

From: BNP Paribas Securities Corp.

Subject: Comments on Dec 3rd Repo Task Force Proposal

Comment:

ADDRESS

BNP Paribas Securities Corp. (BNPPSC) welcomes the invitation to submit comments to the Tri-Party Repo Infrastructure Reform Task Force (“the Task Force”), under the auspices of the Payments Risk Committee (PRC), on the proposed 3-Way Confirmation and Standardized Settlement Times recommendations published December 3, 2010. BNPPSC fully supports the Task Forces aspiration to reduce intraday exposure and diminish systemic risk. We further seek to help support implementation of these recommendations in the most efficient and effective manner.

Our comments are focused on providing the Task Force and interested parties with information based on BNPPSC’s operational experience, specific to the processing, clearance and settlement of Tri-Party Repo, (TPR), eligible securities. We embrace any invitation to further clarify the ensuing comments.

COMMENTS

3-Way Trade Confirmation Process Proposal

BNPPSC fully supports the Task Force’s proposal for a 3-way trade confirmation process and its ambition to improve the quality and timeliness of TPR trade information. Operations at BNPPSC fully believe that there will be challenges in achieving this goal within the proposed July-August 2011 timeframe. The main challenges that we believe to be in meeting these deadlines are listed below.

- **The inclusion of additional trade data on the transmission to the clearing bank.** This will require a yet to be identified level of IT development by our 3rd party back office vendor. BNPPSC is confident that we can internally develop a feed from our front-end system to our back office vendor’s platform, as is the case with many of the Primary Dealers who utilize their software, and are totally dependent on the vendor to include the new fields in their linkage to the clearing bank. The vendor has affirmed that this functionality will be delivered in a new software release that is scheduled in Q2. The concern is that with the compressed timeframe from the vendor delivery of the software, installation and successful testing, this may jeopardize several dealers in meeting the proposed deadline.

- Technology methods and potential workflow on 3 way match trades** - BNPPSC recommends workflow number 1, (page 7 of white paper), whereas the cash investor affirms the TPR via the clearing agent utilizing a web based solution. This workflow requires limited technology requirements and poses less operational risk by not introducing a third party. BNPPSC has no issue if the cash lender opts to create an internal process to transmit TPR trades to the clearing bank. However, if the cash lender intends to transmit their TPR trades via a 3rd party vendor, this may become a concern. If the 3rd party vendor's product is consistent with their current processes for matching and forwarding transactions, they will only transmit matched trades to the clearing corporation. This would mean that BNPPSC would need to communicate TPR trades with multiple vendors, resulting in additional IT development for our service provider. Since the clearing bank must be the ultimate matching agent on the TPR trades, BNPPSC see this workflow as an inefficient usage of IT resources and money. We are proposing that 3rd party vendors transmit all of the cash lender's TPR trades to the clearing bank, regardless if TPR trade is matched or unmatched.
- Clearing Bank IT development to ensure that current collateral projection functionality continues to ensure proper blend of end-of-day collateral** - BNPPSC has developed several controls to insure the accurate funding of its collateral. BNPPSC and its clearing bank have developed an intra-day projection function which is a control that ensures that BNPPSC has the correct collateral quality to pledge against our lenders requirements in order to fill all TPR shells for that business day. Our clearing bank will need to review this projection functionality now that the collateral will be locked up until 3:30 to ensure that the correct TPR collateral is included in our 1:00PM intra-day projection. This projection allows our operational staff to work with trading to correct any collateral mismatches, therefore having to allocate cash to a TPR.

3:30pm – 4:30pm Settlement Window Proposal

The 'Settlement Window Proposal' is intended to gradually move the TPR settlement to 3:30pm in order to reduce the clearing bank's intra-day credit risk. While BNPPSC strongly supports the reduction of intra-day credit risk to the clearing bank, we sense that this initiative is not aligned with highly regarded liquidity endorsing programs, such as the Daylight Overdraft, (DOD), charges and TMPG (Treasury Fails Charge), initiatives.

- In several conversations with our clearing bank, the 3:30pm settlement window for TPR trades will eliminate the intra-day borrowing of unencumbered securities, (commonly

referred to as UNCLs), that assist firms in making deliveries over the Fed Wire system. This intra-day borrowing promotes liquidity by reducing failed transactions and acts as a clearance catalyst within that system. This intra-day borrowing of securities is common practice amongst all broker\dealers and their clearing banks. We feel that an industry study should be completed that identifies the positive effect of intra-day borrows and the resulting effect if terminated.

- BNPPSC also has concern with the “Phased Approach” of the delayed settlement window. The timeline indicates that the settlement window will be delayed until 10:00am in July 2011 and then rapidly leap to 3:30pm in August 2011. We feel that this timeline is overly aggressive. We suggest that the settlement be delayed until 1:00pm in August 2011; until such time that an industry study can be completed that evaluates the resulting elimination of intra-day risk to the clearing banks. If the results at the 1:00 deadline meet or exceed the recommended risk reduction target, then BNPPSC would recommend that the 1:00 release remain in effect to promote settlement liquidity.

In summary, while we fully support the reduction of intra-day credit risk to the clearing banks, BNPPSC does not wish to increase a firm’s operational risk or reduce the liquidity now provided over the Fed Wire clearance system. We believe that a 1:00pm settlement window would provide a suitable timeframe for a clearing bank to become aware of a broker\dealer’s potential credit issue and yet allow operations to continue to operate in an efficient and controlled environment. BNPPSC respectfully suggest that the Task Force remain flexible on the July and August 2011 implementation target based on an active assessment of all market participants’ and their vendor’s ability to deliver within that time-frame.

We commend the Task Force in their efforts to address the concerns and risks in today’s TPR market and we appreciate the opportunity to comment on the proposal. BNPPSC is available to reply to any questions about the above comments and assist in facilitating the goals of the Task Force. For any questions, please contact Steven Mischia at (201) 850-5575.

Sincerely,

BNP Paribas Securities Corp.

Questions for Public Comment

3 Way Trade Confirmation Process Proposal

1. What additional considerations are important as we execute the 3-way confirm process? [The additional IT development and training needed by dealers and vendors with regards to meeting proposed deadlines](#)

Of specific interest, how various lender segments will confirm trades. [The industry expects cash investors to employ all three methods of confirmation: \(1\) through the agent bank portal, \(2\) direct electronic transmission and \(3\) through the utilization of a vendor as an intermediary.](#)

2. Specifically which additional fields, if any, are worth considering in order to for a repo trade to be considered successfully matched? [The defined fields and details, as outlined in the proposal, are expected to be sufficient to confirm a matched trade.](#)

3. The document currently envisions a window from 7am - 3:30pm to perform three-way trade confirmations. Task Force discussions have highlighted the potential benefits of earlier confirmations (e.g., by 10am), especially during stressful market conditions. Is it feasible to expect that the bulk of confirmations, including allocations, can be performed by 10 am, or if not, by some other time prior to 3:30? Would it be more feasible to set a target for confirmations without allocation detail by 10 am? Please indicate views on the relative benefits and costs of these alternatives. [BNPPSC does not believe it is feasible to expect that the bulk of confirmations and allocations will be performed by 10:00am. The majority of allocations are currently received after 3:30PM. BNPPSC fully supports the 10:00am confirmation of the unallocated block trade and then the confirmation allocation breakdown later in the day. The early morning bulk trade confirmation will ensure that there will not be major financing miscalculations at the end of the day.](#)

3:30pm – 4:30pm Settlement Window Proposal

1. The document mentions the segment of lenders that close their funds at 5 pm, thereby making early allocations difficult. Which other characteristics of the settlement proposal will prove challenging to other lender segments. [For the market to work under the new guidelines, we believe that the majority of allocations \(ideally greater than 90%\) would need to be received by 3:30 p.m.](#)

2. What changes will dealers and lenders need to make as a result of the removal of the daily unwind?

Netting among the same fund within the same clearing bank would help make the market work under the new guidelines:

Some dealers are very focused on the ability to re-optimize allocations in some fashion. Originally a dynamic collateral optimization (DCO) for the collateral substitution process was meant to be available. Due to competing demands this may no longer be the case – some have explicitly asked for full collateral unwind each afternoon for a full re-optimization of the allocation nightly. Clearing banks have apparently engaged the Fed on this and are awaiting a response. This could represent a risk to these dealers who have been focusing on having the DCO ability.

Dealers would need to compress their 8:00 a.m. – 6:00 p.m. processes down to a 3:30 p.m. – 6:00 p.m. timeframe with potential implications for systems, personnel resources, and collateral optimization/adjustment processes and capabilities.

Dealers would add that the securities lending programs (e.g. BNY's UNCL program) of the clearing banks are widely used. The task force may want to examine the metrics of usage of these programs among dealers and the potential impact of the clearing banks removing this service (e.g. increased fails) due to the settlement time change. For example, there may be decreased liquidity, slower settlements/increased fails, and impacts on programs that have promoted liquidity such as Daylight Overdraft and TMPG Treasury Fails Charge.

3. What changes will need to be made in order to enable cash lenders to wire cash into clearing banks by 3:30? NA for BNPPSC

4. How will lenders who may have become accustomed to early morning return of tri-party cash be able to source sufficient alternative intraday liquidity once the settlement window is changed to 3:30? N/A for BNPPSC

Implementation Timeline

1. What key risks to a phased implementation should the task force keep in mind? BNPPSC has concerns with the "Phased Approach" of the delayed settlement window. The timeline indicates that the settlement window will be delayed until 10:00am in July 2011 and then delayed until 3:30pm in August 2011. We feel that this timeline is overly aggressive. We suggest that the settlement be delayed until 1:00pm in August 2011; until such time that an industry study can be completed that evaluates the resulting elimination of intra-day risk to the clearing banks.

2. Which specific implementation challenges to the 3-way trade confirm process should the task force keep in mind? BNPPSC recommends that the cash investor affirms the TPR trades via the clearing agent utilizing a web based solution. This workflow requires limited technology requirements and poses less operational risk by not introducing a third party. BNPPSC has no issue if the cash lender opts to create an internal process to transmit TPR trades to the clearing bank. However, if the cash lender intends to transmit their TPR trades via a 3rd party vendor, this may become a concern. If the 3rd party vendor's product is consistent with their current processes for matching and forwarding transactions, they will only transmit matched trades to the clearing corporation. This would mean that BNPPSC would need to communicate TPR trades with multiple vendors, resulting in additional IT development for our service provider. Since the clearing bank must be the ultimate matching agent on the TPR trades, BNPPSC see this workflow as an inefficient usage of IT resources and money. We are proposing that 3rd party vendors transmit all of the cash lender's TPR trades to the clearing bank, regardless if TPR trade is matched or unmatched.

3. Which specific implementation challenges to the 3:30pm settlement time should the task force keep in mind?

BNPPSC would add that the time frame compression of all-day processes that have occurred heretofore from 8:00 a.m. – 6:00 p.m. down to a 3:30 p.m. – 6:00 p.m. time frame may be drastic and create risk. The elimination of credit risk to the clearing banks may create operational risk (e.g. system glitches/failures, personnel resources) for dealers. Firms may be at risk of failing to optimize collateral or being able to adjust collateral appropriately since the unwind would occur after the securities wire is closed. Dealers think there may be an alternative time frame that allows the clearing banks to reach 90% credit extension reduction, while not introducing significant risks to dealers; dealers have suggested that a mid-day settlement time of 1:00 p.m. may achieve this.

4. Which specific implementation challenges to the committed credit facilities should the task force keep in mind? In several conversations with our clearing bank, the 3:30pm settlement window for TPR trades will eliminate the intra-day borrowing of unencumbered securities, (commonly referred to as UNCLs), that assist firms in making deliveries over the Fed Wire system. This intra-day borrowing promotes liquidity by reducing failed transactions and acts as a clearance catalyst within that system by facilitating deliveries and positively reduced the number of street-wide failed trades. This intra-day borrowing of securities is common practice amongst all broker\dealers and their clearing banks. We feel that an industry study should be

completed that identifies the positive effect of intra-day borrows and the resulting effect if terminated.