

THE SECURITIES FINANCING TRANSACTIONS (SFT)

Regulation (EU) 2015/2365 of the European Parliament and the Council on the **transparency of securities financing transactions (SFTs) and of reuse**

1. Presentation



The 2008 global financial crisis revealed significant holes in the regulation of the financial system. It also highlighted the need to improve transparency and monitoring not only in the traditional banking sector, but also in the sectors where non-banking credit activities take place, which is known as the “parallel banking system” and named **SHADOW BANKING**.

In order to closely follow the market trends concerning entities whose activities can be considered as pertaining to the parallel banking system, in particular in the area of securities financing transactions, the Commission feels it is necessary to implement transparency obligations.

The proposed regulation concerning the structural reforms of the banking sector of the EU which accompanies this proposal is the last piece of the new regulatory framework, which guarantees that even the biggest banks within the EU will become less complex and able to be the subject of an effective resolution with minimal consequences for taxpayers.

According to the EC, an obligation for reporting via trade repositories could remedy the problems found.

The securities financing transactions in the parallel banking system would thus be subject to appropriate surveillance and regulation. Their use would not be prohibited or limited by specific restrictions as such, but would benefit from increased transparency.

The securities financing transactions targeted by this regulation are transactions of the parallel banking sector which principally comprise:

- The repurchase agreement or repo;
- Securities lending;
- The buy-sell back and sell-buy back transactions;
- And the margin lending transactions.

For UCIs: The periodic reports that the undertakings for collective investment in transferable securities (UCITS) management companies or UCITS investment companies and alternative investment fund managers must currently produce (beyond the AIFM and UCITS V directives) would thus be completed by this additional information on the use of securities financing transactions and other equivalent financing structures.

One of the major key points of this proposed regulation was the introduction of governance of re-hypothecation by fixing minimum conditions to be respected during transactions by the parties concerned, such as the existence of a prior written agreement signed by the counterparties, total respect for the conditions of this agreement, full information on the potential risks in the event of default of a counterparty, and the prior transfer of the collateral to the account of the counterparty.

In the last version of the draft Regulation, the Italian Presidency of the EU had decided to replace **RE-HYPOTHECATION** by **RE-USE**. But the definition of re-use and SFT, which go beyond securities lending operations and/or repos, remains vague and unclear. Moreover the collateral term is not defined in the relevant regulation.

2. Chronology of events



- ✓ **29 January 2014** – The European Commission published its banking reform aiming to impose new rules to prevent the biggest and most complex banks, **TBTF (Too big to fail)** from practising trading on their own account, a risky market activity implying a structural reform of the European banking sector and measures aiming to increase transparency of certain transactions in the parallel banking sector.

Alongside this reform, the European Commission imposes the transparency of certain transactions in the parallel banking sector (and notably **securities lending/borrowing transactions** because they pertain to SHADOW BANKING).

- ✓ **23 March 2015:** Vote in ECON Commission.
- ✓ **27 April 2015:** Vote in plenary session at the European Parliament.

- ✓ **17 June 2015:** Political agreement on the final compromise during the trilogue as of 17 June 2015.
- ✓ **26 June 2015:** UE Council publishes the entire final compromise.
- ✓ **29 October 2015:** The European Parliament adopts the European Commission.
- ✓ **16 November 2015:** Council vote.
- ✓ **23 December 2015:** Publication in the EU Official Journal.
- ✓ **12 January 2016:** Entry into force of the regulation **even if most of the provisions** will be applicable after a certain period.
- ✓ **11 March 2016:** ESMA publishes a **consultation paper** (187 pages) on the SFT regulation. Answers were expected for 22 April 2016. It concerns exclusively data regarding reporting. There is nothing with regard to art. 15 (Reuse of collateral).
- ✓ **31 March 2017:** ESMA published its final report regarding RTS as well as some changes for EMIR.
- ✓ **October 2017:** ESMA published an excel spreadsheet with a set of rules to be applied by the Trade Repositories. It follows the EMIR validation rules.
- ✓ **On 22 March 2019,** final transparency rules of reporting requirements were published in the Official Journal of the EU. The reporting obligation of securities financing transactions (SFTs) to trade repositories (TR), except the ones concluded with a central bank are now effective.
- ✓ ESMA published its final guidelines on **6 January 2020** with the expected information on reporting rules, notification to Trade Repositories and a statement on Legal Entity Identifiers (LEI).
- ✓ ESMA approved 4 trade repositories with effect from **7 May 2020: DTCC, UnaVista TRADEcho, Krajowy Depozyt Papierów Wartościowych and REGIS-TR**. Last reporting timeline has been implemented for NFCs. A one year **remediation plan until Jan 2022** is necessary to close any technical breach.
- ✓ On **29 March 2021**, ESMA published Guidelines on Reporting under Articles 4 and 12 SFTR in order to clarify a number of provisions of SFTR and to provide practical guidance on the implementation of some of those provisions.

The three main measures of this Regulation

- ✓ Obligations regarding re-use of assets (art.15): They have been less stringent and will depend on the outcome of the working group dedicated to re-use and led by the FSB. Collateral & master agreements must reflect new provisions contained in the regulation (**client consent granted for transferring or no entitlement**). Provisions came into force on **13 July 2016**.
- ✓ Information to investors (art.14): Current UCIs have 18 months (**13 July 2017**) to update pre-contractual documents like the prospectus. However for **art.13** (annual & half-yearly financial reports) it was **13 January 2017**. UCIs **closing before the date of 13 January 2017** had to include new information listed in **Annex section A of the regulation**.
- ✓ Compulsory notification of SFT (art.4): Delegated and implementing regulations entered into force on 11 April 2019 and **SFTR reporting requirements apply as follows**:
11 April 2020 new 11 July 2020 for banks and investment firms, **11 July 2020** for CCPs & CSDs; **11 October 2020** for other financial counterparties which include AIFs and UCITS, Pension Funds and Insurance/Reinsurance Companies; **11 January 2021** for Non-Financial Counterparties.

3. Reference text(s) and date of entry into force

Text has been published in the Official Journal of the EU on 23 December 2015.

Link: <http://eur-lex.europa.eu/legal-content/FR-EN/TXT/?uri=CELEX:32015R2365&from=en>



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