

EMIR and SFTR reporting – two sides of the same coin?

With the start date for reporting in relation to securities financing transactions (**SFTs**), such as repos and securities lending, fast approaching, counterparties will need to ensure the necessary systems are in place for their compliance with the Securities Financing Transactions Regulation ((EU) 2015/2365) (**SFTR**). While previous experience of implementing systems for the analogous reporting requirement for derivative transactions subject to Regulation (EU) No 648/2012 (**EMIR**) will provide a framework for preparing for SFTR reporting, there are some key differences between the two reporting regimes.

In response to the global financial crisis, the European Union sought to enhance transparency of some of the more opaque parts of the financial system, including through the enactment of EMIR, as amended by Regulation (EU) 2019/834 (**EMIR Refit**), and SFTR. While EMIR aims to increase transparency of the over the counter (**OTC**) derivatives market, SFTR looks to do the same in respect of securities financing markets.

The way in which these regulations seek to achieve transparency is by imposing obligations on counterparties to derivative transactions and SFTs¹ to report trade details, with obligations under SFTR starting to come into force in April this year. Counterparties must provide these trade details to a trade repository registered with, or recognized by, the European Securities and Market Authority (**ESMA**) upon entry into, modification or termination of the contract.

The key concerns for the market have centered around differences between the regimes, with SFTR requiring more than EMIR, and how delegated reporting imposed by the relevant legislation will operate in practice.

Following a review of the legislation in the context of EMIR Refit, such reporting requirements were deemed to impose disproportionate costs on smaller counterparties.

Reporting under EMIR (as amended by EMIR Refit):

Prior to the introduction of EMIR Refit, the requirement to report derivative contracts under EMIR applied equally to both financial counterparties (**FCs**) and non-financial counterparties (**NFCs**), though it has always been possible for a counterparty to delegate reporting. Following a review of the legislation in the context of EMIR Refit, such reporting requirements were deemed to impose disproportionate costs on smaller counterparties. Accordingly, EMIR Refit amended the reporting obligation such that, from June 18 2020, FCs that enter into an OTC trade with an NFC that is below certain clearing thresholds (an **NFC-**) will be “solely responsible” for reporting those trades on behalf of both parties. (Please see the Annex to this article for the relevant clearing thresholds.)

Reporting under SFTR:

Under SFTR, the requirement on FCs and NFCs to report details of an SFT is being implemented in staggered phase-in dates depending on the status of the relevant counterparty, with phase 1 applying from April. (Please see the Annex for the relevant phase-in dates). Similarly to EMIR, as amended, where an FC enters into an SFT with an NFC that is considered a small or medium sized entity (**SME NFC-**) for accounting purposes, the FC will be responsible for reporting the trade details for both parties. Given that the reporting obligation on NFCs under SFTR is not due to kick in until January 11 2021, however, the FC will not be required to report on behalf of an SME NFC- before then. If an SFT is between an FC and an NFC (excluding an SME NFC-), both counterparties are mandatorily obliged to report, but it is possible for the NFC to delegate reporting to its FC counterparty in the same way that parties to derivative transactions can do under EMIR.

¹ Pursuant to article 3(11) of SFTR, an SFT means a repurchase transaction, a securities or commodities lending or borrowing transaction, a buy-sell back or sell-buy back transaction and a margin lending transaction.



Key differences between EMIR and SFTR reporting:

Extra-territoriality

One of the key differences between reporting under EMIR and SFTR is the extraterritorial application of the reporting obligation. EMIR does not place any reporting obligation on third-country counterparties, even if such a counterparty is entering into a derivative transaction with an EU entity. SFTR reporting on the other hand applies extraterritorially in two circumstances: (i) when a non-EU branch of an EU entity enters into an SFT and (ii) when an EU branch of a third-country entity enters into an SFT. Nevertheless, even though EMIR reporting does not apply to third-country entities, an EU counterparty entering into a derivative contract with a third-country counterparty will still seek certain minimum information from its counterparty to ensure compliance with EMIR.

Reporting requirements

Another key difference between the two reporting regimes is the level of detail concerning trades required to be included in trade reports. In particular, for SFTR, the details of any collateral being posted and any reuse of such collateral is required to be reported. The trade report expected to be made in relation to derivative transactions is set out in the Annex to Commission

Delegated Regulation (EU) 2017/104, which requires details of any initial and/or variation margin being posted, including the currency of the collateral and, if relevant, the value of any excess collateral. In comparison, the trade report in relation to SFTs set out in the Annex to Commission Delegated Regulation (EU) 2019/356 (**SFTR RTS**) not only contains fields for the amount of collateral being provided, but also the quality of the collateral (e.g. investment grade), information on the issuer of the collateral if securities are used and details on the reuse of such collateral. In accordance with Article 4 of the SFTR RTS, it is the counterparty receiving the collateral that is expected to complete the relevant fields of the trade report relating to collateral reuse.

The extensive reporting requirements under SFTR in respect of collateral reuse have arisen in response to a concern of regulators that collateral is often used multiple times resulting in 'complex collateral chains', posing a risk to financial stability. By increasing transparency, it is hoped that this risk can be mitigated and confidence of counterparties to trades can be increased, especially in instances of bankruptcy.

For further details on the differences between the trade reports, and additional differences between the two regimes, a comparison table is set out in the Annex below.

Master Reporting Agreement:

In order to provide a framework for the delegation of reporting under SFTR and EMIR, a working group comprised of various industry bodies (including the Association for Financial Markets in Europe, the Futures Industry Association, Inc., the International Capital Markets Association, the International Securities Association and the International Swaps and Derivatives Association, Inc.) published the Master Regulatory Reporting Agreement (**MRAA**) on December 19 2019.

The MRAA is a template agreement that can be used by two counterparties to derivative transactions and/or SFTs and which designates one of the parties as reporting entity so as to make clear how both parties' reporting obligations under EMIR and SFTR will be met.

The MRAA is divided into two main sections and provides for both elective delegated reporting (**Delegated Reporting**) and mandatory reporting (**Mandatory Reporting**). In respect of EMIR, if an FC is required to report on behalf of an NFC- or, in respect of SFTR, if an FC is required to report on behalf of an SME NFC-, provisions to deal with such situation are set out in the Mandatory Reporting section. If no such mandatory reporting is applicable, but the counterparties wish to delegate reporting, the relevant provisions have been included in a section entitled 'Delegated Reporting'. A considerable amount of optionality is built into the MRAA, for example, if the counterparties are entering into both derivative transactions and SFTs, they can elect for Mandatory Reporting to apply in respect of derivative transactions (if one party is an FC and the other party is an NFC- for the purposes of EMIR) and Delegated Reporting in respect of SFTs (if the NFC- is not an SME NFC- for the purposes of SFTR reporting).

Each section includes an obligation on the non-reporting party to provide relevant information for completing the trade report to the reporting party. However, if the non-reporting party fails to provide such information and Delegated Reporting is applicable, the reporting party will be under no obligation to submit such data on its behalf, whereas if such a scenario occurs and Mandatory Reporting is applicable, the non-reporting party will breach its obligations under the MRAA, but the reporting party will still be subject to its regulatory reporting requirements.

There are two product specific annexes to the MRAA; one for derivative transactions (the **Derivatives Annex**) and the other for SFTs (the **SFT Annex**). There is considerable overlap between the annexes, in particular (i) the ability to select which type of reporting applies (either Delegated Reporting or Mandatory Reporting), depending on the type of derivative transaction or SFT being entered into, and (ii) the ability to elect for the automatic transition from Mandatory Reporting to Delegated Reporting (and vice versa) to address a situation where the status of a counterparty changes. There are a few notable differences, however, including the provision of an opt-out election for an NFC- that has invested in a reporting system in the Derivatives Annex and the ability to opt-out of producing "backloading" reports on behalf of the non-reporting party in the SFT Annex (i.e. reports in relation to certain legacy transactions that remain live after the reporting start date).



Final thoughts

The differences between SFTR and EMIR reporting, as highlighted above, are a primary concern for the market, especially in respect of the information relating to collateral reuse that must be included in an SFTR trade report. There remains some uncertainty around the interaction between these regimes and what SFTR requires. Other key questions we are being asked by parties to SFTs are as follows:

- Could a credit support arrangement in connection with a derivative transaction fall within the scope of SFTR reporting as well as EMIR? Can a party comply with its reporting obligations under both the EMIR and SFTR regimes by submitting a report under only one regime in the case of such a transaction?
- How specific does the reporting of collateral reuse need to be, given the parties will not necessarily know from the effective date of a transaction what the collateral will be used for in the future? Do the parties need to update reporting when use of the collateral changes?
- What obligations apply where one party to an SFT is required to report under SFTR but its counterparty is not yet caught because the relevant phase-in date is in the future? Will this lead to difficulties in obtaining reporting information as the other party will not be obliged to report and, therefore, will be less incentivised to provide such information?

Contacts



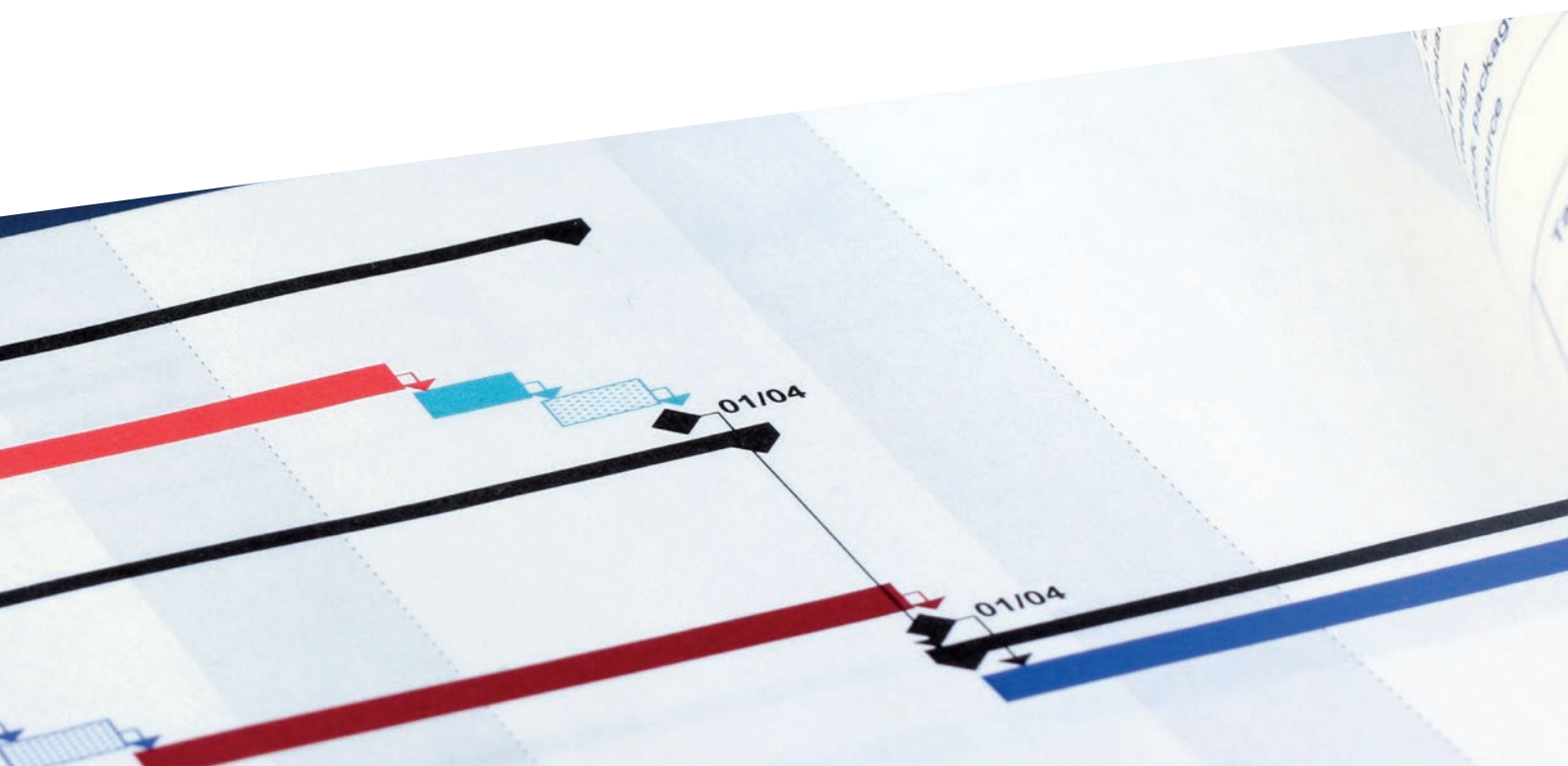
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Annex

	EMIR			SFTR		
1 Which transactions fall within the scope of the regulation?	Derivative contracts (including both OTC and exchange-traded derivatives).			<ul style="list-style-type: none"> • Securities and commodities lending and borrowing; • Repo transactions; • Buy-sell backs / sell-buy backs; and • Margin lending. 		
2. When must a transaction be reported?	Conclusion, modification or termination of the transaction.			Conclusion, modification or termination of the transaction. (See section 7 below for phase-in dates.)		
3. Who is required to report the transaction?	Party	Party	Reporting Obligation	Party	Party	Reporting Obligation
	FC	FC	Both	FC	FC	Both
	FC	NFC+	Both	FC	NFC+	Both
	FC	NFC-	Both *FC as of June 18 2020	FC	SME NFC-	FC
	<p>An NFC- means a non-financial counterparty that does not meet any of the clearing thresholds. A clearing threshold is met if the entity's aggregate month-end average position at group level in derivative contracts (excluding for hedging purposes) is:</p> <ul style="list-style-type: none"> • ≥ EUR 1 billion: for either credit and equity derivatives; or • ≥ EUR 3 billion: for either interest rate, foreign exchange or commodity derivatives. 			<p>An SME NFC- means a non-financial counterparty that has at least two of the following:</p> <ul style="list-style-type: none"> • Balance sheet total of < EUR 20,000,000; • Net turnover < EUR 40,000,000; or • Average number of employees during year < 250. 		
4. By when does the transaction need to be reported?	The following business day (T+1)			T+1		

	EMIR	SFTR										
5. Number of fields to populate in the trade report:	129	153 (product dependent)										
6. What information needs to be included in the report?	<p>The trade report is split into two sections: 'Counterparty Data' and 'Common Data'.</p> <p>Counterparty Data:</p> <ul style="list-style-type: none"> This section includes counterparty details (e.g. FC or NFC), general contract details (e.g. is it at a hedging transaction, mark to market value of the contract and details on the posting of collateral). <p>Common Data:</p> <ul style="list-style-type: none"> The common data sets out the general commercial terms of the contract, including maturity date, termination date and price. There are also fields specific to the type of derivative (e.g. commodity derivatives, options and credit derivatives). 	<p>The trade report is split into four sections: 'Counterparty data', 'Loan and collateral data', 'Margin data' and 'Re-use, cash reinvestment and funding sources'.</p> <p>Counterparty data:</p> <ul style="list-style-type: none"> Similar counterparty details to the EMIR trade report, in addition to branch office details if relevant. <p>Loan and collateral Data:</p> <ul style="list-style-type: none"> This section sets out the details of the trade, including the collateral arrangements, such as substitution of collateral, whether collateral is available for reuse and any haircut. <p>Margin data:</p> <ul style="list-style-type: none"> In respect of cleared SFTs, details of initial margin, variation margin and excess collateral. <p>Re-use, cash reinvestment and funding sources:</p> <ul style="list-style-type: none"> One of the main details to be included in this section is details of collateral reuse (e.g. value of reused collateral and currency). 										
7. What are the key deadlines?	Fully implemented	<table border="1"> <thead> <tr> <th>Implementation date:</th> <th>Entity:</th> </tr> </thead> <tbody> <tr> <td>April 11 2020</td> <td>Banks and investment firms</td> </tr> <tr> <td>July 11 2020</td> <td>Central counterparties and Central Securities Depositories</td> </tr> <tr> <td>October 11 2020</td> <td>Remaining FCs (eg. Insurance/ reinsurance firms, UCITs, AIFs and pension schemes) and third country entities</td> </tr> <tr> <td>January 11 2021</td> <td>NFCs</td> </tr> </tbody> </table>	Implementation date:	Entity:	April 11 2020	Banks and investment firms	July 11 2020	Central counterparties and Central Securities Depositories	October 11 2020	Remaining FCs (eg. Insurance/ reinsurance firms, UCITs, AIFs and pension schemes) and third country entities	January 11 2021	NFCs
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