

Transparency of securities financing transactions and of reuse

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In accordance with Regulation (EU) 2015/2365 on the transparency of securities financing transactions and of reuse (SFTR), the Commission presented a report on the progress in international efforts to mitigate the risks associated with SFTs.

Regulation (EU) 2015/2365 aims to get a better understanding of the effects of shadow banking (non-bank credit intermediation) and to address the risks posed by securities financing transactions (SFTs).

SFT markets play an essential role in today's financial system by supporting market participants in their secured funding and collateralisation needs. Repos are particularly important for the functioning of interbank markets, offering an alternative to unsecured interbank lending and time deposit, to cover reserve requirements and manage liquidity needs.

By facilitating credit growth, SFTs create leverage beyond the banking system with its prudential regulation.

The specific contribution of SFTs to the build-up of leverage is difficult to assess due to a lack of granular data (e.g. the volume of margin lending transactions, data on the reinvestment and reuse of collateral) and the potentially different purposes for which SFTs are undertaken.

Recommendations of the Financial Stability Board (FSB): in August 2013 and November 2015, the FSB published reports that set out recommendations for addressing financial stability risks in relation to SFTs. These recommendations broadly aim at:

- enhancing the transparency of securities financing markets via frequent and granular regulatory reporting and disclosure;
- introducing regulatory standards for cash collateral reinvestment;
- introducing principles for the re-hypothecation of client assets;
- introducing regulatory standards for collateral valuation / management; and
- introducing qualitative standards for methodologies to calculate collateral haircuts and implementing a framework for numerical haircut floors.

The report concluded that to a large extent, **the FSB recommendations on SFTs have been addressed in the EU** through the adoption of SFTR and specific provisions in sectoral financial services legislation and guidelines. As such, there **does not seem to be a need for further regulatory action at this stage**.

Collateral haircuts: the FSB framework on haircuts recommends a two-prong approach:

- **qualitative standards for methodologies used by market participants to calculate collateral haircuts.** The minimum standards for the methodology used to calculate haircuts complement the existing entity-based regulation of leverage (for credit institutions and investment firms) and specifically address pro-cyclicality. There are currently no such standards applying to all market participants in the EU. However, ESMA's Guidelines on ETFs and other UCITS issues contain such standards for UCITS;
- **numerical haircut floors** seek to address the build-up of system-wide leverage outside the banking system. The scope of the numerical haircut floor recommendation is narrower (i.e. non-centrally

cleared SFTs, in which financing against collateral other than government debt securities is provided to non-banks) than the one of the recommendation on the methodology to calculate haircuts. Currently, **there are no regulatory requirements at EU level as regards numerical haircut floors** for the bank / non-bank to non-bank SFTs in the scope of the FSB recommendation.

As regards the cross-sector qualitative standards for the calculation of haircuts and the introduction of numerical haircut floors, an assessment of the need for and the scope of a potential regulatory action in this field should be based on **comprehensive and detailed data** on SFT markets which will be available once the SFTR reporting obligation becomes effective.

Moreover, the current market dynamics reinforce the need for a **certain degree of caution** and robust evidence when reflecting on regulatory action implying quantitative requirements.

Progress at **international level is comparable to the EU** (i.e. in the early assessment phase) and no other region has taken a decision on regulatory action on haircut floors at this stage. If applicable, the introduction of numerical haircut floors should ideally happen in a globally coordinated manner to avoid compromising a level playing field or putting market participants in the 'first-moving' jurisdiction at a competitive disadvantage.

The Commission will continue to **thoroughly monitor** developments in SFT markets and the international regulatory space. The Commission will **reassess the added value of qualitative standards and haircut floors** on the basis of a report to be prepared by ESMA once comprehensive SFT data is available.