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Securities Financing Transactions Regulation (SFTR)

Providing a full end to end regulatory reporting solution for SFTs

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 Transactions 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 from start Q1 2020.

SFTs in Scope

- Repo/ Reverse Repo and Buy/Sell back

- Securities loans and borrows

- Commodities loans and borrows

- Prime brokerage margin lending transactions
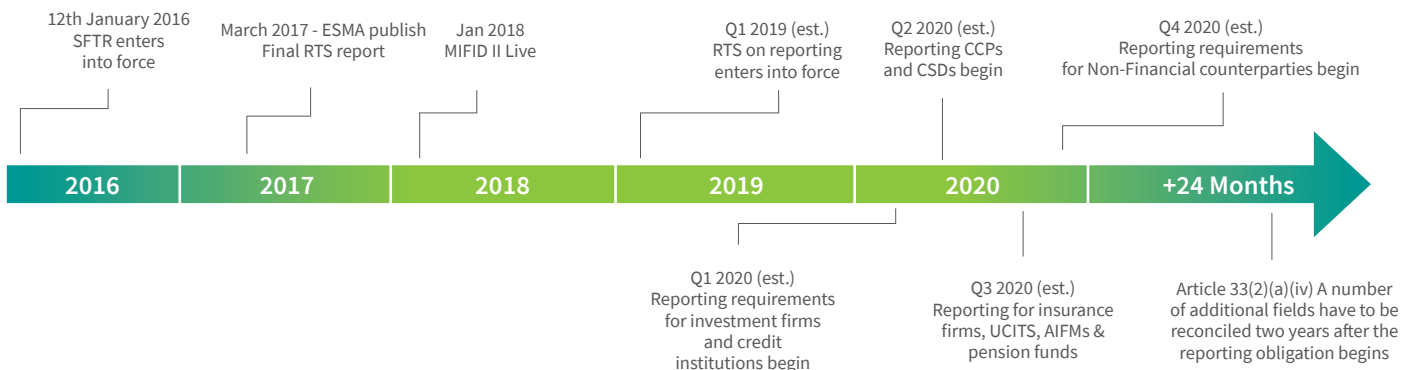
- Collateral Re-use

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

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 Q1 2019 with reporting to go live Q1 2020 and phased requirements continuing until end 2020.

How does SFTR affect you?

Counterparty Type	Impact
Buy Side	Beneficial Owners established in the European Union who participate in lending, buy sell backs or Repo will have a reporting obligation under SFTR. Where their lending programme is managed by an Agent Lender they may delegate the reporting to the Agent (see Article 4.2), however the responsibility to ensure this is completed remains with 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 reporting requirement an increased emphasis will be placed on the accuracy and timeliness of the ALD data received from Agent Lenders
Repo Dealer / Equities 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 because of the non-disclosed nature of the information. Any repo and buy / sell back trades executed by EU market participants will also fall into scope
Prime Brokers	Prime 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

Reporting Requirement by Counterparty Location

		Counterparty B			
	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 (row label, left side)

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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 or collateral details for Repo on S+1
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
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

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A full end to end regulatory reporting solution for SFTs

Data Exchange

Clients will be able to connect to the solution, leveraging multiple existing data pipes, therefore reducing the implementation burden:

- Fully interoperable solution accepting data from front & back-end systems
- Leverage existing IHS and Pirum connectivity to tri-party agents, platforms and CCPs
- Overnight batch combined with intraday feeds
- Multiple secured data exchange mechanisms
- Inter vendor communication protocol allowing for easy connectivity

Data Warehouse

The IHS Markit managed data warehouse will sit at the heart of the solution. This module will collate the multitude of industry data sources and provide the standardized golden copy of all the industry's trading and collateral activity, regardless of source:

- Referential data enrichment & static data management
- Connected to public GLEIF LEI database
- 7+ year full audit trail (on screen and reports)
- UTI lifecycle and exception management
- All SFTR processing data is persisted in the warehouse

Reconciliation

Pirum brings its deep expertise in post trade reconciliation with a matching engine that will generate the UTIs mandated by SFTR. The solution will also offer a fully transparent pre-reporting reconciliation tool that allows industry participants to monitor the reconciliation status of their trades, before reporting them:

- Industry leading reconciliation provided by Pirum (98% matching rate of the $1.7t trades it currently processes daily)
- UTIs generated as part of the matching process
- Exception based management

Reporting

Two-way modular transaction reporting connectivity that will automatically deliver in scope transactions to client's chosen trade repository or ARM (MiFID II):

- Event creation: a rule based regulatory reporting engine for SFTs
  - Automatic determination of in-scope SFTs
  - Application of SFTR and MiFID II rules
  - Generate ready to be reported dataset in ISO 20022 format
- TR connect: connectivity with TRs and MIFID ARMs:
  - Full audit trail of file communication
  - Flexible affirmation logic
  - Connected to all approved TRs and ARMs for SFTs
  - Retrieval of daily TR/ARMs reports from IHS Markit SFTR solution

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**

IHS Markit SFTR Highlights

SFTR data is ring-fenced: Contractually and physically (separate bespoke technology and staffing)

All SFTs covered: Securities lending, repo, sell/ buybacks, margin lending, commodities finance

Full end to end solution: A complete solution for SFT reporting: enrichment (Equity and FI), reconciliation, eligibility checking, reporting (including delegated), exception management, TR daily reports, file status and historical data retention

Modular construction: Allowing the solution to fit each client's unique business model

Fixed cost: Fixed yearly cost allowing for accurate costing/budgeting

Dedicated onboarding team: Each client benefits from a dedicated onboarding contact allowing seamless integration and implementation

Combined SFTR and MiFID solution for SFTs: One single solution to cover both regulatory regimes for SFTs. Can also support Solvency II reporting

Delegated reporting: Supports "on behalf of" reporting using flexible affirmation models

Unique data enrichment capabilities: LEIs (synchronised connection to GLEIF), timestamps, asset type, security quality, jurisdiction and LEI of issuer, CFI code and market value (pricing EQ and FI)

Real time processing: Real time data feeds, processing (amendments), enrichment and matching

7 year+ audit trail: Ability to audit data via immediate on-screen reports or via bespoke reporting

Single contract: One contract covers the entire solution

Next Steps

We would advise firms to consider the regulation in depth, specifically the reporting requirements, and begin preparing for the implementation date.

To find out more about our SFTR project please contact us directly at:

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