ICMA EUROPEAN REPO COUNCIL

Financial Stability Board
Centralbahnplatz 2
CH-4002 Basel
Switzerland

14 January 2013

Dear Sirs,

Response submission from the ICMA European Repo Council

Re: Three FSB Consultative Documents "Strengthening Oversight and Regulation of Shadow Banking"

Introduction:

On behalf of the European Repo Council ("ERC") of the International Capital Market Association ("ICMA"), the purpose of this letter is to provide feedback primarily concerning the repo oriented aspects of the Financial Stability Board's ("FSB's") three 18 November 2012 consultative documents regarding "Strengthening Oversight and Regulation of Shadow Banking". These three documents are (i) "An Integrated Overview of Policy Recommendations"; (ii) "A Policy Framework for Strengthening Oversight and Regulation of Shadow Banking Entities" and (iii) "A Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos". The ERC notes that the FSB has invited comments on these consultative documents, which forms part of a package of documents regarding the FSB's work on shadow banking, and that this consultation will contribute to the determination of final recommendations expected to be published in September 2013.

The repo market is one of the largest and most active sectors in today's money markets. It provides an efficient source of money market funding and securities borrowing for financial intermediaries, while providing a secure home for liquid investments. An efficient repo market is pivotal to the liquidity of both primary and secondary debt markets, and for the management of collateral for other activities (such as CCP margining). Repo is also used by central banks as their principal tool in open market operations to control short-term interest rates. Repos are attractive as a monetary policy instrument because they carry a low credit risk while serving as a flexible instrument for liquidity management, which benefits the functioning of financial markets. Central banks are also able to act swiftly as lenders of last resort (and have done so) during periods of market turbulence by way of the repo market.[1] In a repo transaction securities are exchanged for cash with an agreement to

[1] The ERC has published a White Paper on the operation of the European repo market, the role of short-selling, the problem of settlement failures and the need for reform of the market infrastructure. This paper sets out in greater detail what the repo market is and its benefits and is available via the ICMA website at http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Repo-Markets/European-repo-market-white-paper.aspx.

repurchase the securities at a future date. The transaction is collateralised, with the cash securing the seller's securities and the securities securing the buyer's cash. In the event of default, the collateral can be sold and exposure to the defaulting party can be netted off without delay, minimising exposure to adverse market movements. Collateral and netting are key to the proper functioning of repo markets.

The ERC was established by ICMA in December 1999, to represent the cross-border repo market in Europe. It is composed of practitioners in this market, who meet regularly to discuss market developments in order to ensure that practical day-to-day issues are fully understood and dealt with adequately.

Commentary:

Whilst there are many elements being considered in the FSB's overall examination of Shadow Banking, the ERC is primarily focused on those aspects that bear most directly on repo. Given this these comments are relatively general in responding to the first two of the consultative documents and rather more specific concerning the third consultative document ("A Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos"), much of the content of which is of direct significance to the ERC.

A. Comments regarding "An Integrated Overview of Policy Recommendations"

Given that this consultative document is itself an overview, the ERC's few responsive comments really provide a general opening ahead of the more detailed points made further on in this submission.

Considering WS1: Banks' interactions with shadow banking entities (paragraph 1.2.1), the FSB notes a number of measures that should strengthen the resilience of the banking sector against some risks posed by shadow banks, including increased capital requirements for short term liquidity facilities provided to securitisation vehicles. Whilst efforts to increase banking resilience are understandable it should be remembered that there is an inevitable balance to be achieved. The ERC observes that one impact of this particular change is that it makes the cost of collateral higher, thereby contradicting the G20's aim of making markets safer. The ERC, through ICMA, is supporting the Collateral Initiatives Coordination Forum's ("CICF's")[2] cross industry efforts on collateral.

Considering WS2: Money market funds ("MMFs") (paragraph 1.2.2), the FSB's recommendations include a specific item concerning MMFs' practices in relation to repos. In considering any guidelines responsive to this recommendation, the ERC respectfully suggests that regulators should make use of the ERC's established market practice guidelines; and more broadly the ERC's efforts in respect of repo market education and the establishment of a sound legal framework, embodied in the GMRA. The ERC's April 2012 position paper "Building and Sustaining the European Repo Market", which was included as an appendix to the ERC's 22 May 2012 response to the FSB's "Interim Report on Securities Lending and Repos", provides a more detailed description of these existing elements of the European repo market.[3] The ERC also draws your attention to the stability of MMFs' repo investment during the crisis, that was revealed in an analysis of SEC returns by Arvind Krishnamurthy, Stefan Nagel and Dmitry Orlov in their paper on "Sizing Up Repo" (November 2011).

2 http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/collateral-initiatives-coordination-forum/
3 http://www.icmagroup.org/assets/documents/Maket-Practice/Regulatory-Policy/Repo-Markets/ERC-contributions/FSB-interim-SB-report-re-repos_ERC-response_final.pdf

Considering WS3: Other shadow banking entities (paragraph 1.2.3), authorities are to identify shadow banking risks by reference to "the framework of five economic functions". One of these five functions is described as "intermediation of market activities that is dependent on short-term funding or on secured funding of client assets". Whilst recognising that such an economic function can play a part in shadow banking activity, the ERC notes that this description covers an important economic activity, which may involve funding through repos or securities lending, that should not in itself be discouraged. What is important is to understand the risks being taken and to ensure they are appropriately managed.

Considering WS4: Securitisation (paragraph 1.2.4), the ERC has no particular comments at this stage.

Considering WS5: Securities lending and repos (paragraph 1.2.5), the ERC's comments are included under point "C" (below) of this submission.

B. Comments regarding "A Policy Framework for Strengthening Oversight and Regulation of Shadow Banking Entities"

As an overall suggestion, the ERC feels that, given the increasing pressure on collateral, it may be useful to establish a global workshop / study. The aim in doing so would be to provide adequate focus on cross-regulatory initiatives and analysis regarding collateral availability impacts. In relation to this, the 1st step could be to look to the ad hoc COGESI working group, which is looking at collateral eligibility requirements as established by the major central banks (this ECB study should be released in the 1st quarter of 2013).

Concerning intermediation of market activities that is dependent on short-term funding or on secured funding of client assets, the consultative document describes two examples (at paragraph 2.3). In principle the ICMA considers that both banks and non-bank financial entities engaged in these activities should be subject to equivalent regulation, oversight and legal protection. The market should present a level playing field for those involved from the sell-side; and equally for those involved from the buy-side.

In relation to the "Management of client cash pools with features that make them susceptible to runs", the consultative document describes "Restrictions on maturity of portfolio assets" as a policy tool (at paragraph 3.2.1, Tool 1). One of the examples given of such restrictions is "limits on the duration.. ..of the fund's portfolio". The ERC is concerned that the application of such limitations could seriously impact market developments and efficiency; and accordingly suggests that particular care be taken in this area. The concern perceived is that the risk of individually well intentioned policy initiatives having conflicting impacts which unduly constrain the availability of longer term finance. For example, prompting funds to shorten their investment requirements somewhat contradicts requirements for bank to reduce reliance on short term funding.

The same overall section of the consultative document moves on to describe "Liquidity buffers" as another policy tool (at paragraph 3.2.1, Tool 3c). The description of this tool refers to "Liquidity buffers comprised of highly liquid cash or near-cash instruments..". The ERC highlights that the downside of this approach is that, incremental to concerns already much debated in respect of proposed bank liquidity coverage ratio (LCR) requirements, this would increase the hoarding of collateral, decrease liquidity in the system and may create unintended squeezes on certain bonds. Already much concerned about such difficulties, the ERC, in collaboration with the community of European primary dealers (represented by AFME) have been in discussion with the ECB regarding the possible role which a repo facility could play, by creating the possibility for securities acquired by the ECB to be recycled in the market.

In relation to “Securitisation and funding of financial entities”, the consultative document describes “Restrictions on eligible collateral” as a policy tool (at paragraph 3.2.5, Tool 2). The ERC is very familiar with concerns over the liquidity of collateral and specifically draws the FSB’s attention to the White Paper[4] on “Collateral Fluidity”, published by the Collateral Initiatives Coordination Forum (“CICF”) on 7 November 2012. This White Paper calls for regulatory authorities to focus on the efficient mobilisation of collateral in financial markets and offers the CICF’s vision for improvements in collateral infrastructure.

The same overall section of the consultative document moves on to describe “Restrictions on exposures to, or funding from, banks/other financial entities” as another policy tool (at paragraph 3.2.5, Tool 3). The ERC particularly notes the final sentence of this paragraph, being concerned that, including through their impact on the stock of available collateral, there is indeed a risk that such restrictions will lead to “pressures on funding for the financial entities concerned and.. .. possible adverse implications on market efficiency.”

C. Comments regarding “A Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos”

i). General comments

The ERC welcomes the work which the FSB is doing, particularly as there is a strong need to ensure that any reforms develop in a way which is internationally consistent; both as to content and timing. The ERC is also pleased to have this further formal opportunity to comment on the FSB’s evolving output from this workstream, but considers that, particularly as there is the potential for damage to overall market efficiency and liquidity, more time does need to be allowed for detailed and careful reflection on the draft recommendations.

The ERC wishes to draw specific attention to two papers written by Mr Richard Comotto[5] in February and March of 2012, which are directly relevant to the debate on repos and shadow banking. These papers were already heavily referenced in the ERC’s 22 May 2012 response to the FSB’s “Interim Report on Securities Lending and Repos”. Particularly since it does not believe that there is a sound rationale for imposing mandatory minimum haircuts, the ERC considers that these earlier papers remain highly pertinent; and respectfully requests that they be carefully read and fully considered alongside the particular remarks contained in this consultation response.

The ERC considers that transparency to the authorities is the crucial area where immediate progress needs to be made. The ERC considers that if initial efforts focus on leveraging existing pools of data and the use of surveys, this can be done on a timely basis. Effecting such a short term improvement in transparency will in itself make it far easier for officials to assess the true requirements for longer term development. It will also facilitate the design of any relevant regulations for application to the market; and will in any case be essential for any meaningful calibration of new regulations.

The ERC suggests that it would be very helpful to the FSB’s further consideration of the idea of a trade repository if it were to organise a dedicated workshop meeting along similar lines to the ECB’s 3

[4] http://www.icmagroup.org/assets/documents/Media/Press-releases-2012/Collateral-Initiatives-Coordination-Forum-(CICF)-calls-for-urgent-focus-on-collateral-fluidity-7Nov2012v2.pdf
[5] http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/short-term-markets/Repo-Markets/shadow-banking-and-repo/

December 2012 workshop “Repo market and securities lending: towards an EU database”. At the very least the FSB should closely follow this ECB initiative, which aims to produce a blueprint by the end of June 2013; and other similar efforts, such as the work already done under the auspices of the Bank of England’s SLRC.

The ERC perceives that the heart of the concern about shadow banking lies in the need to avoid undue risk accumulating outside of the established framework of regulated financial intermediaries. As such, if there are to be measures such as mandatory minimum haircuts, these should focus on controlling the activities of unregulated entities rather than those of regulated financial intermediaries (which would otherwise suffer inappropriate duplication of requirements). The ERC continues to have fundamental doubts about the cost-efficiency of the idea of mandatory minimum haircuts, given that the driving analysis was of a very narrow sector of the US repo market, while other work (including that of the CGFS) suggested changes in haircuts were not significant.

Overall the ERC considers that the FSB’s proposed recommendations do appear to be reasonably balanced. In particular, with respect to some of the key debated topics, the ERC is pleased to note the following points:

- Trade repositories – the proposed recommendation does not say that one should be immediately set up, but rather that “The FSB should consult on the appropriate geographical and product scope of such TRs” and “the FSB should establish a working group to identify the appropriate scope and undertake a feasibility study for one or more TRs at a global level. Such feasibility studies should involve market participants”;
- Minimum haircuts – the proposed recommendation does not say they must be introduced, but rather that “The FSB should consult on whether a framework of numerical floors would be effective and workable” and “Regulatory authorities should introduce minimum standards for the methodologies that firms use to calculate collateral haircuts”… which … “seek to minimise the extent to which these methodologies are pro-cyclical”;
- Re-hypothecation – the proposed recommendation does not suggest broad measures potentially affecting re-use, but rather only calls for appropriate “regulations governing re-hypothecation of client assets”;
- CCPs – the proposed recommendation does not say they must be introduced, but rather that “Authorities should evaluate the costs and benefits of proposals to introduce CCPs in their securities lending and repo markets”; and
- Bankruptcy law – the proposed recommendation does not say that repos must further share in losses, but rather that changes “should not be prioritised for further work at this stage due to significant difficulties in implementation”.

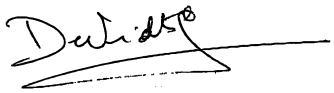
ii). Responses to specific questions

This consultative document articulates 22 specific questions, which the ERC has addressed sequentially in the Annex to this response.

Concluding remarks:

The ERC appreciate the valuable contribution made by the FSB’s examination of the issues articulated in this consultative document and would like to thank the FSB for its careful consideration of this response. The ERC remains at your disposal to discuss any of the above points.

Yours faithfully,



Godfried De Vidts
Chairman
ICMA European Repo Council

cc :	*Andrew Hauser,*	*Head of Sterling Markets Division, Markets, Bank of England;*
	Daniela Russo,	*Director General, DG Payments & Market Infrastructure, European Central Bank;*
	Nadia Calviño,	*Deputy Director-General, DG Internal Market and Services, European Commission;*
	Emil Paulis,	*Head of Directorate G, Financial Markets, DG Internal Market and Services, European Commission;*
	Patrick Pearson,	*Head of Directorate G2, Financial Markets Infrastructure, DG Internal Market and Services, European Commission;*
	Mario Nava,	*Head of Directorate H (acting), Financial Institutions, DG Internal Market and Services, European Commission;*
	David Wright,	*Secretary General, International Organization of Securities Commissions;*
	ICMA European Repo Committee	

Annex

Specific ERC responses

– regarding the twenty two questions enumerated in the consultative document "A Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos"

Introduction: General questions

Q1. ***Does this consultative document, taken together with the earlier interim report, adequately identify the financial stability risks in the securities lending and repo markets?***

Are there additional financial stability risks in the securities lending and repo markets that the FSB should have addressed?

If so, please identify any such risks, as well as any potential recommendation(s) for the FSB's consideration.

A1. The ERC does not feel that there are additional financial stability risks in the repo market that the FSB should have addressed.

On the contrary, it is the ERC's belief that the extent of the financial stability risk in the repo market continues to be exaggerated. The ERC perceives that this stems from too ready an acceptance of the so called "run on repo". As detailed in Mr Richard Comotto's February 2012 paper "Haircuts and initial margins in the repo market", the actual pattern of behaviour evident in the European repo market differed markedly from the very specific and limited segment of the US repo market upon which the authors of the "run on repo" based their analysis. And across the US repo market as a whole, there is also evidence that changes in haircuts did not in fact play a significant role in the withdrawal of liquidity (see CGFS and Krishnamurthy et al).

Q2. ***Do the policy recommendations in the document adequately address the financial stability risk(s) identified?***

Are there alternative approaches to risk mitigation (including existing regulatory, industry, or other mitigants) that the FSB should consider to address such risks in the securities lending and repo markets?

If so, please describe such mitigants and explain how they address the risks.

Are they likely to be adequate under situations of extreme financial stress?

A2. Leading international banks play a key role at the heart of the European repo market. They are already subject to significant and increasing levels of regulation. This includes increased capital and liquidity requirements (designed to be effective through the cycle e.g. through the inclusion of countercyclical buffers), amongst which is the imposition of a leverage ratio requirement. The effect of these measures on this central segment of the industry will already play a significant part in mitigating the financial stability risks arising from their involvement in the repo market. Regulation of institutions is a more efficient means of preventing the build-up of excessive leverage than attempting to achieve this by means of intervention in market pricing through minimum haircuts. It is important to keep in mind that the key risk which further measures should bear upon relates to that segment of the repo market which lies outside the authorised financial institutions sector.

Q3. ***Please explain the feasibility of implementing the policy recommendations (or any alternative that you believe that would more adequately address any identified financial stability risks) in the jurisdiction(s) on which you would like to comment?***

A3. The two overriding factors which the ERC considers do need to be borne in mind are cost and time, as further discussed in response to questions 4 and 5 below.

Q4. Please address any costs and benefits, as well as unintended consequences from implementing the policy recommendations in the jurisdiction(s) on which you would like to comment?

Please provide quantitative answers, to the extent possible, that would assist the FSB in carrying out a subsequent quantitative impact assessment.

A4. The ERC appreciates that the objective of improvements to financial stability is a longer term saving which such stability will deliver. Nevertheless, margins in repo markets are relatively thin and it would not take a great deal of incremental cost to significantly undermine the economics of the business. Accordingly where implementation will generate short term costs care should be taken to minimise these. Failure to do so could be counterproductive, as driving some of the market out of business would quite likely lead to an increase in financial instability – as the important financing channel provided by the repo market would be weakened, as would the vital role which the repo market plays in the delivery of collateral needed to satisfy safety requirements (such as liquidity buffers and margins for derivatives).

Q5. What is the appropriate phase-in period to implement the policy recommendations (or any alternative that you believe would more adequately address any identified financial stability risks)?

A5. The ERC sees the need for sufficient time to be allocated, both to permit the identification of thoughtfully designed detailed measures capable of operating in a coherent manner across international markets; and to allow for their implementation. Too much haste will not only deliver less complete and beneficial outcomes but also drive up costs. Where possible, existing data sources should be leveraged.

Policy recommendations:

Improvements in market transparency

Q6. Do you agree with the information items listed in Box 1 for enhancing transparency in securities lending and repo markets?

Which of the information items in Box 1 are already publicly available for all market participants, and from which sources?

Would collecting or providing any of the information items listed in Box 1 present any significant practical problems?

If so, please clarify which items, the practical problems, and possible proxies that could be collected or provided to replace such items.

A6. In articulating the case for improvement in regulatory reporting the consultative document states (at page #5) that there is a risk that "A large financial institution could suffer a liquidity shortage during a period of market stress due to an excessively short maturity profile of its financing." The ERC notes that this is a clear instance where, for banks, the risk has already been addressed through other regulatory changes – this being exactly the risk which the new liquidity requirements are designed to meet. The residual question is, therefore, in which way, if at all, measures should be taken to address this risk in the case of non-bank financial institutions? The ERC wishes to make clear that it does not consider that the right way is through the introduction of mandatory minimum haircuts, as it does not believe the case has been made that this would remove the risks facing firms relying heavily on repo for funding. More importantly, leverage and liquidity need to be suitably managed.

In articulating the case for improvement in market transparency the consultative document states (at page #5) that, for example, "The sudden request to return cash collateral posted against borrowed securities could lead to large losses and fire sales if the instruments in which cash collateral has been invested become illiquid." The ERC notes that, in the European context, this is an example of a concern where another reform measure has been introduced which exacerbates the problem. Finalised ESMA guidelines announced on 4 December 2012 state that UCITS should only enter into repurchase and reverse repurchase agreements if they are able to recall at any time any assets or the full amount of cash.

Considering fire-sales, the ERC notes that in case of default intermediaries within a chain of repos will not liquidate collateral, but net obligations (i.e. only the buyer at the end of a chain needs to liquidate). It is important therefore not to assume that the scale of potential liquidations would be commensurate with the size of the repo market on a one-for-one ratio

Turning to consider the list of repo market transaction level data proposed in Box 1 of the consultative document (at page #5), the ERC notes that collateral asset class ought probably to be derived by reference to ISINs, avoiding any ambiguity about which assets have been allocated to particular asset classes. Repo rate is probably best derived by reference also to repurchase amount, according to an agreed convention; and similarly haircut should be consistently derived, be reference also to asset value (to avoid complications with alternative usage of haircuts and initial margins). The FSB presumably anticipates that counterparty will be captured in a manner consistent with the LEI project.

Considering the list of firm-level data proposed in Box 1 of the consultative document (at page #6), the ERC observes that tenor composition, collateral composition and haircut ranges are suggested to be analysed by "asset class". The ERC highlights that the notion of asset class will need to be clearly defined, maybe by ISIN code, or category of instruments; otherwise there will be scope for great confusion. Point vii of this proposed list of repo market firm-level data specifies "For reverse repos: Type of collateral obtained and availability to re-hypothecate". The ERC draws attention to the fact that it is established repo market practice, as reflected in the GMRA, that this is always stipulated.

Also, considering the list of aggregate data which could be published, as data proposed in Box 1 of the consultative document (at page #6), the ERC wishes to offer a word of caution concerning "repo rates". It is necessary to anticipate that such average repo rates, published by an official body, would take on the character of an official price index. The ERC notes that, moreover, there are technical challenges. In order to make sense, the repo rates would have to be classified by tenor, type and quality of counterparty, and type and quality of collateral; and GC would have to be differentiated from specials.

The consultative document goes on to explicitly state (at page #7) that there should be "Increased transparency to the public". The ERC questions what is meant by "the public", as it is not made clear exactly what benefit is expected to be achieved through such increased transparency. Assuming that "the public" interest arises in respect of what would otherwise be termed the "retail market", the ERC draws attention to the fact that retail do not have access to the repo market, which only operates in so called "wholesale markets". Hence the ERC considers that care should be taken to firstly define what is meant by public interest and why this arises; and only then appropriately to tailor any related requirements.

Considering information which is already publicly available and practical problems associated with the provision of other data, the ERC highlights that one important concern is confidentiality. In performing the ERC European repo market surveys (see the answer to question 7 for more detail of these) this has proved to be a practical challenge. Information may, if wrongly used, create a run on a bank due to a shift by one market participant in its required haircuts for another market participant. This sort of problem can also be anticipated assuming that data collection is widened to also capture the buy-side. A further practical problem will also lie in the issue of the specific identification of collateral.

The ERC would like to raise one question regarding the list of items considered in Box 1 which is not answered so far in the consultative document. What specifically does the FSB aim to learn from all the information gathered in such a comprehensive data collection? In the meeting organised by the ECB on 3 December the ERC made a similar remark; delivering the data as highlighted in the proposal will be expensive for market participants and the practical process of gathering it into any useful form will prove equally time consuming and expensive. But such an effort will not in itself deliver the intelligence which we expect the FSB aims to receive, namely timely signals of changed behaviour that could undermine the policy recommendations you are aiming for. Hence, before starting work on the collection of such data, it would be beneficial to the community if the FSB can clearly express the exact aim of having such data. Research on market behaviour through regular contents with major market participants may provide better insight and help regulators/central banks to adjust policy in a much better way ahead of events, instead of re-active interventions based on data collected in the way envisaged in this proposal.

Q7. Do you agree TRs would likely be the most effective way to collect comprehensive market data for securities lending and/or repos?

What is the appropriate geographical and product scope of TRs in collecting such market data?

A7. The ERC notes that Box 2 of the consultative document (at page #8) summarises three "Alternative ways to collect data" and that Annex 2 (at pages #29 - #32) considers "Different approaches to data collection", including some comparison of the relative merits of regulatory reports, surveys and trade repositories. The ERC believes that it is important to avoid a situation in which market participants have duplicative data requirements imposed upon them. There will be significant expense involved in the development of new reporting technology and tools, so it is important to first allow for detailed discussions, contemplating the full range of needs of different public authorities, regarding the design of any reporting requirements.

Noting that the second of the alternatives is "Official survey", the ERC wishes to draw detailed and specific attention to the European repo market survey[6]. Performed every June and December since June of 2001, these surveys provide an important public series of data concerning the evolution of the European repo market. All of these surveys have been compiled by Mr Richard Comotto, who is available to provide a full and detailed explanation of how this has been done and what the results have shown. One very important point which arises from this is that simply collecting the data is not particularly helpful. What makes the difference is to also obtain market intelligence regarding the picture revealed by the data.

The ERC acknowledges that its existing surveys are not fully comprehensive. Not all market participants provide data, nor do all possible data elements get captured. This does not negate the value of the survey, which nevertheless does provide a meaningful semi-annual snap shot of market development based upon data from a majority of the leading European repo market's participants. This is one benefit of the flexibility that exists with the survey approach, which does not fail to operate notwithstanding the lack of a single comprehensive source of information on the entirety of the market.

The ERC sees that building on such market surveys and looking to other existing consolidated data sources, in particular CCPs and triparty agents would appear to present opportunities to make timely improvements in transparency, whilst not excluding the possibility to work towards the identification of a cost effective approach to the longer term establishment of more comprehensive consolidation of trade level information. Indeed, with the benefit of short term transparency improvements it would become far easier to assess the true requirements for longer term development; and to design and calibrate any relevant regulations for application to the market. When progressing such work there will be an array of more detailed questions to resolve, including which data elements to capture, at what level of aggregation and with which periodicity?

The ERC's experience suggests to it that the value of data about the composition of collateral is unlikely to depend on high granularity. Most repo is in government securities (80% in Europe) or government-guaranteed (e.g. Agency and Agency MBS). What is most relevant in these sovereign collateral cases (and is similarly the case for collateral issued by supranationals) is the question of which government is the issuer/guarantor, with maturity and other details typically being of lesser significance. Given the relatively small share of non-government collateral, increasing granularity is likely to offer diminishing returns.

The ERC notes that Recommendation 1 in the consultative document specifically applies to "large international financial institutions" ("LIFI"s), which are also the subject of the work of the FSB Data-Gap Group. This concept of focussing distinctively on LIFIs is not particularly developed and could be further considered, whilst also seeking to fully appreciate the emerging information requirements of other public authorities, including central banks. Considering the entity coverage of a potential TR, the ERC observes that an efficient compromise might be for LIFIs to report to a trade repository and for smaller and/or domestic financial institutions to

[6] http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/short-term-markets/Repo-Markets/repo/

provide limited regulatory reports and to be encouraged to participate in national or regional surveys, possibly by industry associations (i.e. a combination of all three methods may be appropriate). TR costs would likely have greater influence on non-LIFIs, whilst their addition to the data set would provide rapidly diminishing incremental benefits.

Considering the geographical scope of a potential TR, the ERC considers that there should ideally be a global view, as opposed to purely local TRs. That said there would still be value in being able to capture data for Europe as a single block, so long as whoever leads the development of a TR template does design it whilst keeping the rest of the world in mind. Whilst the interest of individual central banks is inevitable closely associated with the data for the particular currency which they manage, it is clear that in principle we should look at all currencies; and most certainly Europe would wish to capture US dollar collateral trades.

Q8. What are the issues authorities should be mindful of when undertaking feasibility studies for the establishment of TRs for repo and/or securities lending markets?

A8. Recommendation 3 in the consultative report proposes an "interim step". From a European perspective the ERC considers that it is highly desirable that this be developed directly in conjunction with the existing ECB led initiative towards an EU repo database. Multiple or duplicative efforts should be avoided.

The ERC notes the recent Russian initiative to require the reporting of repos (and other OTC transactions), entered into under master agreements, to the National Settlement Depository ("NSD"). This already illustrates the need for a coordinated global approach, rather than piecemeal national developments, particularly since it includes an undesirable aspect. Under the new Russian requirements unreported transactions will not be eligible for the purposes of calculating netted close-out amounts. This seems likely to create unintended consequences and the ERC considers that it is inappropriate to link such commercial elements into the operation of what ought to be not-for-profit reporting entities.

From a practical standpoint, the ERC also wishes to highlight the sheer volume of data required to manage transaction level information over the life of trades. Authorities should be mindful that they need to be able to consume the data while it is still relevant and also that, at a transaction level at least, submissions of bi-lateral would need to be agreed and matched. It is worth recognising that there are a number of potential sources of data (triparty agents, trading platforms, CCPs, settlement agents, CSD's, bi-lateral market participants). Knowing more exactly which attributes concerning which population of trades and for which required timing of submission are essential to meeting the authorities' requirements, will greatly assist the market in establishing the most efficient and reliable way of sourcing the data.

Improvements in corporate disclosures

Q9. Do you agree that the enhanced disclosure items listed above would be useful for market participants and authorities?

Would disclosing any of the items listed above present any significant practical problems?

If so, please clarify which items, the practical problems, and possible proxies that could be disclosed instead.

A9. The consultative document states (at page #9) that "Disclosure is particularly poor in relation to transactions, such as collateral swaps, that do not involve cash." A key question allied to the achievement of improved disclosure of such transactions is how best to collect the applicable information. It may be that global custodians and agency lenders can provide useful disclosures, akin to reporting already in place to the UK FSA for certain transactions.

Generally speaking, the ERC agrees that the enhanced disclosure items listed would be useful for market participants and authorities. The ERC proposes that a template should be set up, which market participants can then fill in. Such a template should explain why the information is needed and by whom (e.g. central banks; regulators). This will help to ensure proper understanding amongst market participants, which will improve the quality of completion. A clear distinction must be maintained when considering which information is useful to the public.

Improvements in reporting by fund managers to end-investors

Q10. Do you agree that the reporting items listed above would be useful for investors?

Would reporting any of the items listed above present any significant practical problems?

If so, please clarify which items, the practical problems, and possible proxies that could be reported instead.

A10. It appears to the ERC that these should indeed prove to be useful items to report to end-investors, whilst remaining mindful of the need to maintain an appropriate balance in relation to confidential information provided through a TR by market participants (to avoid any inappropriate use of such information).

Minimum haircuts – key principles

Q11. Are the factors described in section 3.1.2 appropriate to capture all important considerations that should be taken into account in setting risk-based haircuts?

Are there any other important considerations that should be included?

How are the above considerations aligned with current market practices?

A11. The ERC notes that it is essential to maintain a very clear distinction between minimum standards for haircut methodologies, the objectives of which relate to the management of the risk that losses may be suffered upon collateral liquidation, and the entirely separate concept of an official framework of minimum haircuts, set by reference to an official objective to mitigate perceived leverage and procyclicality risks. In case minimum haircuts are introduced, there should be clear recognition that such amounts provide regulatory capital relief against any otherwise duplicative requirements imposed on regulated financial intermediaries.

The ERC is concerned by the consultative document's proposal (on page #12) that haircuts should be calculated with reference to maximum price declines derived from "a time series of price data that covers at least one stress period". Whilst improved data sets will emerge over time in response to measures to enhance transparency, there will be a much less comprehensive and consistent quality to historic data. Given the short term, high volume nature of repo activity it would be extremely costly to introduce any requirement to back-load data in order to create a historic time series. Consequently, it is important to focus requirements on what can be currently achieved; and on how this can be improved over time.

The consultative document goes on to state (on page #12) that consideration should be given to "the possibility that stressed market conditions may lead to a widening of bid-ask spreads." The ERC notes that there are many factors which can be responsible for widening prices, including differences in the underlying repo collateral. Additionally, using widening prices is not the only way to measure liquidity.

The ERC notes that in section 3.1.2(ii) of the consultative document (on page #12) there is a discussion relating to "the wrong-way risk between collateral value and counterparty default." The ERC considers that true wrong-way risk would involve the situation of a firm giving its own issued securities as collateral, which is not good market practice. Of course there may nevertheless be correlation risks, capable of leading to concurrent declines in the creditworthiness of a firm and the value of the collateral it has given in a repo, which do need to be suitably risk managed. The ERC recognises that interconnectedness does create challenging problems of this sort, as demonstrated in the example of the recent Spanish sovereign debt crisis. In this case Spanish banks had invested mainly in their domestic sovereign bond market; and their difficulties proved to be accentuated by the fact that they were also clearing these in a domestic CSD and/or CCP in their home currency.

The ERC observes that haircuts should also reflect any lack of robust documentation; as such a lack increases legal risk (e.g. the possibility of a challenge to a firm's right to collateral).

Minimum haircuts – numerical floors on haircuts

Q12. What do you view as the main potential benefits, the likely impact on market activities, and possible unintended consequences of introducing a framework of numerical haircut floors on securities financing transactions where there is material procyclicality risk?

Do the types of securities identified in Options 1 and 2 present a material procyclical risk?

A12. The ERC observes that the consultative document states (at page #11) that "Minimum regulatory haircuts for repos and securities financing transactions (whether bilateral, tri-party or CCP) may limit the build-up of excessive leverage and reduce procyclicality in the financial system via the financing of risky assets, in particular by entities not subject to prudential regulation." The ERC is particularly concerned by this principle, since it seems that it is more likely true that minimum haircuts "may not" deliver the desired outcomes. The ERC's scepticism, regarding both the rationale for and the benefits of mandatory minimum haircuts, is fully articulated in the two papers written by Mr Richard Comotto in February and March of 2012.

The ERC wishes to highlight that collateral is only a risk mitigant and, as such, is a second order risk consideration. Counterparty risk is the primary risk and bank risk department will almost certainly stop any repo trading with a counterparty that is perceived to be in difficulties. So the ERC continues to feel that the specific focus on mandatory haircuts is misguided, as the introduction of such a requirement will not change banks' primary risk behaviour, which is the cutting, or removal of counterparty risk lines.

The ERC also notes that declines in the value of collateral that generate higher margin calls will wash through chains of repos, so that only the transferor at the end of each chain will suffer the effect of the increase. It is important therefore not to assume that the scale of higher margin calls would be commensurate with the size of the repo market on a one-for-one ratio.

In section 3.1.3 of the consultative document it states (on page #13) that "A risk in both approaches is that numerical floors become de-facto market standards for haircuts." The ERC cautions that there is a further risk which follows from this. By becoming more associated with the determination of risk management standards, regulators may themselves become the target for criticism in case events subsequently transpire which, with the benefit of hindsight, make it appear that incorrect haircut levels had been set.

The ERC is struck by the fact that the consultative document itself highlights (on page #14) that the proposed approach "may also lead to an increased recourse to central bank refinancing operations if central bank haircut schedules are lower." The ERC considers that this statement of concern is well founded and therefore sees that this is indeed a good reason why not to pursue the proposal.

Furthermore the consultative document goes on to state (on page #15), in recommendation 7, that "the FSB should be mindful of possible unintended consequences for market liquidity and the functioning of markets." The ERC is pleased to see that the FSB has acknowledged this need. This is indeed important and is another good reason why to be careful in pursuing the proposal.

Q13. ***Do you have a view as to which of the two approaches in section 3.1.3 (option 1 – high level – or option 2 – backstop) is more effective in reducing procyclicality and in limiting the build-up of excessive leverage, while preserving liquid and well-functioning markets?***

A13. Assuming the need to adopt one of the two options, the ERC believes that option 2 would be more effective. This is particularly reflective of the fact that this option better addresses the notion of "excess" and will give a better outcome from the perspective of preserving liquid and well-functioning markets.

The ERC is aware that there has been a recent consultation at the level of European Debt Management Offices, in which we understand that proposals have been aired relating to these two options. The ERC considers that the impact on fluidity/liquidity flows with sovereign bonds as collateral needs to be better understood. It may very well be counterproductive; and further jeopardise work around secured indices which are currently being discussed[7].

Q14. Are there additional factors that should be considered in setting numerical haircut floors as set out in section 3.1.3?

A14. The ERC observes that, as stated (on page #3) in the consultative document, the "policy goal is to restrict, or put a floor on the cost of, secured borrowing against assets subject to procyclical variation in valuations/volatility. The ERC notes that any such approach will need to be suitably calibrated for the type of asset, including but not limited to sovereign bonds.

In section 3.1.3 of the consultative document it states (on page #13) that "WS5 was also of the view that basing numerical floors on a variant of the Basel III standard supervisory haircuts had the important benefit of consistency with capital rules and with the approach recommended by the BCBS-IOSCO working group on margining requirements (WGMR) for non-centrally cleared derivatives." The ERC appreciates the thought concerning the benefit of consistency, but notes that ideally the focus of any framework development should be on its consistency with actual market practice.

The ERC agrees with the consultative document statement (on page #14) that "the proposed haircut schedules for non-centrally cleared derivatives and securities financing transactions do not necessarily need to be identical in order to be compatible."

The ERC notes that the consultative document goes on to highlight (on page #14) that the Basel II framework affords 0% risk weights to certain sovereign exposures. As is now widely recognised, this of course does not mean that sovereign debt is literally "risk free".

The ERC considers that one important factor to consider is that in practice haircuts are dynamic and can indeed change on a daily basis. This needs to be recognised in setting any haircut floors, the levels of which would necessarily need to be subject to periodic reassessment.

Finally, market practice has been to use sovereign collateral (of a reasonable, robust nature) as the preferred collateral for interbank repo transactions. The growth in this market segment is clearly linked to the demise of the unsecured interbank market. Mandatory haircuts could well increase costs to all; and, as such, the transmission of central bank liquidity throughout the banking system may very well be damaged. Current market practice is for zero haircuts on such interbank transactions and the ERC strongly believes that this should not be contradicted by regulation, particularly given that any move to further protect one bank in such an arrangement would equally increase the exposure of the counterparty bank (i.e. it would confer no net benefit on the overall stability of the system).

Q15. In your view, how would the numerical haircut framework interact with model-based haircut practices?

[7] For example, you may note BrokerTec and MTS's 13 December 2012 launch of the RepoFunds Rate daily repo index - http://www.icap.com/news-events/in-the-news/news/2012/121213-brokertec-and-mts-launch-repofunds-rate-daily-repo-index.aspx

Also, how would the framework complement the minimum standards for haircut methodologies proposed in section 3.1.2?

A15. The ERC considers that, by definition, there will be a conflict with model-based haircut practices. This will naturally occur whenever the model output implies a haircut below the level set for any minimum mandatory haircut.

Recommendation 6 in the consultative document states (at page #12) that "Regulatory authorities should introduce minimum standards for the methodologies that firms use to calculate collateral haircuts." The ERC agrees with this in principle, as it is beneficial for the market as a whole that all market participants should follow good minimum standards for all aspects of their business. However, recommendation 6 goes on to state that "Those guidelines should seek to minimise the extent to which these methodologies are pro-cyclical." The ERC is troubled by this proposal as it is important that individual firms remain able to set risk management policies to manage their own shareholders' interests.

Minimum haircuts – scope of application of numerical floors

Q16. In your view, what is the appropriate scope of application of a framework of numerical haircut floors by: (i) transaction type; (ii) counterparty type; and (iii) collateral type?

Which of the proposed options described above (or alternative options) do you think are more effective in reducing procyclicality risk associated with securities financing transactions, while preserving liquid and well-functioning markets?

A16. In section 3.1.4(i) of the consultative document it states (on page #16) that "WS5 recommends that any numerical floors should apply only to securities financing transactions where the primary motive is financing, rather than to lend/borrow specific securities." The ERC appreciates the idea of making such a distinction but is concerned with the practicalities. How will reporting reflect this distinction, which is not something that is uniquely defined within the normal transaction data fields?

In section 3.1.4(ii) (ii) of the consultative document it is suggested (on page #17) that the numerical haircut regime might "allow financing of regulated financial intermediaries (e.g. banks, broker-dealers) to be excluded on the grounds that they are already subject to direct appropriate regulation of liquidity and leverage (the possibility also exists that certain other specific entities could be designated to be of such significance that they should be brought within the existing framework for regulated financial intermediaries; and hence also then become excluded). That would leave the numerical floors to apply to exposures of regulated financial intermediaries to other entities and exposures amongst other entities".

Taking the assumption that there should indeed be a regime of numerical haircut floors, this approach appears broadly sensible to the ERC, which considers that other entities, such as funds, may equally well already be suitably regulated. Of course this does not mean that there would never be haircuts on transactions for financing of regulated financial intermediaries, the case simply being that haircuts would only apply in case voluntarily imposed on a bilateral basis or through imposition by a chosen CCP. Indeed the ERC believes that it should also be considered that this same line of thought rationally extends even to the case of exposures of regulated financial intermediaries to other entities, where the pressure of regulatory requirements will already serve to deter the regulated financial intermediary from transacting on a basis which would generate any undue amount of risk.

The consultative document goes on to state (on page #17) that "Option (iii) is by far the most straightforward option to implement". Whilst the ERC agrees this would be true from a practical perspective, it is important to consider that a key problem with any such proposal is that the determination of appropriate haircut levels is in fact dependent on a range of variable inputs which stretch across all three of the identified parameters (so market distortions would inevitably arise in case of any attempt to design a simplified template defining certain fixed minimum haircuts). The following bullet point on page #17 of the consultative document then states that option (ii) addresses the concern for "Limiting the potential negative impact on the liquidity of the repo market at the short end of the money market curve and related possible impairment to central bank refinancing operations". The ERC perceives that particular care needs to be given to the way in which any new measures might impinge upon central bank refinancing operations; and would be particularly concerned in case there were to be any impairment of this essential mechanism. No actions should be decided upon which would lead to such an impairment.

The ERC is pleased to see that the consultative document acknowledges in section 3.1.5 that globally consistent implementation is desirable but also, understandably, challenging. The ERC wishes to emphasise that the achievement of global consistency needs to encompass not just the content of requirements but also the timing of their adoption.

Q17. ***Are there specific transactions or instruments for which the application of the numerical haircut floor framework may cause practical difficulties?***

If so, please explain such transactions and suggest possible ways to overcome such difficulties.

A17. In section 3.1.3(i) of the consultative document it is noted (on page #14) that "market participants may be able to use total return swaps and other derivatives to create transactions that are economically equivalent to repos". The ERC finds that the FSB's approach to synthetic repos is unclear, particularly in terms of how this is intended to relate to the treatment of derivative exposures. To try and aid clarity, the ERC observes that derivative exposures are net replacement costs, whereas synthetic repos involve collateral against the whole notional principal amount of the derivative component. Accordingly it would appear to be the case that any minimum haircut on the collateral in synthetic repos should be exactly the same as on real repos, as the assets sold in both cases perform the same collateral function. Consistently identifying which transactions form synthetic repos is likely to be a challenge.

In section 3.1.4(iii) of the consultative document arguments are made for and against the application of numerical haircut floors in relation to sovereign bond collateral. The ERC feels that if there is truly a case for a regime of numerical haircut floors it would be intellectually inconsistent to then say that there should simply be an exclusion for all sovereign bonds. Nevertheless, as is noted (on page #18) "risk-free" rates are not procyclical, so if there is to be a regime of haircut floors, its design ought quite clearly to be consistent with a focus on illiquid securities rather than impacting on high quality government bonds (and other high quality collaterals issued by entities such as supranationals).

In section 3.1.4(i) of the consultative document it is specifically stated (on page #16) that "In order to prevent such circumvention, numerical floors would also need to apply to collateral swaps." The ERC observes that this is one particular example of the need to achieve consistency of treatment across products and geographies, which will require careful and detailed coordination of international efforts to introduce any new requirements so as to avoid the creation of inconsistencies as to either content or timing of application.

Q18. In your view, how should the framework be applied to transactions for which margins are set at the portfolio basis rather than an individual security basis?

A18. In the ERC's view, recognising the fact that there is a perfectly reasonable case for allowing that margins can be determined on a portfolio basis simply further illustrates the illogicality of proposing that there should be pre-set minimum margins applied across the market. Precisely what the portfolio approach shows is that the relevant amount of margin is always fact dependant, with the possibility existing that incremental trades are risk reducing for the portfolio as a whole; and that haircuts could accordingly fall in consequence of such incremental activity.

Cash collateral reinvestment

Q19. Do you agree with the proposed minimum standards for the reinvestment of cash collateral by securities lenders, given the policy objective of limiting the liquidity and leverage risks?

Are there any important considerations that the FSB should take into account?

A19. Section 4.1 of the consultative document states (on page #21) that "Agent lenders should frequently disclose to their clients (the beneficial owners of securities) the composition and valuation of their portfolio of securities on loan and their cash collateral reinvestment portfolio." The ERC notes that the UK FSA has an existing agent lender reporting regime, which could be usefully used as a model. To the extent shown to be necessary, this model could be extended or otherwise adjusted.

Requirement on re-hypothecation

Q20. Do you agree with the principles set out in Recommendation 9?

A20. The ERC agrees that there should be reasonable restrictions on re-hypothecation and an appropriate level of disclosure to impacted clients, but care needs to be taken to distinguish the right of re-hypothecation of pledged collateral from the right of use of collateral received through a true sale in repo or securities lending. Overall, the ERC considers that these proposed principles may indeed be reasonable. Nevertheless, the ERC specifically draws attention to the fact that these principles refer exclusively to re-hypothecation, which the FSB narrowly defines to mean "re-use of client assets". This distinction is of great significance and the ERC would not support any proposal which sought to apply these principles more broadly; and notes that it will be necessary to also be clear regarding what is meant by the phrase "client assets".

In section 1.2(iii) of the consultative document the FSB describes (at page #3) the effect of re-hypothecation in the following manner: "Re-hypothecation can replace ownership of securities with a contractual claim on a financial institution to return equivalent securities, with ownership of the re-hypothecated securities transferring to this institution". The ERC is concerned that this description of re-hypothecation lacks precision and suggests that care be taken to ensure the exact legal nature of this technical concept is fully understood and precisely articulated.

Minimum regulatory standards for collateral valuation and management

Q21. Do you agree with the proposed minimum standards for valuation and management of collaterals by securities lending and repo market participants?

Are there any additional recommendations the FSB should consider?

A21. The ERC observes that these proposed standards are commendable, but somewhat vague. This creates the risk that they may be interpreted in an overly prescriptive way and would be keen to have the opportunity to provide further detailed input in respect of its own experience in the development and promotion of market standards. The ERC suggests that it might be helpful to insert the need for a robust master agreement, incorporating representations and warranties that no laws or regulations are being breached; margin maintenance provisions; and default procedures.

One of the points underlying this aspect of the proposals is the policy goal, stated (on page #3) in section 1.2(ii), "to mitigate the risk that large forced sales of collateral in one market segment arise as a channel of risk transmission beyond that market segment and throughout the broader financial system." The ERC see that this is an example of the conflict which exists between allowing individual firms the freedom to manage their risks in the interests of their shareholders and the public policy objective to mitigate the potentially adverse effects of collective action. Care needs to be taken to achieve an appropriate balance, in order to avoid a harmful effect on individual firms' risk management.

Section 1.2(v) of the consultative document states (at page #3) that "The policy goal is to improve collateral valuation standards." This is wholly reasonable as a goal and is something which the ERC itself continues to seek to promote. There are, nevertheless, significant constraints which do need to be recognised. The ideal being pursued is daily (if not continuous) evaluation of the current market price of collateral. In practice the market for collateral assets is not able to provide the pricing data to underpin such evaluations and some element of theoretical valuation has to be deployed in order to fill in the gaps. So it is important to ground proposals in practicality, whilst striving to achieve improvement and enhance market efficiency.

Structural aspects of the securities financing markets

Q22. Do you agree with the policy recommendations on structural aspects of securities financing markets as described in sections 4.1 and 4.2 above?

A22. The ERC highlights that the ICMA survey reveals that a significant proportion (and in flow terms this will be even greater – perhaps 40 to 50% – than the outstanding value revealed by the survey) of European market repos are already transacted through CCPs.

Considering CCPs, the ERC believes that they are appropriate for high-volume, liquid repo markets (i.e. typically government markets); but are less well suited to more structured trades (e.g. securities lending) or less liquid products (e.g. corporate bonds). CCP risk management is inevitably more at risk with less liquid products which, if they are to be admitted to the CCP at all, will inevitably attract high initial margin requirements. What matters most is a CCP's capacity to manage the applicable risks, which always needs to be demonstrably the case and is not something for which initial margin can substitute. The ERC recognises the essential need to ensure the safety of CCPs, otherwise instead of helping to mitigate potential systemic risk they may become its source, and therefore sees that great care should be taken not to push the use of CCPs for products to which they are less well suited.

The ERC considers that the "automatic stay", which is mentioned (at page #25) in section 4.2 of the consultative paper, should be preserved. As such the ERC is pleased to note that the FSB's overall recommendation is that "Changes to bankruptcy law treatment… …should not be prioritised for further work at this stage". The ERC also wishes to be clear that repos under its GMRA agreement are not benefiting from a safe harbour treatment. These repos involve a transfer of title identical to that in any other true sale. Interfering with this legal right in repo would pose risks to cash transactions and represent a fundamental challenge to property law.

Section 4.2 of the consultative paper goes on to describe three particular examples of "Policy proposals in relation to bankruptcy law".

"(i) Repos backed by risky or illiquid collateral should not be exempt from automatic stay" – the ERC does not support this proposal. One practical issue with this is that the determination of which collateral is "risky or illiquid" will vary over time. To have the legal effectiveness of the collateral also subject to fluctuation as market conditions evolve would introduce a highly undesirable element of uncertainty.

"(ii) Repos backed by risky or illiquid collateral should be exempt from automatic stay subject to a tax, which could be varied as a macro-prudential tool" – the ERC does not support this proposal, considering that the introduction of such a "tax" would prove to be counterproductive. The same difficulty with the fluctuating nature of what is "risky or illiquid" equally applies in this case.

"(iii) Repos backed by risky or illiquid collateral should not be exempt from automatic stay. In the event of default, lenders of such repos should instead be able to sell collateral only to a "Repo Resolution Authority (RRA)" at market prices minus pre-defined haircuts specified by asset class by the RRA. Then the RRA would seek to liquidate the collateral in an orderly manner. The eventual difference between the amount of the liquidity payment and the realised value of the collateral would be paid to the repo lenders or clawed back from them. The pre-defined haircuts set by the RRA should effectively act as a floor on market haircuts." – consistent with the FSB's overall recommendation, the ERC foresees significant difficulties with any such approach. The ERC also specifically notes that the idea of trying to link market haircut floors to RRA pre-defined haircuts adds further complexity to an already undesirable proposal and considers that this would be counterproductive.