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First exchange of views on the reporting and transparency of Securities Financing Transactions (SFTs)

Economic and Monetary Affairs Committee

4 November 2014, European Parliament, Brussels

All of as working in ECON are very much aware of the unprecedented wave of financial sector regulation we have witnessed over recent years. With the regulation on the transparency of Securities Financing Transactions (SFTs), we are adding a missing piece to the regulatory landscape.

SFTs are at the heart of a smooth functioning financial market as well as pivotal for monetary policy. These transactions entail a temporary exchange of collateral among two counterparties for cash or securities. While being key for the provision of market liquidity, SFTs can also be used in a risky fashion in the shadow banking sector, lead to a build-up of leverage, with a potential for undesired contagion. Just last week, the Financial Stability Board declared that the scale of shadow banking relative to the overall economy is closing in on its pre-crisis peak. This is why putting in place transparency provisions for SFTs is more timely and important than ever.

We have already had a first exchange of views with fellow shadows and I think we are on track towards reaching a good compromise within the ECON timetable.

Let me stress a few points, which I would like our discussions to focus on:

My first point concerns the issue of definitions. It will be important to incorporate into the text a few additional definitions, which the Commission proposal left out, but which would be helpful for the regulation. These include “buy-sell back transaction”, “sell-buy back transaction” and “collateral arrangement.” We will also need to decide whether we prefer cross-referencing definitions to other pieces of legislation (such as EMIR) or whether we wish to spell out these definitions in full. Whichever way we go, we must aim for clarity and precision.

Staying with definitions, for international consistency reasons, we should also employ the word “re-use” when referring to the reality captured by the word “rehypothecation” in the current Commission proposal. We will of course also need to clearly define “re-use.” We know that international discussions on this matter are on-going. This is why it might be too early to think about ways of regulating rehypothecation beyond transparency provisions. Looking ahead however, we should consider adding a review clause to the text stating that within three years of the entry into force of this Regulation, the Commission should assess the outcome of on-going international developments on rehypothecation, (including quantitative limits on it), in particular in the FSB context, and assess whether there is a need to propose further regulatory measures on it.

My second point concerns transactions involving central bank counterparties. The debate here concerns whether counterparties to transactions with central banks should have to follow the disclosure requirements put forward by the SFTs regulation. Such transactions are sensitive however, especially taking into account the fact that repo transactions are so intertwined with monetary policy operations. Thus, due to monetary policy secrecy reasons, we should consider exempting the counterparties to transactions with central banks from requirements imposed by the SFTs regulation.

My third point concerns the possibility of including an SME reporting requirement exemption to the text. SMEs are at the heart of our economies and represent Europe’s fuel for growth. Every time we have the opportunity to make their life easier through our regulations, we should do so. For this reason, we should exempt SMEs from SFTs reporting requirements when engaging in a transaction with a financial counterparty. It should in this case be the obligation of the financial counterpart to report the transaction.

One further matter concerns the requirement put forward by the Commission that counterparties keep a record of any SFT that they have concluded, modified or terminated for at least ten years following the termination of the transaction. This seems to be too burdensome, and we could consider decreasing the period.

Moreover, we must also not forget a number of practical considerations. While transparency in SFTs is fundamental, not the same level of granularity in disclosures is needed by a normal citizen as is needed by an asset manager. We may wish to make a differentiation here. Additionally, we should also try to achieve the most efficient level of costs of the new requirements put forward by this regulation. This will entail making good use of existing trade repositories, as this would have reduce potential costs for investors.

Finally, we have a number of further issues which we need to discuss in light of on-going international work on SFTs. One recent item on the agenda of the FSB board in October was that of global rules on collateral for short-term lending and more specifically the issue of haircuts. This might well be beyond the scope of the current legislation but it is nonetheless an issue we need to bear in mind for the future (maybe once again, a matter to be added to our review clause).

I look forward to discussing these as well as other issues further with my colleagues over the coming months.