



EUROPEAN CENTRAL BANK

EUROSYSTEM

ECB-UNRESTRICTED

Harmonisation areas in debt issuance

3rd DIMCG meeting
16 December 2020



Introduction

- As per its Terms of Reference, the DIMCG needs to look into identifying the harmonisation topics relevant in the area of debt issuance and initial distribution process
- Without pre-empting any conclusions, work could start on elaborating on potential areas already identified / mentioned by several stakeholders
- The aim is to see which areas and specific aspects of debt issuance could be potential targets for harmonisation work (and what should not be in the scope of harmonisation)
- End-goal of DIMCG discussions on harmonisation is to present in the DIMCG advisory report in a structured and detailed way the consensus areas where harmonisation is required, i.e. what / how should be harmonised. At this stage, the objective of the DIMCG is not to endorse standards or to start monitoring compliance of national markets and market actors with harmonisation standards

There are three ‘sources’ of input to the discussion on harmonisation

- I. Existing industry standards / practices
- II. Past feedback from stakeholders (2019 ECB market consultation and preceding DIMCG discussions)
- III. Findings in DIMCG pillar 1 work (based on survey) – expected by Q1 2021 and focused on initial case study (European debt issuance)

Overview

- 1 Existing market standards / market practices**
- 2 Feedback from the 2019 consultation and DIMCG members
- 3 Potential areas for harmonisation
 - 3.1** Investor identification / KYC
 - 3.2** Term sheet
 - 3.3** Business day, day count and rounding conventions
 - 3.4** Documentation
 - 3.5** Data exchange / datamodels
 - 3.6** Timeline / settlement cycle – T+5 / T+2
 - 3.7** Book building / order book management

Mapping existing EU / global market standards applicable for debt issuance

- ICMA Primary Markets Handbook:
 - Content: Focus on pre-issuance, limited coverage of post-trade. Detailed set of principles on behaviour of stakeholders (mainly managers and issuer) systematically structured along the issuance process, contains also model agreement between managers / dealers
 - Scope: syndicated international bonds (excluding high-yield, equity linked, USD)
 - Form: recommendation to all stakeholders, ICMA members expected to comply, monitoring of compliance limited to peer review
- AFME Primary Dealers Handbook:
 - Content: Focus on pre-issuance, limited coverage of post-trade. Detailed overview of national practices across EU countries on primary and secondary sovereign markets
 - Scope: EU sovereign debt instruments (both domestic and international)
 - Form: documents existing practices, no recommendations

Mapping existing EU / global market standards applicable for debt issuance - continued

- ESDM (EFC substructure) hub:
 - Content: Focus on pre—issuance / PD systems, and national procedures with wealth of information on national market conventions and requirements. Some model agreements / clauses defined at EU level (euro area collective action clause)
 - Scope: EU sovereign debt instruments
 - Form: documents existing practices, no recommendations (except model agreements, CAC)
- ISMAG Operation Market Practice Book:
 - Content: Focus on post-trade, new issue information flow (issuance documentation), corporate action notification / processing, income processing
 - Scope: Eurobonds
 - Form: standards, rules for voluntary adherence by issuers, those who legally commit to adhere receive respective label
 - Compliance is monitored via KPIs (only aggregate indicators are published)
- ICMSA Market Guides / Practices
 - Content: Focus on documentation and post-trade, complementing ISMAG
 - Scope: Eurobonds
 - Form: recommended market practices

1 Existing market standards / market practices

2 **Feedback from the 2019 consultation and DIMCG members**

3 Potential areas for harmonisation

3.1 Investor identification / KYC

3.2 Term sheet

3.3 Business day, day count and rounding conventions

3.4 Documentation

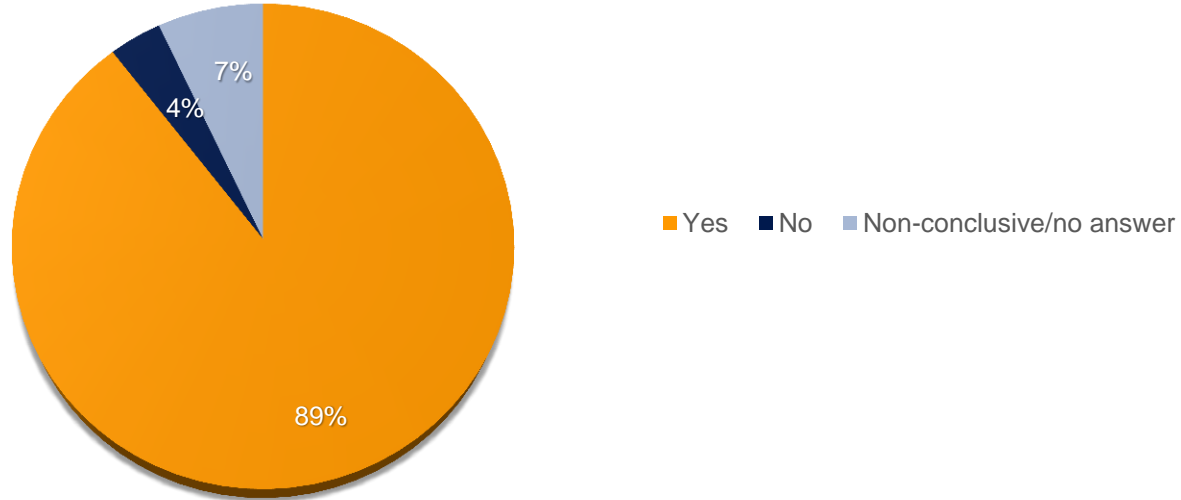
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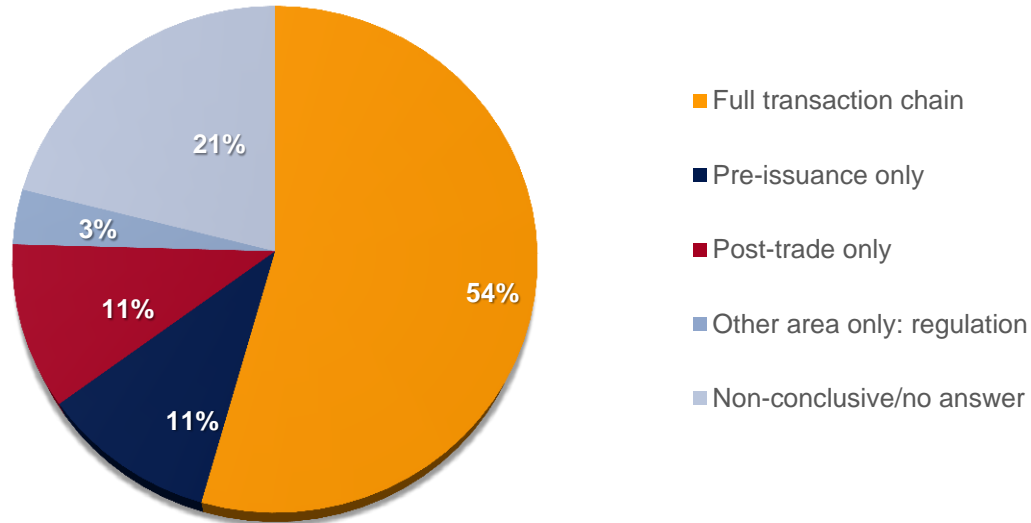
Feedback from the 2019 ECB public consultation

Do you think that there is a need for further harmonisation and standardisation in the area of debt securities issuance?



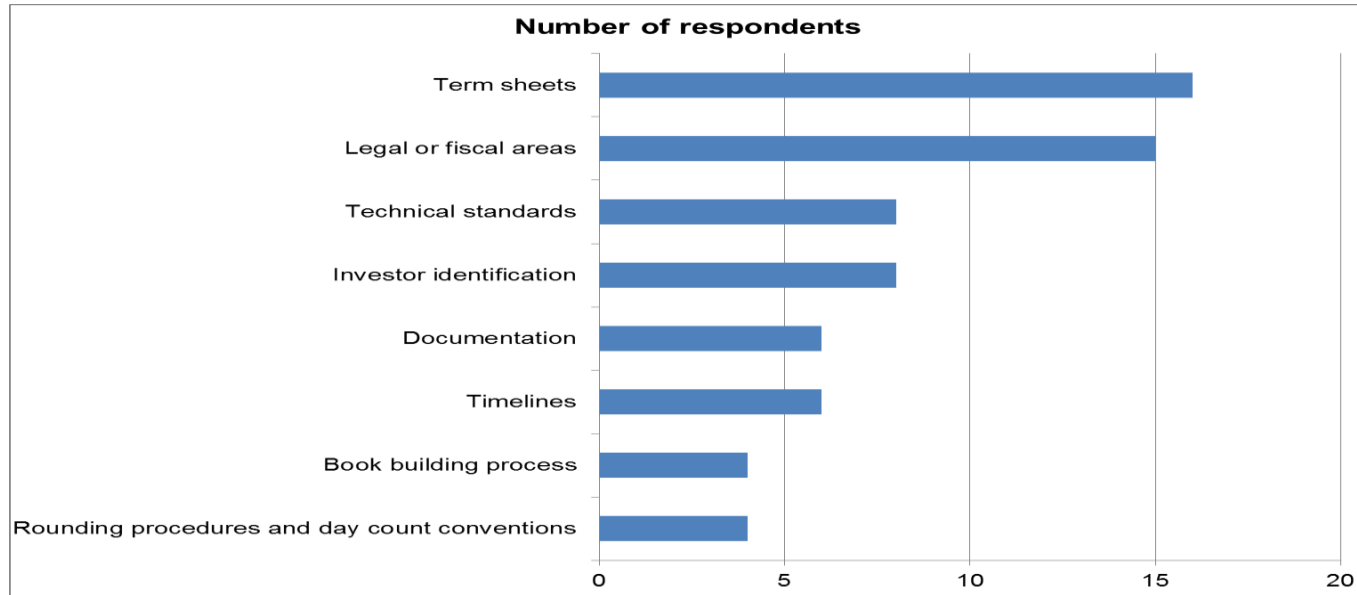
Feedback from the 2019 ECB public consultation

Should the work on harmonisation / standardisation cover the full transaction chain i.e. from pre-issuance to post-trade?



Feedback from the 2019 ECB public consultation

What are your views regarding the pre-issuance harmonisation items/topics? Which processes should be looked at?



Areas mentioned by DIMCG members

- Data exchange – communication channels and data models
- Book building / order book management
- Investor identification / KYC processes
- Ownership / confidentiality of data
- Documentation management / digitisation
- Rounding and day-count conventions
- Automation of announcements, final term sheets, legal docs
- ISIN usage / administration
- Common terminology / taxonomy / glossary
- Ex post aggregate data transparency
- Harmonised timeline / shorter settlement cycle

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Investor identification

- Issue statement:

Issuers and deal managers need to clearly know who the investors (expressing buyer interest in a deal) are and be able to have a consolidated view of the bids by the same investor in an efficient way - unique and consistent identification of investors among issuers and dealers and across deals

- Assumptions:

- Investor identification is not standardised currently (free text names, proprietary ids)
- Aim is to find an identification method that supports digitisation and STP
- Identification encompasses both unique id and (static but up-to-date) reference data

Single standard id and reference data:

- One obvious solution is the Legal Entity Identifier (LEI) as global standard
- LEI opportunities
 - LEI is still not omnipresent but gaining ground fast
 - Regulatory requirements in Europe as well as most other standards relevant for financial services increasingly build on LEI
 - LEI includes basic reference data (legal name, address) and also at Level 2 parent–subsidiary relationships
 - LEI database is publicly available with queries easily automated via file download or API access

Investor identification

- LEI challenges
 - Many legal entities still not having LEIs
 - LEI is at legal entity level, does not contain information beneath, i.e. organisational unit which is relevant for analysing buying interest (e.g. which fund for asset managers, trading unit or ALM unit for banks, etc.)
 - LEI reference data is thin, does not contain key data elements relevant for issuance, e.g. investor type, SSI)
 - LEI code is not an 'intelligent code' in itself, it needs to be looked up in reference data to identify the entity (although look-up function can easily be automated, supported by GLEIF)

Investor identification

Questions for discussion:

What are the drawbacks / barriers to using LEI as single harmonised investor ID? Is the LEI a potential solution?

To what extent is LEI used today to identify investors in issuance?

Are there or should there be alternatives to LEI?

Should LEI be used all through the whole transaction chain, i.e. also in post-trade?

KYC (know-your-customer requirements)

- Issue statement:

A lot of resources are spent on ensuring compliance with know-your customer requirements when on-boarding investors (parallel manual procedures)

- Assumptions:
 - KYC responsibilities remain a core service by dealers / agents, i.e. validation of investor identity is dealers / agents' task but could be made more efficient by more harmonised procedures
 - Regulatory requirements already harmonised via common EU KYC rules
 - Tri-party services seem to exist to support and potentially share KYC data (at least on banks as customers) – regulatory / supervisory requirements may prevent sharing
 - Data ownership needs to be clear – who can do what with shared data

KYC (know-your-customer requirements)

Onboarding and validation of identities

- Done by dealers or issuer agents (depending on form of issuance)
- KYC is also a regulatory requirement.
To note: European Commission is rethinking KYC rules in the context of its Digital Finance package also taking into account the lessons learnt from COVID-19 lockdowns
- Verifying identities remotely (i.e. e-IDs) is assumed to be a key element in this work
- Question of room for improvements in KYC processes: what element of the process is the pain point in issuance, can harmonisation or central coordination help? Or is this more a FinTech solution that is needed?

Data sharing / consolidated databases on investors

- *“A common data base, the basis for a performant syndication tool and possibly direct access in auctions could be an ultimate goal. Currently, dealers provide issuers with an important KYC service on investors, for whom they bear onboarding responsibility. Here also, one could imagine the set-up of a “certified database”, fed by dealers through an onboarding and KYC procedure of investors and issuers alike. This database could be used in different issuance mechanisms : auctions and syndications. It would simplify straight-through handling of allocated orders and increase issuer’s client knowledge.” – **quote from a respondent in the 2019 market consultation***
- Issuers clearly see a need to maintain up-to-date data on their investors in an efficient way – both in relation to the investor bids in a given transaction and on an on-going basis
- On the other hand such data in the context of a transaction may be confidential and may require strict control on who has access to it (GDPR limitations are also relevant)
- Investor passporting and third-party solutions / common tools can greatly help – potential room for harmonisation

KYC (know-your-customer requirements)

Questions for discussion:

What are the main issues with the KYC process and can harmonisation help?

If yes, what should be the focus of standardisation / harmonisation?

To what extent and in what format are static data on investors shared between participants to a deal (issuer, agents, lead managers)?

Do syndicate banks and investors see scope for rationalisation by pooling KYC work instead of parallel work by each bank?

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Term sheets

- Issue statement:

Term sheet generation and processing should be effortless and automated for all stakeholders

- Assumptions:

- The term sheet lists the key characteristics of a debt issue. The content does not change significantly across issuers and issuances / debt instruments
- At the moment, term sheets are produced by the issuer / lead manager via copy-paste of information from the latest deal into a term sheet template from a previous deal
- Layout and structure of the term sheets differ significantly across issuers, but content is very similar. Potential for reducing “confusion” / increasing comparability for all market actors
- Three distinct aspects: i) harmonising the representation of data ii) harmonising content and iii) automating term sheet generation

Term sheets

Term sheet harmonisation

- In substance the data elements of a term sheet seem fairly standard (or is this not the case?)
- Harmonisation could target
 - what data / information elements term sheets should contain (although fairly standard already)
 - content (e.g. day-count convention, rounding rules, see next item)
 - a common template
- it may be easy to define a standard template, but benefits would have to be highlighted

Term sheets

Term sheet automation (automated generation)

- Automation: generating term sheet from relevant data sources and sharing it across parties / stakeholders of the deal → objective is to reduce time / efforts it takes to generate final term sheet
- Harmonisation can help automation but not sufficient. Automation depends on the ecosystem of data sources that need to feed term sheet generation
- For the term sheet automation to have the highest level of benefits, a common platform / data base or an seamless interaction between the different systems of stakeholders would be required. Individual automation by every issuer may not make much sense → Can this be achieved without common tools / infrastructure?

Term sheets

Questions for discussion:

Is the different layout and the manual creation of term sheets an issue today?

Is this about term sheet harmonisation or term sheet automation?

What would be the benefits of harmonising / standardising term sheets?

Is it possible to create a template that fits all European issuers and all the different debt instruments they issue / transactions they execute? What has been done in this respect so far?

Is this relevant only for syndication or also for auctions?

Would it be costly / challenging for issuers and dealers to adapt to single template?

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Business day, day count and rounding conventions

- Issue statement:

There should be a convergence towards the use of a single business day convention / a single day count convention / a single rounding convention in issuance procedures

- Assumptions:

- There are finite sets of business day / day count / rounding conventions – already standards themselves – the issue is that there is too many of them...
- There seems to be a trend towards convergence but slow
- These conventions are applied across wide set of financial instruments and market segments – not only plain vanilla debt but also derivatives, not only issuance but collateral management, etc.
- Consistency is needed across market segments due to operational and economic links (e.g. hedging)
- Link to term sheet harmonisation

Business day conventions

- At least 6 conventions exist all prescribing in different ways when the issuer should make a payment if the scheduled payment (e.g. coupon) day falls on a non-business day
- What is the reason for this co-existence?
 - Legal reasons: e.g. national law requires that payments be made in specific month / does not allow slipping between months
 - Economic / accounting reasons: preference of the issuer out of economic / accounting considerations (e.g. manage financial statements)
 - Pure legacy / historic reason – “was always done this way”
- Diversity creates an issue in post-trade (rules are defined upon issuance)

Day count conventions

- A relatively high number of day count conventions (DCCs) exist
- What is the reason for this co-existence? (operational / economic / legacy)
- ISMAG market practice requires standard definitions to be used by issuers for 'Top 6' DCCs (i.e. for Eurobonds)
- If definitions are clearly agreed / standardised it should be relatively easy to manage / compare / convert different DCCs
- Is the issue of having multiple DCCs or is it that definitions of DCCs differ across stakeholders?

Rounding conventions

- Two dimensions:
 - Round to what? – whole unit / decimals
 - How to round? – round down; round up; commercial / mathematical rounding
- Clear rules in the post-trade / CA space: CAJWG standard, SCoRE standard):
 - For cash: rounding down to number of decimal places permissible in the payment currency
 - For securities: rounding down to permissible decimal places in denomination currency for FAMT and rounding down to nearest whole unit for UNIT
- Is it an issue in issuance and initial distribution? If yes, shouldn't the existing CA standards be followed?

Business day, day count and rounding conventions

Questions for discussion:

Is the co-existence of different business day, day count and rounding conventions / standards an issue?

Should issuance practices converge onto a single of these conventions?

What are the reasons behind the existence of multiple standards?

Is the issue the co-existence of multiple conventions or is rather that definitions / applications of these differ by stakeholders?

On rounding: if this is a harmonisation issue, why aren't the existing CA standards a solution?

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Documentation

- Issue statement:

There is a need for efficient, secure and digital way of creating, maintaining storing and exchanging operational and legal documents in the issuance process

- Assumptions:

- ISMAG market practice provides detailed flow descriptions (from ICSDs point of view) and seems to be a good starting point for discussion
- Is the focus on pre-issuance (pre-trade / trade) or post-trade documents?
- Existing exchange mechanism relies on sending emails with pdf attachments
- Harmonisation / standardisation could potentially help in two areas: i) common templates and ii) streamlining processes related to creation, storage, exchange and other workflows

Harmonising document list, names and templates:

- Key data fields / elements can be agreed for standard templates (but may not necessarily bring substantial benefits)
- Key difference between stand-alone issues and programmes (frequent issuers)
- Is content harmonisation needed / relevant?
 - Flexibility in drawing up agreements and other legal documents should remain with the parties
 - Is there a link to legal harmonisation in case of legal documents?

Documentation

Creating documents

- Automating document creation does not require harmonisation across actors if the document content is only fed by a single actor...
- ...but require standards if documents should be automatically created based on the interaction of multiple actors

Exchanging documents

- Difficult to find alternatives to emailed pdfs unless documents are fully digitalised by
 - common infrastructure / document warehouse (central or DLT)

or

 - e-signatures, e-stamps (e-ID) and machine readable datasets replacing scanned pdfs (link to e-ID developments)

Documentation

Which documents should / should not be in scope?

Pre-trade:

Invitation letters

Announcements (mandate; opening , update, closing of order book; launch; allocation, price fixing)

Agreements / contracts between parties (e.g. agency agreements, agreements between managers)

Legal opinions / comfort letters

Base Prospectus / Prospectus / Offering Circular

Term sheet / Terms and Conditions

Pricing Supplement / Final Terms

Post-trade:

Issuer CSD agreement

Global Note

Trust Deed / Indenture

Other?

Documentation

Questions for discussion:

Is this a relevant area for harmonisation?

How do investors evaluate the importance of harmonising documentation provided by issuers?

Which documents should be in scope?

How should it be further specified what are the pain points / should be the focus?

Is this a question of format or also content, i.e. should content of issuance documentation be subject to a harmonisation discussion?

Apart from not helping STP what are the issues with the current pdf-over-email practice?

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Data exchange / datamodels

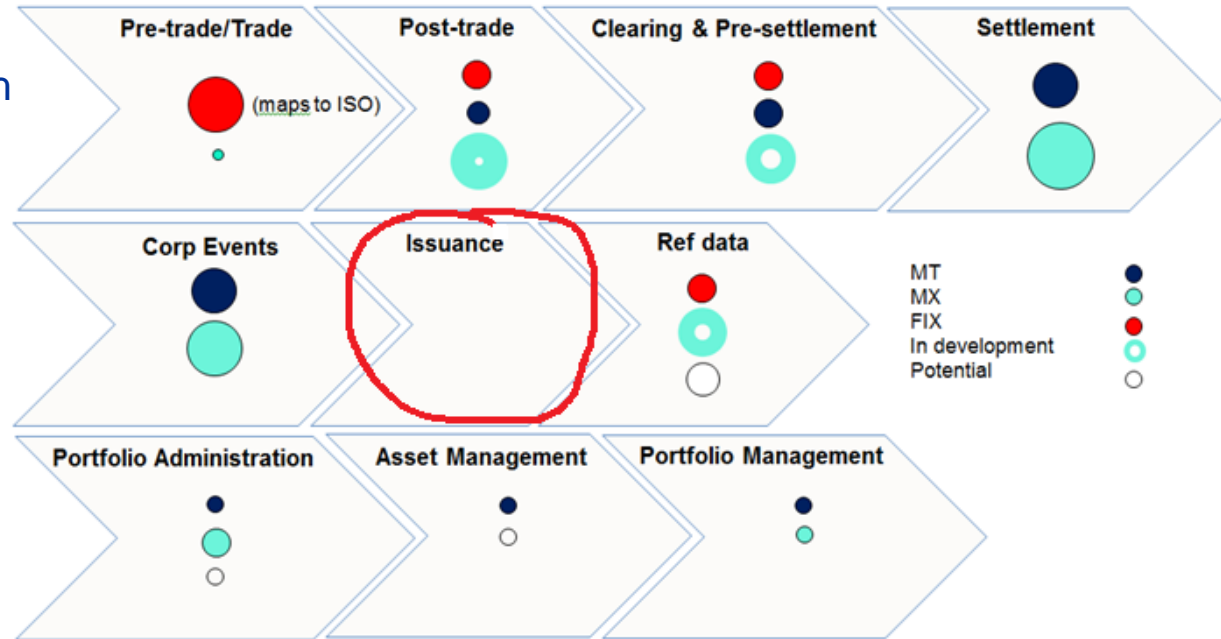
- Issue statement:

Streamlined and efficient data processing and STP in data exchange between the parties across the full issuance transaction chain require harmonised datamodels / single data exchange protocol

- Assumptions:
 - Today, where not all parties to the transaction use the same IT platform, data exchange in the issuance process takes place between parties in proprietary ways and dataformats implying manual data import / export and additional manual work
 - The existing inefficiencies impose limits on what issuers or dealers can do during the issuance process with data (hampering data analysis, simulations, real-time view, etc.)
 - Due to lack of common and widely accepted datamodel / data exchange protocol third-party vendor applications are often not compatible with each other

Data exchange / datamodels

- Issuance seems an area which has been lagging behind others in financial messaging standardisation
- What are the reasons for this?



Source: Standards Messaging Landscape, SWIFT (2013)

Data exchange / datamodels

	Function	Cash Equities & Fixed Income	Forex ⁽²⁾	Listed Derivatives	OTC Derivatives ⁽²⁾	Funds
Issuer	Pre-investment decision		N/A		N/A	
Front Office	Pre-Trade					
	Trade					
Middle Office	Post-Trade	▲ ●	▲ ●	▲ ●		
	Clearing / Pre-Settlement			▲ ●		
Back Office	Asset Servicing	● ◆	N/A			● ◆
	Collateral Management	▲ ●	N/A	▲ ●	■ ●	N/A
	Settlement					
	Pricing / Risk / Reporting	■ ●	■ ●	■ ●	■ ●	■ ●
Investor Supervision	Regulatory Reporting	▲ ●	▲ ●	▲ ●		
Issuer Supervision	Regulatory Reporting		N/A		N/A	

▲	FIX	●	ISO (1)
■	FpML	◆	XBRL

(1) Represents ISO 20022, ISO 15022 and MT messages
 (2) See OTC Derivatives breakout for details:
 - Syndicated Loans, Privately Negotiated FX, and OTC Equity, Interest Rate, Credit, and Commodity Derivatives
 - FpML payload may be used in combination with FIX business processes in dealer to buy side communication

- The **Financial Information eXchange (FIX)** protocol seems to be the best potential candidate to provide a building ground for creating and adopting a standard data exchange protocol for issuance (pre-trade and trade phase)
- Relevant work in the FIX community focused on IPOs / equity issuance
- Several key players have recently mentioned debt issuance as the next area to target with adoption of FIX

Source: Investment Roadmap, Standards Coordination Group (2010)

Data exchange / datamodels

- Commitment by each relevant standards organization (FIX, FpML, SWIFT, XBRL, ISITC and FISD) to the ISO 2022 business model to ensure interoperability
- The respective business processes from all standards / protocols will be incorporated within the ISO 2022 business model for ISO 2022 XML based messages to be created to support the business processes

FIX PROTOCOL
INDUSTRY-DRIVEN MESSAGING STANDARD™

FpML
Financial products Markup Language

ISITC

SIIA / FISD
.net

SWIFT

XBRL
eXtensible Business Reporting Language

ISO 2022 data library and messaging

Data exchange / datamodels

Questions for discussion:

If there are issues with data exchange between parties in the issuance process are they related to lack of standardisation / harmonisation and a lack of common protocols?

If so, why hasn't FIX protocol based messaging been implemented (widely) in the industry?

Are there third-party tools / issuance platforms that rely on FIX or other global messaging protocols?

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Timeline / settlement cycle – T+5 / T+2

- Issue statement:

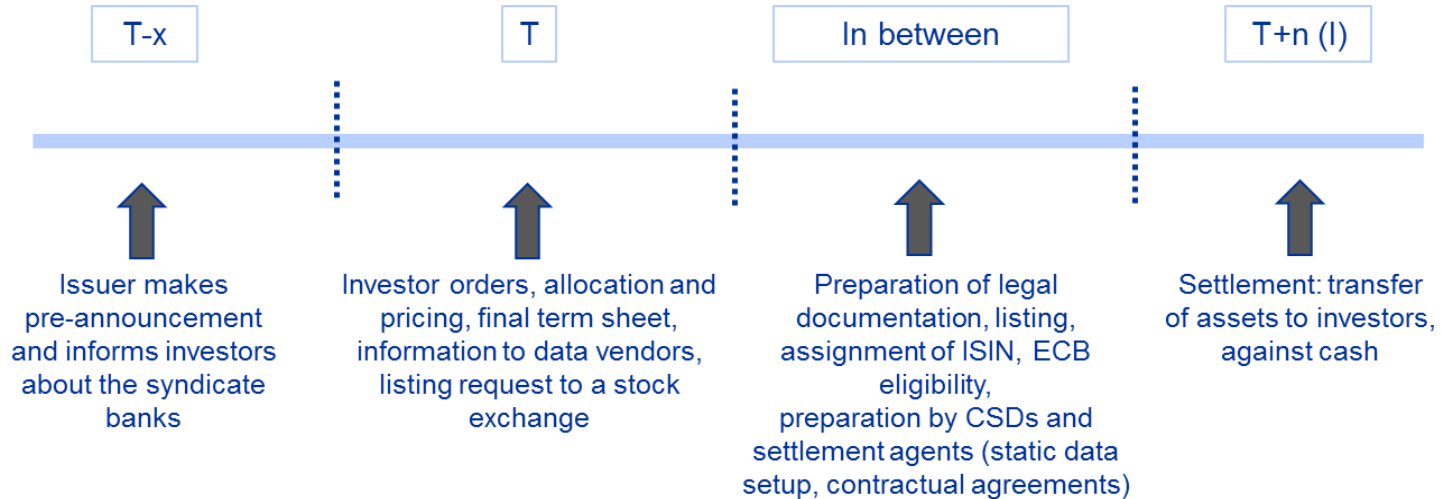
The typical issuance settlement cycle (T+5) for syndication is considered too long by stakeholders and it is at odds with the EU standard secondary market settlement cycle, T+2

- Assumptions:

- Several factors may require currently 5 business days between pricing / final allocation and settlement in issuance:
 - Preparing / signing / distributing final documentation
 - Collecting / building up liquidity at / by dealers
 - Preparing the settlement process by agents

Timeline / settlement cycle – T+5 / T+2

- Assumptions (continued):



Timeline / settlement cycle – T+5 / T+2

- The current settlement cycle seems to be product of challenges in several areas (some already covered):
 - **Creation / distribution of final issuance documentation** – link to potential harmonisation / standardisation and streamlining of process of creating / signing and distributing legal and operational documents
 - **Collecting liquidity** – pre-funding by buyers before settlement date should not be a requirement in highly efficient financial markets – is it a question of internal processes at stakeholders (e.g. investors / dealers) or is it a question of market infrastructure?
 - **Preparing for settlement** – Issuer agent / LM to arrange settlement details with allottees and allottees with custodians of all investors, prepare settlement instructions to CSDs and correspondent banks - with efficient / STP procedures would not require 5 business days (e.g. ISMAG market practice gives 2 business days for these steps)

Timeline / settlement cycle – T+5 / T+2

Questions for discussion:

Is T+5 settlement an issue today? What would be the benefits of a shorter settlement cycle? Who would benefit?

Is this a topic for harmonisation?

Is the settlement cycle also an issue in case of auctions?

Which areas would need improvement in order to allow faster settlement?

Documentation? Liquidity provision? Settlement preparation / interaction with the (I)CSD? Other?

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Book building / order book management

- Issue statement:

There is a significant room for efficiency improvements in the way the relevant parties interact in managing order books in the issuance process.

- Assumptions:

- This is an area that covers the whole of the trading phase, i.e. from the book opening announcement to final allocation and pricing – does / should it also cover pre-trade, i.e. sounding, collecting IOIs for indicative book?
- If not all parties connect to the same IT platform then this process is characterised by exchanging and processing data / information via emails and phone and in proprietary formats (e.g. in excel sheets) implying a lot of manual work
- A number of third party applications / platforms exist but there is a lack of common business rules / protocols – competition for the market instead of in the market
- Issuers would like to see by simply ‘pushing a button’ real-time and consolidated view of the order book at any point in the process

Book building / order book management

Sub-phases:

- Collecting indications of interest IOIs (pre-order book)
- Announcement / opening of order book
- Collection and validation of orders
- Processing, updating, cancelling and cleaning orders
- Order book dissemination / publishing (to those who need to see, co-leads, issuer, etc.)
- Analysis of order book (simulations for issuer decision)
- Closing order book, pricing and allotment / allocation, closing announcement

Book building / order book management

What could be (potentially) harmonised?

- **Business rules**
 - ICMA Primary Market Handbook provides high-level business / behavioural standards of book building for syndication
 - Timing and format of announcements
 - Content / representation of orders
 - Transparency requirements (who sees what when), content of reports on deal statistics / simulation
 - Rules of allotment / allocation
- **Technical rules**
 - Common data exchange protocol / APIs (see as Data exchange as stand-alone harmonisation area)

Book building / order book management

Questions for discussion:

What would be the benefits and drawbacks of harmonising aspects of order book management?

Can / should order book management be harmonised without common IT platform used by all parties to the transaction?

What are the sub-processes / stages that should be in focus?

Is there a demand for business rules / standards going beyond existing conventions (e.g. ICMA Primary Market Handbook, other existing market practices / conventions)?

Potential other areas

Other broad areas mentioned in the public consultation include:

- Withholding tax procedures (WHT)
 - a lot of on-going initiatives most recently by the European Commission with its new CMU Action Plan
 - **This seems to be a post-trade topic, do WHT procedures affect the process of issuance?**
- Legal harmonisation
 - very broad area
 - No progress so far for a EU Securities Law initiative
 - **Is there a specific relevance for the pre-trade and trade phase of debt issuance?**
- **Others?**

Which service solutions could support the above?

- This is more a Pillar 3 DIMCG discussion
- How do current and/or upcoming market solutions support harmonisation across the transaction chain, market actors and national markets?