Repo Guidelines: How Do They Affect the Investing Public? Part II

\\Trinidad and Tobago Securities and Exchange Commission

Table 1 - Minimum Margin Requirements for Non-Institutional Investors

Residual Maturity	Margins	
(In Years)	Sovereign Issues (%)	Other Issues (%)
Up to 1 year	1	2
Over 1 year to 3 years	3	3
Over 3 years to 5 years	4	7
Over 7 years to 11 years	4.5	7.5
Over 11 years	4.5 – 6.0	7.5 – 9.0

We continue our three-part series on Repo Guidelines and focus our discussion this week, on **Sections V** to **XIII** of the **Sales and Repurchase Agreement Guidelines.** According to **Section V** of the Repo Guidelines, Repo sellers must ensure that all collateral securities[1] are either registered with the Commission, or registered in accordance with the securities laws or regulations of an Approved Foreign Jurisdiction. Additionally, collateral for Repo sales to Non-Institutional Investors or the individual/ordinary investor, should be restricted to the following:

a) Treasury Bills and Notes issued by the Government of Trinidad and Tobago ("GORTT");
b) Bonds and Eurobonds issued or guaranteed by the GORTT, provided they were issued in Trinidad and Tobago;
c) Bonds issued by state agencies and statutory bodies of the GORTT; and
d) Corporate Bonds listed on the Exchange.

Participants in the Repo market, according to **Section XI** of the Repos Guidelines, shall treat the names and identities of parties to transactions as confidential except where required by law.

The Seller of a Repo asset shall repurchase the asset from the Buyer at a price determined by the principal amount invested by the Buyer, the interest rate and the term of the Repo. **Section XII** of the Repo Guidelines outlines the characteristics of a Master Repurchase Agreement, an obligatory component of all Repo transactions which should at a minimum:

a) be written in plain English;
b) include a description of the nature and risk of the security;

[1] These refer to the assets pledged by a Repo Seller as security/collateral for a repo agreement. In the event of the Repo Seller defaulting on the repo agreement, the Repo Buyer can claim these assets in lieu of the principal sum to be repaid.

c) provide for the perfection of the interest in the security;
d) specify the custody arrangements, the rights and obligations of the Buyer and the Seller and the events of default;
e) provide for monthly Mark-to-Market transactions, appropriate Margins and for Maintenance of Margins whenever there is a material change in value; and
f) make provisions clarifying the rights of parties regarding substitutions of capital, treatment of interest payments, break rates and the resolution of disputes.

The Master Repurchase Agreement shall not contain provisions that conflict with the Repo Guidelines, the Securities Act of 2012 or any other By-Law of the Commission.

A Repo's maturity date shall be the first following business day when the date falls on a non-business day. The Repo rate is calculated on the basis of actual/365 days per year. According to **Section XIII** a Haircut or Margin shall be applied at the time the Repo transaction is entered. A Haircut or Margin can be defined as the difference between the initial market value of an asset and the purchase price paid for that asset at the start of a Repo.

The margins for Non-Institutional Investors are highlighted in Table 1 below which can be found in Parts A in Appendix 2 of the Repo Guidelines. These can be amended by the TTSEC as needed.

Section V of the Repo Guidelines states that Repo sellers shall adopt policies and procedures to ensure that all collateral securities that are the subject of Repos are either registered with the Commission or registered in accordance with the securities laws or regulations of an Approved Foreign Jurisdiction. However, these collateral securities must not be used to cover short sales or be subjected to margin purchases where these are held by other brokers, nor otherwise pledged or used as collateral.

As stated under **Section IX**, substitutions of Repo Assets should be allowed only where specified in an agreement between the Buyer and the Seller, and should only be permitted by the Buyer where the Collateral to be substituted is of equal or greater value than the original asset. Collateral securities shall not be sold without first assigning another suitable asset in its place and these assets may only be substituted if an agreement between the Buyer and Seller is found. Where collateral securities are sold, the assigned security must be of equal or greater value than the security that was sold.

All securities that are used to collateralize Repos sold to Non-Institutional Investors shall be held under the custodianship of the Trinidad and Tobago Central Depository ("TTCD") or any other custodian approved by the Commission. **Section X, 13-14** states that;

a) A Buyer's interest in securities shall be evidenced by an assignment in the books of the Custodian;
b) The custodian shall maintain adequate and separate records in respect of Collateral Securities including: sales and purchases, in the assigned pool of, or securities subject to repo securities; and physical custody or location;
c) The Custodian shall exercise its fiduciary duty with the degree of care and skill that a reasonably prudent Custodian would exercise in the circumstances; and

d) A sale and repurchase agreement shall not relieve the custodian from liability to a Buyer for losses arising out of the failure of a custodian to exercise the standard of care and due diligence.

Section XIII of the Repo Guidelines further outlines other key aspects such as the valuation methods to be used and the repayment process of margin calls (loans). For instance, margin calls shall be paid in cash or other collateral securities. Non-cash collateral should be of equal or greater value than the current collateral securities being used. Additionally, unless the parties to the trade otherwise agree, all margin obligations shall be settled no later than 5 days after the transaction date.

In next week's article, the TTSEC will conclude its discussion on the Repo Guidelines while providing some statistics on the current size of the local repo market. For more information on the local securities industry, visit us at www.ttsec.org.tt or www.investucatett.com or follow us on Facebook; Twitter; Instagram and YouTube.

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