

New Global Note Structure

for international bearer debt securities
issued through the ICSDs

General article

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Next summer will see the introduction of a new legal and holding structure for international debt securities. This new structure will be mandatory for a newly issued international debt security to be recognised as eligible collateral for Eurosystem monetary policy and intra-day credit operations. Following a recommendation by the Eurosystem concerning the custody structure of international debt securities, the ICSDs have worked with market participants to create a new structure for the issuance, processing and safekeeping of international bearer debt securities issued using a New Global Note (NGN) form for launch in June 2006.

To ensure that the market is properly informed of the new structure and market feedback on relevant matters is received, a dedicated Market Advisory Group (the MAG) has been set up. This group comprises members and observers from a broad cross-section of entities active in Europe's capital markets including issuers, lead managers, paying agents, the International Capital Market Association (ICMA) and the ICSDs¹. Representatives from the European Central Bank (ECB), the Belgian and Luxembourg national central banks and the European Investment Bank attend as observers.

¹ MAG members include: Citigroup (Chairman: George Faux), Euroclear Bank, Clearstream Banking Luxembourg, General Electric, JPMorgan Chase, Deutsche Bank, HSBC, The Bank of New York, BNP Paribas, ICMA, Morgan Stanley and Credit Suisse First Boston.

Key features of the New Global Note structure

As of June 2006:

- New international debt securities in global bearer form can be issued using a new form of global certificate, known as the New Global Note (NGN);
- Under the terms of the NGN, the nominal amount is determined based on the ICSDs' records;
- Issuers provide a signed issuer-ICSD agreement requesting acceptance of the securities with the ICSDs;
- The securities will be serviced by two new types of service provider, the Common Service Provider (CSP) and the Common Safekeeper (CSK), both appointed by the ICSDs; and
- NGNs that are potentially eligible as collateral for Eurosystem monetary policy or intra-day credit operations will need to be deposited, immobilised and safekept with an ICSD.

Eurosystem eligible collateral

Based on information provided by the ECB, the Eurosystem collateral-eligibility criteria currently require that, among other things, a security must:

- be a euro-denominated debt issued by an EEA , G10 or supranational issuer;
- meet high credit standards;
- be listed or quoted on a regulated market or an ECB approved non regulated market;
- be settled in the Eurozone; and
- be held with a Securities Settlement System (SSS) complying with further Eurosystem criteria.

In the future, the Eurosystem will consider two additional criteria, i.e.:

- the international bearer debt security will have to be issued under the NGN form; and
- the NGN will have to be kept in safe custody with one of the ICSDs acting as CSK.

International debt securities issued in classical global note form prior to 30 June 2006 will continue to be potentially eligible as collateral for Eurosystem monetary policy and intra-day credit operations during their lifetime, while international debt securities issued after this date in classical global note form will no longer be considered eligible.

Standard Market Protocol

The process of designing this new structure presented the opportunity for the ICSDs and the International Capital Market Services Association (ICMSA) to review the operational flows underlying the servicing of international debt securities. The outcome of this review will be incorporated in a Standard Market Protocol document to be promulgated by the ICMSA and the ICMA. The objective is to establish best market practice guidelines for securities issued in CGN and NGN form. Issuers, their agents and all market professionals involved in the servicing of these securities will be expected to adhere to these best practice guidelines.

Market-driven future

How will this new structure impact the market? First and foremost, the adoption of the New Global Note as a permanent fixture will be heavily reliant on the uptake and endorsement that it receives from the market. The existing structure, known as the classical or common global note and which is serviced by Common Depositories, will co-exist with the NGN structure.

International debt securities issued through an ICSD in classical global note form prior to 30 June 2006 will continue to be eligible as collateral for Eurosystem monetary policy operations during their lifetime, while international debt issued after this date in classical global note form will be ineligible. It is the responsibility of issuers to ensure compliance with the new collateral-eligibility requirements.

After June 2006, international debt issues not expected to meet the Eurosystem collateral eligibility criteria can also be issued under the NGN structure. In this case, these issues will be safekept by commercial banks (rather than an ICSD) acting as Common Safekeeper.

Issuers wishing to benefit from the new structure will need to update their legal documentation to allow for this new form of issuance. Some operational processes linked to the issuance of new securities and reconciliation flows, as carried out by lead managers and issuing and paying agents, will also need to be adapted.

To facilitate the transition, both ICSDs and the MAG representatives are currently preparing a market roll-out strategy, with the support of the law firm, Allen & Overy LLP. The objective of this roll-out will be, in a first stage, to advise all relevant market intermediaries of the forthcoming change, and in a second stage, to provide all of the pertinent information, especially the appropriate legal documentation. This roll-out will be supported through legal roundtables, brochures, FAQ and website information, with the support of the ICMSA and ICMA.

Managing the changing capital market

We find ourselves in a dynamic, fast-paced and internationally competitive environment. European securities markets have undergone tremendous change in the last decade. The introduction of the euro, increasing levels of globalisation and greater cross-border integration of our financial markets have increased demands on our market infrastructure service providers to continue to craft solutions that meet ever-changing funding and investment needs.

The international securities industry has been a brilliant example of flexibility and efficiency for the past 30 - 40 years. Since the first Eurobond was issued in the 1960s, this market has grown and evolved to become an important part of global funding and investment strategies. These securities are also increasingly in demand for use as collateral.

The implementation of the New Global Note structure will not change any of the current market fundamentals. International debt issuers of bearer securities will continue to enjoy the same flexibility and freedom with respect to how issues are brought to the market. They will maintain full flexibility to issue under the current or new structure, depending on the target investor base. The important new consideration issuers will face is whether or not to structure the security to satisfy the requirements of the Eurosystem.

June 2006 is just around the corner. All market participants who have played a role in constructing the new structure have expended considerable time, effort, and resources to ensure that the NGN will be a viable and flexible option for issuers and investors. In the coming months they will continue to focus on the critical steps and information provision that will be needed for a smooth and seamless launch of the structure, which is poised to become a market standard for the future.

