The Securities Financing Transaction Regulation (SFTR)

Transaction Reporting Requirement - What You Need to Consider

Background - What is the SFTR?

As part of the policies identified by the Financial Stability Board (FSB) to increase transparency across Securities Financing Transactions (SFTs), the EU introduced the Securities Financing Transaction Regulation (SFTR). The regulation includes a number of new rules for market participants including a requirement to report all SFTs to an approved Trade Repository (TR).

EU Regulation 2015/2365 (SFTR)
entered into effect on January 12th, 2016

Key Reporting Requirements - Article 4

- Counterparties have to report details of the 'conclusion, modification and termination' of any SFT to an approved TR on a T+1 basis

- In addition to the reporting of the SFTs, counterparties also have to report the associated collateral to the TR on either T+1 or value date + 1 dependent on the method of collateralisation used

- Counterparties also need to keep records of any SFT for a minimum of five years following its termination

- Phased reporting requirements are expected to begin between the months of August to October 2018

SFTs in Scope

- Securities loans and borrows

- Repurchase transactions (including Buy/Sell backs)

- Commodities loans and borrows

- Prime brokerage margin lending transactions

Who does it cover?

- Both Financial Counterparties (FCs) and Non-Financial Counterparties (NFCs)*

- EU based entities including their Non-EU based branches

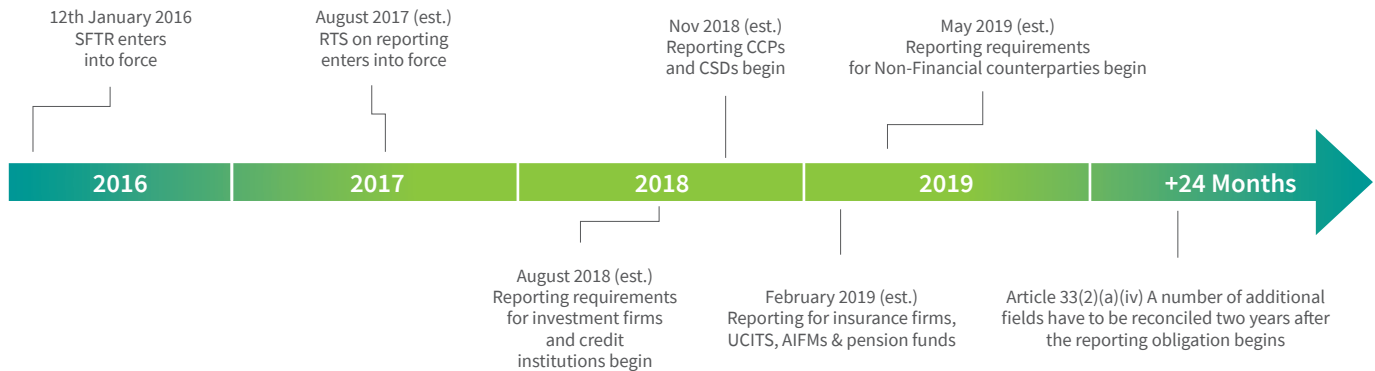- Non-EU entities where the SFT is concluded by an EU based branch

*Some FCs trading with smaller NFCs will have a delegated reporting obligation on behalf of the NFC

Detailed Reporting Requirements

- The SFTR reporting will be on a T+1 basis in line with existing regulatory reporting regimes

- The SFTR is a two-sided reporting requirement, with both collateral provider and collateral taker required to report their side of the SFT to an approved TR

- As part of the two-sided reporting obligation a Unique Transaction Identifier (UTI) must be included by participants in their reports to the TRs. This value will be used by the TRs to match separately received reports from each counterpart to an SFT

- Participants must also use Legal Entity Identifiers (LEIs) to identify their counterparts along with a number of other parties involved in the SFT (e.g. Agent Lenders, CSDs, CCPs)

- For agency loans with multiple underlying principals both borrower and lender will need to report each allocation to a principal as an individually reportable transaction

- The SFTR reporting must also include any collateral linked to the SFTs including the LEI of the counterparty with who the collateral was exchanged and the master agreement under which it was agreed

- Collateral re-use has to be reported daily at S+1 by the reporting entity and not the counterpart

- Margin lending remains in scope but only applies to prime brokerage. The short market value and corresponding margin loan have to be reported using the same UTI

Phased Reporting Timeline

ESMA published the Final RTS Report on March 31st 2017. The standards need to be approved by the European Commission and European Parliament respectively before a process of translation and publication into the Official Journal. This process can take four to six months so the standards are expected to enter into force between August to October 2017 with reporting go live twelve months later and phased requirements continuing until Q2 2019.

12th January 2016
SFTR enters into force

August 2017 (est.)
RTS on reporting enters into force

Nov 2018 (est.)
Reporting CCPs and CSDs begin

May 2019 (est.)
Reporting requirements for Non-Financial counterparties begin

2016	2017	2018	2019	+24 Months

August 2018 (est.)
Reporting requirements for investment firms and credit institutions begin

February 2019 (est.)
Reporting for insurance firms, UCITS, AIFMs & pension funds

Article 33(2)(a)(iv) A number of additional fields have to be reconciled two years after the reporting obligation begins

Reporting Challenges & Impact

The proposed reporting requirements will pose differing challenges to all market participants. We've summarised some of the key issues below so that participants can begin to assess the potential impact to their firm:

Requirement	Challenge
Details of SFTs to be reported on T+1, related collateral to be reported between T+1 and S+1	Some key details will not be available to both counterparts on T+1 in current processes, for example the information on principals to a trade on an agency loan
Matching UTIs need to be included on all SFTs by both counterparts	Trades booked directly in client systems will not automatically be assigned a UTI. Additionally at point of trade, agency loans are usually agreed at the bulked level, with the principal information required to correctly generate UTIs only reported via the Agency Lending Disclosure (ALD) process post-settlement date
Counterparts need to be identified by LEI	Many market participants are currently using internal codes to identify counterparts and do not have LEIs in their primary books and records systems
ALD trades have to be reported at a principal level (e.g. one report per beneficial owner)	ALD information only becomes available to the borrowing party later in the process (often S+1 or later), in addition, non-disclosure requirements mean that information on the underlying principals in an ALD trade can only be seen by a limited number of authorised people within the firm (e.g. Credit and Risk)
Reporting of collateral related to SFTs	Most SFTs are covered by collateral pools with multiple ISINs exchanged to cover multiple SFTs. For agency trades a single collateral pool will often be used for multiple underlying principals and each ISIN delivered in the pool would be allocated to each principal on a pro-rate basis. The information on this principal allocation is only made available to the borrower via the ALD process post collateralisation date
Reporting templates require comprehensive transaction details	Some of the data points included in the current reporting framework are either held in down-stream systems or outside of systems entirely. This may require firms to upgrade existing systems and infrastructure to fulfil the reporting requirement

Requirement	Challenge
Significant number of matching fields with strict tolerances	A high number of matching fields (90+) combined with strict tolerances is likely to result in low matching rates post reporting. ESMA have provided a window of 24 months post implementation date to reconcile certain fields but the list is still extensive and remains a significant challenge
An execution timestamp has to be reported with each individual trade	There is currently no infrastructure in the securities finance industry to agree a timestamp unless the security is traded on a platform. Even if this is the case, only the omnibus delivery itself would have one. The majority of transactions or lifecycle events (trade reallocations, corporate actions) are not executed on a trading venue so an industry agreed protocol for creating a timestamp will have to be agreed

How does SFTR affect you?

Counterparty Type	Impact
Beneficial Owner	Beneficial Owners who participate in an agency securities lending programme will have a reporting requirement under the SFTR. Where their lending programme is managed by an Agent Lender they may receive delegated reporting however the responsibility to ensure this is completed remains with the Beneficial Owner. In addition there may be transactions, for example repos conducted directly by the funds, that will need to be reported directly by the beneficial owner
Agent Lender	Agency lending structures typically involve lending multiple beneficial owners assets in a single transaction, however the reporting requirement will be at the lower, principal level. As borrowers will need this level of information to fulfil their side of the re- porting requirement an increased emphasis will be placed on the accuracy and timeliness of the ALD data received from Agent Lenders
Borrower	Borrowers will have to link agency trades to underlying principal level information received via the ALD process, however this may be technically difficult due to the timing and nature of the current ALD process and functionally difficult due to the non-disclosed nature of the information
Prime Brokers	Primer brokers will have to report details of their margin lending to hedge fund clients, including details of the portfolio of assets used as collateral (e.g. short sale proceeds) as well as the portfolio leverage ratio
Hedge Funds	Hedge funds that are in scope of the SFTR would also have to report their side of the margin loans received from their Prime Broker(s)

Reporting Requirement by Counterparty Location

		Counterparty B			
Parent	**Parent**	**EU**	**EU**	**Non-EU**	**Non-EU**
Parent	Branch		Non-EU	EU	
EU		Both	Both	Both	Counterparty A
EU	Non-EU	Both	Both	Both	Counterparty A
Non-EU	EU	Both	Both	Both	Counterparty A
Non-EU		Counterparty B	Counterparty B	Counterparty B	Neither

Counterparty A

IHS Markit™

The 'one-stop' solution for SFTR

Data Exchange

Clients can leverage their existing connections to two of the market's leading solutions providers to deliver data which cuts down much of the initial operational burden.

The solution will be fully interoperable which will give it the flexibility to accept data from the many front and back end systems currently employed by the industry.

Pirum and IHS Markit have existing connections to BNY Mellon, Clearstream, Euroclear and JPMorgan Tri-party agents and already receives collateral data on behalf of clients. This collateral data can be used in conjunction with existing client feeds to create the complete SFTR report.

Data Warehouse

Raw and unstructured trade and collateral data will be cleansed, enriched and standardized to ESMA's schema prior to entering the data warehouse. This will ensure the data is of a high quality for the subsequent matching process.

The entire cleansing and warehousing process occurs within the solution which ensures clients have full oversight of the complete process for both current and historical trades.

IHS Markit already handles LEI enrichment as part of its EMIR reporting solutions.

Reconciliation

Trade matching and reconciliation will be handled by Pirum, the industry leader in reconciliation which already achieves a 98% matching rate of the $1.7t trades it processes daily.

Generating UTIs from positions matched in Pirum will ensure SFTs submitted to the TRs will have a higher matching rate once reconciled in the TR process, reducing the amount of incorrect reports that counterparts need to review.
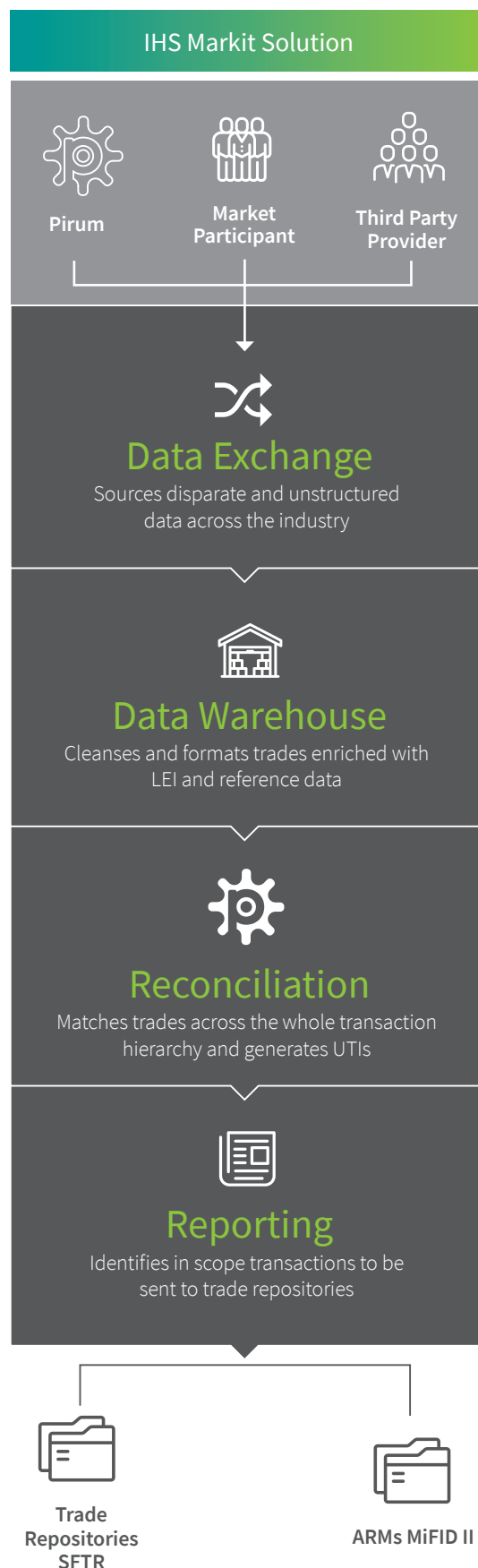
UTIs generated as part of the matching process will be disseminated to both trade counterparts across full trade stacks for entire lifecycles.

Reporting

The solution automates the reporting process by first determining in scope transactions and then giving users the ability to deliver processed trades directly to TRs saving the need to develop individual reporting workflows.

Third party users, such as beneficial owners, will be able to access the solution to monitor reporting activity and the matching rates achieved at the TRs.

Clients can leverage the solution for MiFID mandated trade reporting for trades that fall outside the scope of SFTR but still have to be reported to Approved Reporting Mechanisms (ARMs).

IHS Markit Solution

Pirum | **Market Participant** | **Third Party Provider**

Data Exchange
Sources disparate and unstructured data across the industry

Data Warehouse
Cleanses and formats trades enriched with LEI and reference data

Reconciliation
Matches trades across the whole transaction hierarchy and generates UTIs

Reporting
Identifies in scope transactions to be sent to trade repositories

Trade Repositories SFTR | **ARMs MiFID II**

About IHS Markit (www.ihsmarkit.com)

IHS Markit (Nasdaq: INFO) is a world leader in critical information, analytics and solutions for the major industries and markets that drive economies worldwide. The company delivers next-generation information, analytics and solutions to customers in business, finance and government, improving their operational efficiency and providing deep insights that lead to well-informed, confident decisions. IHS Markit has more than 50,000 key business and government customers, including 85 percent of the Fortune Global 500 and the world's leading financial institutions. Head-quartered in London, IHS Markit is committed to sustainable, profitable growth.

About Pirum Systems (www.pirum.com)

Pirum provides a secure, centralised connectivity and automation hub which seamlessly connects market participants, allowing them to electronically verify key transaction details and fully automate the post-trade lifecycle.

In addition to this processing hub, Pirum's platform provides onward connections to other key infrastructure service providers. This position, at the heart of the Securities Financing market, allows clients to reuse their connection to Pirum to access triparty agents, trading venues, market data companies & CCPs with additional connectivity constantly being added. Financial Institutions from around the world have responded to Pirum's creative approach by joining this secure on-line community, allowing them to increase processing efficiency, reduce operational risk and improve profitability by using Pirum's services to reduce manual processing.

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A new standard for interoperability