medium-term policy challenges. (Chapters 3 and 4 of this GFSR were reported on in [Issue 27 of the ICMA Quarterly Report](#).)

On 26 October 2012, the Steering Committee of the Vienna 2 Initiative [submitted observations and proposals](#) on cross-border supervisory practices to a number of European authorities. These focus on critical aspects of home-host cooperation, which are of particular importance for host countries in Central, Eastern, and South-Eastern Europe where locally systemic affiliates of foreign banks operate. The Vienna 2 Initiative held its [fifth Full Forum Meeting](#) in Brussels on 9 November 2012. This meeting brought together banking sector supervisors, central banks and fiscal authorities from host countries in emerging Europe and home countries of major EU cross-border banking groups operating in this region, the representatives of the parent banks as well as officials from the European Commission, the EBRD, the EIB, the IMF, and the World Bank (the ECB, ESRB and

FSB were observers). Recognising that decisions taken within the euro area need to take into consideration the interests of parties outside the single currency bloc, the meeting considered how necessary measures, in the area of bank recovery and crisis management and the Banking Union, impact the relations between home and host country authorities.

On 30 October 2012, the ECB published a report that summarises the [work of the Macroprudential Research Network \(MaRs\)](#). Since its establishment in spring 2010, MaRs has been pursuing and promoting research in three areas:

- macro-financial models linking financial stability and the performance of the economy (work stream 1);
- early warning systems and systemic risk indicators (work stream 2); and
- assessing contagion risks (work stream 3).

In response to experiences of the crisis, MaRs has the goal of developing models and analytical tools to broaden the basis for research in support of macroprudential oversight in the European Union. The ECB also made available research papers presented at the [second MaRs conference](#), held on 30 - 31 October in Frankfurt.

On 27 November 2012, the IMF made available a [March 2012 paper](#), *Enhancing Surveillance – Interconnectedness*

and Clusters. This presents a simple conceptual framework to better understand cross-border trade and financial interconnectedness. Countries are grouped together into “clusters” on the basis of having relatively tight trade and financial connections. Clusters are connected to one another through “gatekeepers” (eg Austria is a gatekeeper to the Central and Eastern Europe, and Sweden to the Baltics), and countries that are central to the whole network are in the “core” (the systemic-5). It is suggested that gatekeepers in particular can play a role in dampening or amplifying and propagating shocks.

On 3 December 2012, a [CGFS report was published](#), entitled *Operationalising the Selection and Application of Macroprudential Instruments*. With the aim of helping policymakers in operationalising macroprudential policies, this report specifically draws out three high-level criteria that are key in determining the selection and application of macroprudential instruments:

- the ability to determine the appropriate timing for the activation or deactivation of the instrument;
- the effectiveness of the instrument in achieving the stated policy objective; and
- the efficiency of the instrument in terms of a cost-benefit assessment.



This report specifically draws out three high-level criteria that are key in determining the selection and application of macroprudential instruments.

REGULATORY RESPONSE TO THE CRISIS

In trying to operationalise these criteria, this report proposes a number of practical tools.

On 10 December 2012, the US FDIC and the Bank of England [released a joint paper](#) outlining resolution strategies for large and complex firms. The approach outlined in the paper is based on legal powers provided by the legislative reforms enacted since the crisis, as well as – in the case of the UK – the proposed EU draft Recovery and Resolution Directive. It is designed to ensure that sound business, including operating companies (domestic and foreign) can be kept open and operating, limiting the effect on financial stability through contagion effects and cross-border complications. This process of cross-border dialogue illustrates more broadly how resolution planning can work on a cross-border basis.

The BIS 11th Annual Conference took place in Lucerne, Switzerland on 21 - 22 June 2012. The event brought together senior representatives of central banks and academic institutions, who exchanged views on the conference theme of *The Future of Financial Globalisation*. On 18 December 2012, the papers presented at the conference and the discussants' comments were [released as BIS Working Papers](#).

On 14 December 2012, the ECB published its [latest Financial Stability Review](#). This highlights a tangible easing of euro-area financial stability strains since the summer that has been evident across various market indicators. Nevertheless, key financial stability risks remain and there is no room for complacency. These potential risks stem from imbalances and vulnerabilities in the fiscal, macroeconomic and financial sector domains and they can be grouped into three categories:

- possible aggravation of the euro-area sovereign debt crisis, partly because of implementation risk for agreed policy measures at the national and EU level;

- further deterioration in bank profitability and credit quality owing to a weak macrofinancial environment; and
- fragmented financial markets amplifying funding strains for banks in countries under stress.

The systemic dimension of these possible risks originates not only from each of them individually, but also from potential amplification as a result of the interplay among them. Some progress has been made to date in addressing these root causes of stress, but continued momentum is needed to improve the robustness of the financial system, while completing the foundations of EMU, in order to durably strengthen euro area financial stability.

On 20 December 2012, the ESRB General Board held its [eighth regular meeting](#) and the second issue of the [risk dashboard](#) was published. Considering the current situation, it was noted that financial market sentiment has improved in recent months, though downside risks to growth continue to add to concerns about the macro-financial environment in the EU; and that indicators of systemic risk have also improved. Looking to the medium term, the General Board discussed four potential risks to financial stability in the EU: (i) the potential risks of under-provisioning and related forbearance; (ii) CCPs potentially becoming new too-big-to-fail institutions as a result of the mandatory clearing requirement for standardised OTC derivatives; (iii) the need to investigate possible implications of a low interest rate environment on the ability of long-term investors, including insurance companies and pension funds, to generate adequate returns; and (iv) possible risks posed by the overvaluation of some housing markets. The General Board also discussed how to tackle these risks from a macroprudential perspective.

In addition, the General Board considered two structural developments:

- first, asset encumbrance, which has grown in significance alongside the rising importance of secured funding. Future access to unsecured markets and correct pricing of risks may as a consequence become more difficult. In addition, encumbrance tends to be pro-cyclical, with collateralisation requirements rising during stress periods; and
- second, MMFs in Europe, where (consistent with initiatives being taken by other international authorities) the ESRB supports EU regulatory reform, building on the work of ESMA and ideally as part of a global standard.

As discussed in [Issue 27 of the ICMA Quarterly Report](#), IOSCO's research department has initiated a process of preparing *Securities Market Risk Outlook* reports, which aim to identify and assess potential systemic risks from securities markets. Work towards the development of the second such outlook, to be published in September 2013, is currently under way, with the IOSCO membership being asked to share their views through a short survey. This step is considered to be critical in analysis of systemic risk and risk build-up in securities markets as, in some cases, emerging risks may not be captured in the available data.

Published on 27 December 2012, the fourth issue of the ESRB's macroprudential commentaries deals with [lending in foreign currencies as a possible source of systemic risk](#). This paper examines the phenomenon of loans extended in, or indexed to, foreign currencies, taken out by unhedged borrowers in central and eastern European countries.

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Credit Rating Agencies

On 18 April 2012 ESMA published its (positive) technical advice to the European Commission on the equivalence of the regulatory regimes for Credit Rating Agencies (CRAs) in the USA, Canada and Australia (see [Issue 26 of ICMA Quarterly Report](#)). Responsive to this, on 5 October 2012 the Commission adopted decisions recognising the equivalence of the legal and supervisory frameworks of the USA, Canada and Australia. The difference which these positive decisions make is that, once the Commission has declared a third-country regime to be equivalent to the EU regime, CRAs which are established in that specific third country can submit their application to ESMA to be certified in the EU in accordance with the CRA Regulation. Upon any such certification, the ratings of such a CRA may be directly used for regulatory purposes by EU-authorized financial institutions. (This is entirely distinct from the process under which EU-authorized CRAs may endorse ratings from certain third country CRAs for such use in the EU). Hitherto, such an equivalence decision only existed for Japan (dating from 28 September 2009).

On 16 October 2012, the European Commission published a [Delegated Regulation](#) establishing the rules within which ESMA will operate when imposing fines on CRAs when they breach EU legislation. The EU's CRA Regulation includes a full list of infringements that, if committed by a CRA, may trigger fines, eg conflicts of interest, obstacles to supervisory activities or non-disclosure of certain information.

In [Issue 24 of the ICMA Quarterly Report](#), the European Commission's 15 November 2011 proposed draft Directive and draft Regulation, to toughen the EU's CRA regulatory framework, were discussed. Following much work on these proposals, on 28 November 2012

the [Cyprus Presidency announced](#) that, together with the European Parliament and the European Commission, it had achieved political agreement on versions of these texts. It is considered that the implementation of these agreed texts will ensure that financial institutions do not blindly rely on credit ratings for their investments (reducing overreliance), while further eliminating conflicts of interest. The new rules also seek to increase competition, make CRAs more accountable for the ratings they provide and better regulate the issuance of sovereign debt ratings. The agreed texts require official confirmation from the European Parliament, which [anticipates a plenary vote in January 2013](#); and have been [confirmed by the Council](#).

In the meantime, ESMA has decided to dismantle its CRA Consultative Working Group (CWG). In support of this decision, ESMA notes that:

- ESMA and the supervision of CRAs in the EU have undergone major changes since the creation of the CWG during CESR times;
- the growing number of [registered CRAs](#) (currently 18 registered and 1 certified CRA) was not appropriately reflected in the composition of the CWG; and
- ESMA has [created the SMSG](#) for consultation on ESMA-related matters, including CRA regulatory issues.

On 20 December 2012, ESMA launched a consultation paper on [Guidelines and Recommendations on the Scope of the CRA Regulation](#). The draft Guidelines aim to provide clarification on certain aspects of the scope of the CRA Regulation to registered CRAs, other market participants operating on the perimeter of this sector and to national securities markets regulators. The closing date for responses is 20 February 2013 and an open hearing on the consultation will take place in Paris on 22 January 2013.

On 21 December 2012, IOSCO published [two reports](#) on CRAs: the final report on *Credit Rating Agencies: Internal Controls Designed to Ensure the Integrity of the Credit Rating Process and Procedures to Manage Conflicts of Interest*, and a consultation report on *Supervisory Colleges for Credit Rating Agencies*. Both of these reports form part of IOSCO's effort to improve the integrity of CRAs, as part of the global effort to enhance investor protection and the fairness, efficiency and transparency of securities markets. The final report summarizes the information received in response to a questionnaire and a [May 2012 consultation paper](#). It concludes that CRAs tend to adopt different policies and procedures to ensure the quality and integrity of the rating process, and to manage conflicts of interest, because they vary in size. However, despite these differences, all surveyed CRAs have adopted some form of policies and procedures to provide internal controls and safeguard against conflicts of interest. The consultation report, comments on which are requested by 15 February 2013, recommends establishing supervisory colleges for internationally active CRAs and provides preliminary guidelines on how to establish and operate them.

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OTC (derivatives) regulatory developments

Hosted by the UK FSA, the OTC Derivatives Regulators' Forum [met on 16 - 17 October 2012](#). The first day of the meeting was focussed on CCPs and the second day on trade repositories. A wide range of updates and progress reports were delivered and representatives of CCPs and TRs were invited in for discussion sessions.

REGULATORY RESPONSE TO THE CRISIS

On 31 October 2012, the FSB published its [fourth six-monthly progress report](#) on the implementation of OTC derivatives market reforms. The report takes stock of the readiness of market infrastructure across the FSB's member countries to provide clearing services, collect and disseminate trade data and provide organised trading platforms for OTC derivatives. The report also reviews the progress made by standard-setting bodies and national and regional authorities towards meeting the commitments made by G20 Leaders at the Pittsburgh 2009 Summit that, by end-2012, all standardised OTC derivatives contracts be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties (CCPs); OTC derivative contracts be reported to trade repositories; and non-centrally cleared contracts be subject to higher capital requirements. The key messages of the report are as follows:

- market infrastructure is in place and can be scaled up;
- the international policy work on the four safeguards for global clearing is substantially completed and implementation is proceeding at a national level;
- regulatory uncertainty remains the most significant impediment to further progress and to comprehensive use of market infrastructure.

A 5 November 2012 [FSB Secretariat information note](#) describes *Jurisdictions' Declared Approaches to Central Clearing of OTC Derivatives*. All FSB member jurisdictions have made a decision about their approach to central clearing of OTC derivatives. The majority of countries (16) report that they will adopt mandatory clearing requirements or a combination of mandatory clearing requirements and incentives to meet the G20 commitment to have all standardised OTC derivatives contracts centrally cleared; whilst seven

countries note that they anticipate initially only using incentives to meet the G20 commitments. Most jurisdictions (17) also note that market participants from their jurisdiction will be able to use either domestic or cross-border CCPs, as clearing services may vary. Still, several jurisdictions anticipate that, because of the characteristics of the domestic market, their participants will (at least initially) clear through domestic CCPs. Two jurisdictions note that they anticipate that their market participants will rely on cross-border CCPs, since domestic CCPs are not available for clearing OTC derivatives.

As described in a [4 December 2012 statement](#), *Operating Principles and Areas of Exploration in the Regulation of the Cross-Border Derivatives Market*, leaders of authorities with responsibility for the regulation of the OTC derivatives markets in Australia, Brazil, the EU, Hong Kong, Japan, Ontario, Quebec, Singapore, Switzerland and the US met on 28 November 2012, to discuss reform of the OTC derivatives market. Recognising the need for a consistent approach to the regulation of a global market, the statement describes:

- understandings reached amongst the authorities on clearing determinations;
- sharing of information and supervisory and enforcement cooperation; and timing; and
- identified areas for further exploration, covering scope of regulation and recognition or substituted compliance for cross border compliance.

A further meeting will take place in Brussels in early 2013.

On 19 December 2012, the European Commission announced its adoption of nine regulatory and implementing technical standards for the Regulation on OTC Derivatives, Central Counterparties and Trade Repositories (EMIR). These were developed by the ESAs and

have been endorsed by the European Commission without modification. The technical standards will enter into force on the twentieth day following publication in the EU's *Official Journal*; and, as with any other EU Regulation, their provisions will be directly applicable across the EU from the day of entry into force. One technical standard submitted by ESMA, on the specific point of colleges for CCPs, was not endorsed because of concerns as to the legality of some of the provisions. The European Commission will ask ESMA to redraft the standard and it will be adopted at a later stage. However, this will not affect the timing of the clearing obligation, or the timing of authorisation of CCPs under EMIR, since the provisions of this technical standard are not a prerequisite for CCPs to begin applying for authorisation under EMIR.

On 20 December 2012, ESMA [published a consultation paper](#) on *Guidelines Regarding the Assessment of Interoperability Arrangements for CCPs*. CCPs enter into such agreements to allow their users to execute trades with a counterparty that has chosen another CCP. ESMA's guidelines are aimed at providing a level playing field for CCPs in the EU by improving the rigour and uniformity of standards applied in the assessments of CCPs' interoperability arrangements. The guidelines define what national regulators should look at in assessing those arrangements and the aspects of the interoperable arrangements CCPs will need to focus their attention on in order to have safe and sound agreements in place. The closing date for responses to this consultation is 31 January 2013 and the feedback received will be used to help finalise the guidelines.

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French banking reform

by Nicholas Pfaff

France is the first country in Continental Europe to propose comprehensive [banking reform legislation](#) in the aftermath of the [Liikanen report](#). This draft legislation offers a pragmatic middle way on recommendations of Liikanen and the approaches being progressed across the Channel and the Atlantic (respectively [Vickers](#) and [Volcker](#)). It may also provide a blueprint for the Continent with its focus on accommodating the European universal banking model. French proposals are characterized by a compromise on the key issues of the segregation of proprietary trading and the role of market making. This is balanced by a substantive and forward-looking reinforcement of the powers of supervisory authorities including in key areas such as the oversight of trading activities and the execution of bank resolution. The reform also includes new measures designed to increase industry funding for the support of failing institutions and to reposition taxpayer support as an absolute last resort. Finally, the draft legislation aims to reinforce supervisory and regulatory powers for an effective financial stabilization policy. The text is generally designed to anticipate and work within future European reforms and the plans for a [European Banking Union](#). It is being presented to the French Parliament for debate and a vote that should take place in the first half of 2013.

Under French plans, market making activities are both recognised as legitimate and essential for market liquidity. Contrary to a key Liikanen recommendation, market making would remain within the normal perimeter of a bank's activities. Indeed, although a segregation of certain trading activities is required, this pertains to a restricted list of proprietary activities defined as speculative and "not economically useful". These activities, subject to as yet defined thresholds, would be ring-fenced by July 2015 in a separately capitalized entity that would have strictly limited access to funding from its banking shareholder and would be expected to stand alone in case of financial difficulty. Proprietary trading on agricultural products and the use of high-frequency trading are further subject to complete bans. Conversely, in addition to market making, client and group hedging, treasury management, and securities held for investment purposes are all considered economically justified.

This comparatively moderate approach to immediate structural reform for French banks is paired with a substantial strengthening of the powers of supervisory bodies to investigate and sanction,

as well as initiate and manage resolution in a manner that clearly draws on the [European Commission Proposal on Bank Recovery and Resolution](#). The [Autorité de Contrôle Prudentiel](#) (ACP) of the Banque de France becomes the [Autorité de Contrôle Prudentiel et de Résolution](#) (ACPR – literally the Prudential Control and Resolution Authority). The ACPR will have the ongoing ability to investigate in detail all trading activities, and can ban outright those that are considered excessively speculative. It will have the power to suspend or cancel a financial institution's banking license in case of a wider pattern of rule breaking. The ACPR also gains an extensive remit to handle bank resolution. Major banks will thus be required to prepare living wills under its oversight. If necessary, the ACPR will have the power to take control of failing institutions, terminate management and nominate an administrator. It can also carve up, in this case, an institution's activities and transfer them, as necessary, to other institutions. Furthermore, it will have the authority to bail in equity and subordinated debt holders in order to protect depositors and ultimately taxpayers.

The reform also aims to modify France's deposit guarantee mechanisms with the objective of limiting recourse to public funds in future crises. The current [Fonds de Garantie des Dépôts](#) becomes part in this way of the new resolution mechanisms and is renamed the [Fonds de Garantie des Dépôts et de Résolution](#) (FGDR). Piloted by the ACPR, it will intervene in support of the resolution process with the objective, when possible, to avoid taxpayer funded support. In line with this, the FGDR is targeted to grow through industry contributions to a total of €10 billion by 2020.

Finally, the reform also proposes changes to promote preventive financial stabilization measure with the creation of the [Conseil de Stabilisation Financière](#) (out of the Banque de France's existing [Corefris](#) Council). This renamed entity will be charged with evaluating systemic market risks and speculative bubbles. Most significantly, it will have the power to address and deflate these preventively by requiring increases in bank capital and through credit controls.

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by David Hiscock

Short-Term Markets

European repo market

Shadow banking: The European Parliament's (EP's) ECON Committee adopted (39 votes for / none against) a 25 October 2012 [report on shadow banking](#). Within the explanatory statement, paragraph "D" (page #13) states: *"The repo and security lending market fulfil an important function in financing financial institutions. However, more transparency is urgently needed; therefore regulators should be allowed to impose minimum haircuts or margin levels for the collateralised financing markets"*.

From a repo market perspective, it is also particularly relevant to review the points numbered 7 - 13 (pages #5 & #6); 28 (page #8); and 30 (page #9). These paragraphs in the EP's report clearly illustrate the approach which it is seeking to adopt in the coming debate over necessary EU legislative measures for repo and shadow banking. Besides far reaching demands for increased transparency (trade repository / central database), this includes calls for increased standardisation, minimum haircuts/margins, limitations on re-hypothecation of collateral and a review of bankruptcy privileges.

This EP report was [adopted in plenary](#) on 20 November 2012, by a show of hands.

In its [18 November 2012 press release](#), the FSB announced the release of a set of three further consultation papers, for comment by 14 January 2013, which relate to its ongoing work on shadow banking. These include [A Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos](#).

In developing its policy recommendations relating to securities lending and repos, the FSB's work stream 5 (WS5) focused on addressing perceived financial stability issues. WS5 has endeavoured to ensure that its recommendations minimise the risk of regulatory arbitrage as well as undue distortion of markets, and are consistent with other international regulatory initiatives. The policy recommendations of WS5 are categorised in three broad groups in accordance with the nature of the recommendations: improvement in transparency (Section 2 of the paper); regulation of securities financing (Section 3 of the paper); and structural aspects of the securities financing markets (Section 4 of the paper). The FSB's 13 recommendations are then summarised in Annex 1 of the paper.

Application of the proposed policy recommendations may vary in details across jurisdictions, depending on existing regulatory frameworks. (In the EU, the

European Commission's largely parallel shadow banking project will progress with broadly equivalent proposals). The implementation of recommendations and their consistency across jurisdictions will be monitored by the FSB after they are finalised. The FSB seeks comments on these proposals (there are 22 specific questions included in the paper) by 14 January 2013 and expects to publish final recommendations in September 2013.

Upon initial reading, the FSB's recommendations appear reasonably balanced. Points to note with respect to some of the key debated topics are:

- *trade repositories*: the recommendation does not say that one should immediately be set up, but rather: "The FSB should consult on the appropriate geographical and product scope of such TRs"; and "the FSB should establish a working group to identify the appropriate scope and undertake a feasibility study for one or more TRs at a global level. Such feasibility studies should involve market participants". It is worth noting that Annex 2 of the paper considers "different approaches to data collection", including some comparison of the relative merits of regulatory reports, surveys and trade repositories;
- *minimum haircuts*: the recommendation does not say they must be introduced, but rather: "The FSB should consult on whether a framework of numerical floors would be effective and workable"; and "Regulatory authorities should introduce minimum standards for the methodologies that firms use to calculate collateral haircuts"... which ... "seek to minimise the extent to which these methodologies are pro-cyclical";
- *re-hypothecation*: the recommendation does not suggest broad measures potentially affecting re-use, but rather only calls for appropriate "regulations governing re-hypothecation of client assets";
- *CCPs*: the recommendation does not say they must be introduced, but rather: "Authorities should evaluate the costs and benefits of proposals to introduce CCPs in their securities lending and repo markets"; and
- *bankruptcy law*: the recommendation does not say that repos must further share in losses, but rather that changes "should not be prioritised for further work at this stage due to significant difficulties in implementation".

The ERC is studying this paper in detail and will submit an appropriate response.

The ECB has published the [introductory remarks delivered by Vítor Constâncio](#), Vice-President of the ECB, at the 3 December ECB workshop, *Repo Market and Securities Lending: Towards an EU Database*. This workshop gathered together key representatives from public authorities, regulators and market representatives with the aim to achieve a common understanding of the following key issues:

- First, what are the expected benefits from requiring additional and more granular data for monitoring repo and securities lending markets and which data is essential to make such a data collection effort useful for all relevant stakeholders?
- Second, how could these data be better collected to inform the public authorities' assessment about firm-level and systemic risks?

In his remarks, Mr Constâncio recalled that at the European Commission's Shadow Banking Conference on 27 April 2012 (as reported in [Issue 26 of the ICMA Quarterly Report](#)) he launched a proposal to create an EU central database on repos, as a joint effort by public authorities and the financial industry. While this should be read in full, here are a few specific extracts from the text:

"I am counting on this workshop to launch the practical discussion about the main issues and the challenges to be addressed and, most importantly, the possible solutions for this proposal to become reality."



Upon initial reading the FSB's recommendations appear reasonably balanced.

“However what is important is ensuring a timely and detailed, complete central view on the market. In fact, the ECB does not need to centralise itself the data gathering, provided it has access to all the information it requires.”

“Assuming a specific home-currency for the transactions covered, six transaction specific information items are essential: (1) the counterparty of the transaction, (2) the principal amount, (3) the interest rate or lending fee, (4) information on underlying collateral (including type, issuer, maturity, currency and valuation of the collateral), (5) information on the applied haircut as well as (6) the tenor or maturity of the transaction. I would add to these also information about re-use of securities.”

“I would like to point to the potential use of a trade repository to establish a new benchmark on secured financing. The discussions on potential improvements of current unsecured or secured rates pointed to the need to move to more transactions based figures. A repo trade repository at first sight looks as a promising candidate for establishing and calculating a new benchmark for repo rates based on actual transactions.”

“It will be indispensable today to identify practical solutions on how information can effectively and efficiently be retrieved and fed to a database, by whom, and to whom, under what governance and technical channels, and what shall be the indispensable confidentiality requirements to ensure an appropriate level of data disclosure taking into account the needs of authorities and different stakeholders.”

As part of ICMA's ongoing engagement with the regulatory authorities, a delegation from the ERC Committee and the ERC Operations Group attended this workshop. During the discussions they offered concrete support for the creation of this EU database. As a result, the forthcoming 24th ERC Repo Survey will be used as part of the work to promptly establish such an outcome. The full report of this survey will be presented at the next ERC AGM, in Paris on 11 March 2013.

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ECP market

ABCP: The European Parliament's (EP's) ECON Committee has adopted (39 votes for / none against) a 25 October 2012 [report on shadow banking](#). Of note within the explanatory statement are paragraph “A” (page #12) and paragraph “E” (page #13), each of which relates to specific points on securitisation (and are therefore relevant to ABCP); and paragraph “F” (page #13), which concerns the regulation of MMFs.

Also particularly relevant are the points numbered 22 (page #7) and 29 (page #9), in relation to securitisation (including ABCP); and the points numbered 31 - 32 (page #9), in relation to MMFs. These paragraphs in the EP's report clearly illustrate the approach which it is seeking to adopt in the coming debate over further necessary EU legislative measures for securitisation (including ABCP) and MMFs. This includes a proposed limit on the number of times an asset can be securitised, further risk retention and more standardisation of securitisation; and controls over MMFs, particularly those offering stable NAV.

This EP report was [adopted in plenary](#) on 20 November 2012, by a show of hands.

On 16 November 2012 IOSCO [published](#) a new report, entitled [Global Developments in Securitisation Regulation](#). This report on securitisation (which includes ABCP):

- makes observations about the role sound securitisation markets can play in supporting economic growth and the role regulation can play in reducing systemic risk and restoring investor trust and confidence;
- provides a snapshot of the global securitisation markets;
- summarises key themes, observations and issues coming out of the responses to IOSCO's [June 2012 consultation paper](#) in relation to approaches to risk retention, transparency and standardisation;
- makes recommendations in relation to risk retention, transparency and standardisation; and
- identifies other medium or longer-term priorities for policy consideration.

There is one ABCP-specific segment in the report, which is on page #21. This discusses feedback to

the consultation paper, which highlighted conflicting differences between EU and US proposed rules.

On 27 November 2012, IOSCO [published its final report](#) on *ABS Ongoing Disclosure Principles*. This contains principles designed to provide guidance to securities regulators who are developing or reviewing their regulatory regimes for ongoing disclosure for asset-backed securities (ABS). The objective of the *ABS Ongoing Disclosure Principles* is to enhance investor protection, by facilitating a better understanding of the issues that should be considered by regulators in relation to ongoing disclosure regimes for ABS.

On 18 December 2012, the BCBS [published a consultative document](#) concerning potential revisions to the Basel securitisation framework. The objectives of these revisions are: to make capital requirements more prudent and risk-sensitive; to mitigate mechanistic reliance on external credit ratings; and to reduce current cliff effects in capital requirements. In the coming months, the BCBS will also conduct a quantitative impact study (QIS) on the proposals, the results of which will be considered alongside responses, to be submitted by 15 March 2013, to the public consultation.

Two portions of the text appear of potentially particular significance for ABCP. First, to reduce complexity, the BCBS proposes to have only one look-up risk-weight table for short-term credit exposures. The short-term ratings-based approach look-up table used in the current standardised approach for securitisation would be retained, with its application expanded to banks that use internal ratings for the type of underlying exposures for a given securitisation exposure. The proposed risk weights for securitisation exposures with short-term ratings are:

External credit assessment	A-1/P-1	A-2/P-2	A-3/P-3	All other ratings
Risk weight %	20	50	100	1,250

Second, also to reduce complexity, there should be elimination of special treatment for certain exposures, impacting: (i) second loss or better positions in ABCP programmes; (ii) fall-back option for internal ratings-based liquidity facilities; and (iii) preferential credit conversion factor for eligible liquidity facilities under the standardised approach.

[Moody's 10th Annual ABCP](#) Conference took place on 15 November 2012, with analysts from Moody's ABCP group being joined by market participants to discuss issues which affect the EMEA ABCP market. The opening session *The ABCP Market and Banking Sector Outlook* and the closing session *Trade Receivables – Performance, Trends and Analysis* involved presentation from applicable Moody's analysts. In between times there were two moderated panel discussions, with the investor panel focussing on the *Rationale and Challenges in Investing in ABCP Today*; and the sponsor panel on *How Conduits are Adapting to the Regulatory and Economic Environment*. In the centre of the event's programme there was also a law partner's presentation under the heading *Regulatory Developments Affecting the ABCP Market*.

Money market funds (MMFs): On 9 October 2012, IOSCO [published a final report](#) on *Policy Recommendations for MMFs*, which proposes recommendations to be the basis for common standards for the regulation and management of MMFs across jurisdictions. These are articulated around key principles for valuation, liquidity management, use of ratings, disclosure to investors, and repos. The IOSCO Board approved this report during its meeting on 3 – 4 October in Madrid. (While there were no other objections, it was noted that a majority of the Commissioners of the US SEC did not support publication).

As requested by the FSB, the current 15 recommendations for MMFs seek to supplement the existing frameworks where IOSCO considers there is still room for further reforms and improvements, following reforms undertaken on MMFs both in the US and in Europe in 2010. Also, compared to the 2010 reforms, which mainly focused on the asset side of funds, the present recommendations address vulnerabilities arising from the liability side, as well as the crucial issue of valuation and the display of a constant net asset value (CNAV). In particular, the recommendations seek to address the vulnerabilities around the risk of run and first-mover advantage which could have broader consequences for the financial system.

Implementation of the recommendations may vary from jurisdiction to jurisdiction, depending on local conditions and circumstances, as well as according

to the specificities of the existing domestic legal and regulatory structures; and the implementation of some of the recommendations may need to be phased in, in order to avoid disruptive impacts on the MMF industry and the functioning of the financial system at large. IOSCO proposes to conduct a review of the application of these recommendations within two years with a view to assess whether they should be revised, complemented or strengthened.

In the US, as reported in [Issue 27 of the ICMA Quarterly Report](#), the SEC's work on MMF reforms has stalled. This has prompted action on the part of the Financial Stability Oversight Council (FSOC). First, on 27 September, Treasury Secretary [Geithner sent a letter](#) to the FSOC members on necessary MMF reforms. This was discussed at the FSOC's [28 September meeting](#) and it was agreed that work should be done to prepare a recommendation for the FSOC to consider at its November meeting. This was done, and at the FSOC's [13 November meeting](#) it was duly resolved that the proposed recommendations would be [released to the public](#) and published in the Federal Register, initiating a 60-day public comment period.

Meanwhile, the SEC has [published a study](#) by the staff of the Division of Risk, Strategy, and Financial Innovation, dated 30 November 2012, which is entitled *Response to Questions Posed by Commissioners Aguilar, Paredes, and Gallagher*. This study addresses questions: (i) concerning the causes of investor redemptions of prime MMF shares and purchases of Treasury MMF shares during the 2008 financial crisis; (ii) covering the efficacy of the 2010 MMF reforms; and (iii) relating to how future reforms might affect the demand for investments in MMF substitutes and the implications for investors, financial institutions, corporate borrowers, municipalities, and states that sell their debt to MMFs.

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Liquidity Coverage Ratio

The Group of Governors and Heads of Supervision (GHOS), the oversight body of the Basel Committee on Banking Supervision (BCBS), [met on 6 January 2013](#) and unanimously endorsed a package of amendments to the formulation of the [Liquidity Coverage Ratio \(LCR\)](#). The package has four elements: revisions to the definition of high-quality liquid assets (including expansion of the definition to allow the inclusion of certain highly rated RMBS, with a 25% haircut; and corporate debt securities rated A+ to BBB and certain unencumbered equities, with haircuts of 50%) and net cash outflows; a timetable for phase-in of the standard (the LCR will be introduced as planned on 1 January 2015, but the minimum requirement will begin at 60%, rising in equal annual steps of 10 percentage points to reach 100% on 1 January 2019); a reaffirmation of the usability of the stock of liquid assets in periods of stress, including during the transition period; and an agreement for the BCBS to conduct further work on the interaction between the LCR and the provision of central bank facilities. GHOS members endorsed two other areas of further analysis. First, the BCBS will continue to develop disclosure requirements for bank liquidity and funding profiles; and second, it will continue to explore the use of market-based indicators of liquidity to supplement the existing measures based on asset classes and credit ratings.

The GHOS also endorsed a new Charter for the BCBS (which sets out the BCBS's objectives and key operating modalities, and is designed to improve understanding of its activities and decision-making processes); and discussed the BCBS's medium-term work agenda. Review of the Net Stable Funding Ratio (NSFR), which remains subject to an observation period ahead of implementation in 2018, will be a priority for the BCBS over the next two years. Over the next few years, the BCBS will also: complete the overhaul of the policy framework currently under way; continue to strengthen the peer review programme established in 2012 to monitor the implementation of reforms in individual jurisdictions; and monitor the impact of, and industry response to, recent and proposed regulatory reforms.

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LIBOR and other benchmarks

by David Hiscock

On 17 October 2012, the UK Government reaffirmed its commitment to reforming the submission and administration of the LIBOR benchmark by [accepting the recommendations](#) of Martin Wheatley's independent review of LIBOR (as discussed in [Issue 27 of the ICMA Quarterly Report](#)) in full.

In particular, Baroness Hogg will now lead a panel that will identify an appropriate successor to the British Bankers' Association (BBA); and the Government will amend the Financial Services Bill, which is currently before Parliament:

- to bring LIBOR activities within the scope of statutory regulation, including the submission and administration of LIBOR;
- to create a new criminal offence for misleading statements in relation to benchmarks such as LIBOR, as well as amending the language of existing offences; and
- to provide the new Financial Conduct Authority (FCA) with a specific power to make rules requiring banks to submit to LIBOR, with reference to a Code of Practice produced by the rate administrator.

Prompted by the recommendations of the Wheatley review of LIBOR, [on 8 November 2012](#) the BBA [launched a consultation](#) on how initial changes should be implemented. Specifically, the consultation outlined the BBA's proposed timescale for a phased discontinuation of certain LIBOR currencies and maturities in line with the sixth recommendation of the Wheatley review. Following on from its 7 September

2012 [response to the Wheatley review](#), the ICMA submitted a [response to the BBA](#), ahead of the 9 December 2012 deadline.

On 14 December 2012, the BBA [published an initial feedback statement](#). Importantly this states that the BBA has revised the timetable and scope of the proposed changes, to allow for a greater period of market adjustment. Details of the refinements are as follows:

- for those tenors being removed from all currencies in the LIBOR framework, this change will now be implemented at the end of May 2013 (rather than January 2013) in order to allow time for users to adapt, and protocols to be developed, to deal with the changes;
- publication of Australian and Canadian dollar fixings will now be discontinued at the end of May 2013, rather than the end of February and March respectively as originally proposed; and
- for those currencies which remain in the LIBOR framework after May 2013, the two-month tenor will be retained.

All other changes will be implemented as

proposed in the consultation paper.

As reported in [Issue 27 of the ICMA Quarterly Report](#), on 5 September 2012 the European Commission [launched a consultation](#) inviting stakeholders to comment on possible new rules for the production and use of indices serving as benchmarks in financial and other contracts. Whilst the European Commission invited responses to 46 specific questions, the ICMA determined that it would be of greatest value for its submission to focus on those few points of most direct relevance to the international capital market and where it seems most likely that the ICMA may have distinctive points to contribute. Accordingly the ICMA prepared a response which primarily reflects the ICMA submission which was made on 7 September 2012 to the Wheatley review. This [response was duly submitted](#) in accordance with the 29 November 2012 deadline.

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The consultation outlined the BBA's proposed timescale for a phased discontinuation of certain LIBOR currencies and maturities.

Primary Markets



by Ruari Ewing

Prospectus Directive review

Over the last quarter of 2012, there were limited specific developments concerning the review of the Prospectus Directive, as markets and regulators continued their struggle to come to terms with the practical workings of the revised regime.

However, further thought has been given by the market to the practicalities surrounding general consent to prospectus use in a retail cascade, should an issuer want distributors wishing to rely on such consent to comply with certain requirements. These might relate to cascade offer terms, selling restrictions, etc, and be potentially extensive and detailed. Clearly, it will not be possible for such distributors to sign agreements with the issuer, as their identity will be unknown. An early tentative approach was to make the consent itself conditional on compliance with the relevant obligations. However, because of the potentially draconian consequences of non-compliance (effectively public offerings without an approved prospectus), an alternative approach is being developed.

The proposed alternative approach involves the construction of a contractual relationship between the issuer (and, if desired, the lead managers involved) and each distributor that relies on the general consent. Instead of signing a specific agreement with the issuer/managers, each distributor would enter into the contract (the terms of which would be set out in some readily available place such as the prospectus, or a website identified in the prospectus) by its conduct. Specifically, as a condition of the general consent, a distributor would be required to

state on its website (i) that it is relying on the general consent and (ii) that it accepts the terms of the contract.

Separately, ESMA has published the *18th Updated Version of its Questions and Answers on Prospectuses*. Whilst this deletes or updates 27 items, regarding Eurobond issuance this seems on an initial reading to be mostly consequential to: (i) ESMA's evolution from its CESR predecessor; (ii) the changes brought in by the Prospectus Directive review or (iii) the removal of certain regulators' dissenting views. However, more detailed examination will be needed before any firm conclusions can be reached in this respect. This version of the *Questions and Answers* also includes one new item – #83 – on the type of underlying. This states that, though all known information needs to be included in a base prospectus, where an issuer has not decided on the details of the underlying(s), the minimum information to be included in the base prospectus is whether the underlying(s) is/are: an equity security, a non-equity security, an interest rate, an index or a commodity. The type of underlying should be defined if not within the listed categories.

Despite the above developments, the enduring uncertainty is such that ICMA remains unable to publish updated *pro formas* of final terms and pricing supplement or new model retail cascade language – any queries should in the meantime continue to be directed to the author of this article.

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MAD review

ICMA continues to focus on those aspects of the ongoing review of the EU's current Market Abuse Directive (MAD) that affect primarily the Eurobond issuance markets, as many other organisations are focused on aspects of the review that impact the markets more broadly and not just Eurobond issuance.

Following several interim Presidency compromise proposals, the EU Council has adopted a [general approach on the proposed new Market Abuse Regulation \(MAR\)](#) and also a [general approach on the proposed accompanying new Market Abuse Sanctions Directive \(MAD II\)](#), which will serve as the basis for the Council's Trilogue negotiations with the European Parliament and Commission.

The Council's general approach on MAR is a clear improvement over the original [Commission proposal](#), notably in terms of its definition of inside information, where the impractically wide proposed Article 6.1(e) relating to "relevant" information has been deleted. The Council's general approach retains, pretty much unchanged, the explicit safe harbour for pre-sounding first included in the [3 September Presidency compromise](#) and discussed in the [Fourth Quarter 2012 edition](#) of this Quarterly Report.

Whilst the general approach seems conceptually workable in terms of bringing an explicit "soundings" regime within the MAR structure (to the extent this is felt necessary), there seem to be several apparent ambiguities, inconsistencies or unintended potential consequences. These namely concern: (i) soundees involving sounders in their internal consultations; (ii) Chinese wall requirements potentially being inconsistent with general organisational trading incentives; (iii) honouring existing contracts (required

by law) being subject to a vague "good faith" test; (iv) defined "legitimate behaviour" defences seemingly being inapplicable where undefined "illegitimate reasons" are also involved; (v) sounders seemingly being compelled to purportedly cleanse soundees though there can be no reliance in this respect (the law making each party responsible for their own assessment); (vi) sounders being superfluously required to keep records of why a stricter approach to sounding is adopted; and (vii) an issuer obligation to disclose inside information immediately when rumours are sufficiently accurate seeming to encourage fishing.

Separately, the European Parliament also adopted its [report on MAR](#), which seems to include a weaker definition of inside information, notably retaining the Article 6.1(e) "relevant" information element. The report also provides that the stabilisation safe harbour only applies when relevant information about the stabilisation is both "disclosed to and approved by the competent authority". This concept, also applicable in the buy-back context (incidentally helpfully proposed to be extended from just own shares to all securities), was not present in the preceding draft report or any of subsequently published proposed amendments. It is unclear how this approval would practically operate in terms of stabilisation timelines (which can begin from pricing – ie within hours of a transaction being decided and announced by an issuer) and also on what basis such approval would be decided, since the current information disclosure requirement is objective rather than subjective. Parliament also adopted its [report on MAD II](#).

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It is unclear how approval would practically operate in terms of stabilisation timelines.

PRIPs

Work on the EU's Packaged Retail Investment Products (PRIPs) initiative continues with the Joint Associations Committee on Retail Structured Products (JAC), of which ICMA is a participant, publishing a [position paper](#) on the preceding [Commission proposal](#) (discussed in the [Fourth Quarter 2012 edition](#) of this Quarterly Report, together with the main underlying considerations now picked up in the JAC position paper). Subsequently at Council level, an [initial Presidency compromise text](#) was published, which in many ways is a marked improvement on the Commission proposal.

Most notably, civil liability for the "key information document" (KID) only arises where the KID "is misleading, inaccurate or inconsistent with the other binding contractual documents" and the KID's purpose is narrowed to just "helping" investors take informed investment decisions. Whilst much improved, the liability focus (as referenced to contractual documents rather than prospectuses where available) seems to imply that KID content will focus on structure and market information and not on issuer credit information, which would be sensible but will need to be confirmed. The compromise includes a distinct heading for manufacturer default, separate from payout outcomes, but it is unclear whether this is intended to (i) simply flag the theoretical risk and consequence of default (which could seem workable) or (ii) involve a substantive assessment of such risk occurring and even likely loss given default (which could not be meaningfully addressed). The limited KID purposes – effectively (i) helping investors to sort which PRIPs to consider further and (ii) acting as a basis or a "map" for subsequent discussion with a MiFID intermediary or subsequent reading of a full prospectus – though improved, could be clarified further.

The compromise seems to limit the scope to only those retail products that are structured, though the drafting seems at risk of also catching simple floating-rate notes. Other products are left open to national rules, though one may wonder whether the maximum harmonisation provisions of the Prospectus Directive might limit this to an extent. Other improvements include abandoning the inclusion of various non-commercial ethical "labels", no longer reversing the burden of proof and emphasising

existing national ADR processes. The compromise also extends scope to advising on PRIPs (and not just selling them), establishes a regulatory power to ban marketing of some PRIPs (which implies KIDs will not be subject to prior regulatory approval but also seems to overlap with similar intervention powers being developed under MiFID) and includes a target market description within the KID. Some ambiguities and areas of potential concern include: (i) who will be the competent regulator; (ii) KID updating obligations once a PRIP is no longer being offered by, or on behalf of, its manufacturer; (iii) how a risk indicator could meaningfully operate; (iv) whether some distributors might be characterised as manufacturers in ways that might not be intended; (v) capping KID length at 3 pages; and (vi) ongoing incoherence with the Prospectus Directive's summary requirements.

Separately, at the time of writing of this article, the European Economic and Social Committee, the European Parliament's ECON Committee and the European Parliament's IMCO Committee had just published their respective [opinion](#), [draft report](#) and [draft opinion](#) on the PRIPs proposal. Opinions of the European Parliament's JURI and LIBE Committees are also expected. On initial reading, the ECON draft report seems *inter alia* to: (i) split KID responsibility between manufacturers and distributors according to the type of information concerned; (ii) immediately extend the scope of the KID concept to all vanilla bonds distributed to retail; and (iii) grant KID pre-approval and MiFID product intervention powers to regulators. Further coverage will follow in the next edition of this Quarterly Report.

In continuing work on the PRIPs initiative, it may be worth reflecting on a point made by ESMA's Chair, Steven Maijor, in his opening statement at ESMA's 12 December Investor Day: "*Behavioural finance suggests that biases and competence failures are unlikely to be dealt with through disclosure. And the problem of information overload has also been well documented. Disclosure has considerable attractions as a retail market tool, but the challenge for regulators is to resist the temptation to make disclosure the panacea for investor protection.*"

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The ICMA Primary Market Forum

On 15 November 2012, the sixth ICMA Primary Market Forum took place as a half-day conference designed to bring together the international fixed income community, including borrowers, arranging banks, investors and law firms, to discuss the current business issues and regulatory developments affecting the issuance of international debt securities.

The regulatory and market challenges in the current environment were discussed in two panels, one on legal and documentary issues and the other on market-driven processes and the outlook for debt capital markets.

The discussion on the impact of the Prospectus Directive and its first review, which seems likely to continue pretty much until its second review expected in 2015, can be summed up not only as being costly and time-consuming in terms of the need consistently to update relevant documentation, but also as risky due to the sometimes inconsistent approach of competent authorities around Europe.

FATCA is also an ongoing topic, which will hopefully be further supported by the conclusion of further intergovernmental agreements in the near future.

Interestingly, the US Internal Revenue Service has recently announced that at least the grandfathering for obligations that produce “foreign passthru payments” and “dividend equivalent” payments (but not other US-source payments) will be extended from end of 2012 until six months after the date on which final regulations defining such payments are published. This seems helpfully to postpone one challenging aspect of FATCA until further notice.

Questions that have recently arisen were also considered, such as the enforceability of one-way hybrid jurisdiction clauses following a recent French Supreme Court decision that was thought most unlikely to be followed in a UK court.

Changes in the execution process were highlighted given that investors are increasingly reluctant to be “wall-crossed” with inside information in the course of pre-soundings.

From a purely “market” perspective, however, the future for new issues seems to be rosier than the discussion of the legal issues may have indicated.

All in all, it was agreed that regulatory initiatives are today often completed at great speed, which is not always helpful for those who have to comply with them.

The interest in the Forum shows once more that the various new regulatory initiatives, as well as the resulting lack of certainty in the current market environment, are a substantial challenge for the financial markets to meet now, and also in years to come.

It seems as if there is a lot on the agenda to keep the industry busy in 2013.

The *International Financial Law Review* has published further [coverage](#) following the Forum.

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Review of the ICMA Primary Market Handbook

We reported in the [Quarterly Report for the Third Quarter of 2012](#) on the work being done to review the ICMA Primary Market Handbook. This work is continuing apace in a Wider Working Group made up of interested ICMA members. It is hoped that the Wider Working Group will be in a position to

submit, for feedback, a draft revised Handbook to ICMA's Legal and Documentation Committee and Primary Market Practices Committee later in the year.

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The Financial Institution Issuer Forum in 2012



by Katie Kelly

The [Financial Institution Issuer Forum](#) (FIIF) convened four times in 2012, in each case with good attendance and lively participation. 2011 concluded with a discussion on the restoration of confidence in the markets, a theme which continued to underpin the agenda of the FIIF in 2012. A summary of this and the other main focuses of the FIIF in 2012 follows.

Capital issues: It has been widely recognised that clarity is needed as to what constitutes the various tiers of capital required under the Capital Requirements Directive and Regulation (CRD IV/CRR), which will hopefully be assuaged in 2013 with the European Parliament vote on CRD IV/CRR scheduled for early 2013 (and with it, the uncertainty which inevitably leads to confusion for investors).

Further to the production of a termsheet for Buffer Contingent Capital Securities by the European Banking Authority (EBA), ICMA conducted a survey of a variety of market participants by way of posing comparatives between CoCos with an Additional Tier 1 host (as prescribed by the EBA's termsheet) and a Tier 2 host as between differently-rated issuers (all as reported in more detail in the [Second Quarter 2012](#) edition of this Quarterly Report). In conclusion, the survey suggested that the types of issuers which need to be able to bolster their capital would find it difficult to come to market with the EBA CoCo, and even if they could come to market, it would be economically unviable for issuers with lower credit ratings to do so. However, there would be significantly more appetite in the market for a CoCo with a Tier 2 host.

The ICMA, with substantial input from the FIIF, also responded to the EBA's consultation on *Own Funds* (as reported in more detail in the [Third Quarter 2012](#) edition of this Quarterly Report), with the underlying theme being the need for a balance between regulatory requirements for a capital conservation

Additional Tier 1 instrument, and an ability to market it to fixed income investors without them being subordinated to common equity holders. Adjustments to the Additional Tier 1 characteristics as a result of this industry consensus are widely anticipated but have yet to be released.

Debt write-down tool: The European Commission released a discussion paper on *The Debt Write-down Tool – Bail-in*, to which the ICMA submitted a response addressing the Commission's specific questions in detail with input from both the issuer and investor perspectives (all as reported in more detail in the [Third Quarter 2012](#) edition of this Quarterly Report). In overall terms, the response stated that, whilst being supportive of the Commission's endeavours, the ICMA perceives that there remain some significant overriding challenges to be overcome in the final design of a senior unsecured debt bail-in regime, and believes that it is essential that the application of the bail-in be respectful of the hierarchy of claims, with senior unsecured debt holders only expected to absorb losses after all other less senior ranking providers of capital. The ICMA also considers that other measures to increase the quality and quantity of capital and the stability of the financial system should be completed before introducing a bail-in regime.

Transparency: Transparency was also in the spotlight in 2012 – in particular, how to balance the interests of the market as much as possible on the one hand with the national regulators' requirements on the other, while still being able to strategise and maintain the duty of confidentiality to, and integrity of, the bank.

Asset encumbrance: As reported in the [Second Quarter 2012](#) and [Fourth Quarter 2012](#) editions of this Quarterly Report, a Working Group comprised of members of the FIIF, the ICMA [Asset Managers and Investors Council](#) and some regulators resulted in



The continued participation of the FIIF members in 2012 has ensured animated debate and related action surrounding issues such as capital, bail-in and asset encumbrance.

structured and qualitative debates on the relevance of asset encumbrance, including the definition of encumbrance and whether it should include repo, transparency issues and consideration of the appropriateness of hard limits. ICMA will be continuing to engage with the relevant parties on this work stream in 2013.

Consumer protection: Linklaters were invited to attend the FIIF to discuss prudential issues from the perspective of issuers. While a regulatory balance needs to be drawn between protecting consumers and, at the same time, providing greater investment opportunities and encouraging issuers to use the markets, a variety of regulatory tools employed in the name of consumer protection may give rise to inconsistencies in ways that are damaging to both issuers and investors. These tools include disclosure and product description; control of the selling/distribution process under MiFID; (increasingly) product regulation, which could also involve product-banning; redress for getting it wrong; and the education of investors. Ultimately however, regardless of whether legal, regulatory and disclosure requirements have been satisfied, there should be more responsibility on the issuers themselves to get it right first time, particularly having regard to the reputational risks which may be suffered not just by issuers but by the issuing community as a whole.

Exit consents in liability management transactions: Slaughter & May reported to the FIIF on a recent English law High Court case on exit consents, in which bondholders who did not accept an exchange of new bonds for old were offered a significantly lower economic value for their existing bonds by way of a call option (the “Anglo Case”, as reported in the [Fourth Quarter 2012](#) edition of this Quarterly Report). In summary, when carrying out a liability management

exercise, issuers were advised to take advice from counsel on their particular structure, and should take a view as to whether the economic differences offered are sufficiently different from those in the Anglo Case. In addition, it is essential to check the terms of the Trust Deed to ensure there is no question over *vires* and that all procedural steps have been complied with.

EBA relationship: Members of the FIIF met representatives of the EBA in September 2012. This was an ideal opportunity for the EBA to give an overview of its workload, priorities and limitations, as well as for the FIIF to air concerns on behalf of the industry over the role the EBA has on the day-to-day operations of the FIIF members in terms of investor reaction, rating action and regulation, and in particular the impact of bail-in and a lack of definitions on capital instruments on a bank’s ability to fund itself and therefore, the wider economy. The meeting heralded the start of what will hopefully be a positive working relationship between the ICMA, the FIIF and the EBA, with the latter willing to engage with the industry experts at a working group level as required. Representatives of the EBA also attended a meeting of the FIIF in November 2012, where a qualitative debate over issues raised by the FIIF members ensued.

These are just some of the highlights of the FIIF in 2012. We are grateful for the continued enthusiasm of the FIIF members, whose active participation has ensured that the FIIF remains an invaluable, high-level platform for constructive debate. We are also very appreciative of the guests who took the time to attend and present at the meetings in 2012, and we look forward to another productive year ahead with a variety of interesting and very relevant work streams.

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by Leland Goss

Argentina bondholder row: a threat to sovereign restructurings?

The United States Court of Appeals for the Second Circuit in *NML Capital Ltd. v. Republic of Argentina* has focused the minds of many around the world on, of all things, the meaning of *pari passu* clauses in sovereign bond issues. The Court said this long standing “equal treatment” language found in the terms of most sovereign bonds did not permit Argentina to favour bonds issued in restructurings and bond exchanges back in 2005 and 2010 (where the participants agreed to receive roughly 33 cents for every dollar invested) over those held by the plaintiffs, “hold out” creditors who refused to participate in the restructurings/exchanges and have been demanding 100% payment on the original pre-exchange bonds issued back in 1994 under a Fiscal Agency Agreement (“FAA bonds”) governed by New York law. Argentina defaulted on the FAA bonds in 2001 and has not paid interest or principal on them since then. Argentina is, however, current on payment to holders of the exchanged bonds.

The case has other complicating dimensions, which will not be addressed here, including the remedies ordered by the lower court binding also on third parties, raising speculation as to how Argentina might seek to practically circumvent the court ruling(s) by paying restructured bondholders outside the jurisdiction of the US; and the fact that this latest decision is part of on-going legal skirmishing, ie it is one of several rulings that have already taken place nor is it likely to be the last one, with some expecting the dispute may end up before the US Supreme Court in 2013. For those interested, there are other publicly available materials addressing the case in more detail (See, eg, Clifford Chance, Briefing Note, *Sovereign Pari Passu Clauses: Don't Cry for Argentina - Yet*, December 2012). The focus of this note, however, is on the wider ramifications that the case's final resolution could have for future sovereign debt restructurings, the international capital markets and ultimately the world economy. The case has thrown

into relief a tension between two important conflicting goals: the need for legal certainty for investors holding sovereign debt, versus the need for governments, particularly in the developing world, to retain the ability to agree restructuring plans with creditors.

Pari passu

The US court decisions on the arguments raised by NML Capital have come out against Argentina and in favour of the hold-out investors by ruling that the holdout FAA bonds' *pari passu* clause, referred to by the courts as the “Equal Treatment Provision”, prevents Argentina from discriminating against the holdout bonds in favour of its subsequent unsubordinated foreign bonds *and*, importantly, that this means also that Argentina must not pay the restructured bondholders without paying, in full, the holdout bondholders. There is room for much debate as to whether the US courts have interpreted the *pari passu* clause correctly. Indeed, a patchy body of law across various jurisdictions suggests that, notwithstanding the mention of “payment” in the clause, the US courts have got it wrong, taking the meaning too far. This view maintains that equal treatment only means that the legal or formal *ranking* of the bonds cannot be legally or formally subordinated, ie with other subsequent debt issues, and that this does not require the borrower to pay all bondholders equally or not to pay one series of bonds before any others (the “ranking interpretation”).

The counter-argument, put forward by NML and accepted by the US courts thus far, is that the FAA *pari passu* clause by its terms and the specific mention that the “payment obligations” of Argentina of those bonds “shall at all times rank at least equally [with its other bonds]” in order to make sense has to not only require equal ranking but also that the sovereign must pay its creditors equally (the “payment interpretation”). One of the problems in all of this is that *pari passu* clauses can differ widely in

their drafting, such that for some it is possible that “ranking” is the right interpretation while “payment” is the correct meaning for others. A further problem is that the Argentina wording probably falls into a middle category that is ambiguous.

Impact

As things stand, the court arguably has changed the relative bargaining power of the bondholders vs. the sovereign in a very significant and high profile manner, potentially empowering other holdout creditors further and making it even more difficult, if not impossible, for sovereigns to negotiate and agree to restructuring plans with their creditors. The implications are stark from a global financial perspective: if a single creditor is able to thwart the implementation of an internationally supported restructuring plan, this could undermine decades of effort governments and international financial institutions have expended to encourage a system of cooperative resolution of sovereign debt crises, for example, as was the case in the 1980’s under the Brady Plan. In this regard, the US Government in its *Amicus Curiae* (friend of the court) brief noted that, unless reversed, the court ruling “*would have adverse consequences on the prospects for voluntary sovereign debt restructuring, on the stability of international financial markets and on the repayment of loans by international financial institutions. Accordingly, the United States opposes the adoption of the [court’s interpretation] of the pari passu clause as contrary to United States policy interests.*”

The 2nd Circuit Court of Appeals, on the other hand, took the contrary view saying that “it is highly unlikely that in the future sovereigns will find themselves in Argentina’s predicament. Collective action clauses (CACs) – which effectively eliminate the possibility of “holdout” litigation – have been included in 99% of the aggregate value of New York law bonds issued since January, 2005 [. . .]. CACs included in the terms of a new bond issue allow a vote passed by a prescribed majority of bondholders to bind all bondholders, for example regarding a restructuring/exchange offer. However, this ignores the fact that there are billions of dollars of sovereign bonds outstanding issued previously that do not contain CACs and which may have *pari passu* provisions which could be vulnerable to the Court’s interpretation of the *pari passu* clause. Moreover, while the significance of *pari passu* clauses

and the problem of holdout creditors would diminish over time, this also ignores the fact that most CACs currently used lack “aggregation”, ie they apply to bonds of a single issue but not across all of a sovereign’s issues, allowing creditors to establish a blocking stake in one issue potentially more easily than where aggregation is envisaged in order to keep that issue out of any restructuring. It will be some time before all sovereign debt, for example in the euro area, will contain CACs with aggregation.

Where do things go from here?

An obvious question in all of this has to be, why are so many different types of *pari passu* clauses still being used? A sovereign alone, Greece may well have over a dozen versions of a *pari passu* clause in its indebtedness instruments (and this is not accounted for just by issuances being done under different governing laws). More importantly, if most sovereigns presumably would prefer to avoid a future holdout creditor problem, why do they not use a different available formulation, as mentioned above, more carefully drafted so as to avoid the “payment” variation so that they could then be confident that the clause would be interpreted by most courts to mean that the sovereign was not obligated to make payment to holdout creditors? The answer to this mystery might be that sovereigns just do not want to change, or saw the risk of a holdout problem as too remote at the time of drafting and issue – a lot would have to happen first before becoming relevant, ie the domestic economy failing, a change of government, substantially making it almost a moot point for many elected officials. Or, it could be reliance on CACs, but as discussed above, these often are not holdout proof due to the lack of aggregation.

In the meantime, the court saga continues, with a number of parties seeking leave of the court to intervene as interested non-parties. Whatever the outcome, for new sovereign debt issues, borrowers, lead managers and their lawyers should be considering very seriously taking the practical steps of including both a CAC – with aggregation – and a more carefully drafted *pari passu* clause that should leave little doubt that it will be interpreted as a “ranking” and not a “payment” provision.

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by John Serocold

In brief

This is an edited version of John Serocold's remarks to the Dealer Model Forum held in London on 12 November 2012, covering a broad range of commercial, regulatory and structural pressures on the dealer model. The focus is on the European Market Infrastructure Regulation (EMIR), the MiFID II package and the proposed Central Securities Depositories Regulation (CSDR), setting them in context and highlighting some challenges.

Secondary Markets

The dealer model in the bond market

I want to start by emphasising the scale of the opportunity. The US and EU are a similar size, in terms of population and economic activity. US-based companies are 75% market financed and 25% bank financed; for EU companies, it is broadly the case that the opposite holds true. So EU financial markets, including credit markets, have the opportunity to increase in size substantially.

What is stopping us? I see a number of factors in the general environment:

- *The macroeconomic conjuncture:* The key fact about this is that everyone finds it difficult to see into the future.
- *This leads to a lack of confidence:* For corporates, that manifests itself in the hoarding of cash: and clearly if a corporate is holding a lot of cash, it will be hard for it to see the need for a bond issue. For investors, the current conjuncture leads to a "flight to quality" – so we see the German Government, for example, able to borrow for a few basis points per annum and the concomitant "reach for yield".
- *The third area is lack of trust in banks and financial intermediaries:* Trust is a key enabler for markets and it is particularly important for international markets. At ICMA, we have some mechanisms to buttress trust, in the form of our rules and recommendations;

and our mediation and arbitration service – but we cannot create it.

- The lack of public trust – society's trust – manifests itself in *wide-ranging and detailed regulatory intervention* in the financial sector in general and financial markets, especially OTC markets, in particular.

Here is a – non-exhaustive – list of regulatory interventions, actual and prospective, which are impacting, will impact, or have potential to impact our markets:

- First, changes to insurance regulation which are increasing the percentage of portfolios allocated to bonds but are also requiring investors to do a credit assessment, which tends to push them towards a "buy-and-hold" model.
- Second, reform of bank capital means that capital is scarcer and more expensive – and, given the risks of trading, more of it needs to be allocated to support banks' trading books. This is an awkward combination of factors.
- Third, looking further out, moves to reinstate separation between banking and securities businesses. This comes in various different flavours – a ban on proprietary trading while allowing client-facing market making in the US, called the Volcker rule; a "ring fence" for the wholesale markets businesses to keep it separate from the High Street businesses, called Vickers in the UK;



and a *mélange* of these proposals, with a strong additional emphasis on the proper governance of risk, from a group of EU “wise ones” led by Erkki Liikanen, a Finn with direct experience of a banking crisis.

In addition, we have:

- the European Market Infrastructure Regulation (EMIR) which is the main way in which the European members of the G20 have delivered their commitment to move OTC derivatives: (i) onto trading platforms, where sufficiently standardised; and (ii) into central clearing, for those OTC derivatives subject to the clearing obligation;
- a ban on short selling, but with a limited carve-out for market making – the Short Selling Regulation. Although this mostly affects equities and government bonds, it has the potential to make credit traders’ lives more difficult and expensive;
- new transparency requirements and market structure reform, in the markets in financial instruments package – the MiFID II package, which is discussed in more detail below and in the accompanying box;
- the Alternative Investment Fund Managers Directive, under which all funds not covered by UCITS – ie hedge funds, private equity funds, etc – are regulated. Observers expect that this will influence financial market liquidity, financial market functioning and price discovery;
- reform of the regulation of Central Securities Depositories, the subject of a separate article in this Quarterly Report; and
- a proposed reform of the law relating to the holding and disposition of securities, which could adversely affect the repo and secured lending markets.

To these must be added concerns from the clients’ perspective:

At ICMA, we want to support members on the long journey to MiFID implementation with up-to-date services and products as well as events.

- Are we being properly rewarded for the risk we are taking (market risk, default risk, interest rate risk)?
- Can we trade these bonds if we change our view?

I turn now to three new European laws. The first has been passed and is being implemented. The other two are at different stages of legislative scrutiny. They are the European Market Infrastructure Regulation (EMIR), the Markets in Financial Instruments package – the MiFID II package – and Central Securities Depositories Regulation (CSDR).

EMIR is already sucking capital into clearing houses – US\$150 million at Eurex and US\$500 million at LCH Clearnet, by way of new equity, for example – but these sums could pale into insignificance once the swaps business migrates to central clearing and participants have to post collateral to the clearing house.

The key effect for present purposes is that hedging – of interest rate risk, credit default risk and foreign exchange risk – has now become more difficult and – potentially – expensive.

The MiFID legislation comprises two legal texts, the recast of the 2004 Directive, and a new Regulation, MiFIR. Together they are referred to as the MiFID II package.

There are two key aspects to bear in mind about the MiFID II package. First, it is very wide-ranging; second, it is very detailed, and contains within it extensive powers granted to ESMA and the Commission to create binding technical standards –

binding on regulators in the European Union and beyond – and subordinate legislation, filling in the detail. So we do not yet know exactly what we are dealing with.

What is the current status of the MiFID Level 1 texts? The proposals were published in October 2011 and the European Parliament passed a package of amendments on 26 October 2012 in its plenary session. Negotiations are continuing in the European Council Working Group between Member States. So we do not yet have a stable text, but we are close. The latest information on the position in some key areas of interest to ICMA is given in the MiFID II box, which contains a brief summary of the latest position in ICMA’s priority areas.

The main milestones to implementation are as follows:

- The first step is to complete the primary legislation. That step will take some months yet.
- The next step is for ESMA to give advice to the Commission on a number of subjects, including on the transparency provisions.
- The third step is for the Commission to make subordinate legislation on these subjects.
- In parallel, Member States will be implementing the primary legislation in MiFID in their own jurisdictions; and third countries will be considering what changes, if any, to make to their national regulatory regimes in order to achieve

“equivalence”. This is particularly important for Switzerland, whose financial sector is heavily involved in providing services to European investors.

- ESMA and the national competent authorities also have much work to do in setting new standards and policies in relation to the new powers and responsibilities they have been granted.

And we can look forward to extensive consultation on the detail of these changes over the coming years.

Implementation of MiFID II is therefore not expected to be complete until at least 2015.

We are in the early stages of a long journey to MiFID II implementation. At the ICMA, we want to support members on that journey, both with events and by ensuring that the services and products we provide are up-to-date and take account of the changes to our markets and the wider world. We also respond to consultations on a selective basis, through our small but experienced regulatory policy team working closely with business managers and experts from our members. For our part, ICMA will continue to consider changes to the ICMA Secondary Market Rules and Recommendations in the light of this legislation – and the other legislative provisions discussed here – as they evolve.

We look now at a number of provisions of particular interest to the international markets and which provide important context to discussions about the future of the dealer model. There are two sides to these proposals: a markets side and an investor side.

Taking the markets side first, the biggest single change affecting the international capital market is the introduction of mandatory price transparency for the fixed income market. While equity markets in Europe have long been subject to

mandatory transparency requirements, transparency in the fixed income markets is seen by policy makers as more of an *ad hoc* patchwork. The provisions bringing transparency to the fixed income markets are brief. They give ESMA a mandate to develop regulatory technical standards, binding on regulators rather than market participants; and they empower the European Commission to legislate to make these binding. The Commission is also empowered to make detailed rules covering a number of important areas, including arrangements for delayed publication and waivers from the main requirements. The overall objective is to make fixed income markets sufficiently transparent for market users to have confidence and for regulators to have information about market conditions both for their supervisory work and to help address concerns about the overall safety and soundness of the system.

The transparency requirements cover both pre-trade transparency, the provision of prices and sizes to market users ahead of a trade, and post-trade transparency, the publication of the prices and sizes of business that has been done.

A key area of debate in relation to these proposals is the need to define the delays for the publication of large trades; and the circumstances in which the obligations do not apply, referred to as “waivers” in the jargon. Transparency has the potential to damage liquidity, if dealers are no longer willing to commit capital to the trading business. But it can also improve market conditions, by giving market users the ability to make more informed choices and to deploy more and more sophisticated trading tools. We have seen these developments in the equity markets.

The second change is to introduce a new category of trading venue, the Organised Trading Facility (OTF). While this was primarily developed to provide a European framework similar to the Swap Execution Facility mandated under Dodd-Frank,

the framework is potentially of interest to dealers wishing to provide a single dealer platform for their clients, alongside the Systematic Internaliser structure.

A key point here is whether the operator of an OTF will be able to commit its own capital to carry out transactions on the OTF. The Commission proposed that it should not; but many voices have been raised in the debate seeking an amendment to permit this. The outcome is not yet clear. But this design feature will have a material effect on whether firms build these platforms and whether they provide a valuable service to clients.

The third group of changes on the markets side relate to the ability of the various market infrastructures – trading venues, clearing houses and settlement systems – to obtain access to each other and to “interoperate”, in the jargon. While this development may seem to be of less direct interest to the international markets, which pioneered such arrangements with the “bridge” between Euroclear Bank in Belgium and Clearstream in Luxembourg, the proposed changes have the potential to make members’ life more complicated – but also perhaps cheaper, if the vision of the promoters of these proposals is realised. The purpose of mandating access and interoperability is to sharpen competition between the various platform providers, thereby leading to technical progress, innovation and – hopefully – lower prices.

The second category of changes introduced by the MiFID II package applies to investor protection and therefore to the relationship ICMA members have with their clients.

The first change to note here is that the customer classification rules are being tightened up, so that more investors will receive the full benefit of the investor protection rules and fewer investors will be treated as intermediate customers and eligible counterparties.



Given that global financial markets are independent of geography, there are fears that the proposed “third country” rules will prove to be wholly impractical.

The second change relates to payments between product providers and intermediaries, often referred to as the “inducements” rules. Such payments can potentially conflict with the obligations owed by an intermediary to its clients and, if they are banned or substantially reformed, this could potentially have a significant impact on revenue lines and business models, with knock-on effects to the international capital markets.

The MiFID II package also contains a wide range of other measures, some of which will require technical and business changes to other parts of our members’ businesses.

One particular aspect is of special interest to international market participants. This is called, in the jargon, “third country” access. Third country questions cover both access to the EU Single Market from non-members and access by EU investors to other markets, thinking particularly about the non-EU markets in the Middle East, Asia and Latin America, not forgetting Switzerland and the US, of course.

There is a risk that, if introduced in their original form, the provisions could lock third country firms out of the EU markets, which would have an extremely damaging effect on European financial markets, including the international bond and repo markets based in Europe. Given that global financial markets are independent of geography, there are fears that the proposal will also prove to be wholly impractical.

The third country provisions set the conditions for access to the Single Market by firms which do not have a

European subsidiary or branch; and also affect access by EU investors to non-EU domestic markets, because they may use local brokers and will often use local custodians or correspondent banks. For firms from jurisdictions deemed to be equivalent, they can have access to the Single Market. Firms from other jurisdictions would have to establish a branch or subsidiary in the EU and carry on business with retail investors, in particular, through that entity. The entity will be subject to EU capital adequacy and conduct of business rules.

Another important new provision in MiFID II is the grant of new powers to the regulators, including a power to ban financial products on an EU-wide level. It remains to be seen what impact this will have on financial markets in general; members involved with the design and distribution of complex financial instruments may want to look further into this. Again, this is an important change but not one we expect will have a big impact on our market.

Turning to the CSD Regulation, while much of it is desirable and sensible, there are a couple of provisions which affect the international capital markets, and where we have sought changes with some success.

The first is settlement discipline: the original proposal applied daily fines to all late trades and provided for mandatory buy-in. The European Parliament’s counter-proposal is for settlement discipline to apply only to trades on trading venues and for buy-in to be invoked by the “unsatisfied buyer” – as today.

The second is more complex and controversial, and relates to the ability of the ICSDs, our settlement partners, to provide credit and to settle in central bank money. If these services are restricted, or become significantly more expensive, this is an additional layer of complexity and cost to be borne by market users: including, in the first instance at least, dealers. Further details on ICMA’s recent work in this area and our policy stance are given in the separate article on the CSD Regulation.

This provides a formidable list of obstacles and concerns, but there are also reasons to be cheerful. One such reason is that we have been here before: we – our predecessors – built this market against the odds, in a world living with the threat of nuclear annihilation, with exchange controls and extremely high personal and corporate tax rates, at least by today’s standards.

So the lesson of history is that we can navigate these headwinds. More concretely, entrepreneurial businesses are joining the debate, not with rhetoric but with practical business solutions. They have drawn on their experience of adjacent markets – government bond markets and the US market, for example – to bring forward, among other things, transparent public limit order books with central clearing and variations on that theme, to complement their existing offerings which, typically, support the request-for-quote or exchange-trading models.

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The MiFID II package

In the previous Quarterly Report – [Issue 27](#) – we reported on the European Parliament's expected adoption in October of a position on the proposed revision of the Markets in Financial Instruments Directive (MiFID II) and its accompanying Regulation (MiFIR), and that the EU Member States in Council were aiming to agree a position on these measures by the end of 2012.

As expected, the European Parliament agreed its position on the recast [MiFID](#) and [MiFIR](#) in a plenary vote on 26 October 2012. But because of differences among Member States which are summarised in the Cypriot Presidency's [Progress Report](#), it is now apparent that agreement among the Member States in Council will be delayed until early 2013. It seems likely that attempts to reconcile Member States' positions on key aspects of the legislation, some of them in areas of priority interest for ICMA members, may continue for some time. The Trilogue discussions, in which the European Parliament, the Council and European Commission negotiate a final text, will be correspondingly delayed.

Members will recall from previous Quarterly Reports that ICMA's priorities focus on two areas.

First, in the case of the treatment of third country (ie non-EU) firms, and its impact on the international capital market, the Parliament has broadly retained the Commission's proposal to require third country firms to establish a branch in the EU when dealing with retail customers, and to register with the European Securities Markets Authority (ESMA) when dealing in wholesale markets. In both cases the requirements are subject to a proviso that the Commission has assessed the third country as having regulatory arrangements with equivalent effect to those of the EU. As reported last quarter, it seems that the Council is likely to agree on such restrictions only for the retail market, but without the passport for such branches that is envisaged by the Commission and Parliament.

Second, in the case of the proposed new requirements on market structure and trading transparency in fixed income and other non-equity markets, readers will recall that the Commission proposed a new category of regulated Organised Trading Facility (OTF) to regulate any form of organised multilateral trading interaction; an extension of Systematic Internaliser (SI) quoting obligations to fixed income and derivatives business; accompanying pre-trade transparency rules for all multilateral trading venues, and a comprehensive regime of post-trade reporting for non-equity instruments. The Parliament proposes to restrict OTFs to non-equity markets; to prohibit a firm from deploying its own capital in an OTF that it operates, even to facilitate client business; to narrow the scope of non-transparent OTC business; but also to restrict the transparency requirements to smaller trades in more liquid instruments. While the Council also seems to be steering towards an OTF regime for non-equities only, and focusing transparency on liquid instruments and smaller trades, recent draft compromise texts published by the Council Presidency have suggested a range of approaches on important outstanding issues, including the scope and obligations of the new OTF category, the treatment of OTC business, and the scope of pre-trade transparency and the circumstances in which it is appropriate for regulators to waive it.

On the first area, the treatment of third country firms, the positions of the Parliament, the Council and the Commission seem to be clear, albeit divergent. These differences are therefore likely to need to be resolved during the Trilogue.

On the evidence of the published draft compromises, which seem to be seeking to find a package of rules on market structure and trading transparency that can command qualified majority support among Member States, it is in the second area (among some other points), that

discussions among Member States appear to be continuing. At the time of writing it remains unclear how far the Council will converge with or diverge from the European Parliament's position.

As discussed in more detail in the accompanying article on the dealer model in the bond market, once the text of the new legislation is agreed, first among the Council Members, and then among the three European institutions in Trilogue, the next stage of the process will begin, developing implementing legislation and ESMA technical standards, so as to fill in the prescribed legislative and regulatory detail of the new requirements. Until we see the final text of the main legislation, though, and begin to understand how the Commission and ESMA envisage filling in the detail, it will remain difficult to predict and plan at an operational level what the impact on the international capital market will be, including the impact on ICMA's Secondary Market Rules and Recommendations.

We foresee that ICMA will wish to provide input to the EU authorities on technical aspects of the legislative detail, and we will be in touch with members further as the broad framework and the timetable become clearer. As always, the ICMA Secretariat would be happy to receive input from ICMA members on any particular points relevant to our markets which you think it important for ICMA to pursue or protect as the detail of the new requirements develops.

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The CSD Regulation

Status: The current parliamentary timetable calls for the European Parliament to take a position in the first quarter of 2013. This relatively short, technical measure, comprising 70 articles and one annex, had attracted a total of 686 amendments by the deadline, including 127 in the [Swinburne report](#). At the time of writing, we expect the Level 1 legislative process to be completed in the first half of 2013, but it seems that this *dossier* is competing for attention at the European Council with a number of other files which are politically charged and technically complex.

Purpose: The initiative is an important part of the European Commission's agenda to enhance the safety and soundness of the financial system. Together with the Regulation on OTC Derivatives, Central Counterparties and Trade Repositories (EMIR) which entered into force on 4 July 2012 and the Markets in Financial Instruments Directive (MiFID, currently under legislative debate following a review), it will form a framework in which systemically important securities infrastructures (trading venues, central counterparties, trade repositories and central securities depositories) are subject to common rules on a European level.

Key provisions: An initial assessment of the proposed Regulation was given in [Issue 25](#) of the ICMA Quarterly Report and the key provisions were summarised in [Issue 27](#), together with an analysis of the [Swinburne report](#), published on 17 July and debated in the ECON Committee of the European Parliament in September.

The key provisions of the proposed Regulation include:

- harmonisation of the settlement cycle to T+2;
- standardisation of settlement discipline and buy-in procedures;

- settlement in CSDs imposed for all instruments listed or traded on regulated markets and issuance to be in book-entry form through immobilization or dematerialisation;
- definition of CSD core functions covering the operation of a Securities Settlement System, together with the notary services and the central maintenance services where applicable;
- separation of CSD and banking activities into two legal entities operating under distinct licences ("2+2 model") unless a derogation is granted by the Commission (Dr Swinburne proposed the deletion of the provision permitting this derogation);
- banking activities limited if both CSD and bank belong to the same parental group, but unlimited if provided by an external supplier;
- credit institutions providing banking services to CSDs must be compliant with the Capital Requirements Directive and obtain a specific authorisation;
- outsourcing or expansion of services by CSDs will be subject to strict conditions and to prior authorisation by regulators;
- definitions of "ancillary services", which are regarded as complex;
- a requirement for regulatory approvals for links between CSDs;
- a requirement that settlement in central bank money must be adopted where available and practical (to be defined by the European Commission);
- choice of CSD for issuers;
- open access for CSDs to other CSDs, CCPs and trading venues; and
- a harmonised framework for the supervision of all EU CSDs.

A key question is how the proposed changes will impact the daily operation of the international primary and

secondary markets.

ICMA's work: We have been seeking to ensure that the appropriate balance is maintained between competing policy objectives. First come safety and soundness, as these are explicitly the goals towards which the proposed Regulation is aimed. But for ICMA members and market participants generally, practical arrangements allowing choice and further progress towards more cost-efficient markets remain important. The repo market's agenda to improve the safety, soundness and efficiency of the current arrangements underpinning this market remains central to ICMA's policy stance.

In the quarter under review, our focus has been on the potential impact of the proposals on the ICSDs and, through them, the potential impact on our members and on our core markets: the international capital market for credit instruments and the associated financing markets.

We held a meeting on 15 October 2012 at which the ICSDs presented their assessment of the impact of the proposed Regulation. In summary, we understand that the ICSDs continue to believe that:

- there is no requirement from any stakeholder for a full technical and operational separation between CSD and bank;
- a 2+2 model creates unnecessary costs and complexities for market participants, does not really decrease risks and ignores the possible implementation of a suitable recovery and resolution regime, with no guarantee that the model will work effectively;
- a 1+2 model with a "limited" banking model provides the best combination of efficiency, safety and risk reduction for European markets;



At first sight, a fresh approach to the question of separation provides an elegant solution to the problem of achieving improved safety and soundness at reasonable cost and without sacrificing hard-won efficiency gains.

- commercial bank money settlement is the only practical solution to the ICSDs' multi-currency activities;
- a requirement for multiple competing settlement banks that are unlimited in their banking activities, will greatly increase both systemic risk and direct costs to users of the ICSDs; and
- there is significant inconsistency between the approach of CPSS/IOSCO on Resolution and Recovery Regimes and the CSDR.

In a discussion of the ICSDs' views, a number of these propositions were subject to robust challenge by other ICMA members. The meeting concluded that it would be desirable to make the European Commission and European Parliament aware of the discussion held with the ICSDs and the concerns of the industry related to the different approaches and this has been done. Further copies of the [report](#) on central bank money and commercial bank money commissioned by the European Repo Council (ERC) from Mr Richard Comotto in 2011 have also been distributed to relevant policy makers.

Our policy stance: We believe that:

- *EU policy makers should clarify that a legal separation of the entities carrying on (i) securities settlement processing and (ii) the provision of cash and credit extended to perform their activities are sufficient to meet their goals.*

It became clear in our discussions that going beyond the legal separation, forcing a technical separation, would create inefficiencies, complexity, cost and risk as delivery-versus-payment (DVP) would no longer be as effective as today. We recognised that any change in the current 1+2 model beyond a legal separation would carry a considerable cost for financial markets, particularly in relation to additional contractual and operational complexity. However, we remain concerned that the additional costs of a forced technical separation would not achieve the goal of safer, more robust and a more resilient securities market infrastructure.

- *Policy makers should recognise the considerable efforts made in recent years with the aim of increasing safety and operational efficiency while reducing cost.*

While we consider that the market works adequately at present, work continues towards these objectives. To give a concrete example, in recent years we recognised that the liquidity transmission was not optimal because of the "silo" nature of each ICSD triparty product.

Commitment has now been made by both ICSDs to upgrade the "bridge" between them, helping to avoid the situation where liquidity is trapped in one ICSD, held against collateral trapped in the other. This industry-guided process, if brought to a

satisfactory conclusion, will enable access by all market participants to their CCP of choice, irrespective of the location of the securities. Other CSDs and, potentially, new ICSDs will also be able to benefit from this improved market efficiency, directly providing a more competitive settlement landscape in Europe, ahead of T2S.

Furthermore, our recent meeting highlighted the need for and benefits of the current ICSD model in light of the global access they provide to the international capital markets. Both ICSDs provide reliable and safe settlement of a full range of currencies (the major currencies being US dollar, euro, sterling and Japanese yen) while allowing a wide range of securities including equities to be settled in different currency denominations under a DVP method, commonly known as cross-currency settlement. One of the major benefits of the current model is that settlement is made in commercial bank money. In particular for institutions not having access to central bank money, this remains the most efficient way of settlement in a safe environment. The ICSD triparty service is increasingly used by the central bank community while the European Central Bank has also indicated its readiness to accept delivery of collateral through the triparty service.

- *Changes may need to be made to achieve a better and safer environment, especially to allow uninterrupted access to securities accounts, in the event of a liquidity shock to the banking entity.*

The proposed 2+2 model, limited to legal separation and without technical and operational separation, should achieve these goals.

It has also been suggested that it might be desirable for all concerned regulatory bodies to hold a series of technical meetings on the topic in order to seek a solution that adequately increases the safety of the ICSDs' model while best preserving the efficiency of settlement.

We also held a roundtable on the CSD Regulation on 20 November 2012, at which Godfried De Vidts, Chairman of the ERC, Paul Symons, Head of Government Affairs of the Euroclear group, and the responsible official from HM Treasury presented different perspectives on the proposal. This was followed by a lively question and answer session during which a range of interesting points were debated.

As usual, we have been seeking to cooperate with like-minded associations where we can.

Recent developments: As part of the process of consideration of the 686 amendments by the ECON Committee of the European Parliament, we understand a fresh approach to the question of separation is being discussed in parliamentary circles. In summary, this approach replaces the proposed derogation with an explicit authorisation process for CSDs which provide ancillary banking services. The proposed authorisation process provides three alternatives:

- a single legal entity may provide CSD services and ancillary banking services, on very strict conditions including a capital surcharge and a plan to assure continuity of service (1+2 model);
- a different entity in the same group as a CSD may provide ancillary banking services alone, so long as the ancillary banking entity does not also provide CSD core services (2+2 model); and
- a CSD may designate one or more banks to provide banking ancillary services, so long as those designated banks do not themselves also provide CSD core services (1+n model)

At the time of writing, before the amendments have been considered in Committee, it is not clear whether this proposal has widespread support in the ECON Committee or the European

Parliament more broadly and the reaction of the other legislative actors remains to be seen. On first impressions, the proposal compares well to the concerns expressed in our policy stance above and provides an elegant solution to the problem of achieving improved safety and soundness at reasonable cost and without sacrificing hard-won efficiency gains.

Current CSDR timetable:

Past dates

7 March 2012: Legislative proposal published: COM(2012)0073 (Summary)

15 March 2012: Committee referral announced in European Parliament, 1st reading/single reading

17 July 2012: Draft Swinburne report to the European Parliament published

19 September 2012: Debate in Committee on the Swinburne report

12 November 2012: Amendments 127 to 407 to the proposed Regulation published

13 November 2012: Amendments 408 to 686 to the proposed Regulation published

Expected dates

21 January 2013: Vote scheduled in Committee, 1st reading/single reading

21 May 2013: Indicative plenary sitting date, 1st reading/single reading

Likely timings

1Q or 2Q 2013: Trilogue begins

From 2H 2013: ESMA technical standards developed

From 2H 2014: Implementation

Sources: European Parliament [website](#); Economic and Monetary Affairs Committee [website](#); ICMA analysis.

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Asset Management

by Annika Wahlberg

ICMA Private Wealth Management Charter of Quality

On 4 October 2012, the Luxembourg Bankers Association (ABBL) became the first signatory to the [ICMA Private Wealth Management Charter of Quality](#) at an ICMA/ABBL event – at which both the Luxembourg Minister of Finance and the Head of the Luxembourg regulator (CSSF) spoke – at the offices of Banque de Luxembourg.

Since then, 47 institutions and banks have signed the Charter of Quality in Luxembourg, 33 of which are also ICMA members or affiliates of ICMA members.

On 3 December 2012, the CSSF sent a Circular Letter to more than 250 banks and investment firms in Luxembourg requesting them to inform the CSSF whether they have signed the Charter of Quality.

ICMA again presented the Charter of Quality in Luxembourg at a meeting on 12 December of wealth managers and family offices belonging to *Association Luxembourgeoise des Professionnels du Patrimoine (ALPP)*. The Board of ALPP is currently considering next steps. On 17 December, the Liechtenstein Bankers Association became the second association to sign up to the Charter of Quality.

Discussions are well advanced with the Italian private banking and Swiss banking associations and with APCIMS in the UK and discussions have been initiated with the German banking association. We plan to introduce the Charter of Quality to the banking

associations of Austria, Belgium and France in the first quarter of next year. In time, we also hope to promote the Charter of Quality in Asia.

In an environment where regulation and compliance for the wealth management industry are playing an increasingly important role in client relationships, the Charter of Quality sets out in a single document the overall guiding principles of the private wealth management industry in a straightforward manner which clients will find easy to understand.

The Charter of Quality is designed to be consistent with relevant regulation at European Union and national level, and to complement principles such as the Wolfsberg Principles on Anti-Money Laundering and the global recommendations of the Financial Action Task Force.

The three main principles, which are of paramount importance to the nature of business relationships with clients, are the foundation of the Charter of Quality, namely:

- *integrity*: in business relationships; of markets, financial products and services; and of staff;
- *transparency*: towards clients, and regarding the regulatory environment;
- *professionalism*: regarding the primacy of clients' legitimate interests and efficiency.

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Shadow banking, appropriately conducted, provides a valuable alternative to bank funding in support of real economic activity.

Shadow banking

The “shadow banking system” can broadly be described as “credit intermediation involving entities and activities (fully or partially) outside the regular banking system” or non-bank credit intermediation in short. Such intermediation, appropriately conducted, provides a valuable alternative to bank funding in support of real economic activity.

At the Cannes Summit in November 2011, the G20 Leaders agreed to strengthen the oversight and regulation of the shadow banking system, and endorsed the initial recommendation of the Financial Stability Board (FSB) and its work plan to further develop policy recommendations during 2012.

The FSB published a number of documents on 18 November 2012. The documents outline the current status of the consultation and set out clear policy recommendations in respect of the different work streams that the FSB had identified.

The consultation documents refer to two of the five work streams (WS) established in 2011 to address the potential systemic risks associated with shadow banking in five specific areas: those relating to “other shadow banking entities” (WS3 below), and securities lending and repos (WS5 below):

- *WS1*: chaired by the BCBS: to mitigate the spill-over effect between the regular banking system and the shadow banking system.
- *WS2*: chaired by IOSCO: to reduce the susceptibility of money market funds (MMFs) to “runs”.
- *WS3*: chaired by FSB: to assess and mitigate systemic risks posed by other shadow banking entities.
- *WS4*: chaired by IOSCO: to assess and align the incentives associated with securitisation.
- *WS5*: chaired by the FSB: to dampen risks and pro-cyclical incentives associated with secured

financing contracts, such as repos and securities lending, that may exacerbate funding strains in times of runs.

The third consultation paper, *An Integrated Overview of Policy Recommendations*, sets out the FSB’s overall approach to shadow banking issues and provides an overview of its recommendations across the five specific areas which its shadow banking work streams have been addressing.

The FSB also highlighted two sets of final shadow banking policy recommendations which have been published by IOSCO, and which have relevance to the asset management and investor industry, namely

- IOSCO’s policy recommendations for WS2: *Policy Recommendations for Money Market Funds* (MMFs) (published on 9 October): These contain final rules following its consultation in April 2012. The recommendations set international standards for MMFs’ regulation and management practices, and set out 15 key principles for valuation, liquidity management, use of ratings, disclosure to investors and use of repos. In addition, the recommendations address valuation and requirements to maintain a constant net asset value (CNAV), and seek to address the risk of runs on MMFs;
- IOSCO’s policy recommendations for WS4: *Global Developments in Securitisation Regulation* (published on 16 November).

The anticipated Communication from the European Commission, initially anticipated before the end of 2012, is now expected during the first quarter of 2013.

The AMIC is monitoring closely developments in the shadow banking debate and consultations and will continue to discuss the work streams that affect the asset management industry in 2013.

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Solvency II timetable

On 21 November, the Chairman of EIOPA, Gabriel Bernardino, said that the EU political institutions remained committed to the implementation of Solvency II. But he also said: *“Even if a credible timetable will probably point to an implementation date not earlier than 2016, it should be possible in an interim phase to start to incorporate in the supervisory process some of the key features of Solvency II, namely some elements related to Pillars 2 and 3. EIOPA is exploring this possibility, based on its powers under the EIOPA Regulation. This interim phase should be coordinated by EIOPA in order to ensure a consistent application throughout the EU.”*

On 3 December, the European Parliament announced that the plenary vote of the Omnibus II Directive would be rescheduled from 11 March 2013 to 10 June 2013. As final agreement on Omnibus II has not yet been reached it is widely accepted that the proposed timeline of Solvency II transposition by 30 June 2013 and implementation by 1 January 2014 is unrealistic. A revised timetable for Solvency II has not yet been set.

In view of the uncertainty, asset managers in the AMIC Solvency II Working Group are planning to meet on 14 February at ICMA’s London offices to discuss the way ahead.

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The AMIC work programme for 2013

ICMA held an all-day meeting of the Asset Management and Investors Council (AMIC) at Credit Suisse on 23 November 2012, with around 100 participants. A copy of the agenda is available [here](#). The main purpose of the meeting was to discuss trends in the asset management industry and to provide feedback to the AMIC Executive Committee on its work programme for the period ahead. The AMIC Executive Committee subsequently met on 18 December.

A follow-up letter about the 2013 AMIC work programme will be sent early in 2013 to participants in the AMIC Council meeting and to other interested ICMA members:

- In addition to the AMIC Council and the AMIC Executive Committee, the existing AMIC Working Groups – the Covered Bond Investor Council, the

Private Banking Working Group and the Solvency II Working Group – will continue.

- Suggestions for other issues to be considered in 2013 include: the consultations on shadow banking and its implications for the asset management industry; bank debt and the bail-in of unsecured debt; bank recapitalisation; dark pools; fees in the asset management industry; valuation and performance measurement. A pan-industry approach to the implementation of new regulations affecting the asset management industry has also been suggested.

Please do contact the AMIC Secretariat, annika.wahlberg@icmagroup.org, if you are interested in participating in AMIC’s work programme.

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Signing of the ICMA Private Wealth Management Charter of Quality by ABBL in Luxembourg.

Regulatory or collateral cliff: is there a difference?

Personal view by Godfried De Vidts,
Chairman of ICMA European Repo Council



In Europe we seem to be avoiding a “fiscal cliff” at the moment, not least because of the proactive position of the European Central Bank with the, thus far untested, Outright Monetary Transactions (OMT). Whereas politicians failed to contain the sovereign debt crisis despite endless debates and summits, the central bank community rightly pushed for strong debt management measures before intervention could take place.

This will not be enough. Although the large number of regulatory initiatives – need I remind readers of the acronyms like EMIR, MiFID II, SSR, FTT, CSDR, SLL, MAD, CRD IV – have created unprecedented uncertainty, the financial community recognises the need for change. In fact, economic reality since the Pittsburgh G20 has already caused substantial change – and the objectives of the proposed legislation have always been accepted.

Specifically, the use of centralised clearing (CCPs) was already embedded in the repo market well before the crisis. Our experience has given us knowledge of the challenge this poses to the industry. Initial margin and variation margin are parts of the tool kit to protect against counterparty risk, be it through the use of CCPs or even in bilateral markets. The robust set-up

of European triparty is witness to the efforts of the repo industry, where haircuts are very common for this type of funding, simply because the type of collateral used demands a more hands-on approach to the underlying collateral.

In the last 15 years the ERC Committee has been represented in product advisory groups of various European fixed income CCPs. The result can be shown as an illustration of the need for market users to be involved in the risk committees of the respective CCPs, gradually increasing the robustness of the framework that will protect those CCPs in case of turmoil or default of one or more counterparties using their services.

What is not recognised enough is what provides this protection: *collateral*. In the many presentations I have done in the last decade I have always made clear that collateral cannot be a full substitute for counterparty risk. No matter how much protection you receive through collateral the first risk remains the default of the counterparty. Collateral should provide additional protection but this does not come without a price. In a recent publication by the Collateral Initiatives Coordination Forum the focus is on “fluidity of collateral”. And here, we approach a slippery slope.

Despite more than a decade of working groups, starting with the Giovannini barriers, followed by CESAME 1 & 2 and then EGMI 1 & 2, the core of collateral issues in Europe has not been solved. Recent discussions at the ECB’s COGESI (the infrastructure working group chaired by the ECB) have exposed one of the real stumbling blocks to progress: some of the CCPs, which have been tasked by the G20

to be part of the new regulatory framework. Witness an ERC initiative that continues to be challenged by some of these post-trade infrastructure providers, who are displaying resistance to opening up in ways similar to those which we have already seen in the equity markets. Under Commissioner McCreevy the Monitoring Group of the Code of Conduct on Clearing and Settlement (MOG) outlined the need for interoperability between the CCPs for equity markets. This market initiative showed that, without regulatory intervention to compel incumbents to adopt them, such interoperable facilities are hard to achieve.

The interoperability initiative as requested by the ERC between the (I)CSDs, allowing for the free flow of collateral to any of the fixed income CCPs in Europe irrespective of the location of the collateral, has, once again, been derailed by the reluctance of certain of the parties involved to play the game. It is however not a game, as their behaviour is a serious impediment to the creation of a true European securities market fit to serve the needs of the real economy. The recent refusal of certain fixed income CCPs to invest promptly in the necessary infrastructure, allowing access by all actors (MTFs, bilateral counterparties or (I)CSDs) to their facilities, contributes to a potential collateral cliff that threatens to undermine all the regulators' efforts to move towards the G20 goal of avoiding a similar crisis in the future. This request is not new. The ERC first started these discussions ahead of the creation of the euro.

Forgotten in the debate is the function of repo desks in the banking sector. Repo desks are responsible for the allocation of collateral to where it is needed (and that can be internal or external). The crisis has shown that the repo market, used by the central bank community to transmit liquidity to the financial system, is robust, able to deliver and innovative. True, some aspects can be improved. The ERC has in recent discussions with the regulatory community committed to help build the desired trade repository for repo, by providing intelligence, knowledge and time to deliver this project in the near future (for reference, see the ECB's published 3 December speech of its Vice-President, Vítor Constâncio). However, blockages such as those put up by certain CCPs expose a weakness in Europe's post-trade infrastructure. So far initiatives from the European Commission, which has the role of proposing legislation that can overcome national barriers, has failed to deliver an effective Single Market. The



without regulatory intervention to compel incumbents to adopt them, such interoperable facilities are hard to achieve

need for fluidity of collateral throughout the euro area (as a start) needs to be taken seriously. If the financial community has to collateralise OTC derivatives, equities, commodities and fixed income exposures, whether through CCPs or bilaterally, then collateral has to be seen as the equal of cash. Existing national or other infrastructure barriers have to come down rapidly. Failing to recognise this basic principle, so long the focus of attention of the ERC, will lead to a failure of adequate collateral availability in Europe. And without going into detail, today's costs to the industry cannot be ignored either. This will create problems in satisfying the regulatory demands for collateralisation, and hence will bring Europe to its own cliff, whether we call it regulatory or collateral.

Failure to recognise what has long been known as a problem and to do something about it threatens to jeopardise all the improvements which Commissioner Barnier and other officials have been pursuing. The ERC, together with many other industry bodies, has worked tirelessly to make sure collateral can flow where it is needed. Maybe it is time to further debate models which more clearly recognise that CCPs have effectively become public utilities, whilst continuing to recognise the need for strong input from market participants. Avoiding a collateral cliff should be on top of the huge pile of regulatory initiatives. Standing on the edge of a slippery cliff is dangerous. The smallest shortage of vigilance (transfer of adequate collateral in this case) can create havoc as, once even a chip of the cliff gives way, the fact of life is that a big part of the rock will likely come down. I am not sure if this can be called the regulatory or collateral cliff, but it is dangerous out there!

Market Infrastructure developments

ECB: Contact Group on Euro Securities Infrastructures (COGESI)

A regular semi-annual meeting of COGESI was held in Frankfurt on 22 November 2012. The agenda included:

- an update on collateral harmonisation developments, covering the progress made by the *ad hoc* COGESI and its work streams related to the harmonisation of collateral processes/procedures: (i) gap analysis exercise on collateral eligibility requirements; (ii) infrastructural requirements to support liquidity management; and (iii) elaboration of a report on minimum common features for CCPs/(I)CSDs triparty interoperability;
- Eurosystem collateral management developments, providing an update on the enhancements to be introduced to the Eurosystem's collateral management systems in 2014 relating to: (i) the removal of the repatriation requirement; and (ii) the cross-border use of triparty collateral management services;
- ICSD initiatives on collateral management services, including presentations from (i) Euroclear, on its global collateral management highway; (ii) Clearstream, on its Global Liquidity Hub and collateral management; and (iii) Iberclear, on collateral management services;
- an update on (I)CSD links eligible for use in Eurosystem credit operations in the context of T2S;
- the legislative process in the EU, including views on the proposed CSD Regulation; and on EMIR and its technical standards; and
- the CGFS survey on bank funding patterns and demand for high-quality collateral assets.

ECB: Money Market Contact Group (MMCG)

A regular quarterly meeting of the MMCG was held in Frankfurt on 10 December 2012. The agenda included: (i) presentations on recent developments in the loan repo market; (ii) follow-up on the MMCG survey on bank funding patterns and demand for high-quality collateral assets (in relation to work of the CGFS); (iii) update on money market benchmarks and their future; (iv) market initiatives to revive the unsecured interbank market; and (v) review of the latest market developments.

ECB: TARGET2-Securities (T2S)

A T2S Info Session was held in Vienna on 5 October 2012. This included presentations of T2S Project status update and next steps; 4CB project status update; and the new T2S governance, along with insight sessions on T2S auto-collateralisation; and T2S User Testing and Migration. The next T2S Info Session will be held in Helsinki on 17 January 2013.

Mandated to propose common solutions for adaptation to cross-CSD settlement in T2S, the TFAX (Task Force on adaptation to cross-CSD settlement in T2S) was set up by the T2S Advisory Group (AG) in its September 2011 meeting. The TFAX met in Paris on 9 - 10 October 2012 and conducted a detailed review of the responses to the second of its mini-consultations (which covered CCP instructions; issuance practices; message fields; and non-standardised securities). Following on from the first of its mini-consultations, the meeting also continued the TFAX's review of the redrafted priority 1 solution papers. At its subsequent meeting in Frankfurt on 30 October 2012, in preparation for agreeing upon its final report (see below), the TFAX then discussed revised solution papers for all the issues.

The T2S Harmonisation Steering Group (HSG), which is supporting the AG in formulating its harmonisation agenda, met in London on 18 October 2012. HSG members provided updates on T2S relevant initiatives and meetings on post-trade harmonisation. There was also a presentation of the *Third Harmonisation Progress Report* ahead of the final draft Report being presented to 28 November AG meeting. It is envisioned that this Report will be finalised in time for the next AG meeting in February 2013; and published thereafter in view of the Harmonisation Conference of the ECB and the EU Commission in March 2013. Finally, the Chairman of the TFAX updated the HSG members on the progress of its work. The next HSG meeting will be in Frankfurt on 1 February 2013.

On 19 October 2012, the ECB published the second T2S special series paper, entitled *T2S Auto-Collateralisation* and written by Mehdi Mana. The auto-collateralisation function is one of the key features of T2S and is expected to lead to significant savings in terms of liquidity and securities, as well as decreased borrowing costs for banks. This paper explains, from a business perspective, how auto-collateralisation will work in T2S and how users will benefit from it in practice. It outlines the general settings of auto-collateralisation in T2S, gives details on the provision of static data and describes how limits can be set, managed and monitored. Finally, the paper describes each phase of the auto-collateralisation process, as established in the *T2S User Requirements*.

Version 1.1 of the T2S Business Process Description (BPD) was published on 16 November 2012. The BPD describes and illustrates the business processes involving CSDs, central banks and other technically directly connected parties that interact with T2S. Version 1.1 mainly reflects the updates resulting from the relevant change requests that have been



At the AG's 28 November 2012 meeting, the TFAX Chairman presented the TFAX's final report.

approved since the publication of BPD version 1.0 in November 2011.

The AG provides advice to the Eurosystem on T2S-related issues, to ensure that T2S is developed and implemented according to market needs. To this end, the AG is made up of representatives from all stakeholders, ie participating CSDs, banks and national central banks. In particular, the AG addresses T2S issues related to policy, pricing, governance, and harmonisation in the field of securities settlement. On 28 November 2012, the AG held [its 19th meeting](#), in respect of which the agenda and a summary of proceedings have been published. The AG will next meet on 27 - 28 February 2013.

At the AG's 28 November 2012 meeting, the TFAX Chairman presented [the TFAX's final report](#). The HSG was invited to consider the recommendations of the TFAX and determine how to follow up on the TFAX recommendations, ie to assess which could be implemented and which need further work. The HSG view will be considered in the next AG meeting. A [cover note to the TFAX report](#) provides a brief description of: (i) scope of the TFAX analysis; (ii) TFAX findings and recommendations; and (iii) conclusion and outlook. An annex provides the comprehensive list of TFAX recommendations.

On 30 November 2012, the [Autumn 2012 issue of T2S OnLine](#) was published by the ECB. In the editorial, Jean-Michel Godeffroy, Chairman of the T2S

Board, shares some of his thoughts on the first achievements and challenges encountered by the T2S community under its new governance structure. He particularly focuses on the composition of the migration waves and how the change requests raised by CSDs as a result of their feasibility assessments are being handled.

The T2S Project update covers points on: the T2S programme plan; migration waves; change requests; technical documentation; assessment of CSD links; conditions for directly connected participants; harmonisation; software development and testing; and connectivity. Meanwhile the Insight section covers highlights from Sibos, which took place at the [end of October in Osaka](#), and work done by the Task Force on adaptation to cross-CSD settlement (TFAX).

Furthermore, Marc Bayle, T2S Programme Manager, describes the approach that was taken to finalise the migration plan, which needed to respect the provisions stipulated in the Framework Agreement, accommodate the wishes of the T2S markets and, at the same time, ensure a safe and smooth migration to the new platform in 2015-2016. And finally, there is an introduction to the new T2S Board, giving an insight into its structure and responsibilities and a little background on each of the 13 members.

A [joint EU Commission and ECB conference on Post-trade Harmonisation and Financial Integration in Europe](#) has

been scheduled for 19 March 2013. The conference will:

- highlight the link between the Commission initiatives (the CSD Regulation in particular) and those of the ECB, eg T2S;
- foster implementation of harmonisation measures in national markets; and
- demonstrate the determination of the Eurosystem and the European Commission to foster financial integration in spite of the financial crisis.

European Commission: Securities Law Legislation (SLL)

The Commission has reinvigorated its previous work as regards producing a legislative proposal for SLL. A discussion paper, under consideration with a Member States' technical working group, suggests a new approach under the general theme of "who owns what". This aims to learn lessons, from cases such as Lehmans, MF Global and Bear Stearns, on the transparency of ownership and the protection of client assets. Also linked to shadow banking discussions, work encompasses arrangements for intermediaries re-hypothecating client securities and arrangements for protecting clients' securities in the event of their intermediary failing.

Global Legal Entity Identification Numbers

Following on from progress notes published on [23 August](#) and then on [20 September](#), on 24 October 2012 the FSB published its [third progress note](#) on the Global LEI initiative.

On 31 October 2012, the [FSB issued a note](#) seeking the endorsement of the G20 Finance Ministers and Central Bank Governors for the draft [Charter for the Regulatory Oversight Committee \(ROC\)](#) of the Global LEI System. As confirmed in the [communiqué issued](#) following from their 4 - 5 November 2012 meeting

in Mexico, the G20 duly endorsed this Charter (see paragraph #15). Accordingly the ROC will act as the governance body for the global Legal Entity Identifier system to be launched in March 2013. The 31 October note also provides a short progress report on other major elements of the LEI work programme within three broad work areas: governance; operations; and relationship data.

On 8 November, the FSB issued a [statement](#) regarding the allocation of pre-Local Operating Unit (LOU) prefixes for pre-LEI issuance. Following up on this topic as it was described in Annex 2 of the third progress note, this statement lays out a table outlining the prefixes provided to sponsored pre-LOU solutions meeting the specified conditions.

On 11 December, the FSB published its [fourth progress note](#) on the Global LEI initiative. This latest update reports on progress under the headings of Charter for the Regulatory Oversight Committee (ROC); location and legal form of the global LEI foundation; Board of Directors of the LEI foundation; operational workstream; allocation of pre-LOU prefixes for pre-LEI issuance; and relationship data. There is also an annex, headed *Global LEI Foundation Board of Directors (BOD) Eligibility, Selection Criteria and Composition – Preliminary*.

On 20 December, the FSB issued a [request for legal advice](#) on matters regarding Switzerland as the potential domicile for the global LEI Foundation (or similar entity) operating the Central Operating Unit (COU).

IOSCO: Principles for Financial Market Infrastructures (FMIs)

On 14 December 2012, the CPSS and IOSCO published a [disclosure framework and assessment methodology](#) for their April 2012 *Principles for Financial Market Infrastructures* (PFMIs) (which were discussed in [Issue 26 of the](#)

[ICMA Quarterly Report](#)). The disclosure framework and the assessment methodology promote consistent disclosures of information by FMIs and consistent assessments by international financial institutions and national authorities. The assessment methodology is primarily intended for use by external assessors at the international level, in particular the International Monetary Fund and the World Bank. It also provides a baseline for national authorities to assess observance of the principles by the FMIs under their oversight or supervision and to self-assess the way they discharge their own responsibilities as regulators, supervisors and overseers.

CPSS: Red Book

The CPSS publishes reference works (widely known as Red Books) on payment systems and the other financial market infrastructures in various CPSS member and non-member countries. Following the enlargement of the CPSS in 2009, the latest edition of the Red Book is in two volumes. The first volume, covering 10 CPSS countries (Australia, Brazil, Canada, India, Korea, Mexico, Russia, Singapore, Sweden and Switzerland), was [published in September 2011](#) (see [Issue 23 of the ICMA Quarterly Report](#)).

The second volume, which covers the remaining 13 CPSS countries (Belgium, China, France, Germany, Hong Kong SAR, Italy, Japan, the Netherlands, Saudi Arabia, South Africa, Turkey, the United Kingdom and the United States) and the euro area; and includes a chapter on international arrangements, has now [also been published](#).

Separately, in September 2012, the CPSS [has published](#) *Statistics on Payment, Clearing and Settlement Systems in the CPSS Countries – Figures for 2011 – Preliminary Release*. This is an annual publication that provides data on payments and payment, clearing and settlement systems in the CPSS

countries. This version of the statistical update contains data for 2011 (although some of the data is provisional data for 2011 and some not yet available) and earlier years, with detailed tables for each individual country as well as a number of comparative tables.

Collateral Initiatives Coordination Forum (CICF)

Established at the beginning of 2012, the [Collateral Initiatives Coordination Forum](#) (CICF) has been conceived as a joint trade associations' body, in order to facilitate appropriate coordination across the private sector of all collateral-related initiatives. Independent of the participating trade associations, the CICF is chaired by Godfried De Vidts.

As announced in a [7 November press release](#), the CICF published a White Paper entitled *Collateral Fluidity*. In this White Paper the CICF makes the case that, as high quality collateral is in increasing demand to support transactions in financial markets, regulatory measures should ensure that it flows efficiently around the market; and that this requires careful attention to the details of some of the steps being taken and their sequencing. (Further detail regarding this White Paper may be found in the separate box).

Alongside this White Paper, the CICF also published a short primer entitled *Collateral Fundamentals*. The aim of this paper is to aid those interested in the topic of collateral, but new to the associated concepts; and, looking ahead, the CICF will consider opportunities to supplement this paper with similar papers going into further depth on more specific aspects of the overall collateral topic.

Copies of these papers were sent directly to selected officials at key European and international institutions.

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Collateral fluidity

Published on 7 November, the CICF's *Collateral Fluidity* White Paper examines the topic of collateral fluidity.

The importance of collateral has grown over many years, but has accelerated significantly since the advent of the financial crisis in mid-2007. This is in no small measure related to the shift in risk appetite of market participants, with an increased demand amongst them to secure their credit risk exposures through the taking of high quality collateral. Official policy makers have also significantly fuelled the demand for high-quality collateral as they have advanced steps to make markets more robust, to reduce systemic risk and help mitigate the risks of any future financial crises. The European government bond market, although increasing in size in tandem with the bail-out of the banking system, has suffered from the continuous downgrading of debt issues by sovereigns.

It is widely perceived that demands for high-quality collateral will significantly outstrip supply, so it is essential that collateral be managed as a scarce resource. Against this backdrop it is essential that efforts be made to ensure that collateral is able to flow as efficiently as possible, matching sources and uses. This White Paper explores this proposition and seeks to articulate a vision regarding what is necessary to achieve desirable improvements in collateral fluidity.

CICF's vision for improvements is as follows:

More attention urgently needs to be given to collateral fluidity, which in essence concerns the mobilisation of collateral, ie allowing it to be in the right place at the right time.

Achieving this requires that the plumbing be properly fixed, including through finally making progress with the continuing Giovannini barriers to EU cross-border clearing and settlement arrangements. The recently established European Post Trade Group is revisiting some of these points with a view to resolve them as inefficient domestic solutions currently continue to present barriers, as a result of which different collateral assets trade over different timeframes.

With the identified market infrastructure problems solved and the forthcoming transition to T2S achieved, there would then be an appropriately robust post-trade settlement infrastructure to serve as a basis for

the move to standardised T+2 settlement and, if then evidently needed, the market discipline measures, as contemplated by the currently proposed CSD Regulation.

So the CICF considers that at this point a compromise is needed.

Since their on-going existence continues to give rise to technical fails, thereby impeding collateral fluidity, work should be urgently advanced to ensure the elimination of already identified infrastructural inefficiencies and other, non-infrastructural, problems.

At the same time, whilst already overburdened by global regulatory initiatives European market participants will move to provide shorter settlement cycles as demanded by the CSD legislation. And meanwhile market users have pushed the CSDs/ ICSDs to embrace T2S.

Let us deliver on these major IT initiatives and when these latter two massive developments bear fruit we should take stock. If it is then found that there are still fails in the securities markets the time will be right to dig deeper and identify why. In case it is then found that abusive shorts are a problem, we recognise that there would be an appropriate case for mandatory buy-ins to be performed by the right (as yet to be defined) institutions.

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The Collateral Initiatives
Coordination Forum
published a White Paper
entitled *Collateral Fluidity*.



Collateral crunch?

by Serena Vecchiato

As predicted at the beginning of 2012 in the ICMA Quarterly Report (see page 46 of [Issue 24](#)), the shortage of collateral in the global financial markets has been an area of special focus for 2012, and will continue to raise widespread concern in 2013. Should markets expect a collateral crunch?

At a time when investors' confidence remains low and financial institutions are expected to meet new prudential rules, as well as comply with new margin requirements for both bilateral OTC derivatives transactions and those transferred to CCPs, an overall view of the global demand and supply pressures has started emerging. This article outlines some estimates of the demand and supply of collateral, while providing a general frame of reference on the topic. It will highlight that there are significant differences in the various estimates, reflecting differences in scope and the underlying assumptions made in the analysis.

On the demand side, a key source of collateral demand stems from the Basel III Liquidity Coverage Ratio (LCR) for which the EBA reported an aggregate shortfall of liquid assets of €1.17 trillion, according to an analysis conducted on European banks as of 31 December 2011 (see page 27 of [Issue 27](#)).

Furthermore, in an effort to strengthen the OTC derivatives market, regulators have mandated central clearing of standardised OTC derivatives as well as margin requirements for transactions that are not centrally cleared. Although the effect of these reforms will only build up over time, it is widely expected that they will bring a dramatic increase in collateral obligations. Initial margin will have to be delivered by one or both counterparties for all cleared trades and potentially bilateral activity; and variation margin will be required for all trades. Additionally, banks and dealers

will be constrained in their ability to re-hypothecate client collateral.

In an attempt to gauge the impact of the new regulation of the OTC derivatives market on the demand for collateral, many studies have been issued in the course of 2012:

Estimates of regulatory impact on collateral demand

	Products	Resources	Collateral demand (US\$ billions)
IMF (2012)	All OTC derivatives	Additional initial margin and default fund contribution	100-200
ISDA (2012)	All bilateral OTC derivatives	Additional initial margin	800-10,200
BIS (2012)	IRS and CDS	Total initial margin	700
Bank of England (2012)	IRS and CDS	Total initial margin	200-800

Sources: IMF (2012), ISDA (2012), BIS (2012) and Bank of England (2012)

According to the IMF, the direct incremental initial margin and the guarantee funds that will reside at the CCP are expected to amount to between \$100 billion and \$200 billion as a result of moving a critical mass of OTC derivatives to CCPs ([IMF \(2012\)](#)). The ISDA estimates that global initial margin requirements for OTC derivatives that are currently outstanding, but that are not and cannot be cleared, would range from \$800 billion to \$10,200 billion depending on the internal models or standardised schedules which are used ([ISDA \(2012\)](#)). The BIS calculates that, under "normal" market conditions and assuming one CCP for each of the two asset classes, the total initial margin could reach \$700 billion for the interest rate swap (IRS) and credit default swap (CDS) markets alone ([BIS \(2012\)](#)). Finally,

the Bank of England estimates that the total initial margin for cleared and non-cleared (bilateral) trades in the IRS and CDS markets may reach between \$200 billion and \$800 billion, depending on the sensitivity of the assumptions around netting efficiency ([Bank of England \(2012\)](#)).

Turning to the supply side, the expected increase in demand for collateral should be considered in the context of the total pool of safe assets. The problem is not so much an insufficient quantity of safe assets as the fact that the frontier between safe and unsafe assets has shifted over time. The IMF estimates that, if government debts of advanced economies with 5-year CDS spreads above 200 basis points at end-2011 are excluded from the safe-asset universe (because the financial crisis has changed investors' idea of what is a safe asset), the supply of safe public debt will be reduced by more than \$9 trillion by 2016. Furthermore, as for safe assets issued by the private sector, the private sector securitization issuance declined from more than \$3 trillion in the United States and Europe in 2007 to less than \$750 billion in 2010 ([BIS \(2012a\)](#)).

As studies confirm that the demand for high quality collateral will significantly increase against a backdrop of falling supply, it is widely recognised that collateral should be managed as a scarce source. The CICF [White Paper on Collateral Fluidity](#) (which is described more fully in a separate box in this Quarterly Report) explores steps to ensure that collateral is able to flow as efficiently as possible. ICMA will continue to engage with the relevant market stakeholders and contribute to the debate on a possible collateral crunch.

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diary

ICMA organises over 100 market-related events each year attended by members and non-members. For full details see www.icmagroup.org

17 JAN

Les Rencontres des Professionnels des Marchés de la Dette et du Change, Paris, 17 January

This annual conference for fixed income professionals in the French marketplace is organised by six associations including ICMA. Three roundtables will consider: Electronic platforms – essential gateway for the Industry? FX, bonds and money markets; what market funding for SMEs? And: is it still possible to invest without risk?

[Register here](#)

18 JAN

ICMA meeting with Benoît Cœuré, ECB: Euro area financial markets: where do we stand? Paris, 18 January

Benoît Cœuré, Member of the Executive Board of the European Central Bank will be the guest of honour at an ICMA lunchtime meeting in Paris.

This event is free of charge and is open to ICMA members and qualifying financial market participants.

[Register here](#)

31 JAN

ACI and ICMA 2013 Economic Summit and New Year's Event, Brussels, 31 January

organised by ACI and the ICMA Belgian region

An evening event featuring four prominent economists on the outlook for 2013.

[Register here](#)

5 FEB

Japan Securities Summit, London, 5 February

Organised by the Japan Securities Dealers Association (JSDA) with the assistance of ICMA.

The 2013 Japanese Securities Summit will focus on the potential of Japanese securities and government bond markets for international investors. Presentations and panel discussions from the members of a high level delegation from Japan will feature the latest developments in Japanese securities markets, including the evolution of market infrastructure.

[Register here](#)

25-27 FEB

Global Master Agreements for Repo and Securities Lending Workshop, Frankfurt, 25-27 February

The workshop will include a detailed review of both legal agreements and their application, including coverage of the GMRA 2011, together with case studies; and the operational and basic legal characteristics of the repo and securities lending markets.

[Register here](#)

11 MAR

ICMA European Repo Council (ERC) Annual General Meeting, Paris, 11 March

Save the date

The next ERC meeting will be held at the Intercontinental Hotel Opera in Paris, hosted by Euroclear.

13
MAR**European Regulation:
An Introduction for Capital Market
Practitioners, London, 13 March**

This one day, fast-track course on European regulation for capital market practitioners is aimed at sales people, traders, originators, syndicate personnel, and middle and back office staff who would benefit from a better understanding of the current regulatory landscape in the cross-border bond markets. The course provides updates on the major regulatory developments relevant to the market and considers recent case studies in the regulatory crackdown.

[Register here](#)

16
MAY**The ICMA Covered Bond Investor
Council (CBIC) & The Covered Bond
Report Conference, Frankfurt, 16 May**

Following on from the success of last year's inaugural event, the 2013 Covered Bond Investor Conference will focus on topical investors' issues and will once again provide an ideal opportunity for those wishing to engage in a constructive dialogue with the buy-side. As with The Covered Bond Report website and magazine, the conference is free for relevant investors.

[Register here](#)

ICMA AGM and Conference, Copenhagen

22 to 24 May 2013

Registrations will open at the end of January for the 44th ICMA AGM and Conference, which will be held in Copenhagen at the Tivoli Hotel and Congress Centre.

As ever the two-day conference will bring together capital market participants, asset managers, regulators, central banks and infrastructure providers to discuss market and regulatory issues, including:

- Progress in finding solutions to the euro crisis, prospects for European Banking Union and a Single Supervisory Mechanism.
- Regulatory and infrastructure developments affecting the availability of collateral.
- Restoring confidence in the primary debt capital market.
- The evolution of secondary market trading and the future of the dealer intermediation model.
- A buy-side perspective on capital markets.

The following speakers have already confirmed their participation at the conference:

- Per Callesen, Governor, Danmarks Nationalbank
- Erkki Liikanen, Governor, Bank of Finland
- Benoît Cœuré, Executive Board, European Central Bank
- Steven Maijoor, Chairman, European Securities & Markets Authority
- Thomas Borgen, Member of the Executive Board and Head of Corporates & Institutions, Danske Bank
- Fanny Borgstrom, Head of Group Funding, Nordea
- Martin Egan, Global Head of Primary Markets & Origination, Fixed Income, BNP Paribas
- Peter Engberg Jensen, Group Chief Executive, NyKredit
- Michael Gower, Treasurer, Rabobank
- Casper von Kuskull, Executive Vice President, Nordea
- David Marks, Chairman, FIG Debt Capital Markets, J.P. Morgan
- Mattias Persson, Head of Financial Stability, Sveriges Riksbank
- Tony Platt, Executive Director, Morgan Stanley
- Philippe Rakotovoao, Managing Director, Global Head of Corporate and Investor Clients, Crédit Agricole
- Gerassimos Thomas, Director, European Commission
- Daniel Trinder, Managing Director and Global Head of Regulatory Policy, Deutsche Bank

**The conference is open to all financial market participants.
For full details please see the [ICMA website](#)**

ICMA Executive Education in 2013

Register now for these ICMA Executive Education courses in 2013. Check the ICMA website for the full 2013 course schedule and details of the courses.

Part I: Introductory Programmes

Financial Markets Foundation Course (FMFC)

Luxembourg: 11-13 March 2013
London: 8-10 May 2013

Securities Operations Foundation Course (SOFC)

London: 18-20 February 2013
Brussels: 25-27 March 2013

Part II: Intermediate Programmes

International Fixed Income and Derivatives (IFID) Certificate Programme

Sitges, Barcelona: 21-27 April 2013

Operations Certificate Programme (OCP)

Brussels: 17-23 March 2013

Primary Market Certificate (PMC) - Dubai

Dubai: 3-7 February 2013

Primary Market Certificate (PMC) - Hong Kong

Hong Kong: 4-8 March 2013

Primary Market Certificate (PMC) - London

London: 13-17 May 2013

Part III: Specialist Programmes

Collateral Management

London: 3-4 April 2013

Commodities – An Introduction

London: 25 March 2013

Commodities – Trading and Investment Strategies

London: 26 March 2013

Global Custody

London: 3-4 June 2013

Inflation-linked Bonds and Structures

London: 20-21 June 2013

Securities Lending & Borrowing

London: 29-30 April 2013

ICMA Executive Education Skills Courses

Mastering Mandates

London: 21-22 February 2013

Successful Sales

London: 25-26 April 2013

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Glossary

ABCP	Asset-Backed Commercial Paper	G20	Group of Twenty
AFME	Association for Financial Markets in Europe	GDP	Gross Domestic Product
AIFMD	Alternative Investment Fund Managers Directive	GMRA	Global Master Repurchase Agreement
AMF	Autorité des marchés financiers	G-SIBs	Global systemically important banks
AMIC	ICMA Asset Management and Investors Council	G-SIFIs	Global systemically important financial institutions
BBA	British Bankers' Association	HFT	High frequency trading
BCBS	Basel Committee on Banking Supervision	HMT	HM Treasury
BIS	Bank for International Settlements	IASB	International Accounting Standards Board
CAC	Collective action clause	ICMA	International Capital Market Association
CBIC	ICMA Covered Bond Investor Council	ICSA	International Council of Securities Associations
CCBM2	Collateral Central Bank Management	ICSDs	International Central Securities Depositories
CCP	Central counterparty	IFRS	International Financial Reporting Standards
CDS	Credit default swap	IMCO	Internal Market and Consumer Protection Committee of the European Parliament
CGFS	Committee on the Global Financial System	IMMFA	International Money Market Funds Association
CICF	Collateral Initiatives Coordination Forum	IMF	International Monetary Fund
CoCo	Contingent convertible	IOSCO	International Organization of Securities Commissions
CPSS	Committee on Payments and Securities Settlement	IRS	Interest rate swap
CRA	Credit Rating Agency	ISDA	International Swaps and Derivatives Association
CRD	Capital Requirements Directive	ISLA	International Securities Lending Association
CRR	Capital Requirements Regulation	KID	Key information document
CSD	Central Securities Depository	LCR	Liquidity Coverage Ratio (or Requirement)
DMO	Debt Management Office	L&DC	ICMA Legal & Documentation Committee
D-SIBs	Domestic systemically important banks	LEI	Legal entity identifier
DVP	Delivery versus payment	LIBOR	London Interbank Offered Rate
EACH	European Association of CCP Clearing Houses	LTRO	Longer-Term Refinancing Operation
EBA	European Banking Authority	MiFID	Markets in Financial Instruments Directive
ECB	European Central Bank	MiFID II	Proposed revision of MiFID
ECOFIN	Economic and Financial Affairs Council (of the EU)	MiFIR	Proposed Markets in Financial Instruments Regulation
ECON	Economic and Monetary Affairs Committee of the European Parliament	MMF	Money market fund
ECP	Euro Commercial Paper	MTF	Multilateral Trading Facility
EEA	European Economic Area	NSFR	Net Stable Funding Ratio (or Requirement)
EFAMA	European Fund and Asset Management Association	OTC	Over-the-counter
EFC	Economic and Financial Committee (of the EU)	OTF	Organised Trading Facility
EFSF	European Stability Facility	OMTs	Outright Monetary Transactions
EGMI	European Group on Market Infrastructures	PD	EU Prospectus Directive
EIOPA	European Insurance and Occupational Pensions Authority	PR	PD Implementing Regulation
EMIR	European Market Infrastructure Regulation	PMPC	ICMA Primary Market Practices Committee
ERC	ICMA European Repo Council	PRIPs	Packaged Retail Investment Products
ESA	European Supervisory Authority	PSI	Private sector involvement
ESMA	European Securities and Markets Authority	PSIF	Public Sector Issuer Forum
ESM	European Stability Mechanism	RM	Regulated Market
ESRB	European Systemic Risk Board	RPC	ICMA Regulatory Policy Committee
ETF	Exchange-traded fund	RTS	Regulatory Technical Standards
EURIBOR	Euro Interbank Offered Rate	SBWG	ICMA Sovereign Bonds Working Group
Eurosystem	ECB and participating national central banks in the euro area	SGP	Stability and Growth Pact
FASB	Financial Accounting Standards Board	SI	Systematic Internaliser
FATCA	US Foreign Account Tax Compliance Act	SLL	Securities Law Legislation
FIIF	ICMA Financial Institution Issuer Forum	SMPC	ICMA Secondary Market Practices Committee
FMI	Financial market infrastructure	SMSG	ESMA Securities and Markets Stakeholder Group
FPC	UK Financial Policy Committee	SRO	Self-regulatory organisation
FRN	Floating-rate note	SSAs	Sovereigns, supranationals and agencies
FSA	UK Financial Services Authority	SSR	EU Short Selling Regulation
FSB	Financial Stability Board	T+2	Trade date plus two business days
FSOC	Financial Stability Oversight Council	T2S	TARGET2-Securities
FTT	Financial Transaction Tax	TD	EU Transparency Directive
		TRs	Trade repositories



ICMA welcomes feedback and comments on the issues raised in the Quarterly Report. Please e-mail: regulatorypolicynews@icmagroup.org or alternatively the ICMA contact whose e-mail address is given at the end of the relevant article.

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