International Banking Federation

Pinners Hall
105-108 Old Broad Street
London EC2N 1EX

tel: + 44 (0)20 7216 8947
fax: + 44 (2)20 7216 8928
web: www.ibfed.org

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Mr Svein Andresen
Secretary General
Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland
fsb@bis.org

Dear Mr Andresen,

Re: FSB Interim Report on Securities Lending and Repos: Market Overview and Financial Stability Issues

The IBFED appreciates the opportunity to comment on the FSB's Interim Report on Securities Lending and Repos: Market Overview and Financial Stability Issues. The IBFED supports the FSB's work on shadow banking and wishes to ensure a strong securities lending and repo market in the future.

We wish to offer the following comments:

General

Securities lending transactions and repurchase (repo) transactions are of fundamental importance for credit institutions and other market participants to ensure adequate liquidity. The new regulatory framework, in particular for capital and derivatives, will significantly increase the demand for highly liquid and high quality assets in order to satisfy collateralisation requirements (e.g. for CCP-clearing or for bilateral OTC-derivative transactions). At the same time, access to high quality assets is becoming more difficult.

Securities lending as well as securities repurchase (repo) transactions are widely used in financial markets and are essential for securing funding and liquidity. Consequently, any regulatory requirements regarding securities lending and repurchase (repo) transactions should be balanced and take into account the importance of these activities to avoid any unintended consequences.

The IBFED endorses the submission of the International Capital Markets Association/ European Repo Council to the FSB on this issue.

In addition, with respect to securities lending markets, the IBFed would favour increased transparency for these types of transactions with particular emphasis on globally consistent disclosures. However, we are concerned with FSB comments in 5.5 that appear to indicate that when an agent lender indemnifies a loan against borrower default, there could be implications for market stability. In our opinion, such indemnifications reflect the rigorous credit screening and monitoring performed by agent lenders who, as a general matter are better situated than the beneficial owners to perform this function.

The FSB has also raised concerns in 5.6 with regard to reinvestment of cash collateral. Beneficial owners who participate in agent lenders' programs are seeking greater returns on their investments, and reinvestment of cash collateral is a means to achieving that goal. Cash collateral is generally invested in short-term, liquid assets such as short-term money market eligible instruments or high-quality repurchase agreements. The reinvestment program typically involves investments through either commingled funds or separate accounts, under investment guidelines established by the beneficial owner. While the FSB states that there may be conflicts of interest arising from these arrangements, we note that many beneficial owners are subject to regulatory oversight of the reinvestment of their cash collateral, and agent lenders are typically banks under the supervision of relevant OECD regulators. We believe the FSB should exercise caution and fully consider both current practices and regulatory requirements before imposing duplicative regulations for this market.

In addition, IBFed would like to underscore the following key messages:

- **Potential regulation of shadow banking –** While the FSB provides a definition of shadow banking, the IBFED requests that the FSB develop a framework that would help delineate what areas of the shadow banking sector may warrant regulation and areas that would not meet any threshold to warrant regulation.

- **Diversity of funding sources –** if restrictions on repos reduce the size of the securities lending and repo markets, institutions would be forced to depend more heavily on other sources of funding, which could potentially increase risks in other areas.

- **Liquidity -** liquid collateral can act as a substitute for meeting money demand and reducing the availability of this funding source could have significant impacts.

- **Competition -** if the restrictions on shadow banking operations were too prohibitive, it would reduce the competitive aspect with the traditional banking sector, which could distort free market operations and incentivise regulatory arbitrage.

- **Lack of transparency –** participants active in these markets are capable of performing the required due diligence to negate or offset any lack of transparency, or failing that, can adjust their positions accordingly. However, we agree that the markets may be too opaque for regulatory purposes. In any case, the IBFED supports greater transparency in this area.

  It should be noted that the proposed global trade repositories alone will result in hundreds of millions of information points every year, providing greater transparency to OTC markets by bringing data already available together at one point. Strengthening market infrastructures in Central Clearing Counterparties (CCP) will help increase transparency, efficiency and manage counterparty risk. The IBFED believes that existing information should be fully utilised and analysed before any new reporting requirements are added.

- **The case for mandatory minimum.** Haircuts - If mandatory minimum haircuts should be implemented, a differentiated approach to tenors should be envisaged.

- **International alignment** is a key issue and needs to be fully considered in order to ensure a level playing field. The IBFed therefore fully supports the work of the FSB and urges its members to consider appropriate and coordinated global measures to address the identified systemic risks of shadow banking.

Yours sincerely,

Mrs Sally Scutt	Mrs Barbara Frohn
Managing Director	Chairman
IBFed	IBFed Prudential Supervision Working Group