ECSDA
European Central Securities Depositories Association

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ECSDA Comments on the draft SFTR technical standards

This paper constitutes ECSDA's response to the Consultation Paper issued by the European Securities Markets Authority (ESMA) on 30 September 2016 containing draft technical standards under EU Regulation 2015/2365 on securities financing transactions (SFTR). Although some central securities depositories (CSDs) and especially international central securities depositories (ICSDs) offer triparty services for securities financing transactions (SFTs), the majority of ECSDA members do not provide services which fall under the scope of the SFTR.

ECSDA's response is thus very succinct and does not cover all dimensions of the role played by some CSDs as triparty agents in SFTs. It only covers questions 11, 19, 25 and 71 of the Consultation Paper.

1. CSD securities lending and borrowing services (Questions 11, 19 and 25)

Some CSDs provide securities lending services to help prevent settlement failures. This means that, under certain conditions, where securities are not available in the account of the delivering participant on the intended settlement date, a short-term securities loan is automatically triggered to enforce timely settlement. Because they reduce contagion risk associated with settlement fails, such services support market liquidity and settlement efficiency. They form part of the "settlement discipline" framework regulated by the CSDR (EU Regulation 909/2014) and composed of several measures aimed at preventing and addressing settlement fails.

When CSD participants subscribe to the securities lending and borrowing programme, potential fails are typically calculated in the previous overnight settlement process so that borrowings can be automatically generated. While the settlement status is reported to participants, they do not need to instruct or agree on the individual movements, which are generated automatically upon subscription to the programme. The vast majority of such securities lending movements are executed intraday and reimbursed within the day, with only a small proportion of them extending overnight on an open-ended basis.

CSD participants are typically admitted to the programme on the basis of a secured credit line. Under CSDR, any credit granted by CSDs is fully covered by collateral with minimal credit, liquidity and market risk.

ECSDA would like ESMA to consider securities loans triggered to prevent fails in CSDs to be reported under the SFTR. In case ESMA agrees a specific reporting approach for such specific activity, it could do so by including a reference to the CSDR in the SFTR technical standards. Indeed, CSD securities lending and borrowing services are explicitly included in the list of ancillary services which CSDs are allowed to perform, and any related credit risk is subject to specific risk mitigation as included in the CSDR. Under such specific reporting approach, specific issues should be taken into account in the Level 2 standards, as described in the responses to questions 11, 19 and 25 below.

Q11. Do you agree with the proposed report types and action types? Do you agree with the proposed combinations between action types and report types? What other aspects need to be considered?

When a securities loan is executed to cover a settlement failure, loan actions are mostly automatically handled. For example, there can be several automatic partial returns per day on the same transactions, as securities are received in the borrower's account. ESMA should clarify in the Level 2 standards whether reporting counterparties are expected to report each and every intraday change individually, or whether they are expected to report the combined end-of-day variation from the previous day.

Q19. Are the most relevant ways to conclude a securities lending transaction covered by the above scenarios? Are the assumptions correct?

When a securities loan is executed to cover a settlement failure, the CSD is acting either as agent lender and/or as guarantor and will typically not disclose the counterparties. Paragraph 155 (p. 54) of the Consultation paper allows the agent lender to only disclose the lender details on settlement date. ECSDA believes that it should be allowed for CSD-generated securities loans not to involve the disclose of lender details, i.e. it should be possible to report the agent lender or guarantor (i.e. the CSD) as counterparty for the entire life cycle of the transaction. This would also solve the problem of the borrower not knowing if the lender is exempt from SFTR (e.g. a central bank). The "borrower leg" would always be reported between the agent lender and the borrower, while the "lender leg" would only be reported if the lender is subject to reporting requirements under the SFTR. In other words, in scenario 3 described on page 55 of the Consultation paper, securities lending should be extended to an Agent Lender that is not principal to the transaction.

Q25. Are there any obstacles to daily position reporting by margin lending counterparties? Do prime brokers provide information to their clients about intraday margin loans?

When a securities loan is executed to cover a settlement failure, the loan is often closed on the same day. Such intraday loans, which may be free of charge for CSD participants, should be exempt from SFTR reporting requirements. Reporting may be required for securities loans lasting at least one day.

2. Settlement data to be reported in relation to SFTs (Question 71)

Q71. Do you agree with the proposed approach? Please elaborate.

Several respondents to the ESMA Discussion Paper of 11 March 2016, including ECSDA, highlighted specific challenges that would result from requiring SFT counterparties to populate the "place of settlement" and "CSD" fields in their reports under the SFTR requirements. We thus welcome ESMA's decision, explained in paragraphs 322 to 324 of the Consultation Paper (p. 116), not to include these fields in its draft regulatory technical standards (RTS) and implementing technical standards (ITS) on the details of the reports to be reported to trade repositories.

ESMA however decided to maintain "CSD participant or indirect participant" as a required field in the following reports:

- Field 16 (p. 261) in Table 1 on Counterparty data in the Annex of the draft ITS,
- Field 16 (p. 279) in Table 1 on Counterparty data in the Annex of the draft RTS,

We welcome ESMA's effort, in paragraph 324 of the Consultation Paper (p. 116), to answer the questions raised by ECSDA in its comments of 22 April. Nevertheless, we believe that the responses brought by ESMA have not been fully reflected in the drafting of the RTS and ITS. Indeed, the use of the phrase "CSD participant or indirect participant" in field 16 on pages 261 and 279 contradicts ESMA's statement that: "*this field is required in all cases, even if the SFT settles outside of the CSD*" (p. 117). Where settlement occurs at an intermediary in the absence of any CSD, how will counterparties be able to report a "direct" or "indirect" CSD participant? By reference to which CSD?

As suggested by a respondent to the March Discussion Paper quoted by ESMA in paragraph 321 of the Consultation Paper (p. 116), the term "settlement agent" would be more accurate as it would avoid any reference to a CSD. This term may however be too imprecise in scenarios involving several intermediaries.

As a consequence, ECSDA recommends that the field "CSD participant or indirect participant" be renamed "the intermediary acting on behalf of the reporting counterparty" in both the RTS and the ITS.

About ECSDA

The European Central Securities Depositories Association (ECSDA) represents 41 central securities depositories (CSDs) across 37 European countries. As regulated financial market infrastructures, CSDs play a vital role in supporting safe and efficient securities transactions, whether domestic cross-border. If you have any questions on this paper, please contact Ms Soraya Belghazi, Secretary General, at info@ecsda.eu or +32 2 230 99 01.