ISSA

International Securities Services Association

Newsletter

July 2015

Message from the ISSA CEO Office

New Members
- 3 new Members have joined ISSA in the 2nd quarter 2015.

Feedbacks from Industry Conferences
- SIFMA Operations Conference, San Diego
- 8th afme European Post-Trade Conference, London
- World Forum of CSDs Conference, Cancun
- International Capital Market Association (ICMA), Amsterdam
- 15th European Network Management Conference, Athens

New ISSA Projects

The ISSA Operating Committee will convene on September 23, 2015, in order to propose a list of industry topics to be pursued by ISSA.

Suggested topics should contribute to developing and promoting forward-thinking solutions that create efficiencies and mitigate risk within the global securities services industry.

Any topic suggestion from our readership by the end of August 2015 is highly welcome.

Many thanks in advance!
The ISSA Secretariat

www.issanet.org

Message from the ISSA CEO Office

Dear ISSA Members and interested parties

I am pleased to inform you that ISSA is on a successful track regarding its membership and its activities. With three additional members since our April Newsletter, ISSA's constituency reached for the first time 100 members. **Furthermore, we welcome Credit Suisse as a new Board Member institution.**

As concerns our activities, ISSA's main current objective continues to be the launch of the proposed «Financial Crime Compliance Principles for Securities Custody and Settlement». As a consequence, this topic was the focus of the ISSA Board meeting held on May 13. All Board Members were pleased with the achievements and thanked the working group under the lead of **Bob Almanas,** SIX, **Mark Gem,** Clearstream and **Jim Freis,** Deutsche Börse. As a next step, the Board authorized the release of the Draft Principles to the ISSA membership and the regulators for consultation in order to be able to finally approve them by the end of August 2015. At that time they will be made public to the financial industry. With this schedule ISSA is best positioned to discuss the Principles and their adoption at Sibos where transparency and compliance are set as key themes.

Also there has been valuable progress in the other two Working Groups:
- Under the lead of **John Kirkpatrick,** Citi, all CSDs were encouraged to complete ISSA's Corporate Actions and Proxy Voting survey 2015. With 53 feedbacks received we have a representative overview of the implementation of the ISSA recommendations. A respective report will be published by the end of September 2015.
- Concerning the Collateral Management – under the lead of **Angus Fletcher,** Deutsche Bank, – we will report in our autumn newsletter.

During the 2nd quarter the ISSA community attended various conferences around the globe. This Newsletter contains some key thoughts from various speakers: **Andrew Gray** and **Dan Thieke** from DTCC spoke at the SIFMA Operations Conference. **Paul Symons**, Euroclear, **Guido Wille,** Clearstream, **Angus Fletcher,** Deutsche Bank, and **James Cunningham,** BNY, acted as panelists at the 8th afme European Post-Trade Conference of which **Werner Frey,** afme, has summarized some concluding remarks. Finally you can follow a summary of key take aways by the CEO office having attended three other Industry Conferences

We hope you enjoy reading this newsletter and we welcome any feedback as well as recommendations about topics to be addressed.

With best personal regards,
In the name of the CEO Office – Josef Landolt

New Members

Since April 2015 the following 3 new members have joined our Association

- *Zürcher Kantonalbank, Zurich, Switzerland*
- *Central Securities Clearing System Plc, Lagos, Nigeria*
- *Bank Vontobel AG, Zurich, Switzerland*

We welcome these organizations and are looking forward to a mutually fruitful relationship

Board of ISSA

Building Resilient Systems

Risk management emerged as a leading priority for financial firms and policymakers following the 2008 financial crisis, ushering in a period of re-regulation designed to enhance market stability and mitigate the likelihood of another financial meltdown.

Andrew Gray, Managing Director and Group Chief Risk Officer, The Depository Trust & Clearing Corporation (DTCC); Member of the ISSA Executive Board

Expanding the Remit of Risk Management

These changes have also prompted an expansion in the remit of the risk management function, which has evolved from focusing on credit, market and liquidity risk to now include operational, systemic and, more recently, technology, information and physical security risk and business continuity. This evolution reflects the reality that firms can be negatively impacted by a variety of incidents, including technology outages, operational breakdowns or a cyber attack. While these events could be devastating to an individual firm, they may also impact the industry more broadly due to the interconnectedness of the financial system. Now more than ever, firms need a holistic view of risk and a consistent approach to measuring and managing it as well as greater transparency into the connections between various risk types.

Establishing a «Systems View»

The industry also needs to look at the financial system not as a set of stand-alone entities, but rather as a complex, adaptive system with a set of diverse interconnected components. As a result, firms need to better understand their points of connection with other entities. For example, organizations like ISSA are playing an important role in this effort by engaging with their members to address the need for more transparency in the custody value chain.

Building Resilience

Breakdowns are inevitable given the openness of the modern financial system and the increased complexity, diversity and unpredictability of threats. As a result, firms need to be prepared to detect problems and recover from them as quickly and effectively as possible. Therefore, the focus today needs to be broader than just managing risk – we need to focus on building resilience.

Evolving the culture of an organization and establishing frameworks that encourage appropriate behavior with regard to risk are key to accomplishing this goal. Expanding ownership of risk management to all employees of a firm and fostering a learning mindset that raises awareness of what is happening in the organization - looking at what could go wrong, challenging assumptions and embracing the lessons of the past, including near misses - is crucial.

The evolution of risk management has created many new opportunities and challenges for the industry, and while much progress has been made in recent years, we still have a lot of work to do to harden our defenses against the traditional, new and emerging risks facing financial services.

Adapted from a Featured Speech at the SIFMA Operations Conference in April. Click here to read the full remarks.

During the same Conference, Dan Thieke sat on a panel dealing with the topic of Corporate Actions. See next page what Dan talked about.

Corporate Actions in a T+2 Era and Other Topical Issues

Dan Thieke, Managing Director, General Manager, Settlement and Asset Services, The Depository Trust & Clearing Corporation (DTCC

In terms of much-needed automation and standardization of the Corporate Actions (CA) lifecycle, the industry has made progress with custodian banks and broker-dealers on the downstream side. However, from agents and issuers on the inbound side, there has not been nearly the same level of adoption. There remain a large number of agents and issuers that announce CA events in paper form and/or PDFs, which requires manual re-keying of information, introducing the chance of human error, increasing risk to the process and preventing straight-through-processing (STP). There continues to be a great deal of discussion around automating and standardizing the entire CA lifecycle. If you think about the CA lifecycle, both inbound and downstream, DTCC sits squarely in the middle of the process.

Over the past few years, DTCC has worked with organizations such as SWIFT and XBRL US to help raise awareness with issuers and their agents. Despite these efforts, adoption of automation and standardization has been slow; the challenge is that issuers have little incentive to invest in automation given potentially low volumes of events.

One area in which DTCC has been able to make tremendous progress is on the downstream side. As one of 15 sponsoring firms of ISSA (International Securities Services Association), DTCC also participates on the ISSA Working Group on Corporate Actions, which has been contributing to recommendations for standardization and best practices.

Through its multi-year CA Transformation initiative, DTCC has successfully implemented new messaging standards and automation to help its clients achieve greater levels of STP. While there is certainly still work to be done on the inbound side – which DTCC expects to see improvements with future phases of its transformation effort – clients are experiencing the full impact of efforts to modernize the way corporate actions are processed.

8^{th} afme European Post-Trade Conference

The above conference was held in London on May 6, 2015. It was dedicated to the topic of a European «Capital Markets Union» (CMU). The timing was very appropriate as the European Commission's public consultation on the subject closed on May 13, 2015. Four representatives from ISSA Board Member institutions acted as panelists and have provided us with their take-aways mentioned below. Read also Werner Frey's concluding remarks he made at the conference.

Plenary Panel: The Vison of an integrated low cost, low risk Post-Trade System in an EU Capital Markets Union

Paul Symons, Head of Government Relations, Euroclear SA/NV

We have been discussing a European post trade vision now for over 15 years. And we are finally at the point where a significant part of that vision is becoming reality. The delivery of a single rule book for CSDs (through the CSD Regulation) and for CCPs (through EMIR) combined with the delivery of Target2-Securities (T2S) means that we now stand on the verge of a much more integrated post trade landscape. So the first message from the conference was that we should finish these tasks, before embarking on a new vision. T2S will need to bed-down, and the CSDR and EMIR both need to be implemented fully and assessed for their effectiveness, not just for the risk profiles of CSDs and CCPs, but also for the clients and markets which they serve.

One of the great successes of T2S is the work of the ECB and the market in harmonizing a number of areas of post trade activity before the migration of the first wave of CSDs, including a lot of corporate action activity. This is essential for the development of an efficient post trade landscape in the EU. The second message from the conference was that the ECB could extend its harmonization activities to new areas (such as standards for portfolio transfers and withholding tax procedures) and could ensure that non-T2S markets in Europe adopted those practices as well.

CMU itself is a vital and progressive initiative which should lead to a more efficient allocation of capital. The third, and perhaps most significant, message was that in delivering CMU the authorities needed to take a long hard look at the legislation that is already in force to ensure that it is consistent with the principles and ambitions of CMU.

Plenary Panel: Status of the Post-Trade Blueprint – Achievements so far and Current Implementations

Guido Wille, Executive Vice President, Head of Market Development, Clearstream Banking

The panel discussed if there was a defined objective the industry was moving towards and what progress had been made over the last years.
The first result was that the «Post-Trade Blueprint» was at best a moving target. Pre-crisis key objectives were efficiency and harmonization in Europe, both of which were also drivers for the T2S project. But the crisis led to focus on new objectives such as investor protection and transparency. Regulators played an ever increasing role in pushing these subjects higher up the agenda of the industry. There was controversy to what extent the industry had the ability to self-correct and to what extent regulators and public bodies had to force change through with industry representatives defending the ability of market players to self-correct.

A specific subject of debate were the costs and benefits of account segregation. There was agreement that a number of important objectives drove the discussion about segregating accounts further down in the value chain including transparency and the prevention of financial crime – a subject on which ISSA has been working for some time - as well as investor protection and industry needs such as collateral management. There was debate though whether account segregation was the only way to achieve these objectives and whether market players should decide for themselves what level of segregation was best suited for specific clients. Industry representatives pointed to the operational challenges and significant costs of segregating accounts all the way down to the issuer CSD and questioned whether there could be less costly ways of achieving the agreed objectives.

Overall it was a lively and insightful discussion that hopefully contributed to the evolving views in the industry where we should be heading and how to get there.

Plenary Panel: Impact on Post-Trade Structure of Regulatory Initiatives

Angus Fletcher, Head of Market Advocacy & Business Strategy, Deutsche Bank

Significant progress has been made in Europe in the last 10 years, both industry led and most significantly regulatory, moving Europe closer towards a single harmonized post trade landscape – achievements were listed such as T2S, MIFID, CSDR. ESMA was keen to point out that regulators had been the main driving force as a result of the crisis.

It was too early to tell how the achievements would play out in reality – we are still in implementation mode for many of them. This will take at least another 2-3 years to understand and see the implications. There will inevitably be a need for tweaks to the regulations.

There remain many challenges ahead that need to be addressed both at market participant level (banks vs market infrastructures cooperation and competition around pricing, services offered and recovery & resolution regimes), and at regulatory level (eg securities law, harmonized approach to asset safekeeping and custody, the issue of segregation).

Plenary Panel: Next Steps and Missing Pieces for Ensuring Effective Change in Post-Trade Systems

James Cunningham, Managing Director and Senior Advisor, Office of Public Policy and Regulatory Affairs, BNY Mellon

The panel dealt in most detail with the question of what initiatives should be part of the European Commission's action plan for a CMU (Capital Markets Union). Panelists discussed in particular initiatives that could be taken in the areas of securities law, withholding tax processing, shareholder registration and compliance with corporate actions standards. Interestingly, and also sadly, as they highlight areas in which little, or insufficient, progress has been made, these initiatives were already part of the agenda set out in reports published in 2001 and 2003 by the Giovannini Group to tackle the so-called «Giovannini Barriers».

Panellists were asked the question of whether in the intervening years additional barriers had emerged that also needed to be tackled. The answers were very diverse. Among the suggestions were (i) competition (by a representative of a market infrastructure), (ii) regulatory divergence and regulatory nationalism, and (iii) increased regulatory obligations for segregation up the custody chain (as a barrier to market access).

One panelist argued that the CMU project was basically a regulatory story; it would largely be made up of new regulatory initiatives, and of initiatives to correct errors in past regulation; but it was a regulatory story in an environment in which the European Commission and many other parties had very little appetite for new regulation. This meant that it was legitimate to question whether many of the specific initiatives (securities law, tax processing, etc.) would actually succeed in making their way through the European legislative process.

The panelist argued that what was needed was a vision and a focus. The vision was a vision of a European capital market in which all European investors had access to all European issuers and vice-versa. (In an aside, the chairman of the panel termed this the «Heineken» vision of a CMU i.e. the vision of a CMU that «refreshes parts that other CMUs cannot reach»).

The focus was then on the user experience. Users of European capital markets are currently faced with a highly complex experience driven very largely by national specificities in securities and company law, tax processing, shareholder identification, etc. The CMU project needs to tackle these specificities in order to give users of capital markets a safe, predictable and easy user experience. This is a necessary condition for the success of the CMU project.

Concluding Remarks

Dr. Werner Frey,
Managing Director, afme
Post-Trade Division

In the context of the title of the conference, «The role of post trade in European Capital Markets Union» I summarised my concluding remarks in 5 points:

1. Financial market infrastructures and in particular post trade are and have to be an integral part of a CMU. Even if the connection with the CMU's overriding objectives of promoting growth and creating jobs through wider access of issuers to capital markets and increased choice for investors, particularly cross border, may not be obvious at first sight, we should remind ourselves that the proceeds of an issuance of equities or bonds are credited to the issuer's account only after having made use of post trade services; equally the promise of traders – I sell to you, I buy from you – only leads to an effective change of ownership upon such trade having been cleared and settled.
2. The CMU project is an excellent basis to drive and accelerate the process of post trade reform in Europe and to re-balance the priorities of safety and efficiency.
3. Cooperation and coordination of public and private sector initiatives are a recipe for success as is demonstrated by the following examples: The private sector agreed on the need to harmonize settlement cycles but only the CSDR provision mandated a shortening to T+2, which in turn was highly successfully implemented ahead of schedule in most European markets by a concerted effort of the private sector. Equally, the comprehensive set of market standards for corporate actions processing, developed by the industry, dealing with one of the most complex areas of post trade, is nearly fully implemented in major European markets; however, the support of public authorities was required, for example by introducing record dates in French and German law.
4. Yet, more needs to be done. Sticky issues such as securities law reform and withholding tax procedures need to be resolved by means of a commitment of EU Member States in favour of a European CMU. The securities industry in turn must continue to develop solutions of harmonization and standardization areas such as ETF processing and securities registration processes as meaningful contributions to CMU.
5. A pragmatic, step by step approach is advisable and the most complex issues should be started early because they will require more time to be resolved. In essence: there is hardly demand for another good looking and attractive project title; the preference is for tangible results – and we have all intention to contribute thereto.

CEO Office Attendance at Industry Conferences

As has become a tradition, the CEO Office attended various industry conferences in the 2nd quarter. ISSA focuses on a few conferences which the CEO or the Secretary attend with the goal to stay informed, to talk to existing and potential ISSA members and to make use of the opportunity to hold a speech or participate in a panel. Refer to the summaries that follow.

WFC 2015

The World Forum of CSDs held its 13th global conference in Cancun, Mexico, from May 19 to May 22, 2015, which was attended by about 240 participants from 80 countries. Some take-aways from the conference:

Settlement Efficiency

Europe's recent move to T+2 went smoothly, however, no substantial benefits became apparent, whereas admittedly, benefits would be difficult to measure. The US is targeting a move to T+2 by the 3rd quarter 2017. Buy-in and penalty regimes are widely supported; a move to T+1 or even T+0 is not imminent, however, seen as possible, facilitated by new technologies.

Prevention of Fraud / Security Threats
Fraud damage caused globally is estimated to be USD 3.5 billion, with management override (26%), overconfidence / lack of supervision (22%) and greed (18%) representing the major causes. Asset misappropriation and cybercrime are typical in the financial industry. In 2013, two thirds of organizations polled were not prepared for 'talking fraud'. Attackers attack 150 times faster than the victims are able to respond. It often takes up to 9 months to even discover an attack. The protection of integrity ought to be higher valued than the protection of confidentiality.

Investor and Asset Protection
Recent regulatory and enforcement actions have been critical vis-à-vis the Omnibus accounting model. This has prompted ISSA to come forth with its Financial Crime Compliance Principles, soon to be released to the industry. A panel agreed that the different securities accounting models (omnibus, segregated, beneficial owner accounting on CSD level) have their merits and need to be seen in the context of the relevant regulatory environments. Segregation alone may not necessarily improve or guarantee protection. As has become evident from a subsequent panel on CSD Innovation, the Beneficial Owner Accounting Structure on CSD level does in fact offer new business opportunities for CSDs, not necessarily limited to the area of securities services, though.

Technology
From 150 CSDs more closely looked at, 50 are using vendor solutions whereas some 100 are running on legacy systems. Increasingly, technology is an enabler to develop new products or services, such as analytics or utility set-ups. However, disruptive technologies need to be watched carefully, such as entrants into personalized direct investing or digital asset transfer platforms. An example of the latter is the application of the so-called «Blockchain Technology», where distributed ledgers are updated in real-time, eliminating the need for intermediaries. Despite the prevailing concerns regarding information security, this technology increasingly receives attention.

Regulatory Impact on CSD Activities
Sir Winston Churchill was quoted as having said: «If you have ten thousand regulations you destroy all respect for the Law.»

Changes in the CSD Landscape
Moderated by the ISSA CEO, a panel of Senior Executives reflected on the future of financial market infrastructures (FMIs) in the wake of the regulatory developments and the entrance of new technologies and providers. Cooperation and collaboration among FMIs is considered key, they will be more interconnected, also via utilities and will increasingly form partnerships for innovation and sharing of solutions. Care needs to be taken by the industry to focus on the right priorities. Is it wise to spend huge efforts to move from T+3 / T+2 to shorter settlement cycles when for example disruptive technologies would allow a T+0 settlement in a «twinkle of the eye»?

The next WFC global conference will be held in Hong Kong in 2017. Further details will be announced and can be retrieved from the following link:
https://worldcsds.wordpress.com/events/wfc-events/

ICMA Conference

This year, the International Capital Market Association held its 47th Annual General Meeting and Conference in Amsterdam from June 3 to June 5. A record 850 delegates and representatives attended the event. Representatives from European institutions and other capital market experts informed of various current issues affecting global markets, including in particular the **European Capital Markets Union.** The CMU is considered a driver of growth across the EU and it is considered to bolster the Monetary Union. The European Commission is tasked to bring about a well regulated and integrated Capital Markets Union, encompassing all Member States, by 2019. The European bond market offers quite some potential with a **shift from direct bank lending** to financing in the capital market, as experienced in the US. Representatives of market institutions in China were offered the opportunity to inform about developments in China's onshore RMB and corporate credit bond markets. So-called **«Green Bonds»** and their increased demand and supply were another topic. ICMA is acting as «Custodian» for the «Green Bond Principles» applicable to these sustainable products. Representatives of ICMA's European Repo and Collateral Council debated about the increased role of collateral and their changing role to **Collateral Managers**, as Repo transactions suffer from capital constraints. Loans rather than bonds may surface as collateral, also with Central Banks.

The next ICMA Annual General Meeting and Conference will take place in Dublin from May 18 to 20, 2016.
http://www.icmagroup.org/events/PastEvents/icma-annual-general-meeting-and-conference-2/

15th NeMa

The 15th European Network Management Conference was held in Athens from June 9 to June 11, 2015. The first day, dubbed Risk Summit, was devoted to risks in Network Management. The conference itself attracted more than 480 attendees. Some take-aways from the conference:

Risk
There was quite some discussion about whether the industry will have sufficient capital to carry the risks emanating from the custody business, due not least to recent regulatory requirements, such as AIFMD in Europe. The ISSA Secretary informed on the Financial Crime Compliance Principles soon to be issued to the securities industry at large. The merits and drawbacks of «contingency agent networks» were heavily debated. As became evident in the last two NeMa's already, Network Managers are increasingly involved in obtaining and interpreting legal opinions on asset protection, contingency agreements and intensified due diligence. The numbers of topics and subtleties addressed in sub-custodian questionnaires seem to be growing with no end. Frequently, participants suggested that standardizing such documents to a large extent could be an ideal project for an industry association respectively utility services, which might also serve as questionnaire repositories.

Technology
The financial industry is increasingly faced with disruptive technologies, such as Robo Wealth / Robo Advisor. FinTech companies are moving in without legacies. Data is to be considered as a strategic asset and global custodians were encouraged to share their data with asset managers. Sharing real-time data can create operational alpha. IBOR, the Investment Book of Records (single source of accurate, timely and clear data that can be used throughout the organization as the golden record) is considered key. There was also a clear understanding that network management needs automation.

Innovation
Conference attendees were advised to team up with start-up providers / entrepreneurs in developing new solutions and to be part of the opportunities offered by disruptive technologies. The industry is and will increasingly be challenged by entities outside our industry and hence cooperation / utilitiy services will be of essence. The question was asked if the industry has the necessary sense of urgency.

Sub-Custodian Survival Guide
Good relationships alone are no longer a guarantor for successful relationships. Efficiency and competitive pricing are determining factors as well. An audience poll ranked centralization and rationalization higher in significance than outsourcing. Data reporting to customers in terms of operational efficiency, investment patterns, etc. is seen as key. The industry needs to cope with disruptive technologies, regulation, due diligence and compliance issues. Change is in the offing, we just do not seem to know what it is exactly.

The New Cost of Custody
Experience has shown that cost of non-compliance has to be factored into the equation as much as the cost of compliance. Intraday liquidity pricing needs to be considered as well. Sub-Custodian fee hikes have started to kick-in. New fee schedules will tend to follow T2S, i.e. low transaction fees to be recouped somewhat by higher asset servicing fees.

The next European NeMa will be held in June 2016, venue and exact date to be announced.
http://www.nema-event.com/