

Updating the ICMA Buy-in Rules

Call: April 16, 2020

Meeting notes

Members discussed some of the key considerations and questions suggested for the projected market consultation on updating the ICMA Buy-in Rules in light of CSDR. The objective was to identify questions that may be superfluous, as well as any missing considerations. This was a continuation of the discussion of the call of April 6.

PEP (pre-extension period) Buy-in

The PEP buy-in is intended to be used any time from ISD+1 (as now) up until the end of the relevant extension period. The PEP buy-in is intended to remedy the fail before going to a CSDR buy-in.

Final day to agree to negotiate alternative remedy

- It was discussed whether for consistency the current non-prescriptive provision in the ICMA Rules should refer to the CSDR prescribed remedy for cash compensation as a possible resolution for the PEP.
- It was noted that the Level 2 outline for cash compensation was considered inadequate from the perspective of fixed income, and the industry was struggling to come up with a best practice solution to enhance the regulation. Furthermore, any eventual best practice would likely need the approval of individual NCAs across the various jurisdictions.
- It was agreed that flexibility in the cash settlement process was an advantage of the PEP buy-in and it should therefore be retained.

Settlement fail of the buy-in

- It was agreed that the recommendation should remain that the PEP buy-in be completed on successful execution, rather than on successful settlement. This is light of 'guaranteed delivery' and the recourse of the purchasing (receiving) party under Section 180 of the ICMA Rules in the event of failed settlement of the buy-in.
- This has the advantage of allowing the PEP buy-in to be executed up until the end of the extension period, and creates greater certainty for the trading parties.

- It was noted that firms would need to liaise with their operations/risk management teams to see whether they could accommodate divergent practices for assessing buy-in completion – on execution for the PEP and on settlement for the CSDR buy-in.

CSDR Buy-in

Still part of the ICMA Rules, these are the buy-in provisions that would apply post-extension period and are designed to align with the CSDR requirements.

Pre-advice

- It was confirmed that this is being discussed by the AFME CSDR WG, and agreed that ICMA would coordinate to ensure high level consistency in terms of timing and content.

Guaranteed delivery / Settlement failure of the buy-in

- ICMA recapped that while completion of the buy-in based on successful execution, rather than settlement, would be preferable from a risk management perspective, this seemed unlikely to be achievable without a change to the Level 2. Accordingly, the recommendation was that the completion of the ICMA CSDR buy-in also be based on settlement rather than execution. Furthermore, the CSDR buy-in would not require guaranteed delivery.
- It was pointed out that this also had implications for any pass-on mechanism, which would also need to be contingent on the settlement of the buy-in.
- It was noted that this would require different settlement processes (in terms of the timing for canceling the original settlement instructions) between the PEP and the CSDR buy-in. It was further noted that this would also have significant risk management considerations in terms of when the failing party would need to hedge their exposure.
- ICMA confirmed that these trading and operational considerations would be clearly outlined in the consultation for member feedback.

Cash compensation

- It was suggested that the Rules refer to the regulatory provisions for cash compensation, rather than outlining any market best practice that may eventually be agreed.
- It was agreed that this could be revisited, depending on any eventual agreement on best practice.

Timing of communicating the buy-in and pass-on

- It was noted that currently the ICMA Rules require that the buy-in or pass-on be communicated to the relevant selling (delivering) parties “immediately”.
- The Level 2, however requires that *the receiving trading party shall notify the results of the buy-in to the failing trading party at the latest on the last business day of the applicable period* (i.e. the end of the buy-in timeframe). Furthermore, *the receiving trading party shall ensure that the relevant CSD receives the information notified without undue delay*. [Art 31(4)].
- It was agreed that from a risk management perspective this was insufficient, and that the failing party would need to know that the buy-in had been successfully completed (whether this is based on execution or settlement) immediately, and not at the end of the buy-in period.
- It was also noted, that the only requirement in the regulation for immediacy (“without undue delay”) related to informing the CSD and not the relevant trading party.
- This raised the question of when to inform the failing party of the results of the buy-in. It was broadly felt that they would need to be informed as soon as the buy-in is successfully completed, which would be on successful settlement.
- However, it was also argued that they would probably want to know as soon as the buy-in was executed, since they may take a view that, in probability, the buy-in will settle, in which case they would want to hedge their risk immediately after the buy-in execution.
- The issue of multiple notifications was raised, and whether it would be necessary to inform the failing party immediately following both execution and settlement. A possible compromise was suggested by which the failing party could request additional notification on execution. Again, this would be subject to consultation.
- With respect to timing for notifying the failing party of either or both the successful execution and settlement of the buy-in, it was felt that it was impossible to be prescriptive. It was suggested that any communication relating to the buy-in, including along a pass-on chain, would ideally need to be as close to real-time as possible. Therefore, the use of wording such as “immediately” or “without undue delay” would be sufficient, so long as it was used consistently in both the PEP and the CSDR Buy-on Rules.

Sell-outs

- ICMA confirmed that they would need to consider further whether there was a need to amend the ICMA sell-out rules so that they mirror the revised buy-in rules, or whether the existing sell-out framework would continue to be adequate.

Scope (markets)

- ICMA recapped that the current Rules, while applying to “international securities”, which are defined as securities intended to be traded on a cross-border basis and capable of being settled on an international CSD, historically have been developed for and applied to cash bonds (including credit, sovereigns, securitizations, emerging markets, etc.).

- It was suggested that firms could elect to apply the Rules to other securities (or not), as they wished, based on their own assessment of whether they were appropriate or suitable and noting the potential differences and nuances of non-bond markets.
- It was noted that depending on how firms have incorporated the ICMA Rules by reference, they would already need to consider their application to different markets and product types. There was also the flexibility for ICMA members to opt out of all or part of the ICMA Secondary Market Rules & Recommendations.

Scope (extraterritoriality)

- The question was raised of applicability of the ICMA Rules in the case of transactions that are out of scope of CSDR. The view was that in this case firms would probably not elect to use the CSDR buy-in, but instead it may be possible to apply the PEP buy-in, but with an indefinite timeline (as now). However, this would need to be considered in the drafting of the revised Rules. It was also felt that given the application of the current Rules, which are largely applied to trades settling on the ICSDs, it was likely that the application to trades out of scope of CSDR would be a relatively small subset.
- It was asked whether the need to determine whether a transaction was in or out of scope, and so which provisions of the ICMA Rules to apply, would create additional administrative burden, and if it may be more efficient to have a single 'CSDR-based' set of provisions that apply in all cases. It was countered that firms are already required by the regulation to determine whether transactions are in scope, so this should not require any additional work.

It was agreed that ICMA would aim to update the outline of considerations for the proposed consultation and circulate with the Group. WG members would be encouraged to share and discuss internally with their various stakeholders (trading, operations, legal) for further feedback to help inform the final questions and details of the consultation.

