

Briefing note

29/01/2015

Securities Financing Transaction Regulation (SFTR) – European Parliament Draft Report

Securities financing transactions (SFTs) serve a critical role enabling effective collateral flow in the financial system and facilitating funding of market participants and central banks. Whilst AFME supports the objectives of the SFTR, it is of vital importance that the SFTR strikes the right balance between increasing transparency and preserving the important function of the SFTs.

The requirements should be appropriate for re-use & rehypothecation (Articles 3 & 15)

As the FSB published, re-use and rehypothecation are different. The FSB defines “re-use” as any use of securities delivered in one transaction in order to collateralise another transaction and “rehypothecation” as re-use of client assets (i.e. assets to which the collateral provider retains proprietary rights). The FSB further recommended transparency in relation to rehypothecation. To ensure international consistency, the EU framework needs to be aligned with the FSB definitions.

AFME believes that it is inappropriate for the requirements under Article 15 to apply to a title transfer financial collateral arrangement (TTCA). Under a TTCA, full legal ownership is transferred to the collateral receiver - the collateral provider has no remaining proprietary rights to the collateral. The collateral receiver then treats this collateral the same as it would other assets it has full legal ownership of, which it may receive under other title transfer arrangements (such as an outright purchase). Therefore, introducing a right to reuse and an exercise of that right under limited circumstances (such as the provision of consent) creates legal issues by undermining legal ownership rights and would also adversely impact collateral flow in the financial system by restricting the ability of firms to use collateral they own. In contrast, rehypothecation involves a security interest over client assets and a separate contractual arrangement to exercise a right of reuse to take full ownership of the collateral (consistent with the FSB’s definition of rehypothecation).

Therefore, Article 15 should be limited to rehypothecation as proposed by the FSB. Alternatively, TTCA arrangements could be expressly excluded from Article 15; however, full alignment with the global approach is our preferred solution.

We support the Rapporteur’s amendment 59 on Article 15(2)(b) as it clarifies that collateral is transferred from the account of the providing counterparty to a separate account, thereby ensuring that the collateral provider no longer owns the asset.

The haircuts regime should not be introduced under the SFTR (Article 15, paragraphs 3 a-f)

A key item in the draft Rapporteur report is the proposal for the immediate introduction into EU law of the requirement of minimum haircuts for collateral used in SFTs, with specific details deferred to Level 2 to be prepared in accordance with international standards.

AFME supports the implementation of FSB’s regulatory framework for haircuts on non-centrally cleared SFTs published in October 2014. However, we believe that the SFTR proposal is not an appropriate legislative vehicle for the introduction of the framework for the following reasons:

- Haircuts were not part of the Commission’s proposal and, as such, have not undergone a detailed impact assessment – this analysis is essential to consider the specificities of European markets;
- Haircuts regulation is of great significance to the SFT markets – this calls for a full Level 1 debate and policy steer by the European legislators;
- AFME believes that the prudential CRR/CRD framework would be a more appropriate channel for the implementation of requirements in relation to transactions between banks and non-banks as haircuts need to operate in conjunction with the prudential capital regime (Basel has been asked by the FSB to determine the interaction with the prudential regime);
- The introduction of haircuts regulation would delay the implementation of transparency requirements identified as an immediate priority by the FSB and the ECB.
- The FSB haircuts requirements are still under consultation and are yet to be finalised in full; as such there will need to be a global harmonised framework.

The reporting requirements should permit position level reporting (Article 4)

Under the global data reporting templates for SFTs workstream, the FSB has proposed templates for three types of SFTs: repo, securities lending and margin lending. Notably, the templates permit regulators to collect transaction level or position level information. AFME recommends that for securities lending and margin lending position level reporting is most appropriate. Margin lending is typically a prime brokerage activity, which is undertaken at portfolio level; accordingly, unless the reporting is at position level, the data collected will be meaningless. Since Article 4 uses the term “transaction”, this may restrict the ability of ESMA to implement a meaningful reporting regime; therefore, AFME recommends the text be clarified to require counterparties to SFTs to report details of transactions or positions.

Implementation timelines (Article 28)

Policymakers should consider any lessons from the experience with EMIR in designing the timelines for implementation of the SFTR, including options for a phased implementation. Sufficient time should be allowed for the development of reporting capabilities by market participants and for the implementation of requirements following the finalisation of Level 2 measures. We believe that a minimum of 12 months from publication of the regulatory technical standards would be appropriate in order to achieve a full implementation of the framework.

The definition of SFTs should be clear and aligned with the FSB’s global framework (Article 3)

The FSB has proposed SFTs for the global reporting framework to be defined as repos (including buy-sell back or sell-buy back transactions), securities lending and margin lending. AFME strongly recommends that the SFTR contain a clear, unambiguous and objective definition of SFTs so that reporting can be operationalised. Further, the term “economically equivalent transactions” proposed by the Commission introduces a subjective criterion, which would lead to inconsistencies in reporting. As such, we support the Rapporteur draft Amendment 30.

ESMA should have the flexibility to determine who should report and how data should be managed to avoid duplication (Article 4)

For the global objectives of increased information on SFTs to be achieved, good data quality is essential. The FSB has recognised the issue of duplicate reporting under the global data template workstream. AFME recommends that in order to achieve good data quality there must be clear reporting protocols at Level 2 and lessons need to be learned from previous regulations, such as EMIR. Article 4 of SFTR requires two-sided reporting (i.e. all counterparties need to report); we strongly recommend that ESMA be given the mandate at Level 2 to devise the best solution for avoiding poor quality data, such as whether there should only be one-sided reporting.

Further information

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