

## Securities Financing Transaction Regulation (SFTR) and its impact on Commodities Markets

The SFTR text is currently under review by the European Council and Parliament. It is expected to be approved on **27<sup>th</sup> October 2015** and come into force 6 months after this date. The below summary is limited to obligations arising from SFTR in connection with commodities transactions.

<b>Purpose</b>	<p>SFTR intends to provide transparency by requiring reporting of securities financing transactions ("SFT") undertaken in the shadow banking sector. It applies to repurchase agreements, securities lending/borrowing, <b>commodities lending/borrowing, buy/sell back and sell/buy back transaction</b>, as well as "reuse" of collateral.</p> <p>Article 3 (1) (5) states that "<i>securities or commodities lending</i>" and "<i>securities or commodities borrowing</i>" mean any transaction in which a counterparty transfers securities or commodities subject to a commitment that the borrower will return equivalent securities or commodities at some future date or when requested to do so by the transferor, that transaction being considered as securities or commodities lending for the counterparty transferring the securities or commodities and being considered as securities or commodities borrowing for the counterparty to which they are transferred;</p> <p>Reuse is defined under Article 3(1)(7) SFTR as:  <i>"use by a receiving counterparty, in its own name and on its own account or on the account of another counterparty, including any natural person, of financial instruments received under a collateral arrangement. Such use includes transfer of title or exercise of a right of use in accordance with Article 5 of Directive 2002/47/EC9 but does not include the liquidation of the financial instrument in the event of default of the providing counterparty."</i></p>
<b>Who does SFTR apply to? Article 2(1)</b>	<p>SFTR applies to:</p> <ul style="list-style-type: none"> <li>➤ Any EU counterparty; and</li> <li>➤ Third- country counterparty if SFT is concluded in the course of operations of an EU branch of that counterparty</li> </ul> <p><b>Please refer to Table A in the annex for further details.</b></p>
<b>Definitions Article 3 (2) (i)</b>	<p>The relevant definitions of counterparties are taken from Article 2(1) EMIR, including, for example:</p> <ul style="list-style-type: none"> <li>➤ Financial Counterparties (FCs): <ul style="list-style-type: none"> <li>• Investment Firm authorised in accordance with MiFID II</li> <li>• Credit Institution authorised in accordance with CRD IV</li> <li>• CCP authorised in accordance with EMIR</li> <li>• Third Country entity which would require authorisation or registration in accordance with legislation mentioned in points above if it were established in the EU</li> </ul> </li> <li>➤ Non-Financial Counterparties (NFCs): <ul style="list-style-type: none"> <li>• An undertaking established in the EU other than FCs</li> </ul> </li> </ul>
<b>Obligation to report Article 4</b>	<p><b><u>Note!</u></b></p> <ol style="list-style-type: none"> <li>1. <b><u>The reporting obligation for EU and third- country investment firms and credit institutions will apply from May 2018</u></b></li> <li>2. <b><u>The reporting obligation for EU and third-country CCPs and CSDs will apply from August 2018</u></b></li> <li>3. <b><u>The reporting obligation for financial counterparties and third-country entities will apply from November 2018</u></b></li> <li>4. <b><u>The reporting obligation for non-financial counterparties will apply from February 2019</u></b></li> </ol> <p>Counterparties to SFTs are required to report no later than the following working day:</p> <ul style="list-style-type: none"> <li>➤ <b><u>Details of SFTs they have concluded, as well as any modification or termination</u></b></li> <li>➤ To a Trade Repository registered in accordance with Article 5 or recognised in accordance with Article 19.</li> </ul> <p>Back-loading reporting obligation applies to SFTs which:</p>

	<p>➤ Were concluded before the date of entry into force of the Reporting Obligation (May 2018 – February 2019) and remain outstanding on that date if:</p> <ul style="list-style-type: none"> <li>• The remaining maturity of these SFTs on the date of application exceeds 180 days; or if</li> <li>• Such SFTs have an open maturity and remain outstanding 180 days after the date of application.</li> </ul> <p>Delegation:</p> <p>➤ <b><u>Counterparties may delegate their reporting obligations.</u></b></p> <p><b>Note!</b></p> <p>➤ The <b><u>FC shall be responsible for reporting for both parties</u></b> when entering into a SFT with a NFC fulfilling no more than one of the following criteria (Art 3(3) of Directive 2013/34/EU):</p> <ol style="list-style-type: none"> <li>1. Balance Sheet Total: EUR 20m</li> <li>2. Net Turnover: EUR 40m</li> <li>3. Average number of employees during financial year: 250</li> </ol> <p>Record Keeping:</p> <p>➤ Counterparties shall keep a record of any SFTs concluded, modified or terminated for at <b>least five years</b> following the termination of the transaction.</p>
<b>Transparency and availability of data held in a trade repository</b> <b>Article 12</b>	<p>Trade repositories are required to:</p> <p>➤ Regularly publish aggregate positions by the type of SFTs reported to it.</p> <p>➤ Collect and maintain the details of SFTs and ensure the relevant regulatory authorities have direct access to these details</p>
<b>Reuse of Financial instruments received under a collateral arrangement</b> <b>Article 15</b>	<p>Right of Reuse of Financial Instruments received as collateral will be subject to at least the following:</p> <p>➤ Counterparty has been duly informed in writing by the receiving counterparty of the risks and consequences that may be involved in:</p> <ul style="list-style-type: none"> <li>• Granting consent to a right of use of collateral provided under a security collateral arrangement; or</li> <li>• Concluding a title transfer collateral arrangement; and</li> <li>• that may arise in the event of default of the receiving counterparty.</li> </ul> <p>➤ The providing counterparty has granted prior express consent to a security collateral arrangement or to provide collateral by way of title transfer.</p>
<b>Administrative sanctions and other measures</b> <b>Article 20 and 21</b>	<p>Breach of Article 4 or Article 15:</p> <p>➤ Member states may elect to impose criminal sanctions</p> <p>➤ Competent authorities will have power to apply administrative sanctions listed under Article 20 (4) (a) to (h), taking into account all relevant circumstances when determining the type and level of such sanction.</p> <p>Breach of Rules in Article 4 shall <b><u>not</u></b> affect validity of terms of SFT.</p>
<b>Reporting of breaches</b> <b>Article 22</b>	<p>Counterparties are required to have in place appropriate internal procedures for their employees to report actual and potential breaches of Article 4 and Article 15 to competent authorities.</p>
<b>Amendments to EMIR</b> <b>Article 27 b</b> <b>(For your information only)</b>	<p><b>Note!</b></p> <p>NFC should be aware that Article 2(7), EMIR has changed the definition of OTC derivative contract under EMIR. It includes all derivatives not traded on an EU regulated market or third country equivalent under MIFID.</p> <p>“OTC derivative” or “OTC derivative contract” means a derivative contract the execution of which does not take place on a regulated market within the meaning of Article 4(1)(14) of Directive 2004/39/EC or on a third-country market considered as equivalent to a regulated market in accordance with Article 19(6) of Directive 2004/39/EC.</p>

## Annex

Table A

***SFTR applies to:***

EU	Non-EU
EU counterparty to a SFT	All branches of an EU counterparty to a SFT, irrespective of where they are located
EU branches of <b>third country counterparty</b> if the SFT is concluded in the course of business of the EU branch	
UCITS Management/Investment Companies	
Alternative Investment Fund Managers (AIFMs)	
EU counterparty engaging in reuse	
EU branches of third country counterparty engaging in reuse if the reuse is concluded in the course of operations of the EU branch	A counterparty engaged in reuse where the reuse concerns financial instruments provided under collateral arrangement by a counterparty established in the EU or an EU branch of a counterparty established in a third country.

