EUROPEAN CENTRAL BANK

SUMMARY OF THE 14TH MEETING OF THE CONTACT GROUP ON EURO SECURITIES INFRASTRUCTURES (COGESI)

(HELD IN FRANKFURT ON 18 MAY 2006 FROM 9.30 A.M. TO 4.30 P.M.

IN THE ECB'S EUROTOWER, CONFERENCE ROOM V)

1. Opening remarks by Mr J.-M. Godeffroy, Chairman

After some general remarks regarding the meeting, the Chairman touched upon two topics but said that he preferred not to discuss them in detail at that stage. The first topic was the work on TARGET2 interactions with securities settlement systems (SSSs). He emphasised that, for the time being, this was an internal issue for the Eurosystem, but he knew that it was now widely known in the market that central banks were discussing how they could, in the medium to long term, provide central bank money settlement for securities transactions. The second topic was the work of the joint working group of the European System of Central Banks (ESCB) and the Committee of European Securities Regulators (CESR), which had been on hold for some time.

2. Eurosystem collateral framework

Mr M. Bayle (ECB) briefed the group on the developments and decisions taken with respect to the Eurosystem collateral framework. In accordance with the decision of the Governing Council of the European Central Bank (ECB), credit claims (bank loans) would be introduced as eligible collateral on 1 January 2007. During the first phase, until 31 December 2011, different national procedures and thresholds would co-exist and, from January 2012, a single harmonised threshold of €500,000 would apply. With regard to risk management, the same haircuts would be applied across the board, from the start of the first phase.

Mr G. De Vidts (ICAP) then updated the group on industry discussions on credit claims, in particular initiatives by the European Repo Council (ERC) and ACI, the Financial Markets Association. He stressed that credit claims were a new asset class gaining increasing prominence in Europe, but that problems remained regarding the practical implementation of their use as collateral (e.g. pre-notification), which could only be solved through close cooperation between central banks and the market.

This view was confirmed by Mr J. Mérère (Chairman of the European Central Securities Depositories Association – ECSDA), who reported on a recent joint ECSDA-ACI meeting on credit claims and said that there should be a consistent credit claim solution for monetary policy operations and secondary market use and that central securities depositories (CSDs) and banks should work together with the central banks to remove the existing obstacles. This would also be a prerequisite if CSDs were to invest money in providing the corresponding services. Ms D. Russo (ECB) acknowledged a lack of harmonisation between the national central banks (NCBs), but recalled that the decision to have a harmonised framework only after 2012 was taken in order not to further delay the adoption of the Single List. She argued that the market was interested in all credit claims, not just those eligible for use as collateral, but the framework created by the central banks for monetary policy and intraday credit operations would not be sufficient to support a secondary market for credit claims. In this respect, rather than limiting their possible involvement to settlement services alone, CSDs should consider the possibility of also providing "notary" services.

During the discussion, Mr R. Hamaui (Banca Intesa) stressed the importance of credit claims, the acceptance of which as eligible collateral would, in his view, have a major impact on the loan business of banks, and supported the chosen step-by-step approach, which he considered more realistic than immediately aiming for full harmonisation. Mr J. Metzger (Deutsche Bundesbank) expressed some reluctance to put credit claims on the same platform as for the secondary market because central banks should interfere as little as possible with the market, although they would be ready to help markets overcome the obstacles, for example with regard to the cross-border use of credit claims.

Thereafter, the discussion turned to the need for further integration and rationalisation of the securities settlement infrastructure in Europe and, in particular, to the wish expressed by market participants for a single European settlement system for securities in order to harmonise procedures, increase efficiency and move securities across borders with ease. The question of whether such a system could be provided by a single CSD or even a single SSS, and whether linkages between CSDs could also be used to create a common set of procedures, was debated. Mr Godeffroy concluded that this interesting discussion on the much broader topic of European integration should be continued on another occasion and that, with regard to credit claims, the ultimate objective would clearly be to harmonise procedures, even if it were decided to start with non-harmonised systems. Ms Russo added that, in order to satisfy the apparent need of banks for information regarding credit claims, information concerning the operational framework adopted in each country would be made available by the ECB as soon as all the relevant decisions had been taken in the countries concerned.

3. Global liquidity management

Mr De Vidts introduced this item with a presentation on liquidity management, focusing on intraday liquidity and the role of central banks. He concluded by stressing the need for close cooperation between the banking industry, regulators and central banks and for full interoperability between all actors until 5.30 p.m. so as to achieve a robust same-day funding market in euro. With regard to the role of central banks as the lender of last resort, the Chairman stated that central banks took this role very seriously and were well prepared. Ms D. Chan (Citigroup) pointed out that more and more financial institutions were confronted with payment deadlines during the day and that missing these deadlines had a domino effect on other financial institutions. Therefore, intraday liquidity solutions were required, one of which was the ability to deploy collateral easily to create liquidity when and where needed. During the discussion, Mr G. Hartsink (ABN Amro) highlighted the differences between the euro and US dollar markets, in particular the charges for intraday liquidity applied by the US Federal Reserve System, and asked whether settlement cycles should be standardised. Mr Godeffroy said that the Eurosystem had no intention of changing its practice of not charging for intraday liquidity and accepting a wide range of collateral. The downside of the US model was the accumulation of payments towards the end of the day, whereas in TARGET half of the payments were settled by midday. With regard to settlement cycles and times, the Chairman questioned whether harmonisation, i.e. settling everything at the same time, was really worth striving for and would in fact increase risks. Market participants argued that there should be a combination of (i) a minimum number of cycles to avoid risks and (ii) an optimisation of the cycles. Misconduct by banks and the importance of penalties to ensure that settlement deadlines are observed were also mentioned in this context. It was concluded that an overview of all current and future settlement cycles and/or times of ancillary systems and the identification of outstanding issues (e.g. reasons why links are not widely used) could be a key project and a topic for discussion at the next meeting. The Chairman tentatively called this item “obstacles to smooth intraday liquidity management” and offered the possibility of having an ad hoc meeting with representatives of market infrastructures, banks and the Eurosystem, for example, two months before the next COGESI meeting.

4. Use of foreign collateral

Ms Russo started by presenting the Committee on Payment and Settlement System’s report on cross-border collateral arrangements and the Payments Risk Committee’s report on global payment liquidity. She concluded that, due to different market needs, it was difficult to come up with a common policy concerning the acceptance of foreign assets as collateral, but that central banks should nevertheless push for greater harmonisation, for example, in the fields of legal practices and operating times in the United States and Europe, and should promote common solutions such as the use of common communication protocols. Ms W. Lucas (UBS) gave a presentation and listed operational issues to be addressed from the perspective of a bank active in all major currency areas, namely transparency in the process of adding securities to the basket of eligible collateral, interoperability between ICSDs and domestic CSDs, and problems caused by multiple jurisdictions. In her closing remarks, she spoke of a need for further development of the cross-border collateral infrastructure as an industry-wide initiative to enhance global systemic stability. This conclusion was supported by market participants during the discussion. The Chairman explained that, although the Eurosystem would be willing to accept foreign collateral in crisis situations, it has no intention to include it in its collateral list for normal payment processing.

5. Business continuity

The discussion of this and the following items were chaired by Ms Russo. Mr T. Kokkola (ECB) presented the draft programme of the business continuity conference, which is set to be held on 25-26 September 2006 in Frankfurt. COGESI members would be invited to attend. During the discussion, market representatives made several comments on the intended subjects and potential speakers. It was proposed, for example, to discuss central counterparty contingency plans, to perhaps hold parallel sessions, and to invite the Continuous Linked Settlement Bank and a network provider such as SWIFT to speak. The Eurosystem would take the comments received into account in preparing the conference.

6. Organisation of COGESI

Ms Russo invited the participants to share their views on the representation and topics of COGESI. In general, the composition of the group and the areas it covered were considered useful, and its open and constructive atmosphere was praised by group members. Some suggested having a more structured and detailed discussion on certain topics and asked for information (i.e. the agenda, minutes and documents) to be sent as early as possible. Ms Russo concluded that, although there was no reason to change the structure of the group or to create permanent sub-groups dedicated to specific issues, it could be helpful to have more in-depth discussions sometimes. It was also decided to circulate the agenda earlier whenever possible and to distribute a first draft agenda to all members of the group.

7. Letter received from the Money Market Contact Group

At the last meeting of the Money Market Contact Group (MMCG), a number of settlement-related issues were raised by participants and forwarded by the chairman in a letter to the Director General Payment Systems and Market Infrastructure of the ECB, Mr Godeffroy. He had decided to put the letter on the agenda of the COGESI meeting to ascertain where (i.e. either in the COGESI or the MMCG forum) and how best to discuss these issues and how to respond to the letter. During the discussion, it was noted that the issues affected different stakeholders and that feedback and input from both groups could be helpful. Ms Russo summarised the discussion by saying that the first two issues raised in the letter were more appropriate for the MMCG to discuss and that the rest should be addressed through COGESI discussions and findings. Furthermore, it was proposed that a representative from the MMCG be invited to attend COGESI meetings as an observer, and that lists of participants, agendas and minutes of MMCG and COGESI meetings be shared on a regular basis to improve coordination between these two bodies and within the banking industry, and especially to avoid having conflicting views presented in the two groups.

8. Relations with the European Commission and the European credit sector

Mr S. Lo Giudice (European Commission) informed the group about work currently under way at the European Commission, which includes a report on the status of the removal of the "Giovannini barriers" in the Member States, work on the Settlement Finality Directive (SFD), and a draft working document on regulatory impact assessment. With regard to the SFD, which was first only sent to the Member States, the European Commission would soon launch a consultation exercise with the banking industry via its website.

Thereafter, Mr D. Hermans (European Banking Federation – FBE) briefed the group on work on the harmonisation of corporate actions processing. His presentation included an update on the implementation of the recommendations made by the European Credit Sector Associations (ECSA) and the ECSDA, and the outcome of an implementation workshop held by the ECSA on 18-19 January 2006. The key outcome of this workshop was a gap analysis to ascertain where countries stood in terms of implementation and to identify common issues. Based on the findings of the workshop, a joint ECSA-ECSDA report on progress made in the field of harmonising corporate actions would be published.

Mr E. Derobert (European Association of Cooperative Banks – EACB) added that a second workshop was planned as a follow-up later this year. During the discussion, Mr P. Stecconi (Banca d'Italia) said that more attention should be paid to the transfer of beneficial ownership. Mr Hermans answered that, although not insuperable, the change of ownership did make the harmonisation of corporate actions more complex and had therefore been flagged and would be considered accordingly.

Finally, Mr Mérère gave a presentation on behalf of the ECSDA on progress and compliance with regard to the removal of barriers 4 (settlement finality) and 7 (operating times). In the discussion, the remarks made by banks and CSDs echoed to a large extent those made in the earlier discussions on settlement times.

9. Other business

The next COGESI meeting will take place on Friday, 17 November 2006.