



EUROPEAN CENTRAL BANK

OPERATIONS MANAGERS GROUP

13 June 2006

SUMMARY OF THE OPERATIONS MANAGERS GROUP MEETING

29 MAY 2006

AT AIB CAPITAL MARKETS IN DUBLIN

1 Introduction from the chairman

The chairman welcomed the participants and introduced the two guests Mr Andrew Wilson and Mr Ted Platt from Merrill Lynch who would give a presentation on Prime Brokerage

2 Approval of the agenda

The members approved the agenda of the meeting.

3 Reporting and presentations

3.1 Money Market Contact Group 17/5

The last meeting of the MMCG took place in Helsinki, where they discussed the following items:

- *A comparison of internal organisations of banks' money market management*
- *Round up on market developments during the last few months*
- *Prime Brokerage – a presentation by a member bank*

The next meeting of the FXCG was scheduled for 31 May.

3.2 Prime Brokerage

Andrew Wilson and Ted Platt from Merrill Lynch gave a presentation on Prime Brokerage. During the presentation an operational overview of hedge funds and the role of the prime broker were addressed. The presentation was composed of 5 parts: i) the characteristics and strategies of hedge funds, which due to the nature of the product are mainly located at lightly regulated locations, ii) an outlook concerning the European hedge fund industry – currently European and global equities make up approximately one-third of the European hedge fund universe and regulatory changes in the EU markets may drive the

creation of domestic hedge fund markets in Germany and Spain, iii) an overview of the operational processes, addressing the segregated roles of the administrator and the prime broker and the interaction between the three parties (hedge fund, administrator and prime broker), iv) credit, leverage & margin, touching upon the margins applied by the prime broker as well as the need for collateralised lending, and v) risk management, as this business seems to increase operational risk. In this context the presenters explained that the transaction process is completely electronically although the usage of SWIFT is not very dominant in the world of hedge funds.

The Chairman thanked the Merrill Lynch representatives for their very interesting presentation, which provided an in depth insight of the functioning of hedge funds and the role of the prime broker and touched upon the related increase in risk. Prime brokerage is a very topical front office issue, and the operational consequences and risks are of specific interest for this group.

3.3 A view on banks' organisation of Operations

Francesco Manuele (Banca Intesa) and René Steenhart (Rabobank) gave presentations on their internal organisation for operations. These presentations as well as the follow-up discussion revealed a different understanding and interpretation of the role and responsibilities of the middle office. It appeared that the way the organisation has developed is often based on 'historical' grounds. For efficiency reasons the trend seems to be consolidating operational services in a limited number of centres using the same infrastructure. At the same time this seems to facilitate the organisation of business continuity arrangements, because it allows one centre to take over the activities of another centre. Other issues that came up during the discussion were: i) the level of STP for the different types of products, which seems to differ from a high STP rate (nearly 100%) for FX & MM transactions to a very low rate (not even 30%) for derivatives, and ii) the distribution of the processing costs between direct costs (processing of confirmations) and indirect costs (ensuring compliance with internal audit, the Sarbanes Oxley act, etc.).

3.4 Global Resourcing

During his presentation, Chris Roberts from HSBC addressed the decision process when evaluating the feasibility of sending work to an offshore office by addressing aspects like managing the onshore impact, selecting the right process & location and key feasibility factors and steps. The presentation initiated an interesting discussion among members concerning the business case for offshoring. Although the costs for resources is a clear incentive, one should also take into account that due to external factors like the difference in culture the offshore location a higher number of resources is required compared to the onshore location, e.g. in some countries staff can leave on the day they hand over their notice.

4 Contingency Planning

4.1 Task Force on Contingency Planning

The chairman of the TF on Contingency planning presented some propositions concerning the unavailability of SWIFT based on bilateral meetings held with ABN AMRO, Calyon and Rabobank.

The common understanding was that the overall resilience of SWIFT is very high, therefore a global failure of the SWIFT network did not form part of the discussions. The scenario of a financial institution or a country losing its SWIFT connection was seen as more problematic (level playing field). While the global players strive for a maximum level of SWIFT resilience using several hubs in preferably different regions, the smaller banks seem to be more vulnerable in this respect. The rather large investments necessary for achieving a high level of resilience for the SWIFT infrastructure seem to trigger considering outsourcing either SWIFT transactions or the IT infrastructure.

The advantages and disadvantages of declaring a bank holiday in case of a major disaster were also touched upon. Some of the members stressed not to be in favour of calling a bank holiday in case of a SWIFT failure as this would introduce more problems than handling interest claims in case of need.

In this context, the possibility to review the interbank compensation guidelines was discussed, with different points of view being expressed. According to some members more clarity on the potential losses covered could avoid strategic behaviour such as the withholding of payments.

Concerning the processing of contingency payments there was common agreement that even without a Service Level Agreement with the Central Bank they would be ready to assist and support the processing of critical payments. However, in view of TARGET2, there was a concern that SWIFT would become a single point of failure, since it is not envisaged to use an alternative network. Subsequently, some members considered that, for those services that only rely on SWIFT (e.g. CLS, TARGET2.). It might be worth investigating the possibility of providing an alternative contingency channel via the internet.

Members agreed that there was a need to further elaborate on the above mentioned aspects before a more detailed reporting to the FXCG and MMCG planned for the second half of this year takes place.

4.2 Resilience Benchmarking project

During the last meeting, it was agreed to further analyse the possibility to organise a similar exercise with a narrower scope, for a specific sub-set of institutions within the euro area. The Tripartite is now working on a 'light' version of the questionnaire (approx. 200 questions) aiming at the same objectives but for the next level of financial institutions. The pilot will start in August, with a full roll out in October. This 'light' version could be a possibility for the OMG to participate, where the focus should be on the euro. It was agreed to further assess this possibility.

5 Global Conference 2007

The secretary of the group briefed on the status of the preparation for the organisation of the global conference. On 10 May a first brainstorming meeting took place to which the chairman of the OMG, the members of Commerzbank, Dresdner and the Bundesbank as well as the secretary of the FXCG participated. The issues discussed were the dates/venue, a possible theme and topics.

The Conference will take place on 23/24 April in the Hilton hotel in Frankfurt and the proposed theme is Treasury Operations - Striking the balance between efficiency and resilience. Potential topics are the following:

- *Operational issues:*
 - *Post trade processing – improving efficiency and reducing operational risk*
 - *STP – definition of STP and how far has STP been implemented (what about exception handling and non-vanilla type trades)*
 - *The Buy-side – the needs of the Buy-side (with corporate speakers?)*
- *Efficiency and reducing costs:*
 - *Offshoring/Outsourcing – preferably a speaker with a positive experience as well as one who decided to return*
- *Regulation and Governance:*
 - *Sarbanes Oxley (SOX) compliance*
 - *Impact of the MiFID*
 - *Legal aspects*
- *Resilience*
 - *Benchmarking exercise ?*
- *Other developments:*
 - *CLS*
 - *TARGET2 & SEPA*

The members expressed their agreement with the proposed list of topics as well as with the proposal to request some further input from the Front office (via the FXCG & MMCG). Another brainstorming meeting will be organised in June 2006 and all members were invited to put forward suggestions for topics and speakers.

6 Any other business

The secretary of the group gave a quick update on the Contact Groups' website project that has made some progress since the last meeting as well as on the testing of the contingency procedures and the restricted access website.

7 Next meeting

The next meeting will take place in Frankfurt on 7 November 2006 and it was tentatively agreed to focus on the preparations for the global conference, the reporting to the MMCG & FXCG on contingency planning and the work of the Task Force on trade confirmations and, at the same time, not excluding the possibility to organise another round of operational organisation presentations.

LIST OF PARTICIPANTS – OMG Meeting 29 May 2006**Host - AIB Global Treasury**

<u>Participant's organization</u>	<u>Name of participant</u>
AIB Global Treasury	Mr Paul Dillon (Chairman and Host)
ABN Amro Bank	Ms Ellen Vollebergh
Banca Intesa	Mr Francesco Manuele
BNP Paribas	Ms Sophie Gatellier
Calyon Bank	Mr Laurent Côte
Commerzbank AG	Absent
Deutsche Bank AG	Mr Ottmar Ackerman
DEXIA-BIL	Mr Romain Thill
Dresdner Bank AG	Mr Heiko Kroeber
Fortis Bank	Mr Marc Camus
HSBC Bank	Mr Chris Roberts
Nordea Bank	Absent
Rabobank	Mr René Steenhardt
Santander Central Hispano	Mr Angel del Amo Arcones
UBS	Mr Simon Gaston
Deutsche Bundesbank	Mr Wolfgang Schulte
Banque de France	Mr Michel Chedhomme (alternate)
De Nederlandsche Bank	Mr Eloy Lindeijer
European Central Bank	Mr Eric Vermeir
European Central Bank	Ms Annemieke Bax (Secretary)
<i>Guest speakers:</i>	Andrew Wilson, Merrill Lynch
	Ted Platt, Merrill Lynch