ICMA quarterly report

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Assessment of Market Practice and Regulatory Policy

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The ICMA Asset Management and Investors Council

Foreword by Robert Parker

The Asset Management and Investors Council (AMIC) was established in 2008 to represent the buy side of ICMA. It has been active in identifying key trends in the asset management industry, in highlighting problematic areas and in engaging with investors and regulators to ensure that the buy side adds value to clients and more generally to the global economy.

AMIC has two conferences annually for its membership – the next one will be held in London on 29 October 2014 – but the continuous work is carried out by a series of working groups, which report to the AMIC Executive Committee. A number of these working groups concentrate on the fixed income markets, and particularly two groups are reviewing the development of Infrastructure Bonds and Green Bonds. There is strong demand to develop finance for infrastructure in the long-term bond markets while, for a raft of reasons, there is interest in developing the Green Bond market.

As banks deleverage their balance sheets, other areas for the investment community to provide finance are in the private placement market and in securitisation. It is notable that the European capital markets are relatively immature in these two areas compared with the United States, and the new AMIC working groups have a clear mandate to ensure the necessary development of euro markets. Another key issue for the AMIC, and ICMA as a whole, is market liquidity in the future and ICMA is carrying out a secondary market study of potential changes in liquidity at a time when US monetary policy is changing. One of the oldest AMIC working groups has been the ICMA Covered Bond Investor Council, which has had a positive impact on the efficient working of the covered bond markets. It must be emphasised that regulators and central banks are strongly supportive of these AMIC fixed income working groups to ensure that markets function and develop in a disciplined and well regulated manner.

Outside the fixed income markets, AMIC has a number of other actual or proposed working groups. One aspect of the deleveraging of the banking market is the transfer of assets to investors, and regulators have correctly expressed concern as to whether this activity leads to asset managers behaving like "shadow banks". This issue is critical if and where investors are moving away from their traditional roles of purely acting as agents for their clients and not taking balance sheet risk. The proposed AMIC Shadow Banking Working Group will highlight risk areas and give guidance on how the asset management industry should avoid systemic risks. A successful AMIC group previously set out guidelines for the ETF industry and highlighted the risks where ETFs have moved away from their traditional role of purely investing in underlying assets.

An important area in the asset management industry which regulators have focused on is the development of long-term investment, typically defined as private equity, infrastructure, real estate and other illiquid asset classes. Where investors have long-term liabilities, clearly there is a case for increasing asset allocation to these asset classes. The AMIC Council panel on this topic will be discussing asset allocation trends to longer-term investment, on the inherent risks and suggested guidelines for the investment community, to ensure longer-term value added to end-clients. An alternative aspect to long-term investment is the argument for holding investments for a period of time as opposed to shorter-term positions, and subsequently an AMIC working group will be addressing this question. A separate topic is the question of good corporate governance and investors' roles in improving governance and more broadly in ensuring trust in the asset management industry. AMIC has carried out over the years reviews of corporate governance codes and it is reasonable to state that, in most markets, corporate governance has improved on trend.

Another area of AMIC's work is in industry groups. One successful example has been the Private Banking Working Group which has produced a Private Wealth Management Charter of Quality. The private banking market is going through a series of significant changes and most notably in the area of cross-border flows and the Private Banking Working Group is ensuring that the private banking market remains robust in the face of these changes.

By most criteria, the asset management industry now has record assets under management, but it has been greatly assisted by easy monetary policies and by the transfer of assets from the banking system. It is critical that our industry addresses this growth intelligently and in a disciplined manner: first, to add value to investors such as savers and pension funds; second, to ensure solid risk management; and, finally, to avoid the asset management industry becoming a source of systemic risk.

Robert Parker is Senior Adviser, Credit Suisse, a member of the ICMA Board and Chairman of ICMA's Asset Management and Investors Council (AMIC) and the AMIC Executive Committee

Message from the Chief Executive

by Martin Scheck

During the period since the last Quarterly Report, the headlines have been largely dominated by disturbing and serious geopolitical events, which have pushed the issue of trust in the industry off the front pages. But we should not be lulled into thinking that this is no longer an issue – quite the contrary. The drip feed of negative news continues to be very damaging and is likely to be so for some considerable time. There is no easy remedy, but we are actively playing our part in trying to improve the situation. Much of what we do at ICMA plays a direct role in restoring trust: our work in setting standards of best practice; fostering robust, transparent and predictable securities markets; providing education for market participants and codes of conduct etc. We have also debated the issue at a number of ICMA roundtables and conferences to sensitise market participants to the enormous challenge ahead. Restoring trust is a multi-year process – we have mentioned it before in the Quarterly Report, and Paul Richards' article in this edition is centred on this theme.

There are a number of other topics I want to highlight in my introduction.

First of all, secondary markets. Prior to the 1 August deadline, we were devoting considerable resource to responding to ESMA's Discussion and Consultation Papers on MiFID II. Part of our response provided input on the trade-off between liquidity and transparency; another segment dealt with the infrastructure of trading and the definitions of the regulated venues to which much of the OTC market must eventually migrate; and we also responded from the perspective of our primary market franchise. At ICMA we have been concerned about the substantial reduction in secondary market liquidity for a number of years and the work on MiFID has been a catalyst for our concerns to be shared with many other market participants and authorities. We are in the process of undertaking a substantial market survey analysing the causes of this reduction in secondary liquidity, and looking at the prospects for future developments in secondary markets. This is a cross-cutting theme for our members, sell side and buy side. We expect to publish our study this autumn.

Another issue which has come to a head since the last Quarterly Report is Argentina. And as we all know Argentina is currently in default. ICMA has been working constructively, again on a cross-industry basis together with the IMF, IIF and others to modernise and improve bond contract terms to facilitate sovereign debt restructurings. I am pleased to say that, following two extensive consultations with interested members, we have reached a consensus which provides a balance between the need for sovereigns to be able to restructure expediently if they are at risk of defaulting, and protecting the interests of investors. The new recommended ICMA model collective action clauses and the revised model *pari passu* clause will now be included in our Primary Market Handbook and we look forward to their widespread adoption by sovereign issuers outside the euro area. Several sovereign borrowers have begun to implement these new measures in their recent issues. Lastly, in its 21 September communiqué, the G20 referred to ICMA's proposals and noted that they were the subject of upcoming discussions at the IMF.

There has been plenty of activity also on the Green Bond Principles, where as reported last time ICMA is running the Secretariat. We have formed a balanced Executive Committee of six issuers, six investors and six intermediaries and issued the first Consultation Paper on the Principles to the 60-plus institutions which are members of this fast growing initiative. The response has been fulsome, with a wealth of thoughtful and constructive comment. We are assessing this and will report at the AGM of the Green Bond Principles early next year.

The ICMA Asian initiative continues to make good progress. We have added one more employee to work alongside our existing senior representative and step by step are building our contacts, credibility and membership in the region. A recent focus has been the high level UK-China Economic and Financial Dialogue in September 2014. The official policy outcomes paper agreed by the two countries during this dialogue specifies that ICMA will co-chair a committee with NAFMII to aid in bond market development in China. This is an extremely exciting and an important initiative and there is more comment inside this Quarterly Report. In addition, the working groups we have started in Hong Kong on the primary markets continue to thrive, and our new Asian Advisory Council has taken shape.

Our regional committee structure is important in making sure that our agenda represents the needs of our members. Hence we revise our regional structure as appropriate to reflect – and anticipate – developments in our membership base. Recently we have taken the first steps to create a new ICMA Africa region to provide a forum for existing and future members on this continent, and to address their needs as domestic markets develop further and internationalise.

Turning to the buy side, covered bonds have been an important, stable and cost-effective funding tool for financial institutions since the crisis. ICMA has followed up its work on transparency and disclosure by commissioning a report on adherence to our suggested standards in various key jurisdictions. The report reveals that there is still progress to be made and highlighted the need for further disclosure of credit relevant aspects of the underlying cover pool.

The Quarterly Report provides an opportunity for us to update you on the many workstreams and initiatives to which we are devoting our resources – far too many to mention individually in this short introduction. In their different ways they are all important. We rely on the input and willing support of many hundreds of individuals from our members, for which we are immensely grateful.

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Restoring trust in the financial system

Quarterly Assessment by Paul Richards

Summary

Following the international financial crisis, in which public trust in the financial system was seriously damaged, the question is how to restore trust. The authorities' response has been to try to prevent a repetition of the crisis by introducing regulations to make financial institutions safer and the financial system more stable. There is an additional political imperative to ensure that taxpayers never have to bail out financial institutions again. But restoring trust also involves raising standards in the industry. One way in which the authorities propose to raise standards is by making the consequences of mistakes very expensive for the industry. Another way is by setting detailed regulatory standards which financial institutions are required to meet. The UK is attempting to raise standards by means of three reviews of the industry which involve input from financial market participants, and depend at least in part on voluntary agreement. Trade associations like ICMA already contribute to the work of raising standards, and can continue to do so in a number of ways.

Introduction

1 It is widely recognised that public trust in the financial system was seriously damaged by the international financial crisis which began in 2007: initially, it was damaged at UK level by the run on Northern Rock in 2007, and at global level by the failure of Lehman Brothers in 2008; subsequently, it was damaged by emerging evidence of misconduct and mis-selling. During the crisis, the authorities had to step in to support short-term financial markets which froze, and to recapitalise financial institutions in trouble. The crisis led to a substantial potential cost for taxpayers, both in terms of public expenditure and in terms of lost growth and unemployment. And quite apart from the quantifiable cost, there is the intangible cost arising from the loss of trust.

Making the financial system more stable

2 So the question post-crisis is how to restore trust in the financial system. The authorities' response has been to try to prevent a repetition of the crisis by making financial institutions safer and the financial

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system more stable. They intend to achieve this through the introduction of much more intrusive financial regulation than before the crisis:

- not only by means of *prudential* regulation: to ensure that banks are properly capitalised, have sufficient liquidity and are not over-leveraged; to ensure that their solvency is checked through asset quality reviews and their resilience is checked through stress tests; to improve the transparency of their accounts; and internally to separate their essential retail banking and payment activities from their wholesale investment banking activities;
- but also by means of *conduct of business* regulation: to ensure that customers are treated fairly, and to prevent misconduct and mis-selling.

3 At the same time, the authorities recognise that they need to avoid imposing on the financial system the stability of the graveyard. There is a fine line to be drawn between making the system safer, on the one side, without making it prohibitively expensive for financial institutions to engage in normal business, on the other. Financial institutions need to be both willing and able to take on financial risk in order to support growth in the economy. Across the EU, there is some evidence that they are beginning to do so. But the financial system is still fragile, as concerns in capital markets over the prospective results of the ECB's asset quality review and stress test have shown. In addition, financial institutions need to cope with the risk of rising short-term interest rates, led by the US as quantitative easing there is unwound, and with continuing political risks (eg in the Ukraine and the Middle East). There is also the risk that a future financial crisis will be different from the last one: eg as a result of cyber attacks on financial markets.

Taking taxpayers off the hook

4 Apart from making the financial system more stable, there is a political imperative to ensure that taxpayers never have to bail out financial institutions again. On the *prudential* side, the authorities intend to ensure this, partly by making it less likely that financial institutions will become insolvent in future, and partly also – if they still do – by bailing *in* the shareholders and large creditors of the institutions concerned, and then by drawing on insurance provided by the banking system as a whole, before calling on taxpayers to bail them *out*. In theory, this should avoid the need for taxpayer support altogether. But in practice, if a systemically important financial institution becomes insolvent in future, there is still a risk that the stability of the system as a whole will be threatened.

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5 Further work needs to be done on how to resolve – without taxpayer support and without disrupting the financial system – global systemically important financial institutions across borders, including by requiring them to write “living wills”, in case resolution becomes necessary. Even in the relatively small recent case in August 2014 involving the resolution of Banco Espirito Santo, where shareholders and junior debtholders were bailed into a separate “bad bank” pending its liquidation, the Portuguese Government lent much the largest proportion of funding required by the Portuguese bank resolution fund to recapitalise a new “good bank”, which included depositors and senior debtholders, pending its sale to the private sector. The Portuguese banking system was not able to make a sufficiently large financial contribution on its own without Government support; and the proposed Single Resolution Mechanism, which is intended to provide a euro-area bank insurance scheme after bailing in senior creditors and large depositors, has not yet come into effect.

6 On the *conduct of business* side, the authorities want standards of conduct in the financial system to improve. If standards do not improve, the authorities' main weapon is to fine financial institutions for misconduct or mis-selling: not just mis-selling of retail financial products, but also wholesale financial products, eg some benchmarks. There are two main concerns about this:

- The first is that, since the crisis, fines have become disproportionately so large that they threaten the financial viability of the financial institutions which have to pay them and put at risk the stability of the system. Fines have been particularly heavy on systemically important financial institutions, leading to the perception – however mistaken – that the level of fines is calculated on the basis of ability to pay rather than the scale of misconduct. Fines on financial institutions have been estimated at over

$200 billion to date, leaving aside other industries. While the authorities need the financial system to be recapitalised to make it more stable, on the one hand, the process of recapitalisation is at risk of being undermined by the scale of fines levied by the authorities, on the other.

- The second is that, although it is the conduct of bank management which has been at fault, it is investors who have to pay for managers' mistakes – and the associated market uncertainty arising from "legal risk" – through the share price. In a Consultation Paper in July 2014 on *Strengthening Accountability in Banking: a New Regulatory Framework for Individuals*, the UK Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) argue that holding individuals to account is a key component of effective regulation. They propose "a new Senior Managers Regime for individuals who are subject to regulatory approval, which will require firms to allocate a range of responsibilities to these individuals and to regularly vet their fitness and propriety"; and "a Certification Regime which will require relevant firms to assess the fitness and propriety of certain employees who could pose a risk of significant harm to the firm or any of its customers"; as well as a new set of rules governing professional conduct.

Raising standards

7 The authorities' proposals are designed to improve standards of behaviour in the industry by making the consequences of mistakes very expensive through the imposition of fines, and by encouraging greater due diligence in risk taking through the imposition of "bail in". But there are also other ways in which the authorities are hoping to restore trust.

(i) Standard setting at global level

8 At global level, under the aegis of the G20, the Financial Stability Board (FSB) published in April 2014 a selection of indicators of a sound risk culture for financial institutions:

- The board and senior management of a financial institution should take the lead in setting its core values and risk culture, and their behaviour should reflect the values being espoused.
- Relevant employees at all levels should understand the core values of the institution and its approach to risk; they should be capable of performing their prescribed roles; and they should be aware that they will be held accountable for their actions in relation to the institution's risk-taking behaviour.
- A sound risk culture should promote an environment of open communication and challenge in which decision-making processes encourage a range of views.
- Financial and non-financial incentives should support the core values and risk culture at all levels of the institution.

9 In addition to these indicators of sound risk culture for financial institutions published by the FSB, IOSCO is working at global level to raise standards across financial markets, as well as to eliminate: differences between national regulatory regimes; the extra-territorial effects of the regime in one jurisdiction on others; and an uneven international approach to cyber resilience. But IOSCO does not, at least yet, have the power to resolve disputes between regulators, except in a very limited way. Both IOSCO and the FSB rely on national governments to implement policies agreed at global level by the G20; and in Europe, IOSCO and the FSB rely on the EU.

(ii) Single EU Rulebook

10 The authorities' approach at EU level, which is intended both to integrate the Single EU Market and to help restore public trust in using it, is to prescribe – both for financial institutions and financial markets – a Single EU Rulebook:

"The authorities' proposals are designed to improve standards of behaviour in the industry by making the consequences of mistakes very expensive.

- This now contains a much more intrusive set of financial regulations than the "principles-based" or "lighter-touch" regime which preceded it in some countries. The intrusive set of financial regulations take effect through implementing and regulatory technical standards which are both mandatory and detailed; and because they are detailed, they need regularly to be reviewed to keep them up to date.
- Their intrusiveness increases the incentive for regulated institutions to escape the regulatory net in order to remain competitive with non-regulated institutions outside it. Consequently, the regulatory perimeter has had to be widened.
- Overall, the Single Rulebook attempts to raise standards by setting detailed requirements across borders in the EU, whether as a norm or as a minimum. Increasingly, this is done by Regulations, which apply directly in all EU Member States, rather than by Directives, which apply indirectly because they have to be transposed by each Member State into its national law.

11 The new President of the European Commission plans to build on the Single EU Rulebook by creating an EU Capital Markets Union over the five year mandate of the new European Parliament and next European Commission to encourage investment and help support economic recovery.

- There is already considerable scope for the international capital market to make a contribution to economic recovery by providing finance to businesses in place of the deleveraging by the banks. Additional steps that would encourage the provision of capital market finance across borders in the EU – debt as well as equity – include: the development of a pan-European private placement market (a market which is currently much further developed in the US than in Europe); longer-term market financing for infrastructure projects; and a revival of the securitisation market, limited to high-quality securitisations.
- It is not yet clear whether Capital Markets Union will primarily be designed to complete the EU Financial Services Action Plan, or whether it will be intended to extend the Single Supervisory Mechanism for banks in the euro area, overseen by the ECB, to cover capital markets, overseen by the EU Financial Services Commissioner and the European Supervisory Authorities, across the EU as a whole. A third option would be a market-based approach, building on the Eurobond market which ICMA has helped to develop for over forty years. The regulatory, institutional and market-based approaches are not necessarily inconsistent. But the outcome could have significant implications for the EU's largest wholesale financial centre: the City of London.

(iii) UK model

12 Beyond new EU regulations, which financial institutions are required to implement, the question is whether standards can be raised voluntarily, and how the financial services industry itself can play a part in helping to achieve this. As an example, the UK is attempting to raise standards in at least three ways:

13 First, in September last year, Sir Richard Lambert was asked by the chairmen of the UK's largest banks and building societies to develop plans for a professional body to promote high standards in banking. The Lambert Review starts from the premise that the banking sector has lost the trust of the public and needs to earn this back; and it accepts that integrity cannot be imposed by regulators. While recognising that the primary responsibility for improving the behaviour of banks lies with the leadership of financial institutions themselves, the Lambert Review has proposed a Banking Standards Review Council (BSRC), which will: rely on voluntary support rather than statutory backing; be funded by banks; but act as an independent champion of better banking standards in the UK. The BSRC's role is limited to the UK and to the banking sector, rather than the international capital market as a whole.

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14 It is planned that the BSRC should promote high standards by:

- requiring participating banks and building societies to commit to a programme of continuous improvement and report back to the public on their performance every year;
- setting standards of good practice by working with market practitioners and others to identify areas where current practice could be improved voluntarily through collective action in the public interest: eg whistleblowing protocols; procedures for resolving complaints; and setting standards for staff values and the governance of behaviour;
- holding a meeting once a year with non-executive directors to discuss progress; and publishing an annual report on progress;
- developing a single principles-based code of practice consistent with regulation: eg to guide behaviour in the event of conflicts of interest or moral ambiguity;
- identifying and encouraging good practice in learning, development and leadership, with a particular focus on behaviour and ethics;
- helping the industry to implement the obligations placed on it by certain new regulations, where these relate to the BSRC's remit; and
- encouraging the industry to increase the value placed on professional qualifications.

15 There appears to be a consensus in the industry that the BSRC should:

- have a narrow remit as a champion of banking standards;
- be independent of the banks and building societies, and not an advocate on their behalf;
- be transparent and open at all times: as the BSRC will have no statutory powers, it will only achieve influence through the power of disclosure;
- avoid duplicating the work of existing organisations;
- align its activities with the work of the regulators;
- focus on encouraging excellence and responsibility rather than discipline, and on good behaviour rather than banking competence;
- work with the industry and its stakeholders to set out high-level principles of excellence and responsibility.

16 Although not originally recommended by the Lambert Review, one of the related issues under discussion is whether individual bankers – like doctors – should be asked to take a Hippocratic oath and whether a chartered institute should be set up to promote it: eg "It is my first duty to provide an exemplary quality of service to my customers and to exhibit a duty of care above and beyond what is required by law." This raises questions, not only about how an oath of this kind should be worded, but also about to whom the oath would apply, how it would be enforced, how effective it would be, what message it would send to the public and how the public would interpret it.

17 Second, the Fair and Effective Wholesale Financial Markets Review, jointly led by HM Treasury, the Bank of England and the FCA, is designed to ensure that financial institutions operate to the highest standards on the basis that this is essential in building a resilient economy and maintaining London as a successful international financial centre. The objectives of the Fair and Effective Review are:

- to reinforce confidence in the fairness and effectiveness of wholesale financial market activity conducted in the UK; and
- to influence the international debate on trading practices, including highlighting issues that can only be addressed through coordinated international action.

18 The Fair and Effective Review is expected to concentrate on fixed income, currency and commodity markets and to make recommendations by June 2015 on:

- principles to govern the operation of fair and effective financial markets (taking account of existing rules and principles);
- reforms to ensure that standards of behaviour within those markets are in accordance with those principles;
- tools to strengthen the oversight of market conduct within both regulated and unregulated markets;
- the question of whether the regulatory perimeter for wholesale financial markets should be extended, taking into account extensions of the perimeter under forthcoming European legislation, and whether international action is necessary to make such extensions work; and
- additional reforms, over and above those already in train in relation to benchmarks, to strengthen the infrastructure which supports these markets.

19 Third, in parallel, the FCA is conducting a Wholesale Sector Competition Review, focusing on competition in wholesale securities and

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The underlying rationale is to put the UK at the forefront of the global debate on how best to raise standards of good market practice within the new regulatory framework.

investment markets, including: markets and market infrastructure; investment banking; asset management; and corporate banking. The Competition Review will be concerned with features of a market or with behaviour which could inhibit or distort competition in the market. It is exploratory and aims to highlight where competition may be weak or not be working properly in the market. Arrangements are being put in place to prevent overlap between the Competition Review and the Fair and Effective Review, which will focus on trading practice.

20 In the case of both the Fair and Effective Review and the Competition Review, there will be input from market practitioners:

- In the first case, the intention is that its recommendations should primarily be for the financial services industry to deliver rather than regulators: eg by ensuring that financial market business done is transparent, fair to clients and consistent with market integrity. The Fair and Effective Review has set up an independent Market Practitioner Panel, led by a Steering Committee of senior industry leaders – representing sell-side and buy-side firms, market infrastructure providers and major corporate users of financial markets – and a series of Expert Groups, coupled with a market consultation, to help do this.
- In the second case, stakeholders have been invited to provide input to the Competition Review.

21 In the case of all three reviews, the underlying rationale is to put the UK at the forefront of the global debate on how best to raise standards of good market practice within the new regulatory framework. The underlying assumption is that good market practice should be seen as a source of competitive advantage for successful firms in the long run, even if it involves short-term costs; and that a reputation for integrity makes a financial centre more competitive in the long run. So the test will be whether London succeeds in doing this, and how far it is followed by other financial centres elsewhere. That may depend on whether steps to raise standards and improve competitiveness are seen as going hand in hand.

(iv) Role of trade associations

22 Trade associations and self-regulatory organisations like ICMA already contribute to the work of raising standards – both in London and in other financial centres – and can continue to do so in a number of ways:

- first of all, by working with regulators to ensure that mandatory new regulations help to raise standards and do not undermine them as a result of unintended consequences;
- second, by promoting voluntary standards of good market practice consistent with the regulatory framework and in compliance with competition law, as ICMA does in the international capital markets;
- third, by acting as a sounding board for central banks and regulators with experts in the international capital markets;
- fourth, by undertaking education and training courses to raise professional standards, as ICMA does, particularly through its work with the ICMA Centre; and
- finally, by supporting work in raising standards by other bodies: eg ICMA supports the Financial Reporting Council’s work on good corporate governance.

23 The UK FCA and PRA say in their July Consultation Paper: “Through the setting and monitoring of voluntary standards of good practice, the industry may seek to attain higher standards than the minimum requirements imposed by the regulators.”

Conclusion

24 Public trust in the financial system was seriously damaged by the international financial crisis in a short period of time. It will take a long time fully to restore. Effective regulation is a necessary condition. But public trust cannot be restored through new regulation alone. Voluntary standard setting has an important role to play. Clearly, standards are more likely to be effective if all those involved agree to abide by them.

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Practical initiatives by ICMA

The purpose of the following list is to summarise practical initiatives on which ICMA is currently, or has recently been, engaged with, and on behalf of, members[1]:

Short-term markets

1 A Roundtable on the theme of the ICMA paper on *Collateral is the New Cash: the Systemic Risks of Inhibiting Collateral Fluidity* was held in Paris on 10 June.

2 A team from the ECB made a presentation on the impact of TARGET2 Securities on the repo market to an *ad hoc* meeting of the ICMA European Repo Committee and Operations Group in London on 26 August.

3 ICMA, through its European Repo Council, has prepared a further paper on *Continually Working to Develop Efficient and Effective Collateral Markets*, which was launched in September, alongside the publication of the latest semi-annual ICMA European repo market survey.

4 The move in standard settlement date from T+3 to T+2 for much of the European bond markets with effect from 6 October will have implications for the underlying repo markets, with a shorter financing window for many securities. To highlight and discuss many of the issues arising, ICMA has published an ERC report: *The Impact of T+2 Settlement on the European Repo Market.*

5 On 1 and 2 September, ICMA held a workshop jointly with AFME on ESMA's proposals on mandatory buy-ins under the CSD Regulation. ESMA invited ICMA and ISLA to a bilateral meeting in Paris on 24 September to discuss this issue.

6 The European Repo Council has commissioned Rule Financial to conduct an industry-wide survey to assess market preparedness for, and attitudes towards, TARGET2 Securities. The results of the survey are due to be presented, together with analysis of how cash bond and repo trading will translate into the T2S environment, in early November.

7 An ICMA Working Group has developed GMRA FATCA language for use with the GMRA 2000, GMRA 2011 and the associated Equities Annexes.

Primary markets

8 ICMA responded to questions on primary markets in ESMA's Consultation Paper on MiFID II Level 2 by the deadline of 1 August.

9 ICMA has published joint supplementary observations to the Bank of Italy consultation on *Information Reporting as Contemplated in Article 129 of the TUB relating to the Offer of Financial Instruments in Italy*; and ICMA has also supported a response by the Joint Association Committee on Retail Structured Products to the CONSOB consultation on the distribution of complex products to retail clients.

10 ICMA responded to the ICE consultation on *Benchmark Administration Error Policy* by the deadline of 19 September.

11 With the support of the Green Bond Principles (GBP) Executive Committee, ICMA has been consulting the market on whether changes to the GBP are appropriate. The GBP are intended to encourage transparency, disclosure and integrity in the Green Bond market.

12 The Public Sector Issuer Forum (PSIF) met at the UK DMO in London on 23 June to discuss international market practice and regulatory issues; and the PSIF is planning to meet again in Washington on 9 October.

13 The standard collective action clause in ICMA's Primary Market Handbook has been revised, and a new *pari passu* clause has been added.

14 The overall review and revision of the ICMA Primary Market Handbook is nearing completion.

Secondary markets

15 ICMA responded to questions on secondary markets in both ESMA's Consultation Paper and Discussion Paper on MiFID II Level 2 by the deadline of 1 August, keeping other trade associations informed.

16 Following ICMA's statement on 20 May, and consistent with the CSDR, the standard settlement cycle set out in the ICMA Secondary Market Rules & Recommendations changed from T+3 to T+2 (ie trade date plus two business days) unless otherwise agreed, with effect from 6 October, to allow for the orderly trading of all fixed income securities traded under ICMA rules.

17 ICMA is conducting a study on the secondary market for corporate bonds in Europe, focusing mainly on issues related to reduced market liquidity and the potential challenges and opportunities this presents. The study is largely qualitative and is based on interviews with a range of market participants, including sell side, buy side, intermediaries and other liquidity providers, as well as issuers. ICMA plans to publish the findings this autumn.

Asset management

18 A new report commissioned by ICMA's Covered Bond Investor Council (CBIC) – *Covered Bond Pool Transparency: the Next Stage for Investors* – reviews progress in the attempt to improve and standardise disclosure of cover pool data for covered bonds in certain national markets in Europe and makes recommendations on future measures.

19 The CBIC responded to ESMA's Consultation Paper launched on 11 July on the clearing obligation under the European Market Infrastructure Regulation.

20 The ICMA Asset Management and Investors Council (AMIC) responded on 5 September to the IOSCO consultation on good practice in asset management in reducing reliance on Credit Rating Agencies.

21 Following the AMIC Executive Committee meeting on 4 September, the AMIC Council will be held on 29 October at Credit Suisse in London with an agenda on investors' contribution to relaunching growth in the current EU economic and regulatory environment.

22 The Pan-European Private Placement Working Group, set up in early 2014 and led by ICMA, is developing a guide to best practice to facilitate common market practice, principles and standardised documentation for the emerging pan-European private placement market.

23 The ICMA Bail-In Working Group has responded to the UK Financial Policy Committee's Review of the Leverage Ratio.

24 The AMIC Executive Committee has decided to establish a new Securitisation Working Group on the buy side.

Other meetings with central banks and regulators

25 Martin Scheck continues to participate in the ECB's Bond Market Contact Group, and René Karsenti to participate in the ESMA Securities and Markets Stakeholders Group. The mandate of Godfried De Vidts on the ESMA Secondary Market Working Group has been renewed.

26 During the ICMA Regulatory Policy Committee in Milan on 10 September, members held a discussion with Giuseppe Vegas, Chairman of CONSOB, and with David Wright, Secretary General of IOSCO.

27 A joint AFME/ICMA Roundtable on *Capital Markets and Growth* was held in the European Parliament on the evening of 30 September for representatives of the AFME and ICMA's Boards with several MEPs from the European Parliament's ECON Committee and officials.

28 Together with the Chairs of key Market Practice and Regulatory Policy Committees, ICMA visited the European Central Bank on 6 October for discussions.

1. ICMA responses to consultations by regulators are available on the ICMA website.

Sovereign debt restructuring, redesigned

by Leland Goss

At the end of August 2014, following two consultations with its members, ICMA published the final version of its sovereign bond contract reforms. The consultations collected comments and contributions from a broad range of investors, intermediaries, sovereign issuers, the IMF and other multilateral and governmental organisations, as well as other trade associations that included a major role by, and close collaboration with, the Institute of International Finance.

The new collective action provisions allow a crisis stricken government to restructure its bonds using three alternative procedures:

- First, it could restructure using the existing series-by-series, non-aggregated approach common in most emerging market bonds today.
- Second, it could restructure using a two-limb aggregated voting procedure, similar to the existing euro-area model CAC.
- Third, it could restructure using a single limb aggregated voting procedure, providing the most effective means to counter holdout creditors.

In addition, ICMA has proposed a new *pari passu* provision to preclude courts from ordering debtors to pay holdout creditors whenever they pay restructured creditors.

The response to these new measures in the press and from commentators has been significant and encouraging. In September, the G20 issued a communiqué that included a positive reference to the ICMA measures and upcoming IMF board discussions in this area. The IMF Executive Board this month has considered the IMF staff's recommendations and paper on sovereign bond contract reforms and is supportive of a market-oriented, contract-based approach to sovereign debt restructurings.

Going forward, the focus of market participants, sovereign borrowers and counsel is very much on implementation. Several government bond issues this month have already moved to adopt these new measures. It is hoped that others will soon follow their lead and embrace the new financial architecture. It is in their interests to do so.

Further reading:

1. ICMA model standard CACs and new *pari passu* provision.
2. The Peterson Institute for International Economics has published a useful article in regard to the ICMA sovereign debt contract reforms, entitled *A Sensible Step to Mitigate Sovereign Bond Dysfunction* by Anna Gelpern on 29 August 2014.
3. Article addressing the resistance to changing boilerplate language in bond contracts *NML v Argentina: The Borrower, the Banker and the Lawyer – Contract Reform at a Snail's Pace*, by Leland Goss, 12 May 2014.

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Regulatory Response to the Crisis

by David Hiscock

G20 financial regulatory reforms

In 2013, the Financial Stability Institute (FSI) conducted a first annual survey to ascertain the status/plans regarding the implementation of Basel II, 2.5 and III in jurisdictions that are members of neither the BCBS nor the EU. In line with the 2013 approach, on 24 July 2014, the FSI published the results of its 2014 survey by disclosing the information received from 90 non-BCBS/non-EU jurisdictions.

On 11 September 2014, the BCBS published the results of its latest Basel III monitoring exercise, based on data as of 31 December 2013. A total of 227 banks participated in the current study, comprising 102 large internationally active (Group 1) banks and 125 Group 2 banks. At the Common Equity Tier 1 (CET1) target level of 7.0% (plus the surcharges on G-SIBs as applicable), the aggregate shortfall for Group 1 banks is €15.1 billion (versus €57.5 billion on 30 June 2013); and the capital shortfall for Group 2 banks is estimated at €2.0 billion (for the CET1 minimum of 4.5%). The weighted average LCR for the Group 1 banks was 119% (up from 114% six months earlier), whilst for Group 2 banks, the average LCR remained unchanged at 132%. Finally, the average NSFR was 111% for the Group 1 bank sample and 112% for Group 2 banks.

The FSB published the 15 September 2014 letter from its Chairman, Mark Carney, to the G20 Finance Ministers and Central Bank Governors, which is headed *Financial Reforms – Completing the Job and Looking Ahead*. In advance of the Brisbane Summit, which will mark the end of this phase of global financial reform, this letter reports on progress. It makes four points:

- During the Australian G20 Presidency, work remains on track to substantially complete the job of fixing the fault lines that underlay the crisis.
- The support of Ministers and Governors is essential to meet the target of ending too big to fail for the Brisbane Summit.
- We are building a system that combines common international standards, consistent implementation and where appropriate deferral to each other's approaches.
- As we move toward the conclusion of this phase of financial reform, the FSB will adjust focus, away from the design of standards to fix the fault lines that caused the crisis and towards new and constantly evolving risks and vulnerabilities.

On 16 September 2014, the FSB published a note describing its monitoring work during the past year in respect of financial regulatory factors affecting the supply of long-term (LT) investment finance – which has consisted of a survey of FSB members; continued engagement with practitioners in LT finance from the private sector; consultation with FSB Regional Consultative Groups; and work by the FSB Secretariat together with the staff of the IMF, World Bank and OECD to develop a set of key quantitative indicators that summarise the main developments in the provision of LT finance.

The FSB's monitoring continues to find little tangible evidence or data to suggest that global financial regulatory reforms have had adverse consequences on the provision of LT finance. Nevertheless, with most regulatory reforms still at an early stage of implementation, it remains too early to fully assess their impact on the provision of LT finance or changes in market behaviour in response to these reforms, so the regulatory community will remain vigilant. Going forward, the FSB will continue to monitor impacts, including to identify any potential financial regulatory impediments to the promotion of market-based financing, to the development of new instruments to finance LT investment, or to the supply of LT financing by either domestic or foreign intermediaries.

An 18 September 2014 press release reports that, at its meeting in Cairns, the FSB discussed vulnerabilities affecting the global financial system and reviewed work plans for completing core financial reforms. Concerning vulnerabilities in the financial system the FSB notes that the core of the financial system continues to strengthen, with overall improvements in bank capital and liquidity. However, there are increasing signs of complacency about risks in financial markets, in part reflecting a search for yield amidst exceptionally accommodative monetary policies; whilst volatility in asset prices has become compressed and asset valuations stretched across a growing number of markets, increasing the risk of a sharp reversal. Furthermore, while market forces and regulatory reforms since the crisis have reduced leverage in the banking system, leverage has picked up in other parts of the financial system, including in corporate debt markets; responsive to which, authorities are stepping up their monitoring of the migration of risks to less regulated parts of the financial system. There are also concerns about the mispricing of liquidity risks; and pressures on market liquidity could exacerbate downward price dynamics and market dislocations during a price fall.

In relation to policy work, the FSB discussed progress towards the goal of substantially completing the key post-crisis financial reforms in 2014, including:

- *Ending too-big-to-fail:* The FSB made further substantial progress in defining the terms and conditions of total loss absorbing capacity for G-SIBs and in finding solutions to remaining obstacles to cross-border resolution.
- *Shadow banking:* The FSB reviewed progress in meeting the deliverables in the shadow banking roadmap agreed at the G20 Summit in St Petersburg in 2013, and will present an updated roadmap in time for the Brisbane Summit; also took note of the preliminary results of an initial information-sharing exercise among jurisdictions on their application of the FSB's high-level policy framework for shadow banking entities – the FSB will launch a peer review on the national implementation of the high-level policy framework in 2015.
- *Making derivatives markets safer*: The Plenary discussed progress in resolving the remaining cross-border issues that have arisen in the implementation of OTC derivatives reforms. Members emphasised the importance of authorities moving quickly to address issues to ensure that the benefits to global financial stability of these reforms are achieved; and welcomed the letter from the OTC Derivatives Regulators Group to the FSB Chair on legal barriers to reporting to trade repositories, and stressed the importance of rapid action by jurisdictions to remove those barriers; and discussed the results of an FSB survey on members' ability to defer to each other's OTC derivatives market regulatory regimes in cross-border contexts. Furthermore, the FSB has conducted a feasibility study on approaches to global aggregation of OTC derivatives data and has published the report and recommendations.
- *Foreign exchange benchmark reform:* Members approved the finalised recommendations for reforms to foreign exchange benchmark practices, which take into account the responses to the public consultation in August. The report was published on 30 September 2014.

Following the meeting of G20 Finance Ministers and Central Bank Governors, in Cairns on 20-21 September 2014, a communiqué was issued (and supporting documents were made available). Much of this communiqué focuses on the importance of economic growth and investment. Amongst other points it is stated that:

- We are mindful of the potential for a build-up of excessive risk in financial markets, particularly in an environment of low interest rates and low asset price volatility. We will monitor these risks and continue to strengthen macroeconomic, structural, and financial policy frameworks, and other complementary measures, as the best response to managing risks, and meet our G20 exchange rate commitments.

> Work remains on track to substantially complete the job of fixing the fault lines that underlay the crisis.

> We encourage jurisdictions to defer to each other when it is justified.

- We will seek to support quality public and private investment, including by optimising the use of the public balance sheet while maintaining appropriate risk controls. We have agreed on a set of voluntary Leading Practices to promote and prioritise quality investment, particularly in infrastructure, and will develop effective approaches for their implementation, including through model documentation. Furthermore, work is currently underway to improve the transparency and functioning of securitisation markets which will promote financing, including for SMEs.
- We have delivered key aspects of the core commitments we made in the wake of the financial crisis in 2008 to build a stronger and more resilient financial system which underpins growth in the global economy. For the Brisbane Summit, work is under way on a plan that will increase consistency in banks' application of the strengthened Basel III rules on capital. We welcome the substantial progress made to date in defining the terms and conditions of a proposal for addressing the too-big-to-fail issue through additional loss absorbing capacity that would further protect taxpayers if these banks fail. We welcome the FSB's statement that it will be in a position to deliver a proposal in time for the Brisbane Summit. The FSB will deliver the remaining core elements of its shadow banking framework and will update the Roadmap agreed in 2013 to support continued monitoring and actions to address potential systemic risks in this area. Our reforms to the OTC derivatives market will reduce systemic risks and increase transparency. We call on regulatory authorities to make further concrete progress in implementing these OTC derivatives reforms as agreed. We encourage jurisdictions to defer to each other when it is justified, in line with the St Petersburg Declaration.
- We welcome the FSB's plans, commencing in 2015, to prepare a consolidated annual report on the implementation of the reforms and their effects. We also welcome the FSB and international standard setting bodies' plans to publish in 2015 information summarising their respective processes for policy development and implementation reviews.
- We welcome the significant progress achieved towards the completion of our two-year G20/OECD Base Erosion and Profit Shifting (BEPS) Action Plan and commit to finalising all action items in 2015. We will begin exchanging information automatically between each other and with other countries by 2017 or end-2018, subject to the completion of necessary legislative procedures.

The communiqué goes on to outline "Issues for further action", including:

- We look forward to the final report of the BCBS-IOSCO Task Force on Securitisation Markets which aims to identify the factors that may be hindering the development of sustainable securitisation markets.
- We look forward to a report in the second half of 2015 from the IMF and FSB on the Data Gaps Initiative highlighting the progress made and including a proposal for a second phase of the initiative.
- We look forward to the FSB's second consultative document jointly prepared with IOSCO on the proposed assessment methodologies for non-

bank non-insurer global systemically important financial institutions around the end of 2014.

- We look forward to upcoming discussions around the ICMA's proposal on possible means to reinforce collective action clauses in sovereign bonds, given the challenges litigation poses to the predictable and orderly resolution of sovereign debt restructuring processes. This proposal and related issues will be discussed at the IMF.
- We look forward to the report from the Global Forum on Transparency and the Exchange of Information for Tax Purposes to G20 Leaders in November
- We ask the OECD to work with all G20 members to propose possible tougher incentives and implementation processes, to deal with those countries which fail to respect Global Forum standards on exchange of tax information on request.

On 23 September 2014, the FSB published its Fifth Implementation Progress Report of the G20 Data Gaps Initiative (DGI), which highlights the progress since the start of the DGI in 2009, provides benchmarks to determine when to call each recommendation complete, and outlines a future work plan. Key messages of the report include that significant progress has been made in implementing the DGI recommendations during the past five years but further work is needed and is critical to reaping the full benefits of the work undertaken to date. Most of the conceptual work has been completed and enhancements of datasets are being made by all G20 economies but at diverse rates of progress, primarily reflecting their varying levels of sophistication of statistical systems. Based on the agreed implementation targets, it is feasible to envisage substantive completion of the DGI by end-2015 provided that there is continued cooperation at the national and international level, and statistical activities are appropriately resourced. A second phase of the DGI could start in

IOSCO

In his introductory comments at the IOSCO Board Meeting with Stakeholders in Madrid, on 1 July 2014, Greg Medcraft, Chair of the IOSCO Board, (i) emphasised the key role markets and the regulation of markets play in supporting economic growth; (ii) outlined IOSCO's work in the last year in supporting these roles; and (iii) set out what he sees as IOSCO's key priorities in the coming year.

In respect of the first of these points he observed that regulators are tasked with creating the regulatory environment that enables markets to provide the funding required for economic growth; and that they do this by working to ensure markets are sufficiently fair, efficient and transparent, thereby allowing investors to be confident and informed when deciding whether to invest. He also noted that there has been a shift in policy focus at a global level over the last twelve months, from restoring the resilience and stability of the financial system to a focus on economic growth.

Concerning the second of his points, he focused on four areas: (i) IOSCO's work on emerging risks; (ii) IOSCO's policy development work; (iii) IOSCO's capacity building initiatives for its growth and emerging markets members; and (iv) the organisation of IOSCO. In the first of these areas he highlighted that IOSCO's focus is on understanding risks that threaten the effectiveness of markets in supporting economic growth, noting the Emerging Risk Roundtables which are now part of IOSCO's Board and Regional Committee meetings; and that these roundtables have discussed cyber-risks and cyber-resilience; the role of behavioural psychology in regulation; the opportunities and threats of social media; the issues faced by growth and emerging economies; and, most recently, corporate governance.

In the second of these areas he commented that particular achievements have been IOSCO's *Principles for Financial Benchmarks*, published in July 2013; work on *Margin Requirements for Non-Centrally Cleared Derivatives*, published in September 2013; and *Report on Regulation of Retail Structured Products*, published in December 2013. Other important projects in which IOSCO is engaged include setting risk mitigation standards for non-centrally cleared derivatives; assessing the implementation of IOSCO's recommendations on securitisation and MMFs; and developing methodologies to identify and regulate SIFI's in IOSCO's regulatory space. He then went on to touch on five topics on IOSCO's current agenda that highlight its role in enabling markets to fund economic growth (i) corporate governance; (ii) improving audit quality; (iii) "long-term finance"; (iv) cyber-resilience; and (v) cross-border regulation.

Finally, regarding the last of his three main points, he stated that his priority as Chairman will be to ensure that IOSCO pays particular attention to three areas which each reflect the significance of markets in driving economic growth: (i) developing appropriate responses to emerging risks which threaten the role markets play in driving economic growth; (ii) delivering policy which guides IOSCO's members in developing regulatory environments and frameworks to enable markets to support economic growth; and (iii) continuing to support IOSCO's growth and emerging markets through a sustainable capacity building programme.

"

The ESAs have overall performed well during their first three years of operations.

2016 to strengthen and consolidate the progress to date and promote the regular flow of comparable and high-quality data across the G20 economies. The specifics of a second phase of the DGI including a revised mandate would be discussed with G20 economies as part of the 2015 work plan; and new data requests could also be added in the second phase, as needs arise from the user community, to ensure that the data collected are relevant for analytical and policy needs.

On a related theme, the FSB also published an 11 September 2014 letter to the G20 Finance Ministers and Central Bank Governors, reporting on the progress of work to address data gaps involving foreign currency exposures.

As reported in a 25 September 2014 press release, banking supervisors and central bankers representing more than 100 jurisdictions met in Tianjin, China, to discuss a range of policy measures relating to the BCBS's post-crisis reform agenda. Participants also discussed the role of banking systems in promoting growth and making financial services safe so that they could support the real economy. Significant points commented upon include:

- *Dealing with G-SIBs:* The BCBS reviewed an updated list of G-SIBs based on end-2013 data, which the BCBS and the FSB will publish in the coming weeks. The applicable higher loss absorbency requirement for G-SIBs will be phased in from the start of 2016 and will be fully implemented from the start of 2019.
- *Endorsement of the NSFR:* The BCBS endorsed the final details of Basel III's NSFR. The final standard will be released in the coming weeks and will take effect at the start of 2018.
- *Finalising securitisation standards:* The BCBS reviewed progress towards finalising revisions to the Basel framework's securitisation standard and agreed the remaining significant policy details that will be published by year-end 2014. It also recognised work that is being conducted jointly by the BCBS and IOSCO to review securitisation markets – the BCBS looks forward to the development of criteria that could help identify, and assist the financial industry's development of, simple and transparent securitisation structures. In 2015, the BCBS will consider how to incorporate the criteria, once finalised, into the securitisation capital framework.
- *Improving consistency in bank capital ratios:* The BCBS, which has been closely examining banks' risk weighting practices, discussed a range of policy and supervisory actions that it has initiated to address the issue of excessive variability of risk-weighted assets. These actions include a review of the standardised approaches (ie the non-internal model-based approaches), the introduction of capital floors, greater restrictions on modelling parameters and assumptions, and improved disclosure. The BCBS will elaborate on these measures in its report to the November 2014 G20 Summit.

On 29 September 2014, the FSB launched a public consultation (for comment by 1 December 2014) on a set of proposals to achieve the cross-border recognition of resolution actions and remove impediments to the cross-border resolution. The consultative document proposes a set of policy measures and guidance consisting of:

(i) elements that jurisdictions should consider including in their statutory cross-border recognition frameworks to facilitate effective cross-border resolution as required by the FSB *Key Attributes of Effective Resolution Regimes for Financial Institutions*; and

(ii) contractual approaches to cross-border recognition that focus on two particular cases where achieving cross-border recognition is a critical prerequisite for orderly resolution: temporary restrictions or stays on early termination and cross-default rights in financial contracts; and the "bail-in" of debt instruments that are governed by the laws of a jurisdiction other than that of the issuing entity.

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European financial regulatory reforms

On 7 July 2014, ECON met to hold its constitutive meeting following the election of its members by the European Parliament on 3 July. The new Chair of ECON is Roberto Gualtieri (S&D, IT). Two Vice-Chairs, Markus Ferber (EPP, DE) and Peter Simon (S&D, DE), were elected; and subsequently, on 14 July, in Strasbourg, the two further ECON Vice-Chair positions were taken by Marianne Thyssen (EPP, BE) and Johan van Overtveldt (ECR, BE). The Committee is larger than previously, increasing from 50 to 61 members; and the political composition of the Committee is EPP 18; S&D 16; ECR 6; ALDE 5; GUE/NGL 4; Greens/EFA 4; EFDD 4; and non-attached 4.

On 8 July, participants from the US and the EU held a meeting of their Financial Markets Regulatory Dialogue (FMRD). Officials held productive discussions on their respective reforms, including those reforms implementing key commitments by the G20 leaders such as the implementation of Basel III capital, leverage, and liquidity rules; the implementation of OTC derivatives reforms (including a discussion of related cross-border issues); and the orderly resolution of global banks. The officials also discussed insurance, MMFs, alternative investment fund managers, securitisation, HFT, benchmarks and other matters. The next FMRD meeting is set for January 2015.

On 8 August 2014, the European Commission adopted the review reports on the European System of Financial Supervision (ESFS), consisting of a report on the operation of the three ESAs (EBA, EIOPA and ESMA) and a report on the mission and organisation of the ESRB. These two reports set out the findings of a review of the functioning of the new supervisory architecture, which was put in place in 2011 as part of the comprehensive reforms in response to the financial crisis. The Commission has assessed in detail the functioning of the ESAs and the ESRB, covering the period from their inception to December 2013. The reports will be forwarded to the European Parliament and to the Council for their consideration; and the Commission will carry out additional work on the matters identified in the report as warranting further attention.

Main findings of the review of the three ESAs: The review shows that the ESAs have overall performed well during their first three years of operations. They have successfully built functioning organisations, started delivering on their mandates and developed their own profiles. Notably by preparing uniform standards and contributing to supervisory convergence and coordination, the ESAs have successfully contributed to shaping the development of a Single Rulebook applicable to all 28 EU Member States and thus to the good functioning of the Single Market. Nevertheless, the ESAs report identifies several areas for

Italian Presidency

Europe: a Fresh Start is the Programme of the Italian Presidency of the Council of the European Union. The section concerning Economic and Financial Affairs includes the following paragraphs regarding Banking Union: "The Presidency will oversee all the necessary arrangements for a successful start-up of the Single Supervisory Mechanism, due to take place in November 2014; it will be looking closely at the process of establishing the Single Resolution Board, which could start as soon as the Single Resolution Mechanism Regulation is published, as well as the process of ratification of the related Intergovernmental Agreement by the participating Member States. In particular, the Presidency will steer the Council's oversight of and communications relating to the finalisation of the agreed comprehensive Balance Sheet Assessment, composed of Asset Quality Reviews and Stress Tests by the European Central Bank, and the national and European follow-up actions, with due regard for financial stability considerations."

The Programme then includes the following paragraphs in relation to *Strengthening the Regulation of Financial Markets:* "The Presidency will continue to work towards strengthening the regulation of financial markets, with a view to facilitating credit flows to the real economy and maintaining confidence in the sound and efficient functioning of financial markets and intermediaries. Financial market integrity, including the prevention of the misuse of the financial system for illicit purposes, will remain a priority.

As set forth in the Commission Communication on the Long-term Financing of the European Economy, Italy expects to contribute to the modernisation of the framework for long-term investors, such as insurance companies, pension funds and other long-term vehicles. In this connection, the Italian Presidency will closely follow the implementing measures aimed at completing the Solvency II framework as regards the insurance sector, with due attention also being given to pension funds through a revision of the Institutions for Occupational Retirement Provision (IORP) Directive. The Italian Presidency will aim at finalizing the legislation concerning the creation of a new category of pooled funds, the "European Long Term Investment Funds".

Furthermore, the Presidency will seek agreement within the Council on possible improvements to the functioning of the European System of Financial Supervision following the review of the first few years of its activities.

The Italian Presidency will endeavour to make further progress on the Regulation proposed by the Commission aimed at restoring confidence in benchmarks, the integrity of which is critical in view of their widespread use as a point of reference in contracts and financial instruments.

In the banking sector, the Presidency will follow on from the Commission proposals to introduce structural measures to reduce the interconnectedness of extremely large banking groups with a view to improving prudential safeguards and reducing the possibility of using public funds in the event that a resolution process becomes necessary. Also the accompanying measures aimed at increasing reporting and disclosure of securities financing transactions in the shadow banking sector will be addressed. Finally, in the quest to subject "shadow banking" activities to proper supervision, the Italian Presidency will address the Commission proposal for the Regulation of money market funds."

Furthermore, from 1 July 2014 to 31 December 2015 the Trio Presidency will be made up of Italy, Latvia and Luxemburg and the new Trio Programme is also available.

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ESAs should give a higher profile to issues related to consumer/investor protection, and strengthen the focus on supervisory convergence.

improvement which can be implemented by the ESAs and the Commission in the short term and would not require legislative action. In particular, the ESAs should give a higher profile to issues related to consumer/investor protection, and strengthen the focus on supervisory convergence, amongst other things by making better use of peer reviews. For the longer term, there could also be a need to further consider other issues which would imply changes to the legislative framework for the ESAs. Any such future steps would also have to take into account the functioning of the Banking Union which is currently being established. Areas for consideration in the longer term would include (i) the governance of the ESAs, in particular to further improve the capacity of the Board of Supervisors to take decisions in the interest of the EU as a whole; and (ii) a revision of the existing funding arrangements so that the ESAs could fulfil their broad range of tasks, taking into account the EU and national budgetary constraints.

Main findings of the review of the ESRB: The review shows that, thanks to its reliance on a unique and wide range of expertise, the ESRB was a crucial driver behind introducing a macroprudential dimension of financial policies. The ESRB has progressed well on the development of the analytical work, notably on interconnectedness. Nevertheless, the review also reveals that certain improvements to the ESRB framework in the short and medium term could enhance the efficiency of macroprudential oversight at EU level. Some improvements could be implemented in the short term by the ESRB itself and would not require legislative action, such as a more proactive communication strategy and further expansion of the ESRB's focus beyond banking risks. At the same time, some issues identified as warranting further attention concern the ESRB's Founding Regulations. The Commission intends to further examine the technical and legal aspects and to assess possible options for addressing these issues, in particular (i) the ESRB's organisational identity with a view to enhancing its visibility and autonomy, while allowing it to continue to benefit from the ECB's reputation and expertise; (ii) the internal governance of the ESRB, in particular to streamline decision-making arrangements involving the General Board and the Steering Committee; and (iii) an expansion of the ESRB's toolbox so that it exercises more "soft power" to enhance flexibility and foster early intervention. This work will have to take into account elements of the overall financial architecture which are not yet fully in place today, such as the various pillars of the Banking Union, national macroprudential authorities and the attribution of macroprudential responsibilities within the SSM.

On 10 September 2014, the new European Commission President, Jean-Claude Juncker, unveiled his team and the new shape of the incoming European Commission, streamlined to focus on tackling the big political challenges Europe is facing. Included amongst the "important novelties" outlined in the announcement are:

- A First Vice-President (Frans Timmermans) who will be the right hand of the President – this is the first time that there is a Commissioner dedicated to a Better Regulation agenda, guaranteeing that every Commission proposal is truly required and that the aims cannot best be achieved by Member States;
- The new Economic and Financial Affairs, Taxation and Customs portfolio (under Pierre Moscovici) will ensure that taxation and customs union policies become part and parcel of a deep and genuine Economic and Monetary Union and contribute to the smooth functioning of the overall economic governance framework of the EU; and
- The new Financial Stability, Financial Services and Capital Markets Union portfolio (under Jonathan Hill) will focus the existing expertise and responsibility in one place, a newly created Directorate-General, and ensure the Commission remains active and vigilant in implementing the new supervisory and resolution rules for banks (see box for further details).

On 11 September 2014, the EBA published its sixth report of the Basel III monitoring exercise on the European banking system – run in parallel with the BCBS at a global level, to gather aggregate results (using data as of December 2013) on capital, liquidity (LCR and NSFR) and leverage ratios for a group of 151 banks (including 42 Group 1) in the EU, whilst the shortfall for Group 1 banks due to the implementation of the leverage provisions would be €22.1 billion. Results show that the Group 1 banks would face a CET1 capital shortfall of €0.1bn to achieve the minimum requirement of 4.5%, and of €11.6 billion to reach the target level of 7.0% or the higher threshold set for G-SIBs. As for the LCR, the exercise reveals a shortfall of liquid assets of €124.5 billion for Group 1 banks. Finally, the NSFR figures show that the total need (across 130 banks) for more stable funding would amount to €473 billion, approximately 2% of banks' total assets.

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Financial Stability, Financial Services and Capital Markets Union

The 10 September 2014 Mission Letter sent by Jean-Claude Juncker, President of the European Commission, to Jonathan Hill, the new Commissioner for Financial Stability, Financial Services and Capital Markets Union, sets out what the President expects from Commissioner Hill as a Member of the Commission as well as specific goals which he will be responsible for reaching during this new Commission's mandate.

It is stated that the Commission as a whole must work together as a strong team, cooperating across portfolios to produce integrated, well-grounded and well-explained initiatives that lead to clear results. The intention is to overcome silo mentalities by working jointly on those areas where the Commission can really make a difference – not seeking to do everything, but rather being bigger and more ambitious on big things, and smaller and more modest on small things. There should also be a focusing of energy and efforts on ensuring effective implementation and follow-up on the ground. Respect for the principles of subsidiarity, proportionality and better regulation will be at the core of the work of the new Commission, which will concentrate its efforts on those areas where only joint action at European level can deliver the desired results; and when the Commission acts, it is always to look for the most efficient and least burdensome approach.

In charge of a new Directorate-General for Financial Stability, Financial Services and Capital Markets Union, Commissioner Hill is to focus on the following goals:

- "Contributing, as part of the project team steered and coordinated by the Vice-President for Jobs, Growth, Investment and Competitiveness, to the jobs, growth and investment package to be presented within the first three months of our mandate, by outlining measures to improve the investment environment and presenting concrete initiatives on the long-term financing of the economy. This will include seeking appropriate ways to revive sustainable and high quality securitisation markets, to reduce the cost of raising capital in the Union and to develop alternatives to our companies' dependence on bank funding.
- Continuing to put in place a regulatory framework which ensures the resilience and stability of the financial services sector. Financial markets and institutions should be appropriately regulated and supervised with, where relevant, appropriate crisis management tools.
- Ensuring that the financial services regulatory framework takes into account the needs and interests of consumers and retail investors and proposing any necessary measures to make financial services work better for citizens.
- Ensuring timely and effective implementation of the financial services regulatory reform agenda, including the accompanying delegated/implementing acts. All necessary arrangements for the Banking Union should be made so that the Single Resolution Board is set up and operational on time.
- Reviewing the functioning and the operation of the ESRB and the three ESAs, including their interaction with the SSM and the SRM. Particular attention should be paid to reviewing the governance and the financing of these Agencies. On the latter, you should find a way to eliminate EU and national budgetary contributions to the ESAs which should be wholly financed by the sectors they supervise.
- Bringing about a well-regulated and integrated Capital Markets Union, encompassing all Member States, by 2019, with a view to maximising the benefits of capital markets and non-bank financial institutions for the real economy.
- Contributing, as part of the project team steered and coordinated by the Vice-President for the Digital Single Market, to ensure the safety and the modernisation of the Union's regulatory framework on digital/electronic payments in order to facilitate online purchases. The safety and appropriateness of certain virtual currencies should also be assessed and, where appropriate, relevant policy measures should be proposed."

Credit Rating Agencies

On 16 July 2014, ESMA launched a consultation (for comment by 31 October 2014) on new supervisory guidelines regarding the information that is periodically submitted to ESMA by Credit Rating Agencies (CRAs). Good quality, relevant, timely data are key to the efficient and effective supervision of the CRA sector and the aim of this consultation paper is to ensure that the information that CRAs are requested to submit supports ESMA's supervisory work in identifying the key risks in the sector. An open hearing on these issues will be held on 15 October.

On 18 July 2014, ESMA published new technical advice to the European Commission. In this technical advice, ESMA identifies several key points concerning the appropriateness of the development of a European creditworthiness assessment of sovereign debt, namely, the independence of the rating process; the review function of rating methodologies; the confidentiality of all rating sensitive information; as well as the need to have sufficient resources to ensure the continuity and the quality of the rating process. The European Commission is expected to submit a report to the European Parliament and to the Council by 31 December.

On 5 August 2014, ESMA submitted a report outlining its staffing and resources needs in relation to its responsibility for supervising CRAs in the EU. The report provides an overview of the tasks ESMA carries out in relation to the supervision of CRAs; identifies the new tasks and responsibilities resulting from the entry into force of the CRA3 Regulation; and sets out staffing and budget needs. It is expected that there will be a small growth in staff numbers in 2015 and 2016 to deal with the additional responsibilities under the CRA3 Regulation.

On 22 August 2014, ESMA published its opinion on how national competent authorities should apply the modifications to the CESR guidelines on MMFs, set out in the report on *Mechanistic Reference to Credit Ratings in the ESA's Guidelines and Recommendations*, when monitoring the application of the CESR guidelines by the relevant financial market participants. The Joint Committee report was published on 6 February 2014, setting out the manner in which the CESR guidelines were to be amended, in particular with respect to the assessment of credit quality of money market instruments by managers of Short-Term MMFs and MMFs.

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OTC (derivatives) regulatory developments

ESMA is maintaining a list of CCPs that have been authorised to offer services and activities in the EU, in accordance with EMIR. ESMA updated the list to include: Keler CCP, on 4 July 2014; CME Clearing Europe Ltd on 4 August; CCP Austria Abwicklungsstelle für Börsengeschäfte GmbH (CCP.A) on 14 August; LME Clear Ltd on 3 September; and BME Clearing on 16 September. There are now 13 CCPs authorised under EMIR (EMIR requires EU-based CCPs to be registered and non-EU CCPs to be recognised in the EU). ESMA is also maintaining the related public register of cleared derivative classes.

ESMA is publishing Questions & Answers regarding the implementation of EMIR, an updated version of which was made available on 10 July 2014.

As reported in Issue 34 of the ICMA Quarterly Report, on 8 May 2014 ESMA sent a letter to the European Commission advancing its intention to ease certain frontloading requirements under the EMIR. In a letter date stamped 8 July, Commissioner Barnier duly responded. In this response it is stated that the Commission is aware of the time constraints to which ESMA is subject and that the Commission is of the view that the frontloading of OTC derivatives should be avoided in cases where it would not ensure the achievement of EMIR's objectives. It is noted that the determination of remaining maturities should not result, in particular,

> IOSCO proposes nine standards aimed at mitigating the risks in the non-centrally cleared OTC derivatives markets.

in the application of the frontloading requirement to OTC derivatives concluded before counterparties could reasonably foresee that those contracts would need to be cleared as a consequence of the frontloading requirement. Thus, the determination of remaining maturities should be carefully assessed and duly motivated on the basis of the goals pursued by EMIR in general, and by the frontloading requirement in particular, taking into account the specificities of the different classes of OTC derivatives and the degree of uncertainty inherent to the different periods mentioned in ESMA's letter of 8 May.

On 11 July 2014, ESMA launched a first round of consultations to prepare for central clearing of OTC derivatives within the EU. The two Consultation Papers seek stakeholders' views on draft RTS for the clearing of IRS (for feedback by 18 August) and CDS (for feedback by 18 September), that ESMA has to develop under EMIR. ESMA is required to draft RTS on the clearing obligation within six months of the authorisation or recognition of CCPs. ESMA has analysed the classes from several CCP notifications and has determined that some IRS and CDS classes should be subject to the clearing obligation. Following the difference in timing of the corresponding CCP authorisations, the IRS and CDS classes are covered in two separate papers and consultation periods. ESMA will use the Consultation Paper feedback to draft its final RTSs on the clearing obligation for IRS and CDS and send them for endorsement to the European Commission. The clearing obligation will take effect following a phased implementation, with the current proposal ranging from six months to three years after the entry into force of the RTS, depending on the types of counterparties concerned.

On 5 August 2014, ESMA issued guidelines and recommendations regarding the implementation of the CPSS-IOSCO *Principles for Financial Market Infrastructures* in respect of CCPs. The subsequent 4 September publication of the translations triggered a two months "comply or explain" period, meaning that the guidelines will become applicable on 4 November 2014.

On 5 August 2014, IOSCO unveiled an information repository for central clearing requirements for OTC derivatives, which provides regulators and market participants with consolidated information on the clearing requirements of different jurisdictions. Established in February 2014, the repository has been available until now only to IOSCO members. IOSCO has since gained sufficient experience, and gathered enough information on central clearing requirements, to open the repository to the public. By providing this reference information, IOSCO seeks to assist authorities in their rule-making and help participants comply with the relevant regulations in the OTC derivatives market. The repository sets out central clearing requirements on a product-by-product level, and any exemptions from them and will be updated quarterly.

On 10 September 2014, the OTC Derivatives Regulators Group (ODRG) issued a report which provides an update to the G20 on further progress in resolving OTC derivatives cross-border implementation issues and identifies a cross-border issue that may call for legislative change. The ODRG provides an update regarding two areas in which it is working to develop approaches to address cross-border issues: (i) potential gaps and duplications in the treatment of branches and affiliates; and (ii) treatment of organized trading platforms and implementation of the G20 trading commitment. The report also addresses four areas in which the ODRG has been working to implement understandings reached previously. The ODRG anticipates that it will submit its next report in preparation for the G20 Leaders Summit in November 2014.

On 17 September 2014, IOSCO published the consultation report *Risk Mitigation Standards for Non-Centrally Cleared OTC Derivatives* (for comment by 17 October 2014), which proposes nine standards aimed at mitigating the risks in the non-centrally cleared OTC derivatives markets. The proposed risk mitigation standards are expected to bring about three main benefits:

- promoting legal certainty and facilitating timely dispute resolution;
- facilitating the management of counterparty credit and other risks; and
- increasing overall financial stability.

The proposed risk mitigation standards, which are developed in consultation with the BCBS and the CPMI, would complement the margin requirements developed by the BCBS and IOSCO in September 2013 in strengthening the non-centrally cleared OTC derivatives market.

To assist authorities' and the market's understanding of the legal capacities and processes jurisdictions have in place, or have proposed, to defer to one another in cross-border contexts, the FSB Chairman wrote to all FSB member jurisdictions on 8 May 2014 asking them to set out their frameworks with regard to OTC derivatives reforms. In particular, the FSB Chairman's letter requested information on frameworks for deference to another jurisdiction's OTC derivatives regulatory requirements applicable to trade repositories (TRs), CCPs and exchanges/

> The FSB supports a multiple-rate approach to the reform of major interest rate benchmarks.

electronic trading platforms (together, "infrastructure providers") and to market participants. In light of the responses received from all 19 FSB member jurisdictions, on 18 September 2014, the FSB reported on jurisdictions' ability to defer to each other's OTC derivatives market regulatory regimes. All but five jurisdictions (Argentina, Brazil, China, India and Indonesia) reported having some capability to defer to OTC derivatives requirements in another jurisdiction.

On 19 September 2014, the FSB published its feasibility study on aggregation of OTC derivatives trade repository (TR) data. To date, a total of 25 TRs in 11 jurisdictions are either operational or have announced that they will be; and hence aggregation of the data being reported across these TRs is necessary, to ensure that authorities are able to obtain a comprehensive global view of the OTC derivatives market and activity. The report compares three basic options: (i) a physically centralised model; (ii) a logically centralised model; and (iii) the collection and aggregation by authorities themselves of raw data from TRs; and finds that aggregation options 1 and 2 are highly preferable to option 3 (albeit that this is the only one of these options that is currently available for use). The report recommends a number of key steps (set out in the executive summary) that should be undertaken either as part of the preparatory work before any formal project is launched to implement a global aggregation mechanism, or that will need to be undertaken irrespective of the particular aggregation model chosen, in order to enable effective aggregation. Next steps, in relation to which the FSB will work with the CPMI and IOSCO, are also outlined.

Concern has been noted that different approaches to the interpretation of MiFID I across Member States mean that there is no commonly-adopted application of the definition of derivative or derivative contract in the EU for some asset classes. The practical consequences of this have come to the forefront with the implementation of EMIR. In light of this, on 29 September 2014, ESMA published a Consultation Paper on *Future Guidelines Clarifying the Definition of Derivatives as Financial Instruments* under the current Markets in Financial Instruments Directive (MiFID I).

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Financial benchmarks

In February 2014, the FSB decided to incorporate an assessment of FX benchmarks into its ongoing programme of financial benchmark analysis. The FX Benchmarks Group (FXBG) was established to undertake a review of FX benchmarks and analyse market practices in relation to their use and the functioning of the FX market as relevant. The FXBG has progressed its work in part by engagement with a wide range of FX market participants across the globe, as well as through independent analysis. To assist in the preparation of its final recommendations and conclusions, on 15 July 2014, the FXBG published an interim report for consultation (requiring comments by 12 August) which sets out fifteen draft recommendations. Once finalised, the report will be transmitted by the FSB to the Brisbane G20 Leaders Summit in November.

The major interest reference rates (such as LIBOR, EURIBOR, and TIBOR, collectively the "IBORs") are widely used in the global financial system as benchmarks for a large volume and broad range of financial products and contracts. In February 2013, the G20 asked the FSB to undertake a fundamental review of major interest rate benchmarks and plans for reform to ensure that those plans are consistent and coordinated, and that interest rate benchmarks are robust and appropriately used by market participants. Accordingly, on 22 July 2014, the FSB published its review of major interest rate benchmarks, alongside plans for reform. The review was carried out by a high-level Official Sector Steering Group (OSSG) of regulators and central banks, drawing on two main strands of work:

- A review of the standards and principles for sound benchmarks, including an assessment of the major interest rate benchmarks against the internationally agreed and endorsed IOSCO Principles for Financial Benchmarks. This IOSCO review was published as a stand-alone Annex 2 to the FSB report.
- A report by private sector experts asked to identify additional benchmark rates and to analyse the transition issues arising in the event of a move to an alternative rate. The OSSG established a Market Participants Group (MPG) to take this forward. This MPG report was published as a stand-alone Annex 3 to the FSB Report.

The IOSCO review relating to LIBOR, EURIBOR and TIBOR (stand-alone Annex 2 to the FSB report) finds that all three administrators have made significant progress in implementing the majority of the Principles. Both completed and on-going reforms have raised the overall oversight, governance, transparency and accountability of the three administrators and their respective benchmarks. This has undoubtedly improved the quality and integrity of the benchmarks. These reforms have occurred in the context of regulatory, operational and organisational changes concerning all three administrators.

The OSSG has assessed the feasibility and viability of the reformed and alternative benchmark rates proposed by the MPG, taking account of the market structure, institutions, and the legal and regulatory framework within different currency areas. Based on the recommendations of the subgroups set up to cover each of these currency areas, and the input from the MPG and IOSCO, the report sets out concrete proposals and plans for the reform and strengthening of existing benchmarks and for additional work on the development and introduction of alternative benchmarks.

While each currency area faces particular conditions that affect the specific recommendations, and which imply that there will be some heterogeneity in implementation, the FSB supports a multiple-rate approach to the reform of major interest rate benchmarks in line with the recommendations of the MPG. The main elements are:

- strengthening existing IBORs and other potential reference rates based on unsecured bank funding costs by underpinning them to the greatest extent possible with transaction data (the MPG terms such enhanced rates "IBOR+");
- developing alternative, nearly risk-free rates. Members believe that there are certain financial transactions, including many derivative transactions that are better suited to reference rates that are closer to risk-free.

To implement the approach, the currency groups will work with and guide the private sector to implement new designs and methodologies for IBOR+; and, where currently absent, identify and develop viable near risk-free rates supported by robust methodologies.

Specific timelines are set out in the report for implementing the recommendations. In particular, in relation to IBOR+, by end-2015, administrators should have publicly consulted on any recommended changes, while currency groups will work to develop transition strategies and address any legal obstacles and risks. In respect of risk-free rates, where suitable, central banks and supervisory authorities should encourage the industry or work with the administrators to implement at least one IOSCO-compliant risk-free rate by 2Q2016. The FSB has mandated the OSSG to monitor and oversee the implementation of the benchmark reforms set out in the report.

On 25 September 2014, based on recommendations by the Fair and Effective Markets Review, the UK Government launched a consultation (for comment by 23 October 2014) on extending the new legislation the UK Government put in place to regulate LIBOR to cover a further seven major benchmarks in the foreign exchange, fixed income and commodity markets, namely:

- Sterling Overnight Index Average (SONIA) and the Repurchase Overnight Index Average (RONIA), which both serve as reference rates for overnight index swaps;
- WM/Reuters 4 pm London Fix, which is the dominant global foreign exchange benchmark;
- ISDAFix, which is the principal global benchmark for swap rates and spreads for interest rate swap transactions;
- London Gold Fixing and the LMBA Silver Price, which determine the price of gold and silver in the London market; and
- ICE Brent futures contract, traded on the ICE Futures Europe (IFEU) exchange, which acts as the crude oil futures market's principal financial benchmark.

On 30 September 2014, the FSB released the final version of its report on FX rate benchmarks, which sets out a number of recommendations for reform in the FX markets and in the benchmark rates that have been identified as pre-eminent by market participants – in particular, the WM/Reuters (WMR) 4 pm London fix produced by the WM Company. IOSCO's *Review of the Implementation of IOSCO's Principles for Financial Benchmarks by WM in respect of the WM/Reuters 4 pm Closing Spot Rate* was also published on 30 September 2014, as part of the FSB's report on FX benchmarks.

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Short-Term Markets


by David Hiscock and Andy Hill

European repo market

On 27 June 2014, the EBA published its final Guidelines on disclosure of encumbered and unencumbered assets, which include a set of principles and three templates (supplemented by a requirement to disclose some additional information on the importance of encumbrance in the reporter's individual funding model) to enable the disclosure of all applicable information. They are the first step towards a harmonised disclosure framework of asset encumbrance in the EU. For the purposes of these guidelines, an asset should be treated as encumbered if it has been pledged or if it is subject to any form of arrangement to secure, collateralise or credit-enhance any on-balance-sheet or off-balance-sheet transaction from which it cannot be freely withdrawn (for instance, to be pledged for funding purposes). All securities financing transactions (SFTs) are amongst the specifically identified types of contracts which should be considered encumbered.

On 21 July 2014, the ESRB published its Annual Report 2013, covering the period from 1 April 2013 to 31 March 2014. From a repo market perspective, two sections of this are particularly worth noting: first, the section under the sub-heading "A number of structural factors in the shadow banking sector further increased the risk of a sudden repricing of risk premia" (starting on page 23). In summary:

(i) the growing importance of collateral-based financial intermediation;

(ii) collateral transformation and leverage through collateral "chains";

(iii) low inventories of market-makers; and

(iv) limited participation of money market funds in the money markets and repo markets.

Second, section 1.3.2, *Beyond Banking: Securities Financing Transactions* (starting on page 30), which discusses points under highlighted paragraph openings, including:

- In the course of 2013 the ESRB made significant headway on assessing the potential macroprudential risks and vulnerabilities associated with SFTs.
- Widespread use of SFTs may have macroprudential implications.
- International bodies, regulators and standard-setters have repeatedly issued warnings about the potential risks of SFTs.
- The ESRB's data collection exercise provided key insights into the potential systemic risks of SFTs in Europe.
- The exercise also identified potential systemic risks arising from the reinvestment of the cash collateral received through SFTs.
- The data collection exercise conducted by the ESRB in 2013 also confirmed the growing importance of central counterparties (CCPs).

Whilst it is based on the case of the US market, it is interesting to note the 13 August 2014 Workshop on the Risks of Wholesale Funding, sponsored by the Federal Reserve Banks of Boston and New York. The purpose of this workshop was to promote a

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They are the first step towards a harmonised disclosure framework of asset encumbrance in the EU.

better understanding of the risks posed by short-term wholesale funding, and to explore policy options for minimizing these risks. The workshop, which principally involved officials and academics, consisted of a small number of papers (most of which are accessible via the agenda) that address risks which wholesale funding can pose to both individual institutions and to the financial system as a whole; remarks from William Dudley, President of the Federal Reserve Bank of New York; and a keynote speech by Eric Rosengren, President of the Federal Reserve Bank of Boston.

On 3 September 2014, ESMA published its *Report on Trends, Risks and Vulnerabilities No. 2, 2014*. As part of ESMA's monitoring of market developments which may present future vulnerabilities, this report provides an in-depth analysis of the systemic relevance of SFTs in the EU; which begins as follows: “This article looks into SFTs in the EU: their significance, their objectives, their main users and their risks. SFTs are essential tools used by market participants for multiple purposes, including liquidity and risk management. They contribute to market efficiency and were at times one of the few liquidity sources available to market participants. However, they are also perceived to have contributed to financial instability during the financial crisis. This prompted global regulators to take a closer look into this area, in order to shed light on existing market practices liable to foster future systemic risk. SFTs have implications for financial stability by contributing to interconnectedness and increasing procyclicality, while features such as the facilitation of collateral re-use illustrate their ambivalent role in terms of market efficiency and financial stability. Risks from securities finance are compounded by a lack of transparency and insufficient data availability or granularity that would allow for a proper assessment of exposures and the degree of risk.”

Alongside the publication of the latest semi-annual ICMA European repo market survey, on 4 September 2014, an ICMA ERC Occasional Paper, *Continually Working to Develop Efficient and Effective Collateral Markets*, was published. This Occasional Paper starts by recalling the CICF's *Collateral Fluidity White Paper*, published on 7 November 2012, which explained the view that the challenge is to mobilise efficiently the flow of collateral inside and between organisations, by eliminating barriers to collateral flows and the development of an efficient market infrastructure. It then also recalls ICMA's 8 April 2013 publication entitled *Economic Importance of the Corporate Bond Markets* and ICMA's 29 October 2013 publication entitled *Avoiding Counterproductive Regulation in Capital Markets*; the latter of which was then followed up by the ICMA ERC's important 3 April 2014 paper, *Collateral is the New Cash: the Systemic Risks of Inhibiting Collateral Fluidity*.

The new Occasional Paper then proceeds to briefly review the ICMA ERC's Triparty Settlement Interoperability (TSI) initiative; the valuable COGESI led collateral initiatives (also detailed in the Market Infrastructure section of this ICMA Quarterly Report); and the recent, significant adaptations to the ECB's collateral processes. Whilst applauding all the efforts made to date, the occasional paper concludes by observing that “ICMA believes that there is a significant opportunity to further coordinate efforts in this arena, both by bringing the efforts of the ICMA ERC to the attention of the public sector and by seeking to ensure that there is full cooperation across the public sector”.

On 16 September 2014, the OECD released its first recommendations for a coordinated international approach to combat tax avoidance by multinational enterprises, under the OECD/G20 Base Erosion and Profit Shifting (BEPS) Project designed to create a single set of international tax rules to end the erosion of tax bases and the artificial shifting of profits to jurisdictions to avoid paying tax. These recommendations may be impacted by decisions taken with respect to the remaining elements of the 15 point BEPS Action Plan, which are scheduled to be presented to G20 Governments for final approval in 2015. At that point Governments will also address implementation measures for the Action Plan as a whole.

One of these first recommendations just released focuses on helping countries to ensure the coherence of corporate income taxation at the international level, through new model tax and treaty provisions to neutralise hybrid mismatch arrangements

(Action 2). Once translated into domestic law, the recommendations in Part 1 of the report will neutralise the effect of cross-border hybrid mismatch arrangements that produce multiple deductions for a single expense or a deduction in one jurisdiction with no corresponding taxation in the other jurisdiction. This is of significance because this report says (at paragraph 56) that "… the most common transaction used to achieve a mismatch in tax outcomes under a hybrid transfer is a sale and repurchase arrangement …". Seeking to negate the tax effect of hybrid transfers achieved through the use of repos may lead to significant incremental tax compliance and reporting burdens, particularly in relation to repos between different legal entities within the same group of companies.

On 23 September, the ESRB published its Occasional Paper No. 6, *Securities Financing Transactions and the (Re)use of Collateral in Europe: An Analysis of the First Data Collection Conducted by the ESRB*. This report presents the results of two data collection exercises that were conducted to gain some initial insights into the structure of the SFT market and the correlated practices adopted by market participants concerning the re-investment or the re-use of the collateral sourced through SFTs or via equivalent transactions. By providing a description of the SFT landscape, the data collection exercises undertaken by the ESRB have a macroprudential dimension in that they provide data at an aggregated level. The first data collection exercise encompassed a sample of 38 EU banks, representing approximately 60% of the EU banking system's total assets. The institutions covered by this sample are the main players in the management of securities collateral. The second data collection targeted 13 agent lenders that are considered to be the largest re-investors of cash collateral in Europe. The sample period of the data is fixed at the end of February 2013.

The data collections were intended to fit in the broader policy context initiated by the FSB and the resulting analyses ultimately address a number of the FSB's recommendations. The first element of the analysis in this report is specifically related to the FSB's fourth recommendation (disclosure of collateral management activities) and, to a certain extent, to the first recommendation (authorities to collect granular information on SFTs of large international financial institutions). The second element is similarly related to the first of the FSB's recommendations, but also the sixth, which requests better disclosure of securities lending activities. The analysis contained thereafter is relevant for the European Commission's proposal on the reporting of SFTs to trade repositories; and the report is in line with the ESRB's earlier outline of a monitoring framework. Looking ahead, there may need to be a properly targeted regular form of data collection, encompassing improvements based on the results of this first exercise. The main findings of the ESRB's report are outlined in the executive summary and also in the conclusions section.

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ECP market

MMFs: On 3 July 2014, IMMFA announced its publication of an updated set of Position Papers on the European Commission's proposal for a new Regulation for Money Market Funds. Within these updated IMMFA position papers, paper number 10 (at page 27) relates specifically to ABCP. This paper describes what ABCP is; the value of ABCP; its role as a key funding source for European companies; and the relevant part of the EC's proposals and the risk of unintended consequences. IMMFA's ABCP related recommendations read as follows:

"The European Commission's reform proposal would result in a contraction of the ABCP market, which would, in turn, damage the public policy objective of stimulating the wider European economy.

IMMFA makes the following recommendations:

- ABCP conduits with both corporate and consumer receivables should qualify as eligible securitisations.
- The requirement that a MMF's aggregate exposure to securitisations should not exceed 10% of its assets should be deleted.
- The maximum maturity limit of the asset pools financed in ABCP conduits that are eligible for MMFs should be extended to at least 5 years, to match the standard maturities of many types of pools financed in ABCP conduits."

On 23 July 2014, the SEC adopted amendments to the rules that govern MMFs. The amendments make structural and operational reforms to address risks of investor runs. These rules build upon the reforms adopted by the SEC in March 2010 that were designed to reduce the interest rate, credit and liquidity risks of MMF portfolios. The new rules (i) require a floating net asset value (NAV) for institutional prime MMFs, which allows the daily share prices of these funds to fluctuate along with changes in the market-based value of fund assets;

> An important area that may not have been given full consideration by the Central Banks is asset-backed commercial paper.

and (ii) provide non-government MMF boards new tools – liquidity fees and redemption gates – to address runs. The final rules also include enhanced diversification, disclosure and stress testing requirements, as well as updated reporting by MMFs and private funds that operate like MMFs.

The final rules provide a two-year transition period to enable both funds and investors time to fully adjust their systems, operations and investing practices; and these newly adopted rules will be effective 60 days after their publication in the Federal Register. IMMFA has responded to these SEC amendments, welcoming the fact that the SEC has taken note of a number of concerns raised by the MMF industry; whilst stating that it is very disappointing that forced conversion to floating NAVs is being imposed on Prime MMFs.

ABCP: In Issue 34 of the ICMA Quarterly Report, the ECP-related article that appears on pages 22-23 makes the point that ABCP needs to be appropriately considered by the official sector, as it considers how to advance the revitalisation of securitisation markets. Subsequent to the writing of this article, AFME published its 7 July response to the 30 May 2014 joint Bank of England / ECB Discussion Paper, *The Case for a Better Functioning Securitisation Market in the European Union*. Fully consistent with the views expressed in Issue 34 of the ICMA Quarterly Report, on page 4 this AFME response states:

"The third broad area on which AFME and its members wish to comment is to note that the term "securitisation", used in its CRR sense, is a very broad term and the criteria suggested, while broadly sensible, do not always take full account of this. An example of an important area that may not have been given full consideration by the Central Banks is asset-backed commercial paper. Although ABCP conduits are "securitisations" in the regulatory sense, they do not fit the paradigm of a securitisation we imagine the Central Banks will have had in mind when developing the criteria in Box 3. As a result, ABCP would not be a QS under the Central Banks' proposals despite the fact that it delivers many of the benefits of securitisation outlined in the DP (eg funding trade receivables and other real economy assets, diversification of funding sources for non-bank clients and warehouseing of assets for later ABS transactions), its robust structure (featuring, eg significant overcollateralization and retention by originators of a dynamically adjusted first-loss tranche) and the fact that most conduits are supported by strong sponsor banks. The definition of "securitisation" has long caused problems of this sort, so adjusting that regulatory definition may be the most sensible solution to this issue. Alternatively, AFME would urge the Central Banks to adjust the criteria to recognise positively the special structural considerations associated with the ABCP market."

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CSDR: impact of T+2 on repo markets

The move in standard settlement date from T+3 to T+2 for much of the European bond markets will have repercussions for the underlying repo and securities financing markets. While repo has no standard settlement cycle and is largely unaffected by the CSDR (with one notable exception), the shorter settlement cycle for bonds will mean a shorter financing window. This is expected to prompt a liquidity shift in the most common start settlement date for repo markets from T+2 to T+1.

This shorter financing window will present a number of risks to settlement efficiency and additional challenges for collateral and liquidity management. There will be a greater urgency to match and confirm

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> This is expected to prompt a liquidity shift in the most common start settlement date for repo markets from T+2 to T+1.

both cash and financing trades earlier, and a need to move market practice to trade date affirmation and confirmation. With more volumes of repo moving to T+1, this will mean that T+0 will become the next date for any funding or position adjustments, which could be problematic where securities are being transferred across different (I)CSDs. Cross-currency repos could also become more difficult to manage when trading for T+1, since spot settlement in the FX market will remain at T+2.

With the majority of financing trades moving from T+2 to T+1, it will also be necessary to update market practice for recalling or re-rating open repo trades, as well as for instructing collateral substitutions. Current market practice for such notifications is 3 pm London time. However, this is likely to move to T+1 and an earlier time, although there may be some exceptions for certain underlying securities. The ICMA *ERC Guide to Best Practice* will be updated to reflect any decisions made by the ERC Committee.

As mentioned, there is also a notable exception to the scope of T+2 as it impacts the repo market, and it relates to trades executed on in-scope trading venues, such as the various electronic trading platforms for repo. It is understood that from 1 January 2015 it may no longer be possible to execute any securities financing transaction on such trading venues where the start settlement date is beyond T+2. Given that SFTs are inherently flexible, and as such have no standard settlement cycle, there appears to be no rationale for this anomaly, and the ERC Committee is involved in discussions with the European Commission and various regulatory bodies regarding what seems to be an unintended outcome of the CSDR.

Despite the regulatory impact for forward-starting repos executed on trading venues, it is important to be clear that, while much of the repo market will experience a shift in liquidity from start date T+2 to T+1, this is not a regulatory requirement, nor best practice, and the market will remain free to negotiate and transact SFTs for any start or end-settlement date.

The implications of T+2 for the repo market are discussed in more detail in the ERC Operations Group paper: *The Impact of T+2 Settlement on the European Repo Market.*

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CSDR: settlement discipline and SFTs

Article 7 of the Regulation on Improving Securities Settlement in the European Union and on Central Securities Depositories (CSDR), provides for mechanisms in the event of settlement fails, in particular mandatory buy-ins and cash penalties for late settlement. The Level 1 text was passed into law earlier this summer, and now ESMA is consulting the industry as it drafts the regulatory and implementing technical standards for settlement discipline. ICMA is heavily engaged in this process, with other industry bodies as well as ESMA, and a more detailed update on this process and the implications of CSDR settlement discipline can be found in the Secondary Markets section of this Quarterly Report.

The ICMA ERC Committee is especially concerned with the proposed treatment of securities financing transactions for mandatory buy-ins. Under the Global Master Repurchase Agreement (GMRA), and similarly the Global Master Securities Lending Agreement (GMSLA), it is not possible to issue a buy-in (or “buy-in like” remedy) against the failing start-leg of an SFT. There are two primary reasons for this. First, the outright purchase of a failing security does not seem to be the right remedy for what is effectively a failing “loan” of a security. Second, given the relatively marginal income generated from repo and securities lending transactions, which generally operate on tight margins, and the significant and unquantifiable costs of being bought in, the risk of being bought in on the start-leg of an SFT, even if relatively low, would be enough to deter many market participants from engaging in SFTs.

The CSDR suggests, however, that some SFTs would be in scope of mandatory buy-ins, with any exemption being determined by "where the timeframe of those operations is sufficiently short and renders the buy-in process ineffective". While "sufficiently short" is not defined, it is understood to mean transactions where the end-leg of the SFT would fall before the practicable settlement date of the buy-in.

The ERC Committee is concerned by this partial exemption for SFTs since this is likely to cause a bifurcation in the repo and securities lending markets between SFTs that can be bought in and SFTs that are exempt, with very different demand and supply skews for each. Lenders of securities will not wish to lend for any term that could bring the transaction into scope of mandatory buy-ins. Meanwhile, borrowers of securities, particularly market-makers who will want to hedge their increased buy-in exposure, will prefer to borrow SFTs that are in scope of mandatory buy-ins. This could have a significant detrimental impact on SFT market liquidity, particularly for term markets, where bid-offer spreads will need to increase to account for this additional risk and lack of willingness to lend securities. A two-tier SFT market will also create additional complexity in the risk management of repo and financing desks. Central clearing counterparties (CCPs) will also need to address how they apply netting across these two pools of SFTs.

On 24 September, a delegation from the ICMA ERC Committee, jointly with the International Securities Lending Association (ISLA), met ESMA in Paris to discuss the practicalities of designing regulatory and implementing technical standards for mandatory buy-ins for SFTs. It is clear that a lot of work needs to be done in terms of reconciling trading level impacts with settlement level regulation, and a consultation on CSDR settlement efficiency and discipline is expected later this year. Settlement discipline mechanisms, including mandatory buy-ins, are expected to be implemented in 2016.

The ERC has produced a briefing note on the practicalities and implications of introducing a mandatory buy-in regime for SFTs.

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"This could have a significant detrimental impact on SFT market liquidity, particularly for term markets.

by Ruari Ewing and Charlotte Bellamy

Primary Markets

Prospectus Directive

Work continues in relation to Level 2 measures under the Prospectus Directive (PD), with ESMA issuing a Consultation Paper on various aspects of the PD regime including incorporation by reference, approval of the prospectus, publication of the prospectus and advertisements on 26 September 2014, with a deadline for responses of 19 December 2014. ICMA will be liaising with its members in preparing a response to the Consultation Paper. The UK FCA is also due to publish proposed guidance in relation to the prospectus disclosure requirements for retail investors in non-equity securities addressing the PD requirement that a prospectus should be "easily analysable and comprehensible".

Those ongoing changes under the current PD regime represent just a fraction of the regulatory reforms to which market participants are adapting. The market is also operating with various aspects of uncertainty under the current PD regime, many of which were caused by the last review of the PD. In the background to that, the implementation of the last PD review in July 2012 meant that most issuers needed to restructure their debt issuance programmes at great expense in order to continue to access the funding they required and provide a range of investment options to investors. As such (and as reported in previous editions of this Quarterly Report), the primary debt capital markets would benefit from a period of regulatory stability in the PD space in order to ensure the primary capital markets can continue to function effectively. That desire for regulatory stability currently overrides the desire for a long-term structural overhaul of the PD regime focusing on the interaction between the PD, TD, MiFID, MAD and other primary market regimes such as PRIIPs. Therefore, in approaching its next review of the PD, it would be sensible for the Commission to focus only on (i) the areas of the PD on which it is required to report; and (ii) correcting certain specific areas of uncertainty that were created during the last PD review.

In relation to the areas on which the Commission is required to report, some areas will not be an area of focus for ICMA's lead manager constituency because they do not impact in practice on the sector of the Eurobond market that is most relevant for them. Changes in other areas, such as the liability regime and the definitions of public offer, primary market and secondary market, could of course represent a fundamental shift in the PD regime depending on the approach taken by the Commission.

- Changes to the liability regime under the PD are unlikely to be welcomed by market participants. The current regime is well known and understood, and any uncertainty introduced by changes would be highly undesirable and could adversely affect the levels of issuance of and investment in securities in Europe. Developing any harmonised, pan-European liability regime would be extremely complex: there are entire legal textbooks dedicated to the subject under English law alone.
- In relation to the definition of public offer, there are various shortcomings with the current definition including the fact that it requires anyone who makes a non-exempt offer to produce a prospectus before doing so. This is an unfair obligation to impose on non-issuer offerors, who have no contact

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The primary debt capital markets would benefit from a period of regulatory stability in the PD space.

with the issuer and therefore no source of information other than that which is already in the public domain. As a result, the current regime restricts non-exempt offers in the secondary market. Another aspect is that there is no need for an on-going prospectus regime for secondary market offers because, once the securities are admitted to the regulated market, the on-going disclosure regimes under the Market Abuse Directive and the Transparency Directive provide the necessary information for secondary market purchasers. This aspect is linked to any definitions of primary market and secondary market that may be introduced and how they would apply.

- In determining any legislative definitions of primary market and secondary market, it is of course important to first identify the purpose for which those terms would be used. Currently, the situations in which the disclosure requirements under the Prospectus Directive apply (ie in connection with public offers and applications for admission to trading) are already clear, and so it is not clear that a definition of "primary market" in the PD is needed.

In relation to correcting specific aspects of uncertainty that were caused under PDII, the five most important areas appear to be: (i) the applicability of investor walkaway rights under Article 16(2) of PDII to exempt offers; (ii) the ability to use supplements to include additional, or amend existing, securities note information in base prospectuses; (iii) how base prospectus summaries and issue specific summaries are set out in base prospectuses; (iv) how risk factors in summaries should be approached; and (v) whether an issue specific summary needs to be attached to final terms relating to exempt offers of securities issued using a base prospectus that also allows non-exempt offers of securities.

The Euromoney Prospectus Rules Conference in London on 24 and 25 September 2014 was a good opportunity to discuss some of these issues with the regulators, lawyers, and other market participants who attended. A number of interesting themes related to the EU prospectus regime and relevant to ICMA's lead manager constituency were raised at the conference, including the following.

- Regulators might take the PDII review as an opportunity to consolidate the provisions of the PD regime, as they are currently split across a number of different directives, regulations and Level 2 measures. For the reasons mentioned above, it is hoped that this consolidation (or "re-cast") will largely re-arrange the existing provisions of the PD regime, rather than being a complete re-draft. Even a re-arrangement of provisions must be handled with care as it can result in legislative uncertainty if provisions are slightly reworded or moved from Level 2 to Level 1.
- The ballooning size of prospectuses raises questions around whether the PD "checklist" approach is working and also the purpose of prospectuses (given many retail investors will not read an 800-page prospectus). With the advent of PRIIPs, the KID is seen as a document that investors will in fact read, but there remain numerous queries surrounding how the PRIIPs regime will work in practice, as reported in previous editions of this Quarterly Report. It is hoped that the PDII review will allow regulators to amend the prospectus supplement requirements to work alongside the PRIIPs regime.
- Given the importance of data to provide information on the impact of regulatory changes, it was welcome to hear that ESMA intends to extend its current data collection to achieve a more granular picture of prospectus approvals.
- As always, it will be important that market practitioners engage with the consultation process in relation to the PDII review (which ICMA intends to do), and this was emphasised by authorities at the Euromoney conference.

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MiFID II Level 2: underwriting, placing and RSPs

On 1 August, ICMA submitted its responses to ESMA's 22 May Consultation Paper on MiFID II/MiFIR. The responses were submitted on the unwieldy ESMA-prescribed form, with a reader-friendly version of the ICMA responses being published by ICMA. The response to section 2.10 and related questions Q58-Q62 (on underwriting and placing) were made from the perspective of the international institutional syndicated investment-grade (Eurobond) primary markets and are briefly outlined below. (See also, in the Secondary Markets section, ICMA's responses on secondary market issues).

Whilst the response did not suggest the inclusion of any additional aspects into the draft ESMA advice being consulted on, it did raise several concerns around the compatibility of the existing provisions of the draft advice with robust primary bond markets – particularly since the consultation seemed to have been drafted without clearly distinguishing between share and bond issues (which are subject to very different dynamics). The response therefore recapped on the salient aspects of the Eurobond issuance process, underlining the issuer's preponderance throughout, before addressing the background statements in the consultation as well as the draft advice itself. Generally many of the potential conflict of interest risks flagged by ESMA in the consultation seem to be academic rather than practical, assume lead managers are not subject to practical limits on what they can do and/or are already appropriately covered by MiFID's Level 1 provisions. Lead managers liaise with issuers on all issuance aspects, but only as and when necessary (issuers will not welcome a requirement to have specifically to discuss points earlier than absolutely necessary or where the lead managers already know the issuer's views).

Specifically, the response noted (in contrast to ESMA's apparent understanding outlined in the consultations) that:

(a) lead managers compete to be selected, ahead of their peers, by issuers for the limited spots on bond issuance mandates and such competition should not be seen negatively as anti-competitively keeping out key competitors;

(b) issuers can and do change lead managers participating in their bond issues;

(c) banks are often hired by issuers just to execute a bond issue with no related advice to undertake the issue, let alone more general corporate finance advice on alternative financing options or debt sustainability levels;

(d) reducing underwriting risk is not of unequivocal value for lead managers (as it also reduces their fees);

(e) lead manager loans that are redeemed by a bond issue are generally advanced by a lead manager as swift bridge financing for issuers whilst the bond issue is being prepared (so lead managers are not preferred by the redemption of their loan);

(f) pricing is an art and not a science, with intentional "mispricing" seeming fanciful as:

  (i) "overpricing" (presumably fixing too low a bond yield) would deter investors from participating in the issue and/or result in a secondary trading sell-off (and so disincentivise investors from participating in future issues); or

  (ii) "underpricing" (presumably fixing too high a bond yield) would cause the yield to tighten too much in secondary trading (though issuers may seek some conservative pricing to maximise issuance uptake though the price itself will not increase the amount raised);

  (iii) lead manager underwriting risk would not be impacted either way given the prevailing use of bookbuilding as an issuance technique;

  (iv) any existing bond owners (in a fungible tap context) would also not be impacted either way since bond values depend on interest rate fundamentals rather than technical demand;

(g) stabilisation (regulated by the Market Abuse Directive) helps lead managers support the secondary price of the bonds and so ensure investors do not regret buying bonds from the issuer's primary offer rather than waiting to buy them in secondary trading (to the issuer's benefit in terms of fostering primary demand for subsequent issuance rather than hedging any lead manager risk);

(h) lead managers may "short-sell" in terms of overalloting bonds (at the offer price) in order to facilitate any subsequent stabilisation (with no relevance to lead manager underwriting risk);

(i) laddering, spinning and *quid pro quo* arrangements have long been recognised as unacceptable;

(j) issuers can and do express their priorities in the context of lead manager allocation policies, but do not need to do so before mandating the lead managers;

(k) allocations may be legitimately be made to active secondary traders to promote secondary liquidity;

(l) lead manager duties in relation to issuer disclosure (and related due diligence defences) have been the subject of decades of statute and case law;

(m) investors will stay away from overly geared issuers or demand commensurately high yields;

(n) recording the individual justification for each allocation decision is not practicable when up to 500 accounts are being decided within an hour (to minimise how long issuers and potential investors are on risk for) – ultimately records should simply be sufficient for lead managers to explain any individual allocations if queried by regulators;

(o) additionally requiring a "complete audit trail of all steps in the underwriting and placing process" is disproportionately absolute;

(p) requiring a record of all "potential" underwriting and placing operations is also disproportionate given lead managers are continuously liaising with issuers on a permanently evolving rainbow of potential bond issuance options; and

(q) lead managers do not have the power to operate a "traffic-light" system of issuance supply and the free market has done very well with no such system in place.

The response also noted how the proposed reintroduction of very onerous issuance reporting obligations to the Bank of Italy for mere statistical purposes risks adversely impacting Italian investor access to the international primary markets and so also the European internal market.

Distinctly, the Joint Associations Committee on retail structured products, with ICMA's support, also submitted a response to the consultation from the retail structured products (RSP) perspective. This response addressed aspects concerning product governance and intervention, fair, clear and not misleading information and also information to clients about investment advice, financial instruments, costs and charges.

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UK FCA temporary restriction on Cocos

The UK FCA announced in August 2014 that it will put in place a temporary restriction on sales of contingent convertible instruments (CoCos) to certain retail investors in the EEA from 1 October 2014. The temporary rules will be in place for one year, and will then be replaced by permanent rules. The rules set out a prohibition on selling CoCos to retail investors and on doing anything that "would or might result in" a retail client in the EEA buying a CoCo or holding a beneficial interest in a CoCo, unless a firm has taken "reasonable steps" to ensure that one or more of the exemptions set out in the rules is met. If an underlying investor could be characterised as a "retail client in the EEA" (which is broad in scope), the exemptions include certified high net worth investors, exempt persons, certified sophisticated investors, self-certified sophisticated investors and indirect investment. The rules follow an ESMA communication and ESAs communication relating to, *inter alia*, investors' ability to understand the risks involved in CoCos, which should be read alongside the new rules. For example, in relation to questions around the territorial and product scope of the rules, the ESMA pronouncement that the risks involved in investing in CoCos can only properly be analysed by investors with the "skill and resource set of knowledgeable institutional investors" should be borne in mind. Moreover, the rules appear to be "results based", meaning banks' compliance with these rules would be judged with hindsight (ie if something goes wrong).

ICMA has been liaising with its Legal & Documentation Committee and Primary Market Practices Committee to assist lead managers in determining the impact of the rules and appropriate steps that should be taken. What seems clear is that no single step is likely to satisfy the "reasonable steps" safe harbour alone. It is likely that banks will use a package of different steps, both "on-deal" and "off-deal", tailored for the individual bank/investor relationship and the individual deal, to feel comfortable that they, and the person to whom they are selling, will comply with the FCA temporary rules.

In addition to the questions around the steps banks will need to take to comply with the rules, there are also questions around the extent to which banks should be applying similar restrictions to products that are similar to those caught by the rules (given the underlying rationale for the rules noted above) and in jurisdictions where the rules do not apply, in order to reflect the spirit and intention of the rules and the ESMA and ESAs communications mentioned above. There are also some technical questions arising from the precise drafting of the rules, on which ICMA is liaising with the FCA in order to seek some clarity.

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Other primary market developments

There have been a few other primary market developments

- *MAR Level 2 consultation – stabilisation and soundings:* On 15 July, ESMA published Consultation Papers on draft technical standards and on draft technical advice on possible delegated acts under the new Market Abuse Regulation. ICMA is working to respond to the draft technical standards consultation by the deadline of 15 October on the aspects of stabilisation and soundings. Initial concerns relate *inter alia* to the unclear jurisdictional workability of the stabilisation safe harbour given MAR's expansion to MTFs and OTFs and also to the purported imposition of procedural requirements on the communication of non-inside information (which is outside MAR's scope).
- *Regulation Concerning Restrictive Measures in View of Russia's Actions Destabilising the Situation in Ukraine:* In light of Regulation 833/2014 concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine (which entered into force on 1 August 2014 and was amended by Regulation 960/2014, which entered into force on 12 September 2014), some competent authorities and stock exchanges have begun to require issuers to confirm that they do not fall within the scope of Article 5 of the Regulation at the time of admission to trading and/or when any documents are filed for review.

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Green Bond Initiative

by Nicholas Pfaff

Devised to provide voluntary process guidelines that recommend transparency and disclosure, and promote integrity in the development of the Green Bond (GB) market by clarifying the issuance process, the Green Bond Principles (GBP) have continued to establish themselves as the best practice standard in the GB market.

There are now more than 60 institutions representing all participants in the GB market that have joined and become members of the GBP. More than half are banks, with the remaining roughly equal between investors and issuers. A further 23 organisations, of which a third are Non-Governmental Organisations (NGOs), have received observer status. As a reminder, membership is open to institutions that have issued, underwritten or placed, or invested in GBs; while observer status is designed to welcome organizations that are not yet in the market and/or are active in the field of green finance such as, but not limited to, NGOs, universities, auditors, and service providers. The full list of GBP members and observers is available on ICMA's website.

As planned, the ICMA Secretariat of the GBP launched this summer the consultation for the 2015 edition of the GBP. The consultation was conducted on behalf of the GBP Executive Committee (GBP Excom) – a group of 18 leading institutions (issuers, intermediaries and investors) representative of the GB market. In line with its governance, the GBP is indeed reviewed annually through a poll of members and observers and updated through a subsequent drafting process conducted by the GBP Excom with the support of the Secretariat. The annual update is then presented to the GBP Annual Meeting.

With more than 35 detailed responses received, the consultation was a great success. Members and observers have provided suggestions that cover a wide range of issues such as expanding the categories of GBs, additional guidance on use of proceeds, further standards of disclosure and reporting; as well as generally the appropriate degree of prescription that the GBP should reflect. A high-level summary of the content of the consultation is being prepared by the GBP Excom with the support of the Secretariat, and will be circulated to GBP membership during October 2014.

In light of the quantity and quality of responses that need to be reviewed following the consultation, the GBP Excom decided to reschedule to the end of 1Q2015 the GBP Annual Meeting (originally announced for November 2014). The GBP Excom also constituted a dedicated working group that will work regularly with the Secretariat to prepare the GBP 2015 update.

Concerning developments in the GB market, issuance continues to be dynamic and has reportedly exceeded $25 billion in 2014 (to mid-September) and appears on track to match estimates (from the Climate Bonds Initiative) for $40 billion for the year. Most recently, it is interesting to note the innovation represented by IFC's issuance of a GB destined for US retail investors. The proceeds of this 10 year bond will be used for renewable energy and energy efficiency projects in developing countries. The bond is being issued under IFC's Impact Notes programme launched in March 2014 and "that for the first time allows US individual investors to buy triple-A rated IFC bonds and support private sector development in emerging markets".

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Social Impact Investment

Personal view by René Karsenti

The growth of Socially Responsible Investment (SRI) has been impressive. Established as a general values-based investment approach, SRI has quickly grown to about $10 trillion over the last 20 years or an estimated 15% of global capital. More than €3 trillion of bond investments in Europe are estimated to be managed under SRI criteria. SRI has mostly focused on negative screening of investment in public companies in areas such as tobacco, defence and occasionally fossil fuel, as well as positive screening of environmentally aware, health, green energy or socially conscious projects or companies.

An example of innovative and successful SRI is a total of $5 billion "Vaccine Bonds" financing the GAVI Vaccine Alliance which has been issued by the International Financing Facility for Immunisation (IFFIm) since its 2006 inception and which I have had the honour to chair since 2012. (See my article in ICMA QR 4Q2012.) Other investments have involved the fast developing Green Bonds segment in which ICMA plays an important role, since its inaugural issue in 2006 by the European Investment Bank.

On 15 September, The Social Impact Investment Taskforce established by the G8 published its report. The report, entitled *Impact Investment: The Invisible Heart of Markets – Harnessing the Power of Entrepreneurship, Innovation and Capital for Public Good*, calls on governments and the financial sector to take action to unleash $1 trillion of private sector impact investment to tackle social problems.

More than 200 government and private sector experts, of which I am honoured to be part, have been engaged across the G8, Australia and the EU, in national advisory boards focused on establishing impact investment as a powerful force in each country, and in working groups formulating recommendations on measurement of impact, asset allocation, international development and mission alignment for profit-with-purpose businesses.

The report lays out several clear recommendations which include:

- encouraging pension funds and providers of tax-advantaged savings schemes and products to include impact investments as part of their offering;
- enabling impact-driven businesses to lock-in their social mission through legal forms and removing regulatory obstacles around fiduciary duty;
- expanding regulatory and tax incentives offered for investment in social enterprises and charitable organisations, enabling investors to offset their impact investment income against tax;
- establishing a kitemark for impact investment products to make them quality certified, accredited, recognisable and differentiated in a complex marketplace;
- developing social impact bonds and development impact bonds;
- appointing a senior government Minister to champion impact investment within and beyond government;

> I believe we are now in the early days of a revolution of social investment.

- reforming legal and regulatory frameworks for charitable organisations to help them to embrace entrepreneurial risk-taking and innovation where it furthers their mission;
- publishing better and clearer data about the cost to government of addressing social issues to encourage more impact investment participants to the market place.

The report also:

- calls on charitable foundations and trusts to allocate part of every charitable endowment and high net worth investment portfolio to impact investments;
- encourages mainstream investors and the wider public to engage in impact investment by providing some investment protection;
- calls on investors, including foundations, pension funds, sovereign wealth funds and independent investment managers to consider impact, risk and return in making investment decisions. Where investors wish to invest in impact-driven businesses, they can encourage them to pursue specific measurable social impact;
- calls on the G20, ASEAN, OAS, and the African Union to put on their agendas the development of social impact investment;
- calls on inter-governmental institutions such as the World Bank, IFC and regional development banks to play a leading role in a new market for social impact and development impact bonds;
- calls on the United Nations, as it resets its Millennium Goals in 2015, to support impact investment as an innovative way of tackling social issues that constrain private sector development and economic growth.

The Task Force has been led by Sir Ronald Cohen, founder of APAX, who had been a key player in the venture capital revolution in the 1970s. And indeed forty years later, our lives have been completely transformed by tech entrepreneurs, who have revolutionised the way we live.

How come these attitudes changed so fundamentally? They did so because the challenge of high-risk/high-return investments was met by the creation of a totally new investment class: venture capital and private equity. Venture capital was a response to the needs of ambitious new companies engaged in high-risk innovation.

I believe we are now in the early days of a revolution of social investment. A rising wave of social entrepreneurship follows the wave of business entrepreneurship. It seeks to make a difference, to be meaningful, to improve people's lives. Today, welfare states designed for the 20th century are throwing up their arms in face of the struggle against the new century's social challenges. They realise that they are not best placed to innovate to bring solutions to social issues. Their projected social expenditure falls far short of expected needs and the yawning gap poses grave challenges for them and for the nature of our society, as mounting social issues impact our values, our social cohesion, and our lives. The primary reason is that traditional philanthropy has focused on the act of charitable giving rather than on achieving social outcomes.

How can we do for social entrepreneurs and organisations what has been successfully done for business entrepreneurs? How can we connect them to the capital markets? The answer is through greater innovation, effectiveness and scale. This requires access to capital providers seeking social improvement and prepared to accept the risks that accompany innovation and growth.

Impact investing is an important part of the answer. Social impact investment aims directly to improve lives. Its objective can be social, environmental or developmental. It includes investment in non-profit organisations and "profit-with-purpose" businesses.

Impact investing is a hybrid of philanthropy and investment that creates a blend of financial, social and environmental benefits. Impact investments are directed into companies, organizations and funds with the intent of generating both financial returns and social or environmental impact.

And what is a Social Impact Bond, its main financial instrument to date? A Social Impact Bond (SIB) is a type of impact investment designed to raise private sector capital to expand effective social service programmes. This mechanism is used to finance a Pay for Success contract, which allows government to pay only for results. In such an arrangement:

- private investors fund a social service programme;
- government repays investors based on the programme's success in achieving predetermined social outcomes;
- if successful, investors can recoup their principal plus a rate of return;
- if the programme does not achieve those outcomes, then government is not obligated to repay investors.

SIBs have the potential to unlock a new and vast pool of investment capital to finance the expansion of effective, preventive social services focusing on measurable outcomes and generating social and financial returns to investors.

In this way, five direct benefits are created: the investor may earn an acceptable rate of capital return; the not-for-profit is financed using new, sustainable capital which enables it to scale-up successful social interventions; the government enjoys a cost-saving (with no up-front investment); financial risk is transferred to the private investor; and the "underlying" social-issue is ameliorated. Therefore, the Social Impact Bond uniquely links the monetary return on the financial product with its social delivery.

These bonds promise not-for-profit up-front capital for their operations while encouraging them to adopt a measurement system which accurately quantifies their social performance. This will, in turn, create innovation within the not-for-profit sector and, for the first time, allow investors to accurately correlate their financial return with the social performance of their investment.

Beyond SIBs, we are seeing quasi-equity, unsecured debt and senior debt coming to supplement grant funding in creating proper balance sheets for non-profits. We see the emergence of a spectrum of investors in search of different combinations of social and financial returns: from those like charitable foundations, prepared to accept low returns, through individual investors who require somewhat higher ones, all the way to pension funds that aim for near market returns. All these investors are motivated by a shared desire to improve lives. It is they who are funding the revolution in philanthropy.

What benefits does impact investment bring to government? The first is innovation. The second is investment to fund it on the basis that government only pays if successful outcomes have been achieved. The third is prevention. Governments everywhere concentrate on the most urgent consequences of social issues. They have little money to spend on prevention. SIBs generally focus on prevention, recidivism, school drop-out rates, homelessness, and so on, and set benchmarks for the effectiveness and cost of social interventions.

So contrary to the fears of some, impact investment is not about government relinquishing responsibility for social issues. It is about government encouraging innovation, paying for successful interventions and driving down the cost of achieving a successful outcome. Nor is it about privatisation.

I am confident that Impact investment represents a real revolution, driven by innovation. We estimate that it will settle over two or three decades between the $60 billon of microfinance and the $3 trillion of venture capital and private equity.

It will drive great innovation particularly as a new asset class in our capital markets and it will come to characterise our times.

Further reading: The Social Impact Task Force Report and Recommendations, and Sir Ronald Cohen's presentation at the Mansion House in January 2014.

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Secondary Markets


by John Serocold and Andy Hill

MIFID II Level 2: secondary markets

The final texts of the Regulation and the Directive were published in the *Official Journal* (OJ) on 12 June 2014. Publication in the OJ sets the date on which MiFID II enters into force as 2 July 2014. The rules enter into effect 30 months later, meaning that all EU firms undertaking investment business or providing investment services to clients must be fully compliant with MiFID II by 2 January 2017. We discussed the process and timetable in the Quarterly Report for the Third Quarter.

We summarise below the key points made in ICMA's 1 August responses ("user friendly" versions of which can be found here) to the ESMA MiFID II Consultation and Discussion Papers; and outlines current plans for next steps.

Consultation Paper

ICMA responded to Q24 and certain questions between Q121 and Q151 from the perspective of its secondary markets constituency.

Q24 relates to title transfer collateral arrangements (TTCA) which underpin the Global Master Repo Agreement (GMRA), among other documents. ICMA obtains legal opinions relating to the validity of netting under the GMRA in over 60 jurisdictions world-wide. This is a core area for us and we are concerned that the proposals are not appropriate to a number of products where the standard market documents have been developed over a number of years and are constructed with TTCA, including the GMRA.

The other questions cover the following areas:

- delineation between bonds, structured finance products and money market instruments;
- systematic internalisation, including:
  - the definition of systematic internaliser;
  - orders considerably exceeding the norm;
  - prices falling within a public range close to market conditions;
  - pre-trade transparency for systematic internalisers in non-equity instruments;
- data publication: access to systematic internalisers' quotes.

The proposals for the regulation of systematic internalisers have caused widespread concern, which we share. The systematic internaliser requirements are new to fixed income markets. "Systematic internalisers" (as defined) in instruments where there is a liquid market (as defined) must publish quotes they provide to clients, and make those quotes available, subject to stated criteria and limits, to other clients. They must enter into transactions under the published conditions where the quote is below the "size specific to the instrument" used for pre-trade transparency waivers.

It will be important to apply the systematic internaliser rules to fixed income markets in a way that recognises the limited liquidity in many instruments. As well as taking account of the exclusion for illiquid instruments, it will be important to give full weight to the specified ability of systematic internalisers to update and withdraw quotes; to decide objectively which clients are to have trading access to them; to refuse transactions on commercial considerations; to set limits on the number of transactions entered into in relation to a particular quote; and to improve on the quote.

Discussion Paper

We responded to the Discussion Paper from the perspective of our secondary markets constituency. The approach taken was similar to the CP, to give our views on core areas and to work with other associations to seek to ensure that the industry's broader concerns were adequately articulated. We covered market structure and transparency (Q101-147) and transparency requirements for the members of ESCB (Q176-177).

Market structure and transparency: ICMA agrees with ESMA's assessment that the most important assessment to be undertaken at Level 2 is the determination of whether an instrument has a liquid market. For these purposes, it is important not to "mirror the equity regime" exactly since, even within ESMA's proposed broad class of bonds, there is more heterogeneity than among equities.

ICMA considers it important not to group all bonds into a single undifferentiated "bond" class. Government bonds, investment grade corporate bonds, high yield bonds, and other categories have different liquidity characteristics, so it will be important to ensure that the transparency regime differentiates appropriately between them, so that in any particular case the transparency obligations are applied in a liquidity-sensitive way to a homogeneous group of instruments. A simple distinction between the proposed limited definition of sovereign debt and corporate bonds would not suffice.

We agree that depository receipts for bonds should be treated as non-equities, and convertible bonds should be treated as bonds.

There are a number of issuers which fall outside the definition in the First Company Law Directive which the market regards as corporate bonds, including non-EU companies, bodies corporate such as universities, limited liability partnerships (LLPs) and charities.

Although a shorter time period for assessing liquidity may introduce more operational complexity, we believe this can be mitigated by the use of appropriate market automation. But for automation to work efficiently, the industry will need to change its practices, particularly in relation to trade matching and allocation; this process is already affected by other reforms such as the move to T+2 settlement (international bonds have previously settled on T+3). Considerable further detailed work will be needed to establish, on the basis of evidence, how best to balance the conflicting demands of liquidity and transparency at reasonable cost.

We believe that the most appropriate method for assessing liquidity in the fixed income market is for the average size to be calculated based on the total turnover over a period divided by the number of trading days in that time period (ADT). We strongly recommend that the ADT should be calculated by dividing the notional volume turnover (rather than market value) by the number of days in the period. In considering the frequency of trades, we recommend that the time period should be monthly rather than annually.

In relation to post-trade transparency, we think it is desirable not to impose a deadline of "end of day" for disclosure purposes. This is because of the risk that market participants will be unwilling to accept risk trades late in the day. The reason for this is that they will not have as much time to unwind the position as they would have if they were allowed to delay publication for a set number of hours based on the

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ICMA considers it important not to group all bonds into a single undifferentiated "bond" class.

> ESMA is expected to consult on the remaining areas where it needs to set standards in December 2014.

trading day. Liquidity varies over the trading day and for other cyclical reasons.

We believe that the ESMA proposal for intra-day deferral carries significant risks to the market. MiFIR Articles 11 and 21 provide that all the details of the trade may be deferred in circumstances where there is a large-in-scale trade, a trade in an illiquid instrument or a trade above a size specific to the instrument.

Transparency requirements for members of the ESCB: MiFID II provides an exemption from the transparency requirements for members of the ESCB in certain circumstances. We believe that only a member of the ESCB is in a position to clarify whether a trade is for monetary, FX or FSB policy operations and therefore covered by the exemption.

In order for the exemption to be workable, the clarification must be provided prior to or at the point of execution. This is because the investment firm/venue must know whether to apply the transparency requirements prior to execution (the transparency requirements need to be complied with prior to execution and after execution but before settlement). However, legal documents are exchanged on the settlement date (ie two days or more after execution of the trade). Therefore, a clarification would occur after the transparency requirements would need to be met.

Therefore, we propose that either (i) the member of the ESCB provides a clarification when requesting a quote, which would require operational builds (special flags) and raises transparency compliance concerns for investment firms and venues (ie how would they demonstrate that the ESCB has provided the clarification and thereby complied with the transparency requirements), or (ii) the request for the quote by the member of the ESCB should be taken as *prima facie* evidence that the trade is for monetary, FX or FSB policy operations. We recommend the second option.

Next steps

ESMA is expected to consult on the remaining areas where it needs to set standards in December 2014; it is expected that the period for responses will be approximately eight weeks. As with our responses to the papers summarised above, we expect to work with like-minded associations, including in collaboration with the Joint Trade Association Group (JTAG).

We discussed the overall architecture of the timetable for implementation in the Quarterly Report for the Third Quarter.

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CSDR: impact of T+2 on secondary markets

Article 5 of the Regulation on Improving Securities Settlement in the European Union and on Central Securities Depositories (CSDR), provides that "transactions in transferable securities … which are executed on trading venues", should settle no later than the second business day after trading takes place (ie T+2).

For the purposes of the CSDR, *transferable securities* are defined as "those classes of securities which are negotiable on the capital market, with the exception of instruments of payment, such as:

(a) shares in companies and other securities equivalent to shares in companies, partnerships or other entities, and depositary receipts in respect of shares;

(b) bonds or other forms of securitised debt, including depositary receipts in respect of such securities;

(c) any other securities giving the right to acquire or sell any such transferable securities or giving rise to a cash settlement determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures."

And *trading venues* are understood to mean:

- regulated markets;
- multilateral trading facilities (MTFs);
- organized trading facilities (OTFs).

While CSDR stipulates that "T+2" should come into effect on 1 January 2015, many of the in-scope venues have agreed to migrate to T+2 settlement on 6 October 2014.

OTC transactions

The CSDR states that the mandatory migration to T+2 does not apply to transactions that are negotiated privately but executed on a trading venue, nor to transactions which are executed bilaterally but reported to a trading venue.

The "ICMA market" refers to transactions in international securities, intended to be traded on an international cross-border basis through an international central securities depository (ICSD), which are often negotiated bilaterally and may be neither executed nor reported to a trading venue; it follows that these transactions will be out of scope for this Regulation.

However, to avoid settlement fragmentation in the European bond markets, and to help support orderly markets and a harmonized migration to T+2, ICMA has updated its Rules and Recommendations for the Secondary Market to change the standard settlement date of "ICMA markets" from T+3 to T+2, unless otherwise stated, with effect from 6 October 2014 (ie in line with the various trading venues).

Unresolved issues

As the migration date of 6 October 2014 approaches, the market has become increasingly concerned as to the treatment of certain securities traded on trading venues and whether they are in scope of the CSDR. This would include non euro-denominated securities that are frequently settled both in European and non-European CSDs. The various trading venues are expected to publish which securities they consider to be in-scope, and so moving to T+2, and it is hoped that there will be a level of harmonized treatment across the venues.

A further unresolved issue relates to whether or not transactions executed on trading venues as a result of requests for quotes (RFQ) are considered "privately negotiated" and so out of scope of the CSDR. It is hoped that the relevant competent authorities will be able to provide clarity on this interpretation of the Regulation.

CSDR T+2 and the impact on securities financing transactions

The move to T+2 settlement for much of the European bond markets will have implications for related securities financing transactions, including repurchase agreements (ie repos). While repos have no standard settlement cycle, and as such remain largely out of scope of T+2, the shortened settlement cycle for the underlying securities is likely to prompt a liquidity shift in the most common start settlement date for many repos from T+2 to T+1. The potential impact of this is discussed in more detail in the Short-Term Markets section of this Quarterly Report.

ICMA communications on T+2

On 20 May 2014, ICMA announced the update of its Rules and Recommendations to support a harmonized migration to T+2.

In September, the ERC Operations Group produced a paper on *The Impact of T+2 for the Securities Financing Market.*

On 22 September 2014, ICMA held a call for members on the logistics and impacts of the move to T+2.

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CSDR: settlement discipline

Article 7 of the CSDR provides for mechanisms in the event of settlement fails, in particular mandatory buy-ins and cash penalties for late settlement. The Level 1 text was passed into law earlier this summer, and now ESMA is consulting the industry as it drafts the regulatory and implementing technical standards for settlement discipline. ICMA is heavily engaged in this process, and has held a number of industry meetings, with the joint participation of other relevant trades associations, to discuss the complex issues arising out of settlement discipline and to achieve a level of consensus around how the Regulation could possibly be designed and implemented with the least negative impacts for secondary market liquidity.

On 16 September, ESMA invited a small group of industry representatives to join a workshop to discuss the regulatory and implementing technical standards for settlement efficiency and discipline. This was followed by an ESMA meeting on 24 September with ICMA and ISLA to discuss the particular practicalities of implementing mandatory buy-ins for securities financing transactions (SFTs). An ESMA Consultation Paper on the Level 2 standards is expected in December 2014.

In preparation for these meetings, ICMA and AFME co-chaired a two-day industry workshop at JP Morgan, with a number of market participants and representative bodies, including the European Central Securities Depositories Association (ECSDA) and the European Associations of CCP Clearing Houses (EACH). The workshop resulted in a number of agreed principles across the various constituents that would be presented to ESMA during the upcoming meetings. These included:

Cash penalties

- Any penalty mechanism for late settlement should be as simple as possible, with a daily *ad valorem* rate applied to all fails, and with no maximum size.
- To be effective and to incentivize settlement efficiency, any penalty mechanism should compensate the disappointed counterparty (thus replicating the real world economics of a fail in a normal interest rate environment).
- There should be no attempt to identify fails chains for penalties; rather all fails are penalized and all disappointed counterparties compensated.
- The applicable penalty, as much as possible, should not be determined by the underlying asset type, transaction type, or liquidity calibrations.

Buy-ins

- Buy-ins should be executed at the trading level by the disappointed counterparty (including CCPs).
- CSDs are not in a position to initiate or manage effectively the buy-in process.
- Trading venues can have rules related to buy-ins, but in the case of fixed income they are not in a position to initiate or manage effectively the buy-in process.
- In the case of sequential fails, the buy-in should be initiated by the disappointed counterparty (including CCPs) at the end of the chain.
- In the case of buy-in chains, affected counterparties should be able to pass-on the buy-in costs along the chain. This will avoid multiple buy-ins being executed off the back of a single insufficient settlement. It still needs to be established how this could work where CCPs are part of the chain.
- In the case of securities financing transactions, as much as possible, the near-leg of the transaction should remain exempt from mandatory buy-ins. (The issue of mandatory buy-ins and SFTs is covered in more detail in the Short-Term Markets section of this Quarterly Report.)
- Furthermore, in the case of both penalties and buy-ins, it will be necessary to know why a trade is failing (and who is at fault) before imposing a penalty or initiating a buy-in.

However, adopting some of these principles may be difficult in light of the Level 1 text, and the biggest challenge for designing and implementing effective settlement discipline mechanisms will be reconciling the market level impacts with what is essentially settlement level regulation.

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ICMA secondary market study

In July 2014, as an initiative of the Secondary Market Practices Committee (SMPC), ICMA commenced a study into the state of the European credit bond secondary market, with particular focus on the investment grade corporate and financial sectors. This is in response to increasing concerns about diminishing liquidity in the credit markets, as a result of both on-going regulation and the current low volatility and low interest rate environment.

The study is designed to be largely qualitative, focusing on interviews with key market participants, including credit trading desks, investment managers, trading platforms and other intermediaries, and issuers, as well as other market experts and commentators.

As well as highlighting the challenges and concerns, the study aims to present a picture of the responses of various participants to the changing landscape and to identify potential opportunities, as well as to promote deeper discourse around the issue of secondary market liquidity.

The study will be completed, and a report of the findings is due to be published this autumn.

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Asset Management

by Dr. Nathalie Aubry-Stacey

Shadow banking and asset management

AMIC members have been discussing shadow banking for some time. The term "shadow banking" is still perceived as very negative by members, a preferred alternative term being "market finance". It is market-based because it decomposes the process of credit intermediation into an articulated sequence or chain of discrete operations typically performed by separate specialist non-bank entities which interact across the wholesale financial market. Shadow banking relies on active secondary markets in order to be able to price assets and relies on the wholesale financial market for funding. The use of the "shadow banking" term reflects the fact that debate has been so far shaped by model thinking – through the lens of banking supervision and the prudential regulatory tool-kit. It also ignores the fact that many "shadow banking" entities and activities are already highly regulated under securities legislation, and afford much protection to investors.

The AMIC Council has been particularly interested in shadow banking in light of the Basel III reforms and their direct impact on traditional banking structures, and indirectly on the asset management industry. In fact, the AMIC Council meeting to be held on 29 October in London will be focusing on the role of the industry in the new banking order.

The AMIC still believes that a key step in the "shadow banking" discussion is to clarify the type of activities understood under this term. The next FSB/IOSCO Consultation Paper – looking at non-bank non-insurance SIFIs – should be reviewing this in more detail. Regulating different products in the same way in itself creates systemic risk. Moreover, the AMIC would like to ensure that recommendations of regulatory reforms take into account current regulatory developments and their impact on the asset management industry; and avoid regulatory overlaps. Problems may result from dual regulation, whether at an EU or global level.

New policy initiatives need to take account of the function of some market finance activities in protecting the end-investor. In fulfilling their fiduciary duty towards their clients, investment managers carefully manage their counterparty exposure to banks. Investment management is an agency-based model where capital controls *de facto* restrict the performance an investment manager can return to his client. Reduced performance on an on-going basis leads to the erosion of savings and retirement income in the long term, which is contrary to wider public policy goals of encouraging savings and stimulating consumption and growth. Fund management activities are governed by extensive sets of rules requiring appropriate authorisation and prudential supervision of the fund manager and, in most instances, also authorisation and marketing notification of each single investment fund.

An AMIC Working Group will review the work that is being done by regulators and its potential impact on the industry – including a discussion of leverage limits, the risks of herding and possible regulatory obstacles to current trading activities.

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Covered bond transparency

The ICMA Covered Bond Investor Council (CBIC) has recently published a report on transparency in the covered bond market.

A couple of years ago, CBIC published a template which served as a forerunner of the national transparency templates which have now been put in place in many jurisdictions. Unfortunately, none of these is identical to the CBIC template, as national covered bond markets have many specific details, but hopefully the original CBIC template proved a useful guide in their development.

Disclosure in the covered bond market is still worse than in the securitisation market, as the ABS sector has pointed out. But there are perfectly valid reasons for this, such as the revolving pool (which slightly detracts from the relevance of current pool data) and

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It is difficult to keep track of the mushrooming of investor protection features.

the greater investor protection provided both in law and in contract.

However, the report explains that several investors noted that it is difficult to keep track of the mushrooming of investor protection features. For example, who has a voluntary over-collateralisation clause? Which issuers have rating triggers on their swaps? It takes time to find out. So the first recommendation of the report is to set up a single place where each individual programme's structural details are disclosed in a format which is easy to understand. Obviously, this will be more relevant in some jurisdictions than others. For countries with highly prescriptive laws this will be little more than the ECBC's existing database comparing those laws. But even in those countries, contractual add-ons are increasingly the norm.

This data are often really difficult to access. The covered bond label initiative and the national transparency templates are two steps in the right direction. But each template is in its own format and not every covered bond is labelled, either by choice or by exclusion. A place where all of this data is easily accessible would be a practical help for some investors. But it would also lead on to something else: analytical tools.

How much exposure does a portfolio have to a particular swap counterparty? Or to a 10% fall in house prices across Europe? Or a 1% rise in interest rates? Investors in the ABS market have a plethora of tools at their disposal to answer this type of question. Covered bond investors have none. Again, cover pool credit is less important than for the ABS market. But clearly it is growing in importance, there are more cross-over investors who will demand this type of information, the Resolution Directive is shifting the balance of credit analysis towards fundamentals and, as paragraph 129(7) of the CRR shows, there is an increasing onus on investors to undertake fundamental credit analysis.

The CBIC will take these recommendations forward in the period ahead, involving all market participants – and interacting with regulatory authorities with an interest in better transparency in the market.

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Reducing reliance on CRAs in asset management

The IOSCO Consultation Paper on reducing reliance on CRAs in asset management pointed to concerns that financial institutions and institutional investors may be relying too much on external ratings and questioned to a certain extent internal credit risk assessments and the soundness of procedures in place. The AMIC response pointed out that this over-reliance can partly be explained by the fact that ratings have been increasingly woven into the fabric of international, European and national laws, regulation and private contracts. As legal requirements for ratings have proliferated, rating agencies have evolved in effect from information providers to purveyors of "regulatory licences".

The AMIC response reiterated that credit rating agencies provide an assessment of the creditworthiness of a corporation or security, based on the issuer's quality of assets, existing liabilities, borrowing history, and overall business performance. Investors look at ratings to predict the likelihood of default on financial obligations and the expected repayment in the event of default. As corporations require more capital and issue debt to the public at large, standardised information about the creditworthiness of issuers whom investors do not know themselves, or with whom they do not have a personal relationship, needs to be made available.

Whilst it is true that investors will consider external credit ratings before investing and throughout the life of their investments – and will establish guidelines to direct investment managers as to the types of instruments that investors wish their fund or managed account to be invested in – most institutional investors do not rely exclusively on ratings.

Many institutional investors are legally obliged to hold only securities of some minimum rating, or may have to hold larger reserves when investing in bonds of lower ratings. Ratings are also used in private contracts, for example to define the investment objectives of bond mutual funds. Accordingly, the AMIC believes that regulatory use of ratings has exacerbated procyclicality in the financial system as a whole. However, in order to reduce private reliance on ratings, credible alternatives or substitutes need to be developed, particularly for institutions that lack resources to assess independently the huge number of available fixed income instruments. The AMIC believes that it is perfectly rational for individual firms and institutional investors to be guided by a rating when making their investment decisions, as long as the quality and integrity of ratings are maintained.

One of the main concerns, as already highlighted in the IOSCO Code, is the assurance of quality and integrity in the rating process, so that the credit rating agencies can fulfil their task of dissolving information asymmetry on the market. A methodical and transparent procedure of compiling the rating product has an important role in ensuring consistent quality and integrity of ratings. Each prognosis can

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Ratings have been increasingly woven into the fabric of international, European and national laws, regulation and private contracts.

only be as good as the data upon which it is based. The assurance of the quality of a rating also requires that the agencies satisfy high professional standards in the training of their personnel.

The AMIC is of the view that the IOSCO good practices should maintain the public-good aspects of credit ratings to avoid unintended consequences such as increased costs and reduced access to capital markets. The current regulatory framework is so reliant on ratings that significant changes can only take place over time. Mandates to use ratings have become part of the fabric of financial markets, and cannot be unwoven instantaneously.

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Securitisation and the buy side

At its most recent meeting, the AMIC Executive Committee approved the setting up of the Securitisation Working Group on the buy side to work alongside the ICMA Covered Bond and Investor Council.

Securitisation, the process in which certain types of assets are pooled so that they can be repackaged into interest-bearing securities, has been an important funding tool in Europe and a channel for borrowers to access the capital markets. Traditionally, it has contributed to funding real economy assets such as residential mortgages, auto loans and SME lending and other assets.

At a time when businesses and households across the EU are experiencing difficulties in accessing finance, securitisation could improve the availability of credit, by allowing banks to free up their balance sheets for further lending. However the securitisation market in the EU continues to be impaired. Public issuance of Asset-Backed Securities (ABS) remains very limited and mostly concentrated in a few jurisdictions.

Many initiatives both from the market and regulators have tried to revitalise the securitisation market. These include:

- The "*skin in the game*" concept: Since 2011 EU lenders are required to retain a share of the resulting ABS, which should motivate them to securitise better quality assets.
- The *CRR* requires that originators apply the same underwriting criteria to loans which are securitised as those applied to loans that remain on the balance sheet,
- Changes to the *Mortgage Credit Directive* should improve underwriting standards across the EU.
- *Loan-by-loan reporting* requirements in the Eurosystem – improved levels of transparency.
- The EBA was tasked by the European Commission with *defining High Quality Securitisation (HQS),* which will affect HQS treatment under CRD IV and LCR.
- Market initiatives have tried to revive the securitisation market in Europe, eg through the *Prime Collateralised Securities* (PCS) securitisation labelling project which identifies market best practices in terms of securitisation quality, transparency and simplicity/standardisation, leading to improved secondary market liquidity.

The securitisation capital framework is currently being overhauled at European and international level. At the same time investors are called upon to contribute to the real economy. However, political discourse does not always match the new regulatory realities. For instance, the European Commission proposals implementing capital requirements in Solvency II, due to be published shortly, are expected to put heavy capital charges on subordinated securitisation (but not on the most senior tranche of an ABS deal). It is worth noting that the European Commission is at odds with the industry and central banks which attempt to identify entire deals rather than single tranches as good quality securitisation.

The buy side will have to be in a position to respond to both regulatory realities and political discourse, whilst managing to fulfil their own regulatory requirements and provide the best service to their clients. The Working Group intends to represent all the interests of the buy side, including institutional investors and asset managers, as different regulatory initiatives affect them. The first meeting of the working group is scheduled to be held in the course of October.

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Bail-in

by Katie Kelly

ICMA's Bail-in Working Group, which consists largely of investors and regulators, focuses on the impact of the impending bail-in regime for financial institutions on investors in securities issued by banks. Amongst the various specific items that the Working Group considers are the practical implications and technical operation of the bail-in regime. In this context, this will include consideration of the EBA's Guidelines on recovery and resolution, and the EBA's consultation on two draft guidelines on (i) the triggers for using early intervention measures (triggers for early intervention) and on (ii) the circumstances under which an institution shall be considered as "failing or likely to fail" (triggers for resolution).

The consultation is addressed to competent authorities and clarifies the conditions for using early intervention measures foreseen by the Bank Recovery and Resolution Directive (BRRD). It aims to ensure a continuum between the on-going supervision conducted by national authorities in line with the Capital Requirements Directive (CRD) and the BRRD by promoting convergence of supervisory and resolution practices in relation to how resolution should be triggered and how to apply early intervention measures.

The Working Group recently responded to the Bank of England Consultation Paper on the *FPC Review of the Leverage Ratio*, which sets out the FPC's analysis on the policy choices that would determine the role of a leverage ratio in the capital framework in the United Kingdom. The responses to the Consultation Paper are expected to inform the final review intended to be published by the FPC by November 2014.

In general terms, the response highlighted that there is insufficient information available about regulatory triggers, levels of capital, "bail-inable" debt and the valuation methods that might be employed when assessing the need for, and quantum of, bail-in, so debt investors are currently struggling to price bank risk. Debt investors are therefore concerned about transparency and adequate disclosure, and will require adequate disclosure to enable them to evaluate and measure the risk of potential impending failure and, therefore, bail-in. And in the absence of such information, debt investors will not be in a position to analyse and, therefore, price the risk properly.

With respect to the composition of the leverage ratio, the response stated that not only should there be clarity and simplicity in any leverage ratio imposed, but that it also needs to be simple to analyse and understand. Additional complexity in designing the leverage ratio is probably not helpful.

The response also clarified that the more subordinated, but higher yielding instruments such as Cocos are very hard to value and there is currently no agreed methodology employed by the market. Therefore, the impact of leverage and overall capital requirements on the pricing of bank debt is unclear given the many areas of uncertainty and the several distorting influences in the primary bond markets.

The Bail-in Working Group continues to attract a lot of interest and, with implementation of the bail-in mechanism being key, we expect that its output will continue to grow.

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Investors are concerned about transparency and adequate disclosure, and will require adequate disclosure to enable them to evaluate and measure the risk of potential impending failure and, therefore, bail-in.

Pan-European Private Placement Initiative

by Nicholas Pfaff

Coordinated by ICMA, the Pan-European Private Placement Working Group (PEPP WG) includes the Association for Financial Markets in Europe (AFME), the Association of British Insurers (ABI), the European Private Placement Association (EU PPA), the French Euro Private Placement (Euro PP) Working Group, the Investment Management Association (IMA) and the Loan Market Association (LMA). It also brings together representatives from leading institutional investors (Delta Lloyd, Federis Gestion d'Actifs, KBC Group, LGIM, M&G Investments, Natixis Asset Management) and observers from the official sector (including the Banque de France and HM Treasury). It also benefits from the support of major law firms, including Allen & Overy, CMS, Herbert Smith, Kramer Levin, Linklaters, Simmons & Simmons, Slaughter & May and White & Case.

As reported, the main objective of the PEPP WG is to promote the development of a dynamic Pan-European Private Placement (PEPP) market. As a key part of this effort, the PEPP WG will publish a European Guide to best practice designed to represent substantial progress towards common market practices, principles and standardised documentation. The target is to publish the first edition of the European Guide by end-2014/early-2015. The Guide builds on the Charter for Euro Private Placements developed by the French Euro PP Working Group, a French financial industry initiative. The PEPP WG will also aim to identify barriers to entry for new issuers and investors into this market.

In order to coordinate and progress the various workstreams that arise from the Guide and more generally from the agenda of the PEPP WG, four Sub-Working Groups (SWGs) were constituted in July 2014. The SWGs are as follows:

- *Market positioning and practices:* This SWG aims to make clear the positioning of the PEPP in relation to domestic PP markets (eg US PP, Euro PP and Schuldscheine), listed debt markets and the loan market. It will also reflect on the branding of the PEPP product.
- *Documentation:* This SWG focuses on the development of a jurisdiction and format (loan or note) neutral term sheet incorporating key standard terms and covenants for PEPP transactions. This term sheet will then be included in the first version of the Guide. In parallel, the Documentation SWG will also coordinate standard loan and note documentation for the PEPP market in close consultation and building on the work of the LMA and the French Euro PP WG.
- *Solvency II:* This SWG will work on the treatment of PEPPs under Solvency II and, amongst others, on the pertinence of a scoring system comparable to the one used in the USPP market (credit scoring provided by the National Association of Insurance Commissioners (NAIC) serving as an alternative to credit rating and with a recognised regulatory treatment).
- *Tax:* This SWG will investigate the tax treatment of PEPPs in the relevant European jurisdictions, focusing especially on withholding taxes. This could lead to a future dialogue with national tax authorities.

The work of the first two SWGs has already led to important progress in confirming the positioning and practices of the PEPP product and market. The PEPP has been defined by the Working Group as financing in the form of medium to long-term senior debt obligations (either in the form of a note or a loan), generally at fixed rate, negotiated with and issued privately to a small group of professional investors. The PEPP will normally be an unlisted and illiquid instrument designed for institutional investors with a buy-to-hold strategy, but will be nonetheless be a registered and transferable security. The PEPP will particularly benefit medium-sized and unrated companies by providing long-term debt funding which may not otherwise be available to them from the loan or bond markets. It may serve in this way as an intermediary and preparatory stage for these companies before they gain access to the public debt markets. The PEPP market will also be able to accommodate larger corporate issuers as the case may be. Intermediaries and arrangers in the PEPP market will typically have an agency rather than an underwriting role.

The PEPP should therefore not be confused with forms of public debt market financing that have other characteristics and/or target issuers, but that may also be "privately placed" to individual or small groups of institutional investors, as in the case for example of reverse enquiry EMTN transactions.

Overall, the activities of the PEPP WG are now on track as a coordinated financial industry initiative designed to boost the emergence of a new market directly targeted at the European corporate sector. This is also in line with the European Commission's recent *Communication on Long-Term Financing of the European Economy* which recognises the potential of the private placement market to provide a significant alternative funding source to European medium-sized companies, and the importance of facilitating its development.

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Market Infrastructure

by David Hiscock

ECB: Contact Group on Euro Securities Infrastructures (COGESI)

The summary of discussions at the 17 June meeting of COGESI (on the "meetings" tab) was made available during July, together with two presentations from the meeting – "COGESI reports: Conclusions and proposed next steps"; and "Impact of regulatory requirements on CCPs" – which relate to the two major meeting discussions covered at items 2 and 3 in the summary. The summary includes five "follow-up" points, the first four coming under item 2 and the fifth under item 3:

- The ECB will present further considerations at the next COGESI meeting on how to monitor the impact of regulatory requirements, market developments and infrastructural improvements on collateral supply/demand/availability. These considerations will include the velocity/re-use of collateral and the monitoring of such activity (members of (I)CSDs/custodians will be contacted individually).
- ECSDA will prepare an overview/table on CSD link operating hours by the next COGESI meeting.
- ERC/EBF/(I)CSDs will provide an update on CoBM developments in the next COGESI meeting (on dissemination/promotion of the recommendations and Bridge).
- TSI parties will provide an update in next COGESI meeting on the TSI model and timeline for implementation.
- It should be verified if/how EU regulators organise a dialogue with market stakeholders on implications of regulatory requirements. COGESI members supported the organisation of a workshop involving authorities and market participants to clarify the objectives regulatory requirements, the tools/market solutions to fulfil regulatory objectives, and the impact of certain rules.

The next COGESI meeting will take place on 25 November 2014.

Also, as of 29 September 2014, triparty collateral management services offered by triparty agents (TPAs) on a cross-border basis are being supported via the Correspondent Central Banking Model (CCBM), subject to the respective TPAs having been approved as eligible for use in Eurosystem credit operations.

ECB: Money Market Contact Group (MMCG)

A regular quarterly meeting of the MMCG was held in Frankfurt on 9 September 2014. The agenda included (i) Review of the main findings of the euro Money Market Survey; (ii) Review of the latest market developments and other topics of relevance; (iii) Single Supervisory Mechanism (SSM): supervisory set-up and impact on the euro money market; and

Collateral

Three new reports promoted by the Ad-hoc Group of COGESI on Collateral (composed of members of COGESI and the MMCG) were published on 7 July 2014.

1. *Collateral Eligibility and Availability: Follow-up to the Report on Collateral Eligibility Requirements - a Comparative Study across Specific Frameworks*: COGESI, building on its July 2013 report on *Collateral Eligibility Requirements Across Various Frameworks*, has set out to qualify the overall supply of high-quality collateral assets in the current new report and to examine what portion of this supply is effectively available and usable for financial institutions. Estimations in this respect are derived from various studies on the global supply of collateral assets for financing arrangements. This new report in particular explains that a non-negligible portion of the overall supply of high-quality assets is not available for use as collateral, and not all of the available collateral is usable due to certain securities settlement limitations. Accordingly, the report aims to establish the level of the "real supply" of collateral in the market.

2. *Euro Repo Market: Improvements for Collateral and Liquidity Management*: Market participants in COGESI, and in particular those active in the repo market, have expressed the need for enhancements to existing settlement arrangements to better support collateral and liquidity management activities. Although a number of changes will be implemented with the go-live of T2S, additional improvements beyond T2S would allow the repo market to better support the mobilisation of collateral throughout the day. These improvements complement earlier initiatives stemming from the work of the Giovannini Group related to the integration of European clearing and settlement markets. This report sets out the objectives and specific measures for achieving a consistent and integrated market for securities clearing and settlement in the euro area. The objectives are twofold: first, to facilitate a more efficient mobilisation of collateral, in particular on a cross-border/cross-system basis in the euro area; and second, to facilitate the use of collateralised transactions at end-of-day for treasury adjustment operations. To meet these objectives, a set of actions are proposed together with a more detailed set of recommendations and principles to facilitate implementation. Progress on the deliverables will be regularly monitored by the ECB, via the COGESI forum, to ensure that the proposed actions are implemented in a timely manner and consistent with the related recommendations set out in this report.

3. *Improvements to Commercial Bank Money (COBM) Settlement Arrangements for Collateral Operations*: The objective of this report (prepared based on input from a joint group of ERC and EBF members) is to explore current settlement practices in commercial bank money (COBM) and propose recommendations to support "better use of collateral", in particular to remove structural constraints and inefficiencies in the settlement of collateral operations in COBM. In doing so, the report focuses on trades with same-day (T+0) settlement of securities, which is required for the daily management of liquidity, resources (cash/securities) and collateral.

(iv) Main developments in the FX swap market. The next regular quarterly meeting is scheduled for 21 November 2014.

ECB: Bond Market Contact Group (BMCG)

The BMCG's seventh meeting took place in Frankfurt on 1 July 2014. Alongside the summary of discussions five presentations from the meeting are available: "Item 1 - Bond Market Outlook"; "Item 2, part I- Some considerations on market making and trading"; "Item 2, part II - Addressing the Liquidity Challenge"; "Item 3 - Demand for sovereign bonds: The importance of diversity"; and "Item 4 - SSM Comprehensive Assessment - Key issues from a market perspective". The next regular quarterly meeting is scheduled for 21 October 2014.

ECB: TARGET2-Securities (T2S)

On 1 July 2014, pilot testing started according to schedule. The pilot testers are three CSDs of the first migration wave, namely Bank of Greece Securities Settlement System (BOGS), Monte Titoli and SIX SIS, as well as six national central banks (NCBs – Banque de France, Bank of Greece, Banca d'Italia, Nationale Bank van België/Banque Nationale de Belgique, Deutsche Bundesbank and Banco de España).

The Eurosystem Acceptance Testing (EAT) continued in parallel to the pilot testing and successfully led to confirmation that the Eurosystem is ready to start user testing as scheduled on 1 October 2014. The decision was made at the meeting of the T2S Board on 29 August 2014, based on, among other things, an assessment of the results of the EAT. The purpose of this testing phase was to ensure that the T2S platform is of the required quality

“ The T2S platform is of the required quality and compliant with the scope-defining documents.

and compliant with the scope-defining documents. Defects identified during the EAT were not considered critical and are being resolved.

The Directly Connected Parties Group (DCPG) is composed of representatives of directly connected parties (DCPs), central securities depositories (CSDs), central banks and the T2S Programme Office. The primary role of the DCPG is to track and monitor the resolution of general concerns relevant to DCPs in their capacity as CSD/NCB customers with a direct connection to T2S. *A Discussion Paper on Cash and Collateral Aspects related to TARGET2-Securities*, dated 14 July 2014, has been highlighted by the DCPG as a key paper. The DCPG is also maintaining a register of its open issues.

The T2S Advisory Group (AG) publishes an annual report on the progress made by T2S markets in implementing the T2S harmonisation standards, which aim at fostering the safety and efficiency of cross-CSD settlement in T2S; and contribute to the EU agenda on financial integration and to the improvement of the competitive environment. A mid-year update, dated 15 July 2014, is an extra publication that the AG has considered important to release before T2S user testing starts on 1 October 2014. This publication is aimed at (i) reporting what is new in the T2S harmonisation work since March 2014 and (ii) identifying new potential deviations from the standards that have become known lately within the T2S community of stakeholders.

The T2S Cross-border Market Practice sub-group (X-MAP) met on 8-9 July 2014 and 9 September; and will next meet again on 16 October. These X-MAP meetings include discussions relating to “CSD Restriction Rules”, on which XMAP’s interim report was delivered to the T2S Harmonisation Steering Group (HSG) for its June meeting. After a long dormant period, on request of the HSG, the T2S Message Standardisation sub-group (MSSG) was invited to give an opinion on the standardisation of the T2S optional matching field contents. This matter was considered in an 8 July 2014 teleconference and a summary, including the MSSG’s conclusions, was published.

Dated 15 July 2014, *Frequently Asked T2S Functional Questions*, was added to the T2S knowledge based repository. This answers to questions regarding access rights, billing, collateral, connectivity, instructions, matching, queries, reports, static data and validation. Dated September 2014, *T2S: Intra, Cross- and External-CSD Settlement Configuration* was added, which aims to address (i) which elements have to be configured for settlement in T2S?; and (ii) how to configure settlement functionality.

The publication of a new issue of *T2S OnLine* was announced on 29 July 2014. In his editorial, Jean-Michel Godeffroy, Chairman of the T2S Board, explains the motivation behind the recent organisational changes within the ECB in the area of market infrastructures and payments. Contents include a comprehensive update on the T2S project, provided by Marc Bayle, Director General Market Infrastructure and Payments; report of a discussion with Paul Bodart, member of the T2S Board, about Europe's new settlement cycle T+2; a summary of the technical session on T2S user testing and migration that took place on 25 June; and an interview with representatives of CSDs and NCBs, providing insight into their preparations and expectations as pilot testers.

T2S Special Series Issue No 4, *T2S: From Issuer to Investor*, was published in September 2014. For the first time, this issue sheds light on the changes expected along the securities chain from issuer to investor as a result of T2S. Those most affected by these changes are given the floor, with views being provided by representatives of issuers, investors, banks, CSDs, and one CCP. The 13 respondents answer specific questions, for example on how issuer services offered by banks and CSDs, and the relationship of banks and CSDs with issuers, are going to change with T2S; or on how T2S will impact the interactions and relationships between investors and their intermediaries.

Global Legal Entity Identifier System (GLEIS)

As reported in Issue 31 of the ICMA Quarterly Report, a note published by the LEI ROC, dated 27 July 2013 (updated 24 August 2014), establishes the principles that should be observed by the Local Operating Units (LOUs) participating in the Interim GLEIS as pre-LOUs. Adding to earlier cases, ROC notes of 22 July 2014, 10 August and 26 August announced the endorsement of further pre-LOUs in accordance with the process described in Annex 1 of the principles. There is a list of the ROC endorsed GLEIS pre-LOUs (operational) and also a broader list of four digit prefixes allocated to sponsored pre-LOUs.

On 24 August 2014, the LEIROC published a note providing additional guidance for portability of LEIs among endorsed pre-LOUs. Endorsed by the ROC, these recommendations have been prepared by the Committee on Evaluation and Standards; and have benefited from input and feedback from pre-LOUs. It is emphasised that an entity should only acquire an LEI if it does not already have one. If an entity wishes to register with a pre-LOU other than the one with which it originally registered, it should request the desired pre-LOU to initiate an action to port the maintenance of the entity's reference data from the original pre-LOU to the new one. In this process, the LEI itself, including the four-digit prefix assigned to the pre-LOU that originally registered the entity, will remain unchanged.

In Issue 34 of the ICMA Quarterly Report, there was a report of the inaugural meeting of the Global Legal Entity Identifier Foundation (GLEIF). On 24 August 2014, the full text of the statutes of the GLEIF (dated 26 June 2014) was made available.

BIS: Committee on Payments and Market Infrastructures (CPMI)

At their meeting in June 2014, the Central Bank Governors of the Global Economy Meeting (GEM) endorsed a new mandate and charter for the Committee on Payment and Settlement Systems (CPSS); and also decided to rename the CPSS as the CPMI. These changes, which became effective on 1 September 2014, align the name and mandate of the Committee more closely with its actual activities; but do not affect the way the Committee operates, its membership and responsibilities. The CPMI's primary task is to promote the safety and efficiency of payment, clearing, settlement and related arrangements, thereby supporting financial stability and the wider economy. Comprising senior officials from 25 central banks, the Committee monitors and analyses developments in these arrangements, both within and across jurisdictions. It also serves as a forum for central bank cooperation in related oversight, policy and operational matters, including the provision of central bank services. The CPMI is a global standard setter that aims at strengthening regulation, policy and practices in this area worldwide.

A report, *Developments in Collateral Management Services*, published on 9 September 2014 by the CPMI, describes how collateral management services are changing in an effort to address expected increases in demand for collateral. It provides an overview of the variety of approaches being undertaken by many of the service providers to furnish customers with better tools to monitor their securities holdings and increase efficiencies in the deployment of those securities. While the report identifies a number of benefits resulting from the ongoing innovations, it also highlights that proposed services have led to increased complexity and operational risks – which both the public and private sectors need to understand, monitor and appropriately manage.

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Macroprudential Risk

by David Hiscock

On 8 July 2014, the EBA published an opinion on the macroprudential tools laid down in the CRR and CRDIV. This opinion assesses whether the current rules are effective, efficient and transparent as well as the possible degrees of overlap across different macroprudential tools and the consistency of the EU framework with global standards. The opinion also includes policy recommendations that the European Commission should consider in its review of the macroprudential toolkit. Besides addressing improvements to a number of rules, the EBA recommends that the different authorities involved in the deployment of macroprudential measures coordinate their actions and that the hierarchy in the activation of the different macroprudential instruments is clarified. The advice provided by the EBA will inform the European Commission, who will report to the European Parliament and the Council on these rules by the end of 2014, and where appropriate, submit a legislative proposal to the European Parliament and the Council.

On 21 July 2014, the ESRB published its Annual Report 2013, covering the period from 1 April 2013 to 31 March 2014. The report includes a chapter reviewing systemic risks in the EU financial system in the reporting period, a chapter on work done by the ESRB on the operationalisation of macroprudential policy, and a final chapter on the implementation of the ESRB recommendations and accountability.

Liquidity Trap and Excessive Leverage is an IMF staff working paper, published on 21 July 2014, in which the role of macroprudential policies in mitigating liquidity traps driven by deleveraging is investigated. When constrained agents deleverage, the interest rate needs to fall to induce unconstrained agents to pick up the decline in aggregate demand. If, however, the fall in the interest rate is limited by the zero lower bound, aggregate demand is insufficient and the economy enters a liquidity trap, but welfare can be improved by *ex ante* macroprudential policies such as debt limits and mandatory insurance requirements. In the authors' model, contractionary monetary policy is inferior to macroprudential policy in addressing excessive leverage, and it can even have the unintended consequence of increasing leverage.

The ESRB and National Macroprudential Measures – its Role and First Experiences was published on 22 July 2014. This commentary first describes the general framework for notifications of national macroprudential measures to the ESRB. It then considers the measures that have been notified and subsequently published on the ESRB's website in the period from January to June 2014, most of which relate to capital measures and, in particular, the use of the systemic risk buffer. The commentary concludes by making some general observations on the first set of published notifications.

Real and Financial Vulnerabilities from Cross-border Banking Linkages is an IMF staff working paper, published on 25 July 2014, which looks at the vulnerabilities stemming from banking sector linkages between countries and their macroeconomic effects.

It finds that credit risks (from a banking system's claims on other countries) and funding risks (from a banking system's liabilities to another) have declined over the past five years; and finds that funding vulnerabilities have real effects. The results indicate that policy makers should pay more attention to understanding cross-border funding risks.

Macroprudential Frameworks: (too) Great Expectations?, by Claudio Borio, Head of the Monetary and Economic Department of the BIS, was published on 5 August 2014. In this, macroprudential frameworks are welcomed as a response to the Great Financial Crisis; but it is noted that macroprudential measures are still very much work in progress. Much scope remains for improving the range of tools available, refining the balance between rules and discretion, and strengthening governance arrangements, both nationally and internationally. Moreover, the experience so far indicates that it would be imprudent to rely solely on macroprudential frameworks when seeking to tame financial booms and busts; and that other policies, not least monetary and fiscal, should also play a role. So, whilst macroprudential frameworks must be part of the answer they cannot be the whole answer.

Macroprudential Policies to Mitigate Financial System Vulnerabilities is an IMF staff working paper, published on 19 August 2014, which analyses how changes in balance sheets of some 2,800 banks in 48 countries over 2000–2010 respond to specific macroprudential policies. Controlling for endogeneity, the authors find that certain measures aimed at borrowers and at financial institutions are effective in reducing asset growth. Countercyclical buffers are little effective through the cycle, and some measures are even counterproductive during downswings, serving to aggravate declines, consistent with the *ex ante* nature of macroprudential tools.

Capital flows and Macroprudential Policies - A Multilateral Assessment of Effectiveness and Externalities is an ECB working paper, published on 20 August 2014, which assesses the effectiveness and associated externalities that arise when macroprudential policies (MPPs) are used to manage international capital flows. Using a sample of up to 139 countries, the authors examine the impact of eight different MPP measures on cross-border bank flows over the period 1999-2009. The results indicate that the structure of the domestic banking system matters for the effectiveness of MPPs and it is found that spillover effects can occur.

Identifying Excessive Credit Growth and Leverage is an ECB working paper, published on 21 August 2014, which aims at providing policy makers with a set of early warning indicators helpful in guiding decisions on when to activate macroprudential tools targeting excessive credit growth and leverage. By using credit to GDP gaps, credit to GDP ratios and credit growth rates, as well as real estate variables in addition to a set of other conditioning variables, the model is designed to not only predict banking crises, but also to give an indication on which macroprudential policy instrument would be best suited to address specific vulnerabilities.

Filling in the Blanks: Network Structure and Interbank Contagion is a BIS working paper, published on 27 August 2014, which explains that the network pattern of financial linkages is important in many areas of banking and finance. Yet bilateral linkages are often unobserved, and maximum entropy serves as the leading method for estimating counterparty exposures. It proposes an efficient alternative that combines information-theoretic arguments with economic incentives to produce more realistic interbank networks that preserve important characteristics of the original interbank market. Using

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Macroprudential frameworks are welcomed; but it is noted that macroprudential measures are still very much work in progress.

the two benchmarks side by side defines a useful range that bounds the cost of contagion in the true interbank network when counterparty exposures are unknown.

As announced on 3 September 2014, ESMA has published its *Report on Trends, Risks and Vulnerabilities No. 2, 2014* and the *Risk Dashboard for 3Q2014*. Overall, ESMA's report finds that valuation risks in key market segments are rising and merit investor attention; yet in the first half of 2014, conditions in the EU's securities markets, asset management industry and market infrastructures remained favourable. Prevailing optimistic market sentiment was at odds with sluggish underlying economic fundamentals, but in line with the ultra-low interest rate environment. Key developments are noted as being:

- *Securities markets:* EU securities markets realized significant gains amid low volatility, underscoring positive market sentiment in a low interest rate environment – which motivated investors to search for yield. Risk appetite remained strong as yields continued to compress and solid high-yield bond issuance was readily absorbed by markets – prompting increased valuation concerns alongside risks of future volatility.
- *Asset management:* the European fund industry continued to expand, partly due to capital inflows, with assets under management growing by about 6.7% (≈ €0.5 trillion) in 1H2014. Investment fund returns were relatively low, but moving up slightly on positive valuation effects. Allocations focused on bonds, notably high-yield and corporate bonds; with investors searching for yield. With an active primary bond market, potentially fewer market makers could limit the functionality of secondary bond markets.
- *Market infrastructures:* activity in trading venues increased strongly before easing off from May onwards; and volumes of securities settled by CSDs were broadly flat before tailing off somewhat in late 1H14. Benchmark panels reported limited withdrawals, but even these decreased as administrators introduced reinforced governance rules.

ESMA also monitors market developments which may present future vulnerabilities. This latest report provides an in-depth analysis of four topics:

- Trading venue developments, operational risk and new challenges;
- The systemic relevance of securities financing markets in the EU;
- Performance and risks of ETFs; and
- Crowdfunding.

The ESRB's General Board held its 15th regular meeting on 18 September 2014. The ESRB General Board discussed risks and vulnerabilities in the global financial system, focussing on the challenges posed by the persistently sluggish recovery and risks from the continued search for yield. It noted that any unravelling of this search for yield could prompt a sharp re-pricing of risk, which could be amplified by low market liquidity in key market segments. The Board also considered developments in those EU Member States that encountered banking sector problems during the summer and took note of possible implications of developments in Ukraine. In addition:

- The ESRB General Board approved an ESRB response to a public consultation by ESMA relating to those classes of OTC credit derivatives that should be subject to CCP clearing;
- The ESRB General Board took note of the report by the European Commission on its review of the ESRB; and
- The ESRB General Board published the ninth issue of the risk dashboard.

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ICMA in Asia-Pacific

by Mushtaq Kapasi

Introduction

Since launching its Asia-Pacific representative office in Hong Kong in September 2013, ICMA has continued to strengthen ties with members, regulators, central banks, intermediaries, and infrastructure providers in the region.

During ICMA's recent discussions in Asia, three common themes have emerged: (i) financial liberalisation, particularly in China; (ii) growth in intra-regional investment and cooperation; (iii) demand for new products to finance infrastructure development and trade. ICMA's own efforts to develop efficient, liquid and well-governed cross-border capital markets across the Asia-Pacific region directly complement these trends.

In Asia, as in other regions, ICMA's main focus will continue to be on international debt capital markets and repo. ICMA has promoted fruitful dialogue between Asia and Europe on emerging reforms and good practices in both regions, and is active in international efforts to avoid regulations that have unintended or contradictory consequences across borders into Asia.

Asian primary markets

Over the last year, ICMA has held four Asia debt syndicate meetings, attended by leading Asian underwriters from global and regional banks. The subjects covered have included investor meetings, order book transparency, pricing iterations, allocations, stabilisation, and the dynamics and risks of a growing market. ICMA has also held three meetings of Asian legal, documentation, and transaction managers, complementing the work of the syndicate meetings with an emphasis on regulations, compliance, contracts and disclosure. Discussions have echoed to some extent many of the topics arising in the ICMA Primary Market Practices Committee and the ICMA Legal and Documentation Committee, but have also shed a light on some areas where Asian perspectives and dynamics differ.

Overall, the ongoing revisions to the ICMA Primary Market Handbook (PMH) are being closely watched by Asian market professionals. The PMH covers internationally syndicated primary debt capital markets offerings, generally excluding high-yield and equity-linked transactions. Although the PMH often does not apply to US dollar-denominated transactions, in Asia the distinctions among G3 issuances are more fluid, and many of the principles and standard provisions of the PMH are followed in cross-border transactions denominated not only in euro, but also in Japanese yen and US dollars. In addition, many of the long-standing principles and standard clauses of the PMH have been borrowed and adapted to local Asian capital markets.

Also, ICMA has had extensive dialogue with China's National Association of Financial Market Institutional Investors (NAFMII) to aid in the development of standards in the onshore interbank bond market as this market continues to grow in volume, attract new entrants, and diversify its products.

Repo

The repo markets in Asia, both local and cross-border, are growing quickly, but remain relatively small and disjointed due to the variety of regulatory regimes and market dynamics. The adoption of international practices and increased use of standard documentation would improve liquidity, collateral risk, and market transparency. Asian repo market participants recognize ICMA's leadership in global market knowledge, regulatory expertise, underlying opinions and documentation. ICMA is organising a number of GMRA and repo workshops in different centres across Asia designed to assist market participants to better understand the instrument and related documentation. The *ICMA ERC Guide to Best Practice in the European Repo Market* has been recognized as a useful model for market conventions in the cross-border Asian repo markets, and work is under way, in cooperation with regional associations, to adapt the Guide to Asia and its various domestic markets.

ICMA has worked closely with NAFMII over the last two years on repo as NAFMII created its own master agreement for the domestic China market, involving both pledge and true sale. ICMA has also led the development of GMRA legal opinions for many Asia-Pacific countries. However, enforcement for some of these is not robust, and work remains to be done to improve the relevant regulatory regimes and judicial procedures to enable more efficient markets. ICMA has renewed dialogue with national regulators to assist them in the development of regulations, infrastructure, and standard documentation relevant to repo in their domestic markets.

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UK-China Economic and Financial Dialogue

As part of the 6th UK-China Economic and Financial Dialogue, Vice-Premier Ma Kai and Chancellor of the Exchequer George Osborne agreed a number of areas of cooperation between the UK and China for the coming year. Both sides agreed that further cooperation between UK and Chinese financial services firms would benefit the development of China's capital markets, and welcomed the creation of a new private sector working group chaired by the ICMA and the National Association of Financial Market Institutional Investors of China (NAFMII).

The formal endorsement of the working group by the UK and China Governments marks a concrete step to further advance the Chinese market in a way that will benefit capital markets globally. By bringing together experts from financial institutions in London and China to share expertise on processes, market access and practices as well as the associated market infrastructure, the international input provided by this group will assist in further developing China's onshore bond market including Panda and local government bonds as well as the domestic ABS market, repo and sustainable finance.

Onshore bonds from foreign issuers

The market for onshore RMB issuance by foreign entities, also known as the "Panda bond" market, has drawn considerable interest from both China and Europe markets. Even though Panda bond issuance to date has been mainly supranational entities, many non-financial enterprises in Europe are interested to explore issuing bonds in onshore China. Panda bonds can potentially allow foreign issuers to fund Chinese operations directly without FX risk, diversify their investor base and liability profile, and obtain a first-mover advantage in an important and developing market.

There are several areas of potential improvement which would allow the Panda bond market to attract a wider universe of issuers. In particular, the market can benefit from more risk-based pricing, a broader investor base, a more streamlined and transparent regulatory review process, clearer disclosure and accounting requirements, and greater certainty on rating agency requirements and criteria.

China local government bonds

Financing for local government in China is an essential aspect of the nation's continued economic development. Local governments have raised funds through a variety of structures and markets, including bonds, bank loans, and more specialised asset-backed vehicles.

Policy makers in China have expressed their desire to promote the further development of the local government bond market in order to improve the transparency of local government debt and provide incentives to borrow more carefully. Ultimately, the goals of the market reforms should be to promote safer and more transparent borrowing by local governments, encourage a wider investor base to participate, and reduce overall systemic risk in China.

Asset-backed securities

Policy makers and market participants in China are eager to expand the scope and size of the asset-backed securities market. In particular, ABS in

China can help to ease the pressure on commercial bank balance sheets; facilitate growth of consumer finance, automobile finance, and equipment leasing; further onshore interest rate liberalization; and offer safer alternatives to other structured finance vehicles in the onshore markets.

Chinese regulators have actively supported product innovation and standardizing documentation and approvals for ABS. However, the legal/bankruptcy regime relevant to ABS remains untested and somewhat uncertain in its application. Also, while foreign investors do participate in the onshore ABS market through onshore subsidiaries or through foreign investment quotas, a true cross-border market (with offshore issuance backed by onshore assets) could benefit from additional technical and capital market reforms.

Repo market

The repo markets in China continue to develop, and NAFMII has taken a leading role to promote standard market practices and documentation with assistance from ICMA. Efficient, liquid, and safe repo markets will be crucial to robust secondary markets and the continued expansion of not only the traditional interbank bond market, but also other relatively new markets such as Panda bonds, local government bonds and ABS.

Green Bonds and sustainable financing

As a primary example of sustainable financing, green bonds (bonds that raising capital to invest only in projects related to environmental protection) have also been named as a policy priority for the Chinese financial markets. China is generally considered to be the largest market for climate-themed debt securities, and ICMA has also emerged as a leader in the development of international standards for Green Bonds with its recent appointment as Secretariat for the Green Bond Principles.

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> **“This represents a significant step in building closer links between the UK and China capital markets. As China stands poised to become the world’s largest economy and continues to expand its economic influence, we believe that robust and well-functioning capital markets are essential both on the mainland and offshore.**
>
> **Spencer Lake, Deputy Chairman of ICMA**

> **“The endorsement by the UK-China EFD reiterates the importance of bringing together international experts to assist in the development of Chinese bond markets. In cooperation with NAFMII and our combined membership base, we will address the key regulatory, legal, operational, and documentation issues to move this process forward.**
>
> **Martin Scheck, Chief Executive of ICMA**

diary

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

26 NOV

ICMA Women's Network Launch Event, London, 26 November

ICMA is launching its Women's Network with an event in London which is open to all ICMA members on 26 November – see the box for details.

The ICMA Women's Network (IWN) has been in development over the last few months under the guidance of a Steering Committee of ICMA members. The initiative is aimed at professional women in the debt capital markets ain the intermediate stages of their career progression. Essentially, the intention is to support the "pipeline" into management and senior management, aligning with the goals of our members who wish to retain and promote women in their businesses.

IWN has a distinct and differentiated offering when compared with other initiatives representing women in finance. Like ICMA itself, it is a cross-border networking hub for those who are active in the international capital market, bringing together like-minded individuals from ICMA member firms. It provides access to a geographically broad but focused network, grounded firmly within a meaningful industry structure. Membership of IWN is open to all individuals from ICMA member firms, all of whom are welcome to the first event in November.

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ICMA Women's Network

Networking. Progression. Support.

"Starting Out..."

Date: 26 Nov 2014 Time: 16.30-18.30 Venue: Côte, St Pauls

Come and meet our panel of inspirational industry figures at the **ICMA Women's Network** launch event, "Starting Out...", to discuss how they got to where they are, what they would tell their younger selves, practical advice on boosting confidence and raising profile, and whether and how they have had to adapt to succeed.

Panellists include:

Angela Clist - Angela is co-head of the Global Financial Institutions Group, a partner in the securitisation team at Allen & Overy and the only woman on the A&O Board.

Kate Craven - Most recently a director in the legal department of Barclays' investment banking arm, Kate received the Europe Women in Business Law IFLR in-house award in 2013 and the IFLR European outstanding achievement award in 2014.

Camille McKelvey (Moderator) - Camille joined Trax in May 2014 as a Commercial Manager to develop the firm's post trade product offering. Prior to this, Camille was Senior Vice President at Citigroup Global Markets.

Margaret Rowe - Prior to running the Investments Legal team for 6 years at Fidelity Worldwide Investments, Margaret spent most of her career in New York, initially with Shearman & Sterling and latterly forming her own law firm.

The panel session will be followed by drinks and focused networking, hosted by the panellists, members of the IWN and the ICMA Board. This event is open to all ICMA members. To register your attendance at the event please click **here**.

To register your interest in the IWN please click **here**.

ICMA Women's Network

Networking. Progression. Support.

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Join us on Linked In

Email us: icmawomensnetwork@icmagroup.org

28 OCT

CSDR Conference, Madrid

Members of ICMA's Iberian region are invited to attend a lunchtime conference on the latest CSDR developments in relation to wholesale markets.

Register

29 OCT

ICMA Asset Management and Investors Council (AMIC) Meeting & Seminar, London

The ICMA Asset Management and Investors Council (AMIC) represents a broad range of international investors drawn from all sectors of the industry, including institutional asset managers, private banks, hedge funds, pension funds, insurance companies and sovereign wealth funds. The AMIC Council meeting is a half day conference, open to private banks and international asset managers who review some of the major topics for the buy-side. This seminar will focus on the growth agenda in the current EU economic and regulatory environment and the contribution of asset managers.

Register

31 OCT

ICMA Seminar – 'Collateral is the new Cash' and Central Securities Depositories Regulation (mandatory buy-ins), Zurich

This ICMA afternoon seminar will focus on two areas of capital market activity affected by various new regulations, the movement of collateral around the system and the specific consequences of mandatory 'buy-ins' under the CSDR on market liquidity.

Register

04 NOV

ICMA Capital Market Lecture Series 2014 - Mario Nava, Brussels

ICMA is very pleased to welcome Mario Nava, Director of the Financial Institutions Directorate, European Commission as the latest speaker in the ICMA Capital Market Lecture Series.

Register

11 NOV

Bond Syndication Practices for Compliance Professionals and Other Non-Bankers - an ICMA Workshop, London

This workshop aims to give compliance professionals an in-depth and thorough understanding of the current practices that are involved in launching a deal in the international debt capital market. It explains precisely how the deal is done, starting with first steps in the pre-launch process - looking at the pitch book, the mandate, the road show and the prospectus - through syndication, including book building and allocation, up to and including the final public launch of the issue.

Register

12 NOV

8th ICMA Primary Market Forum, London

The 2014 ICMA Primary Market Forum will bring together borrowers, syndicate banks, investors and law firms active in debt capital markets in a question time-style debate. Our group of experts from across the securities chain will answer questions on anything from recent market practice and regulatory developments to the outlook for the debt capital markets. Delegates will be invited to submit questions in advance or at the event.

Register

13-14 NOV

Successful Sales, London

A sales and marketing training course for capital market sales people. The focus will be on acquiring sales skills for selling debt, equity and derivative instruments to an institutional client base. It aims to develop market-leading client acquisition and retention skills. The course covers both core telephone selling skills and client meeting skills. The course will acknowledge the natural conflicts in the dealing room and the inter-dependency between sales, trading and new issues and its importance in delivering a strong Capital Markets performance.

Register

diary

19 NOV

ICMA European Repo Council Meeting, London

The ICMA European Repo Council is the industry representative body that fashions consensus solutions to emerging, practical issues in a rapidly evolving marketplace, consolidating and codifying best market practice. The discussions that take place at the ERC meetings underpin the strong sense of community and common interest that characterises the professional repo market in Europe. The General Meeting will cover many aspects of the operation of the European repo markets, including recent regulatory and legal developments. This event, which is open to all European repo market participants, will be hosted by MTS.

Register

02 DEC

ICMA Roundtable: SRI and Green Bond Investments: Moving Towards the Mainstream, Paris

Socially Responsible Investing, deploying investment strategies according to ethical, social or governance principles, has become increasingly mainstream in Europe and the US in the wake of the financial crisis, driven also by increasing concerns about climate change. Green Bonds in particular, whose proceeds are used to fund projects that promote environmental sustainability, have taken off this year with over $26 billion of issuance in 2014 so far. This ICMA Roundtable will take a look at the principles behind SRI together with the benefits and opportunities that it can offer to asset managers.

Register

Save the date for these ICMA events in 2014 and 2015

'Bonds without Borders' by Christopher O'Malley - book launch, London, 2 December, 2014

JSDA/ICMA Conference: Japanese Securities Markets, London, 11 February 2015

ICMA AGM and Conference, Okura Hotel, Amsterdam, 3-5 June 2015

ICMA Executive Education

Book now for these courses in 2014 and 2015

Part I: Introductory Programmes

Financial Markets Foundation Course (FMFC
London: 5-7 November 2014
Luxembourg: 10-12 June 2015

Securities Operations Foundation Course (SOFC)
London: 10-12 September 2014
Brussels: 12-14 November 2014

Part II: Intermediate Programmes

International Fixed Income and Derivatives (IFID) Certificate Programme
Barcelona: 26 October – 1 November 2014

Operations Certificate Programme (OCP)
Brussels: 22-28 March 2015

Primary Market Certificate (PMC)
London: 17-21 November 2014

Part III: Specialist Programmes

Collateral Management
London: 9-10 October 2014

Credit Default Swaps (CDS) – Features, Pricing & Applications
London: 22-23 October 2014

Fixed Income Portfolio Management
London: 27-28 November 2014

ICMA Guide to Best Practice in the European Repo market
London: 17 November 2014

Corporate Actions – An Introduction
London: 12-13 May 2015

Corporate Actions – Operational Challenges
London: 14-15 May 2015

GLOSSARY

ABCP	Asset-Backed Commercial Paper
ABMI	Asian Bond Market Initiative
ADB	Asian Development Bank
AFME	Association for Financial Markets in Europe
AIFMD	Alternative Investment Fund Managers Directive
AMF	Autorité des marchés financiers
AMIC	ICMA Asset Management and Investors Council
ASEAN	Association of Southeast Asian Nations
BBA	British Bankers' Association
BCBS	Basel Committee on Banking Supervision
BIS	Bank for International Settlements
BMCG	ECB Bond Market Contact Group
BRRD	Bank Recovery and Resolution Directive
CAC	Collective action clause
CBIC	ICMA Covered Bond Investor Council
CCBM2	Collateral Central Bank Management
CCP	Central counterparty
CDS	Credit default swap
CFTC	US Commodity Futures Trading Commission
CGFS	Committee on the Global Financial System
CICF	Collateral Initiatives Coordination Forum
CIF	ICMA Corporate Issuer Forum
CoCo	Contingent convertible
COGESI	Contact Group on Euro Securities Infrastructures
COREPER	Committee of Permanent Representatives (in the EU)
CPMI	Committee on Payments and Market Infrastructures
CRA	Credit Rating Agency
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CSD	Central Securities Depository
CSDR	Central Securities Depositories Regulation
DMO	Debt Management Office
D-SIBs	Domestic systemically important banks
DVP	Delivery-versus-payment
EACH	European Association of CCP Clearing Houses
EBA	European Banking Authority
EBRD	European Bank for Reconstruction and Redevelopment
ECB	European Central Bank
ECJ	European Court of Justice
ECOFIN	Economic and Financial Affairs Council (of the EU)
ECON	Economic and Monetary Affairs Committee of the European Parliament
ECP	Euro Commercial Paper
ECPC	ICMA Euro Commercial Paper Committee
EEA	European Economic Area
EFAMA	European Fund and Asset Management Association
EFC	Economic and Financial Committee (of the EU)
EFSF	European Financial Stability Facility
EGMI	European Group on Market Infrastructures
EIB	European Investment Bank
EIOPA	European Insurance and Occupational Pensions Authority
EMIR	European Market Infrastructure Regulation
EMTN	Euro Medium-Term Note
ERC	ICMA European Repo Council
ESA	European Supervisory Authority
ESFS	European System of Financial Supervision
ESMA	European Securities and Markets Authority
ESM	European Stability Mechanism
ESRB	European Systemic Risk Board
ETF	Exchange-traded fund
ELTIF	European Long-Term Investment Funds
EURIBOR	Euro Interbank Offered Rate
Eurosystem	ECB and participating national central banks in the euro area
FAQ	Frequently Asked Questions
FASB	Financial Accounting Standards Board
FATCA	US Foreign Account Tax Compliance Act
FATF	Financial Action Task Force
FCA	UK Financial Conduct Authority
FIIF	ICMA Financial Institution Issuer Forum
FMI	Financial market infrastructure
FPC	UK Financial Policy Committee
FRN	Floating-rate note
FSB	Financial Stability Board
FSOC	Financial Stability Oversight Council
FTT	Financial Transaction Tax
G20	Group of Twenty
GDP	Gross Domestic Product
GMRA	Global Master Repurchase Agreement
G-SIBs	Global systemically important banks
G-SIFIs	Global systemically important financial institutions
G-SIIs	Global systemically important insurers
HFT	High frequency trading
HMT	HM Treasury
IAIS	International Association of Insurance Supervisors
IASB	International Accounting Standards Board
ICMA	International Capital Market Association
ICSA	International Council of Securities Associations
ICSDs	International Central Securities Depositaries
IFRS	International Financial Reporting Standards
IIF	Institute of International Finance
IMMFA	International Money Market Funds Association
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
IRS	Interest rate swap
ISDA	International Swaps and Derivatives Association
ISLA	International Securities Lending Association
ITS	Implementing Technical Standards
KfW	Kreditanstalt fűr Wiederaufbau
KID	Key information document
LCR	Liquidity Coverage Ratio (or Requirement)
L&DC	ICMA Legal & Documentation Committee
LEI	Legal entity identifier
LIBOR	London Interbank Offered Rate
LTRO	Longer-Term Refinancing Operation
MAD	Market Abuse Directive
MAR	Market Abuse Regulation
MEP	Member of the European Parliament
MiFID	Markets in Financial Instruments Directive
MiFID II	Revision of MiFID
MiFIR	Markets in Financial Instruments Regulation
MMCG	ECB Money Market Contact Group
MMF	Money market fund
MOU	Memorandum of Understanding
NAV	Net asset value
MTF	Multilateral Trading Facility
NAFMII	National Association of Financial Market Institutional Investors
NCA	National Competent Authority
NDRC	National Development and Reform Commission
NSFR	Net Stable Funding Ratio (or Requirement)
OTC	Over-the-counter
OTF	Organised Trading Facility
OJ	*Official Journal of the European Union*
OMTs	Outright Monetary Transactions
PD	EU Prospectus Directive
PD II	Amended Prospectus Directive
PMPC	ICMA Primary Market Practices Committee
PRA	UK Prudential Regulation Authority
PRIIPs	Packaged Retail and Insurance-Based Investment Products
PSI	Private Sector Involvement
PSIF	Public Sector Issuer Forum
QMV	Qualified majority voting
RFQ	Request for quote
RM	Regulated Market
RMB	Chinese renminbi
RPC	ICMA Regulatory Policy Committee
RSP	Retail structured product
RTS	Regulatory Technical Standards
SEC	US Securities and Exchange Commission
SFT	Securities financing transaction
SGP	Stability and Growth Pact
SI	Systematic Internaliser
SLL	Securities Law Legislation
SME	Small and medium-sized enterprise
SMPC	ICMA Secondary Market Practices Committee
SPV	Special purpose vehicle
SRO	Self-regulatory organisation
SSAs	Sovereigns, supranationals and agencies
SSM	Single Supervisory Mechanism
SSR	EU Short Selling Regulation
T+2	Trade date plus two business days
T2S	TARGET2-Securities
TD	EU Transparency Directive
TFEU	Treaty on the Functioning of the European Union
TRs	Trade repositories
UKLA	UK Listing Authority

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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