



10 July 2008

## **OUTCOME OF THE SECOND CONSULTATION ON CCBM2 – THE CCBM2 DRAFT USER REQUIREMENTS**

### **Introduction**

On 26 February 2008 the Eurosystem launched a second public consultation on CCBM2 (see <http://www.ecb.europa.eu/press/pr/date/2008/html/pr080226.en.html>), inviting market participants to provide comments on the CCBM2 draft user requirements.

By 29 May 2008 the ECB had received a total of 24 responses:

- nine joint replies from European and national associations of credit institutions, national user groups and other financial market associations;
- ten individual replies from credit institutions;
- two individual replies from ICSDs; and
- three replies from other interested parties (two central counterparty clearing houses and SWIFT).

All respondents in the consultation confirmed their broad support for the Eurosystem initiative to develop CCBM2.

Respondents welcomed the opportunity to comment on the CCBM2 user requirements and reiterated both their interest in the CCBM2 project and their willingness to contribute again in forthcoming phases. Some respondents expressed appreciation for the level of transparency regarding the CCBM2 project and the Eurosystem's open and constructive dialogue with market participants.

This note summarises the main issues emerging from the responses in this second consultation. Section 1 presents the market view as regards the CCBM2 user requirements. Section 2 presents additional comments not directly related to the CCBM2 user requirements.

The replies for which publication was authorised have been published on the ECB's website (see <http://www.ecb.europa.eu/ecb/cons/html/ccbm2-2.en.html>).

### **1. The market view as regards the CCBM2 user requirements**

Overall, the CCBM2 draft user requirements were well received by respondents. Some responses made a point of praising the quality of the draft user requirements document. In others, respondents identified a number of issues which, in their view, were not adequately specified in the user requirements and requested further information/clarification regarding some specific provisions. These often related to specific technical aspects of the CCBM2 functionalities.

In most cases, respondents remarked on the relevance of specific functionalities described in the user requirements, emphasising their particular business case and seeking confirmation that CCBM2 would meet their specific needs as users. In a few other cases, proposals to review selected provisions of the CCBM2 user requirements were also put forward.

This section does not report on requests for further information/clarification, nor on minor/technical amendments to the provisions of the CCBM2 user requirements document (URD). Instead, it provides an overview of the main remarks concerning the current provisions of the URD. These remarks are presented below chapter by chapter.

## **1.1 Introduction to the CCBM2 user requirements**

The modular structure of CCBM2 was not challenged, although the optional nature of some modules and functionalities was sometimes questioned.

As regards the principle of voluntary participation, several respondents encouraged all euro area central banks to join CCBM2 and subscribe to all modules, in order to maximise benefits and efficiency. Some other respondents even suggested that the implementation and use of CCBM2 should be mandatory for all national central banks (NCBs) and that the choice as regards the optional modules to be subscribed to should be made in agreement with the national user community.

Several respondents sought assurances that current operating models are fully reflected and that existing service levels will not be impaired. They had particular concerns with regard to the possibility for Eurosystem counterparties to use as collateral assets held in custody with correspondent credit institutions, as provided for in Chapter 5.3.1 of the General Documentation on Eurosystem Monetary Policy Instruments and Procedures.

## **1.2 Message router**

### **Message formats**

With regard to the message formats handled by the message router, several respondents stressed that, in order to keep implementation costs for market participants low, the application-to-application interface should use SWIFT-based messages, such as SWIFT collateral management messages.

These respondents also recommended supporting both ISO 15022 and ISO 20022 from the start. They indicated that an appropriate capability for conversion from one ISO standard to the other could be implemented in CCBM2, which would allow participants to continue to use current collateral management messages. New messages – e.g. messages for the credit claims module – could be entered directly in accordance with ISO 20022. Respondents also asked that harmonised standards/formats (including standards/formats concerning communication between external collateral management systems (CMSs) and CCBM2) be defined in cooperation with the market.

In this context, SWIFT indicated that their Standards team was currently working on several ISO 20022 message sets – for example in the areas of securities settlement and tri-party collateral management – that could in principle cover a number of the requirements of CCBM2. For other areas, such as auto-collateralisation and static data, further analysis will be needed in order to identify any ISO message gaps.

### **Interface mode**

Several respondents, especially from the German counterparty community, asked that CCBM2 provide the same access rights and functionalities through both the user-to-application interface and the application-to-application interface, which should be offered as full alternatives. They also recommended implementing a “client – sub-client” model for user rights, in which different users/legal entities could be permitted to process instructions on specific accounts. One respondent recommended that the user-to-application interface contain a functionality allowing the direct inputting of data by market participants.

## **1.3 Credit and collateral module**

Remarks on the credit and collateral module concerned the following issues.

### **(i) Earmarking functionality**

One ICSD remarked that the definition of the “earmarking” functionality in the URD could be open to misinterpretation. It noted that, in legal terms, earmarking is commonly understood as the “designation of an entry”, i.e. a means of creating/displaying security interests with regard to certain (usually blocked) security credits in the security account of a collateral provider. As such, earmarking is regarded as an alternative to book-entry credits.

### **(ii) Management of collateral sub-pools**

With reference to the possibility of maintaining several collateral sub-pools per counterparty within the pooling functionality,<sup>1</sup> a national market association noted that there would be a need to set requirements for the access to and management of these sub-pools on different levels (to support inter-entity or inter-group liquidity and collateral management, as well as services offered to third parties, such as indirect participants in TARGET2). In particular, this association asserted that: (i) authorisation for the sub-pools should be managed independently of that of the main pool; (ii) a second legal entity or branch should be able to manage the sub-pool; and (iii) a restricted view is required for liquidity providers.

Several respondents asked that CCBM2 support specific arrangements pertaining to banking groups with a decentralised structure. One association of credit institutions requested a functionality allowing multi-country bank groups to aggregate on an intraday basis the collateral available on a defined set of individual accounts held with various NCBs (i.e. a virtual collateral pooling mechanism similar to the liquidity pooling function in TARGET2). This would allow bank groups to manage liquidity and

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<sup>1</sup> This allows a counterparty to segregate the collateral delivered to its global pool held with a given NCB, distinguishing between collateral delivered by its various back offices, its branches, group members, etc.

collateral in a centralised manner while adopting a decentralised approach for other purposes (e.g. as regards the credit freezing facility).

### **(iii) Credit freezing**

Some respondents explicitly welcomed the introduction of the credit freezing functionality. With reference to its optional nature, one even asserted that this functionality should be mandatory; another hoped that it would be adopted by all participating NCBs. A national association of credit institutions stressed that dynamic management of the credit freezing functionality is required and should be exercised by the treasurer – while a CCP asserted that this should be exercised by the CCP treasury.

Furthermore, some respondents suggested that the credit freezing functionality could also be used, at counterparties' discretion, for purposes other than those indicated in the CCBM2 URD (e.g. for the support of the night-time settlement processes of some SSSs or the provision of guarantees to CCPs – as is currently the case in some domestic markets). It could, for instance, be used:

- to create a “collateral pocket” (consisting of securities and/or credit claims) for use in the event of the TARGET2 contingency module being activated (in this case, in order to obtain fresh liquidity in the contingency module, TARGET2 participants could use pre-reserved collateral in the credit freezing facility, as well as new collateral);
- for CLS payments in contingency situations, e.g. in the event of technical problems on the part of a participant (in which case euro payments can be settled in CLS via TARGET2 on behalf of the “failing” participant) or liquidity needs in the CLS system (i.e. to help participants to make contingency payments via TARGET2); and
- for credit transactions with non-Eurosystem central banks (even outside TARGET2 operating hours).<sup>2</sup>

### **(iv) External collateral management systems and tri-party services**

Several respondents remarked on the importance of providing a connection to external collateral management systems, particularly those systems that had been developed in close cooperation with the market and the NCBs.

In particular, respondents from the German counterparty community stressed their need for a link between CCBM2 and XEMAC, the collateral management system provided by Clearstream, which is currently used by German counterparties to deliver collateral to the Deutsche Bundesbank. They highlighted the fact that XEMAC had proved beneficial, in particular since the beginning of the market turbulences in mid-2007, enabling market participants to achieve the efficient allocation of collateral for multiple purposes, over and above credit operations with the Eurosystem.

They repeatedly recommended that the connection to XEMAC should not imply any adjustments to the system, in order to avoid additional costs for users. These counterparties feared that the establishment of a

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<sup>2</sup> See remark in Section 1.8 below.

standardised business process for connecting to CCBM2 could lead to a loss of synergies and efficiency in XEMAC. In this respect, in its response Clearstream indicated that the “Cancel and replace mode” foreseen in the CCBM2 URD (Section 3.10.1) could eventually accommodate the current interface between XEMAC and the Eurosystem, subject to further investigation.

Moreover, almost all respondents reiterated their request to combine CCBM2 with existing ICSD systems providing tri-party collateral management services. These respondents listed the advantages for counterparties of extending ICSDs’ tri-party services to cover credit operations with central banks, not only in terms of efficiency gains for their own collateral management, but also from a financial stability perspective.

With reference to the two models proposed for the integration of tri-party services (i.e. the “standard” and “interfaced” models),<sup>3</sup> one ICSD recognised that the transaction-by-transaction mode described in the CCBM2 URD (Section 3.10.2) reflects the proposal put forward by the market and expressed its support for the former: full integration with outsourcing to the external CMS. The other ICSD recommended defining a unique interoperability model leading to both harmonisation and greater efficiency (supporting collateral substitution on a 24-hour basis). Another respondent noted that the availability of both interaction models could help other CSDs to develop tri-party services.

Furthermore, one respondent suggested that counterparties could be allowed to access tri-party services provided by foreign (I)CSDs for credit transactions with their own national central bank on the basis of a CCBM-like approach – i.e. allowing the collateral held by the counterparty in the foreign (I)CSD (whether held directly or via a custodian) to be transferred to a correspondent NCB.

Finally, some respondents proposed an assessment of whether common normative/structured criteria defining eligible CMSs could be introduced to mitigate and prevent risks. A couple of other respondents advised considering also non-ICSD providers, such as JPMorgan Chase and the Bank of New York Mellon. Respondents also indicated that tri-party service providers should become direct participants in TARGET2 and T2S in order to ensure settlement in central bank money.

#### **(v) Auto-collateralisation**

Respondents welcomed the introduction of the functionality supporting auto-collateralisation procedures in SSSs, particularly in view of the introduction of T2S and its auto-collateralisation procedure.

As regards the model described in the CCBM2 URD (Section 3.11), some participants requested the establishment, in cooperation with the market, of some predefined times for the automatic return of collateral (i.e. an optional intraday and a mandatory end of day).

One ICSD remarked that the proposed model could lead to less efficient processes for interfaced models and, besides providing some further technical remarks on the process described, stressed that these concerns would be particularly relevant were CCBM2 to be launched before T2S.

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<sup>3</sup> See the proposals put forward in a joint contribution by the Euro Repo Committee and the two ICSDs: [http://www.ecb.europa.eu/paym/coll/coll/ccbm2/pdf/CCBM2\\_Letter\\_18Dec2007.pdf](http://www.ecb.europa.eu/paym/coll/coll/ccbm2/pdf/CCBM2_Letter_18Dec2007.pdf)

## 1.4 Securities module

One ICSD noted that custody services could be outsourced to the respective CSDs. This could prevent both the duplication of investments and the risk of reconciliation issues. The other ICSD observed that, according to the URD (Section 1.3.5), CCBM2 will deal with corporate actions in respect of (i) coupon payments, and (ii) partial or full redemptions. This ICSD therefore suggested refining the formulation of Principle 4 and realigning other provisions of the URD which currently provide room for a broader interpretation of the scope of CCBM2 functionalities in this field.

Furthermore, an association of credit institutions requested the routing to counterparties of all information relating to corporate actions and all information on events pertaining to the securities delivered as collateral.

## 1.5 Credit claims module

One respondent considered that some flexibility should be introduced as regards the registering/recording and mobilisation of credit claims, in order to allow existing high-performance registering/recording systems to connect to CCBM2 as external CMSs. Some respondents from the German counterparty community proposed that consideration be given to using the Deutsche Bundesbank system handling credit claims (the KEV) as the credit claims module for CCBM2.

As regards the procedures proposed in the CCBM2 URD, some credit institutions expressed a preference for the bulk procedure, while other respondents requested that both procedures be retained.

Several respondents noted that further harmonisation of the mobilisation process would be required in order to facilitate cross-border use of credit claims. In particular, besides national legal requirements (which lie outside the domain of central banks), three items were singled out for further harmonisation:

1. details of credit claims that need to be transmitted for the purposes of identification, eligibility checking (including creditworthiness assessments) and valuations;
2. identification codes; and
3. handling procedures, including the fulfilment of legal requirements – e.g. opting for the simplest legal procedure for notification.

As regards identification codes, it was stressed that in order to ensure the confidentiality of client information it is important to introduce a unique code which cannot be mistaken for any other type of collateral or securities. In this context, reference was made to the common identification code tool in use in Belgium and the Netherlands as part of the system established by their respective NCBs.

Finally, one respondent called for the establishment of a harmonised and efficient solution for the mobilisation of credit claims, as this would support the creation of a secondary market for credit claims and potentially the use of credit claims also in tri-party services. Another respondent advocated further cooperation between credit institutions and CSDs with a view to achieving such a result.

## **1.6 Static data**

The ICSDs welcomed the Eurosystem's readiness to share static and dynamic data on ESCB-eligible securities and stressed the need to access extended data in the EADB, including information regarding prices, haircuts and close links. One CSD proposed the daily realignment of data on eligible assets on the basis of the list of securities managed by CSDs.

Some respondents recommended the establishment of a single database for CCBM2, T2S and TARGET2 to prevent duplication and avoid the risk of cross-system inconsistencies in common static data.

## **1.7 Reporting and monitoring**

Several respondents noted that direct and indirect participants need secure tools with functionalities providing detailed and clear information on operations. The tools provided in support of the liquidity management process should allow sufficient analysis and provide sufficient information. Some respondents demanded that CCBM2 support existing evaluation tools<sup>4</sup> and that the respective market requirements be defined by national user groups.

Overall, respondents suggested that national user groups should be involved in establishing the reporting and monitoring standards to be implemented in CCBM2. In particular, some associations of credit institutions asked that forecasting elements concerning usable collateral over the coming days (e.g. the future value of specific assets) be added in order to assess future decisions on collateral and credit.

## **1.8 Collateral in emergency situations**

Many respondents welcomed the introduction of an emergency collateral module dealing with non-euro-denominated collateral and called for technical solutions to be implemented in the first release of CCBM2. Some respondents considered that the use of non-euro collateral (e.g. USD and GBP) should not be limited to emergency situations only.

An ICSD mentioned that ICSDs' tri-party collateral management services would be an efficient way of mobilising non-ECB eligible and foreign collateral assets for the Eurosystem, remarking that a number of major central banks outside the Eurosystem (e.g. the Federal Reserve Bank of New York) already use these facilities today. In this context, a CCP suggested exploring the use of DTCC's repurchase account to access US collateral.

Furthermore, some respondents recommended that this module include a solution allowing the delivery of eligible collateral to Eurosystem NCBs in order to obtain credit in another currency outside the euro area (e.g. in the context of the term auction facility, the auction for the provision of US dollars to Eurosystem counterparties), indicating that the credit freezing functionality could serve this purpose. Furthermore, CCBM2 should also support the use of cash as collateral and allow collateral substitution in such a cross-

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<sup>4</sup> Tools developed for the purpose of providing an overview of all positions relevant to central bank money, i.e. securities holdings (delivered, ECB-eligible, auto-collateralisation-eligible) and the associated payment flows or cash balances.

currency environment. This solution should be possible in different currencies. Some respondents advocated the full participation of the NCBs of the European Economic Area.

In order to minimise the time required for the implementation of such a solution, it was suggested that priority be given to the US dollar and the yen, with a focus on assets currently accepted in the three currency areas (i.e. tier one assets).

One respondent suggested that CCBM2 should act as *“the leading worldwide central bank facility as far as global collateral management with other central bank(s) is concerned”* and encouraged the Eurosystem to *“continue to be forward looking”* and develop a CCBM2 that looked *“beyond the euro area borders from its very start”*. This was presented as the next challenge for the Eurosystem and the banking community, given its legal and technical complexity.

## **1.9 ICT**

Remarks on the chapter dealing with ICT issues referred to the following issues.

### **(i) Communication networks**

Some respondents remarked that network connections should use the infrastructure adopted for the TARGET2 SSP, offering both user-to-application and application-to-application modes for interaction with all CCBM2 modules.

Furthermore, some respondents considered that SWIFT should be the preferred option, while the use of the internet could be an alternative option (e.g. as a back-up for SWIFT), subject to an assessment of the business case (taking into account the question of whether necessary security aspects and user rights management had been developed). Another respondent recommended quantifying the level of support for the web interface before any decision was made, indicating strong reluctance to contribute to any costs involved. For instance, a couple of respondents expressed a preference for a web interface for communications regarding credit claims (e.g. for the bulk procedure), provided that this could be done in a secure and cost-efficient manner, and advocated allowing users to choose from a number of secure alternative network providers. Furthermore, one CSD suggested using dedicated connections with CSDs in order to reduce costs.

In its response, SWIFT confirmed that it was keen to ensure that direct participants in CCBM2 had a simple and cost-effective SWIFT option for their communications with CCBM2. This would allow existing SWIFT infrastructure to be reused where appropriate and would minimise the total investment costs for the financial community.

### **(ii) Eurosystem single interface concept**

Several participants stressed that a common interface should be established for TARGET2, T2S and CCBM2 in order to meet treasurers' need to access information from the three systems. Some stated that the single interface should not only provide a single gateway, gaining the maximum benefit from the required technical investment and granting participants the flexibility to access all or part of the services, but also allow access to consolidated operational information for the three systems.

One respondent specified that, in the context of centralised group liquidity monitoring, group liquidity managers should be able to monitor the collateral positions of their banks, branches and subsidiaries. Functionalities giving treasurers full visibility during TARGET2 opening hours would thus be needed in order to enable group liquidity managers to put in place liquidity control measures appropriate for the group's business and liquidity needs. In this context, it was recommended that CCBM2 information cover:

- group collateral positions for the pooling of the liquidity perimeter in TARGET2;
- credit freezing facilities;
- self-collateralisation positions;
- credit outstanding in CCBM2;
- monitoring of the processing status of transactions in CCBM2; and
- daily margining valuations.

Several respondents requested that TARGET2's existing web browser, the ICM interface, be enhanced to cover TARGET2, T2S and CCBM2, as well as offering application-to-application connectivity together with a portal through which more sophisticated counterparties could build their own bespoke interface in accordance with their needs – e.g. for securities, cash and collateral. This would enable TARGET2 banks to integrate the CCBM2 interface with a “single window” approach based on the SWIFT network (using Fileact and Interact protocols).

### **(iii) IT infrastructure**

Some respondents, especially from the German counterparty community, noted that, given the close interaction between TARGET2, T2S and CCBM2, the three services could be offered on a single shared platform to provide real-time information and an efficient, cost-effective solution (exploiting synergies).

These respondents asserted that, should the Eurosystem decide against such a structure, any resulting additional costs should not be passed on to users, and neither should the overall efficiency of the interaction between the three services be adversely affected.

It was also suggested that consideration be given to the question of whether, irrespective of the responsibility for the development of CCBM2, the servers providing the platform could be situated at the same location as those running TARGET2 and T2S, e.g. in order to make use of their contingency measures. In this case, the CCBM2 operating team could access the infrastructure on a remote basis.

### **(iv) Operating time**

Several respondents recommended establishing common operating hours and a synchronised calendar for TARGET2, T2S and CCBM2 and ensuring compatibility with other ESCB tools (such as night-time settlement), particularly with regard to end-of-day deadlines.

## **2. Additional comments not related to the CCBM2 user requirements**

This section presents comments reported in the responses in the second consultation on CCBM2 which were not directly related to the CCBM2 user requirements.

### **(i) Harmonisation of national practices**

Many respondents recognised that CCBM2, being a collateral management system for NCBs, would not be able on its own to resolve most of the failures encountered by market participants in relation to cross-border collateral management and mobilisation. They therefore called for a complementary harmonisation stream to be launched in cooperation with the market. It was suggested that a public consultation be held on this matter.

These respondents referred to several areas for harmonisation, such as: message formats used by CSDs (the progress made in this area in relation to Giovannini Barrier 1 will help); instruction types across products; CSDs' opening hours and calendars; CSDs' procedures; links between SSSs (to allow intraday mobilisation); legal frameworks; handling procedures for credit claims (e.g. as regards notification); and valuations.

One respondent suggested that national specificities should either represent best practices (in which case, they should be generalised across the euro area) or be phased out, as they act as barriers to the integration of European financial markets.

### **(ii) Timing of the implementation of CCBM2**

Most respondents advocated the early implementation of CCBM2. In particular, several respondents asserted that CCBM2 should be implemented irrespective of any decision on T2S and requested that CCBM2 go live before T2S (and as soon as possible, preferably by 2010).

However, a few respondents advocated conducting an assessment of the profitability of the business case before deciding whether or not to implement CCBM2 before T2S, to avoid any possible impact on end-users.

One respondent proposed adopting a gradual approach, according to which CCBM2 would initially have limited scope as regards securities, while the credit claims module would be implemented at a later stage. Other respondents explicitly stressed the need to implement the credit claims module as soon as possible.

One CCP expressed a preference for launching CCBM2 around the same time as the implementation of T2S.

### **(iii) CCBM2 fees**

Several respondents requested further clarification regarding the recovery of costs and asked that banks be involved in discussions on this matter. Some respondents, especially from the German counterparty community, voiced the expectation that, in accordance with current practices in several NCBs, only third-party costs would be passed on (i.e. there would be no recovery of internal costs).

**(iv) Cooperation with the market**

A couple of respondents suggested that (in addition to COGESI meetings) an ad hoc group comprising European collateral management specialists be established to look at CCBM2.

**(v) Other comments going beyond the scope of the CCBM2 project**

Some respondents used the opportunity presented by this second consultation on CCBM2 in order to put forward a few requests concerning other issues going beyond the scope of the CCBM2 project.

- Removal of restrictions on settlement locations

Some respondents reiterated their requests for the removal of current restrictions, introduced by Eurosystem policy rules, regarding the location of settlement. In particular, they requested:

1. the removal of the repatriation requirement currently applicable in the CCBM;
2. the removal of the limits on NCBs' remote access to foreign CSDs; and
3. the extension of asset eligibility to cover assets held in the European Economic Area.

- Improving the approval process of SSSs' links

One respondent pointed out the need to improve the approval process for direct and relayed links, especially with regard to its duration.