

**Minutes of the Joint Meeting of the European Repo Committee and ISLA Board held on  
23 June, 2015 in Lisbon**

Present:	Mr. Andy Krangel	Citigroup (ISLA Chairman)
	Mr. Godfried De Vidts	ICAP (ERC Chairman)
	Mr. Mohamed Moursy	ABN Amro
	Mr. Dan Bremer	BAML
	Mr. Mark Newton	Barclays
	Mr. Michael Manna	Barclays
	Mr. Rob Lees	Brown Brothers Harriman & Co
	Mr. Stefan Kaiser	BlackRock
	Mr. David Raccat	BNP Paribas
	Mr. Eugene McGrory	BNP Paribas
	Mr. Grigorios Markouizos	Citigroup (ERC Vice Chair)
	Mr. Andreas Biewald	Commerzbank
	Mr. Ronan Rowley	Deutsche Bank
	Mr. Francois-Xavier Bouillet	Goldman Sachs
	Mr. Roy Zimmerhansl	HSBC (ISLA Vice Chair)
	Mr. Jean-Michel Meyer	HSBC
	Ms. Chiara Bacchetti	Intesa SanPaolo
	Mr. Duncan Wilson	JP Morgan
	Mr. Nicola Danese	JP Morgan
	Ms. Martina Szameitat	Morgan Stanley
	Mr. Andy Wise	Morgan Stanley
	Mr. Michel Semaan	Nomura
	Mr. Roelof Van der Struik	PGGM Vermogenbeheer
	Mr. James Treseler	Société Générale
	Mr. Sylvain Bojic	Société Générale
	Mr. Ian Hovey	State Street (ISLA Treasurer)
	Mr. Richard Hochreutiner	Swiss Reinsurance
	Mr. Casey Whymark	UBS
	Mr. Gareth Allen	UBS
	Mr. Arne Theia	UniCredit Bank
Also Present:	Mr. Kevin McNulty	ISLA CEO
	Mr. Andy Dyson	ISLA COO
	Ms. Claire Davis	ISLA
	Mr. David Hiscock	ICMA
	Mr. Andy Hill	ICMA
	Ms. Lalitha Colaco Henry	ICMA (Secretary)
Apologies:	Mr. Mick Chadwick	Aviva Investors
	Mr. Romain Dumas	Credit Suisse

Mr. Tony Baldwin	Daiwa Capital Markets
Mr. Andrea Masciovecchio	Intesa SanPaolo
Mr. Eduard Cia	UniCredit Bank (ERC Vice Chair)
Ms. Lisa Cleary	ICMA
Mr. Richard Comotto	ICMA Centre

## **1. Welcome by Mr. Godfried De Vidts and Mr. Andy Krangel**

Mr. De Vidts warmly welcomed the ISLA Board and the ERC Committee to Lisbon for the first joint meeting and thanked ISLA for kindly hosting the meeting. Mr. Krangel said that it was an important step for ISLA and the ERC Committee to be having a joint meeting.

Mr. De Vidts noted that the minutes of the meeting would be published on the ICMA website. The new ERC Committee had been elected at the last European Repo Council meeting, which took place on 18 May. As a result of that election, Mr. Richard Hochreutiner is the ERC Committee's first buy-side member. Two other buy-side firms have since expressed an interest in standing in the ERC Committee elections in January. However, ISLA's Board has had a diverse membership for a long time, and such diversity is increasingly important. ECB officials have welcomed the broader membership of the ERC Committee. Because the ECB is only able to work with banks, a wider ERC membership gives the ECB access to a more diverse source of market views and information.

## **2. Extension of the ISDA resolution stay protocol and BRRD update**

Mr. McNulty said that the EU Bank Recovery and Resolution Directive (BRRD) went live in many Member State on 1 January 2015 and is designed to address the "too big to fail" issue so that systemically important financial institutions (SIFIs) are able to avoid recourse to public funds should they fail. The BRRD grants regulators extensive powers to deal with banks and other prudentially regulated firms, including the adoption of special resolution regimes (SRR) which enable regulators to step in and either rescue the SIFI or ensure that it is wound down in an orderly manner.

One of the regulatory initiatives concerns the development of a contractual stay that would prevent counterparties from terminating their positions early or exercising cross-default rights in respect of a failing firm for 48 hours. This would give regulatory authorities 48 hours to step in and either rescue the failing firm or ensure that it is wound down in an orderly fashion.

In November 2013, regulatory authorities from six of the G-20 countries (Germany, Japan, Switzerland, France, the US and the UK) requested that ISDA create a contractual stay arrangement for the ISDA Master Agreement in order to plug the gap in relation to cross-border transactions. For example, if both parties to an English law ISDA Master Agreement were organised in the UK, the UK SRR would apply and the stays on exercising the early termination rights in the ISDA Master Agreement would be enforceable. However, where there is a cross-border element to the contractual relationship, e.g. a UK SIFI entering into a New York law ISDA Master Agreement with a Swiss counterparty, it is not clear whether the UK's SRR (and particularly the stay on termination rights) would be enforceable against the Swiss counterparty if the UK SIFI were to enter resolution. Therefore, the regulators want market participants to come up with a solution to plug this cross-jurisdictional gap. ISDA published the ISDA Resolution Stay Protocol in November 2014, which was signed by all 18 global SIFIs.

In early 2015, ICMA, ISLA and SIFMA were asked by the regulators to develop a similar resolution stay protocol for the GMRA, the GMSLA and the MRA by November 2015. SIFMA, ICMA and ISLA have formed a working group with ISDA. The group has had a number of meetings and are working with Cleary Gottlieb who developed the annex to the ISDA Protocol. A draft has now been submitted to the regulators, who are expected to provide their feedback shortly. However, there are still a number of issues the working group need to consider, including how the protocol would work when an agent is involved in the transaction.

Mr. McNulty went on to say that the scope of the BRRD is Europe-wide. There is different legislation in the US, Switzerland and Japan. At the moment, the regulatory authorities appear to be taking slightly different positions on whether overnight repo or securities loans might be subject to standard stay provisions under the BRRD and similar legislation (although it was noted that most regulators reserve quite extensive powers to stay more than just termination rights if they wish). Additionally, Mr. McNulty highlighted that contractual stays in financial contracts are not just an issue for the 18 largest SIFIs, but they are also a market-wide issue. The UK's PRA issued a consultation paper in May proposing rules that would apply to all PRA-authorized UK banks, building societies and PRA-designated UK investment firms as well as their qualifying parent undertakings in respect of financial contracts governed by third-country law. The proposed rule would prohibit firms from creating new obligations or materially amending an existing obligation under such a financial contract without the required counterparty agreement. The prohibition would apply unless the counterparty had agreed in writing to be subject to similar restrictions on early termination and close-out to those that would apply as a result of the firm's entry into resolution if the financial contract were governed by UK law. The PRA's consultation closes on 26 August 2015.

There was some discussion amongst the ERC Committee and ISLA Board about how a stay of early termination rights would work in relation to open transactions. Concerns were also expressed regarding the impact of a stay on contingent liabilities, the ability of counterparties to margin during the stay, and the potential impact on regulatory capital. When the ISDA protocol was introduced in November, there was a lot of nervousness about it in the markets but the protocol does not appear to have caused any problems. However, it was accepted that the ISDA protocol is slightly different because money does not generally change hands in relation to derivatives transactions. If a SFT were stayed it would have knock-on consequences as cash would be prevented from flowing into other transactions.

Mr. McNulty stressed that the regulators are adamant that these proposals will go ahead. Mr. De Vidts said that he had recently met with a number of ECB officials and the ECB may undertake to carry out a study to determine the extent to which this would impact the real economy. Mr. De Vidts added that it was important for firms to continue discussing these issues with the relevant central bank officials. He also suggested that it would be useful if ICMA and ISLA staff could prepare a paper by the end of August on how a stay on early terminations would work in practice.

Mr. McNulty also said that the home authority regulators (working under the banner of the FSB) had asked ISLA, SIFMA and ICMA for data on SFT transactions transacted by the 18 largest banking groups that had adhered to the ISDA Stay Protocol. It is anticipated that the data will be used by the FSB in advance of the G20 Summit in November at which a statement would be made about extending the protocol to cover SFTs. It was agreed to seek Mr. Comotto's input on how best to provide data.

### **3. Repo market study**

Mr. Andy Hill said that ICMA had published a [corporate bond market study](#)<sup>1</sup> in November 2014 which had become a reference point in the discourse on bond market liquidity and bond market efficiency which had raised a flag with regulators. Given the success of the study, ICMA had thought it would be a natural progression to conduct a similar study for the repo market. Accordingly, Mr. Hill will be looking to interview market makers, users, infrastructure providers, tri-party agents, CCPs, DMOs and central banks and will aim to present the findings at the European Repo Council general meeting taking place on 14 October 2015.

### **4. Update on SFTR**

Mr. McNulty said that political agreement had been reached on 17 June on the Level 1 Securities Financing Transactions Regulation (SFTR) text. An official version of the agreed text is expected to be published shortly. The SFTR sets out three areas of transparency. The first relates to the reporting of SFT trades to a trade repository. In this regard, the SFTR is modelled on EMIR. The other two elements of the SFTR concern disclosures by fund managers and the re-use of collateral in relation to which there will be a requirement to disclose the risks of re-use to counterparties. ESMA and the Commission will start developing the Level 2 measures shortly. Mr. McNulty and Mr. Hiscock will meet with the FCA in the coming weeks and with ESMA in September.

How long will it take to implement trade reporting under the SFTR? ESMA will have 12 months to draft the Level 2 text and then it is likely that there will be a further 12 month period before firms will be required to begin reporting. Mr. McNulty said that having spoken with a number of EMIR trade repositories, it is clear that they are not particularly advanced on what they will need to do under the SFTR or what it will mean for them.

Mr. De Vidts said that the ECB had published its Money Markets Statistics Regulation (MMSR) at the start of the year. It will require the 50 or so largest Euro-area banks to report, on a daily basis, all trades in repo (including tri-party repo) denominated in euro with a maturity of up to and including one year entered into with other monetary financial institutions (MFIs), other financial intermediaries (OFIs), insurance corporations, pension funds, general government or central banks. The ECB has nevertheless requested that the ERC continue publishing the results of the semi-annual repo survey, which it will continue to do. However, it will be important to try to ensure that there is no duplication between the reporting required under the MMSR and the SFTR.

Mr. Hiscock said that a lot of work will need to be done to implement the SFTR in the next couple of years. However, before discussing the outline and detail of the Level 2 text with ESMA it will be important to educate ESMA about how the GMRA and the repo markets function; so that when they come to drafting the Level 2 text, they fully understand the impact it will have on the SFT markets. It is also important to remember that ESMA is not just one regulatory authority but is composed of 28 competent authorities and therefore it is important to ensure that the educative

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<sup>1</sup> Alternatively, see: [http://www.icmagroup.org/assets/documents/Regulatory/Secondary-markets/The-state-of-the-European-investment-grade-corporate-bond-secondary-market\\_ICMA-SMPC\\_Report-251114-Final3.pdf](http://www.icmagroup.org/assets/documents/Regulatory/Secondary-markets/The-state-of-the-European-investment-grade-corporate-bond-secondary-market_ICMA-SMPC_Report-251114-Final3.pdf)

efforts extend more broadly than just to ESMA officials. ESMA has warmly welcomed the offer of an education session and a date will be confirmed shortly.

Mr. De Vidts stressed that the SFTR will be an expensive regulation for the industry to implement and it is vital that it not duplicate other regulatory initiatives. Mr. Hiscock said that a report is expected from the FSB shortly about aggregating data from national and regional authorities. This report will colour ESMA's view on what systems to put into place. Mr. De Vidts noted that the ERC Operations Group, in conjunction with the ISLA Operations Group will carry out the bulk of the work to implement the SFTR.

Turning to the collateral re-use point, regarding which there will be a requirement to disclose the risks of re-use to counterparties, Mr. McNulty said that it may be worth ICMA and ISLA working together to develop a standard language. Mr. De Vidts noted that the work of the ERC Operations Group on trade matching and affirmation (TMA) might be usefully leveraged. Mr. Hiscock said that it would be worth discussing this issue more fully with Ms. Lisa Cleary as the GMRA already provides a lot of information about events of default. Accordingly, it is feasible that the notification requirement may be satisfied as long as there is a signed master agreement in place between the two counterparties, but this still needs to be more thoroughly explored.

## **5. Update on CSDR**

Mr. Andy Hill said that in the last six months, ICMA had been heavily engaged on the issue of mandatory buy-ins. ESMA had published draft Regulatory Technical Standards (RTS) in December 2014 and the mandatory buy-in provisions were a cause for concern. In particular, ICMA had advocated that (i) buy-ins should take place at the trading level for non-cleared, fixed income transactions, rather than at the CSD or ATS level; (ii) the maximum extension period of seven days should be applied to all fixed income products; (iii) the start-leg of repos termed up to 21 business days should be exempt; (iv) implementation should be postponed until after the roll-out of T2S, at the very least, which would amount to a 2-year delay; and (v) the link to the MiFID liquidity calibrations in the CSDR should be removed.

Mr. Hill went on to say that the industry had expected the revised RTS to be published on 18 June, but instead, ESMA had informed the Commission that it was delaying publication of the draft RTS till September 2015 in order to accommodate an early legal review. Separately, ESMA's Ms. Verena Ross had indicated that an implementation delay linked to T2S would be a practical way forward, but it is understood that the Commission does not agree with this approach. Mr. De Vidts said that while the industry might be able to assume a delay in implementation to mid-2017 it should nevertheless continue to work on improving trade matching and affirmations and confirmations to reduce the level of technical fails. It is also important for the industry to work out what causes fails. Mr. McNulty said that the incidence of fails had increased since the start of T2S. ISLA are planning on holding discussions on how the securities lending market can become more efficient. Euroclear UK and Ireland have indicated that it may be feasible to offer an automated securities lending facility for securities held in CREST. There was support for the idea of suggesting that regulatory authorities monitor the level of fails before and after September 2015 when the Settlement Bridge between the ICSDs is improved. This would be a more positive and constructive message than simply telling the authorities to delay the implementation of CSDR till after all the CSDs have migrated to T2S, especially given the on-going delays rolling-out T2S.

Finally, Mr. Hill mentioned that the ERC Operations Group have been developing a market-wide template for trade matching and affirmation that can be used by both buy- and sell-sides. The

template is currently going through a review process amongst the big firms and is being considered by various vendors.

## **6. The ECB's Quantitative Easing proposals**

Mr. De Vidts said that he had recently met with various ECB officials. It was heartening to hear that the ECB agrees about the need for robust repo markets in order to have properly functioning cash bond markets. It has now become clear that the FTT will not impact fixed income or repo markets. However, there are a wide range of regulatory initiatives that will impact both repo and cash bond markets – MiFID, CSDR, SFTR, to name just a few. At the same time, CCPs are absorbing a huge amount of collateral. The ECB is aware of this and may consider what this may mean for the markets. One possibility is that the ECB may require CCPs to deposit their excess cash with the national central banks. The ECB is also conscious of the cumulative impact of QE on the markets. To date, the QE programme has gone well, but it is unknown how the markets will fare once the ECB gets to €700 billion. Mr. De Vidts is trying to arrange a meeting of the ERC with the ECB. The ICMA Secretariat will be in touch with the ERC Committee in due course.

The ERC Committee and ISLA Board noted that it might be dangerous for CCPs to be granted access to central bank liquidity as it would be difficult to control. If outstanding liquidity is being parked with the CCP and they place the cash with the national central banks, then even more liquidity is taken out of the market. It was also noted that repo market participants are seeing increasing treasury volumes leaving the repo market due to regulatory pressures.

## **7. FCA CASS rules and Tri-party Collateral Arrangements**

Mr. Andy Dyson said that the FCA's CASS rulebook sets out the requirements relating to the holding of client assets and client money. There are two rules in CASS 6 (Custody Rules) that give cause for concern in relation to custody assets held at triparty agents. The first is a requirement that firms keep such records and accounts as necessary to enable it at any time and without delay to distinguish safe custody assets held for one client from safe custody assets held for any other client, and from the firm's own applicable assets. It is understood that firms have agreed with auditors that being able to receive a report from the triparty agent of collateral assets held within a short time frame (of a few hours) is considered sufficient to comply with the rule

The second and seemingly more problematic issue is a requirement that custody assets must be reconciled against internal asset records (that are independent of the custody record). In the case of tri-party transactions, the tri-party agent's books will be the only source of records and so it will be impossible to satisfy the rule. Accordingly, ISLA members are increasingly failing their CASS audits, with auditors taking a more rigorous approach. ISLA had recently met with KPMG and are looking to arrange a meeting with the FCA to discuss the matter. Mr. Dyson concluded by saying that further updates will be provided in due course.

## **8. AOB and upcoming dates**

***ERC Guide to Best Practice*** – there was a question about the extent to which acceptance of partial delivery should be recommended as best practice in the ERC Guide in order to assist the remediation of fails and to reduce fail sizes. The shaping of trade sizes and whether there should be a limit of 50 million was also mentioned in the context of the Guide to Best Practice. It was

agreed that the point about shaping should be discussed with the ERC Operations Group and also raised at the next ERC Committee meeting for inclusion in the Guide to Best Practice.

**Volker Rule and repo** - there is a question about the extent to which the repo of certain ABS securities creates something akin to an ownership interest in a covered fund which would be prohibited. Apparently, some market participants are going to send client notices or add amendments to the GMRA in order to resolve these issues. It was noted that Ms. Cleary is looking into this issue.

**NSFR** – there are two issues of note. The first relates to linked transactions i.e. linking a borrow/reverse to a cash short means that the NSFR weighting does not apply. Linked transactions are a significant issue for both repo and large prime brokerages. The second concerns the impact of liabilities on derivatives and how they are accounted for under NSFR.

Mr. De Vidts and Mr. Krangel both agreed that the joint meeting was useful.

The ERC Chairman:

The ERC Secretary:

Godfried De Vidts  
16 September 2015

Lalitha Colaco-Henry