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The Securities Financing Transaction Regulation (SFTR)

Annual and semi-annual report considerations

The Securities Financing Transaction Regulation (SFTR) came into effect on 12 January 2016 to help enhance the transparency around the use of Securities Financing Transactions (SFTs) and Total Return Swaps (TRSs) in the shadow banking industry. The purpose of this paper is to provide guidance on some common questions on the SFTR as it relates to and impacts on the annual and semi-annual reports.

Who does the SFTR apply to?

Annual and semi-annual report disclosures required and set out in annex A of the SFTR are imposed on Undertakings for Collective Investment in Transferable Securities (UCITS) management companies, UCITS investment companies and Alternative Investment Fund Managers (AIFMs) and are required in the annual and semi annual report of each UCITS/AIF under management.

When are these disclosures required?

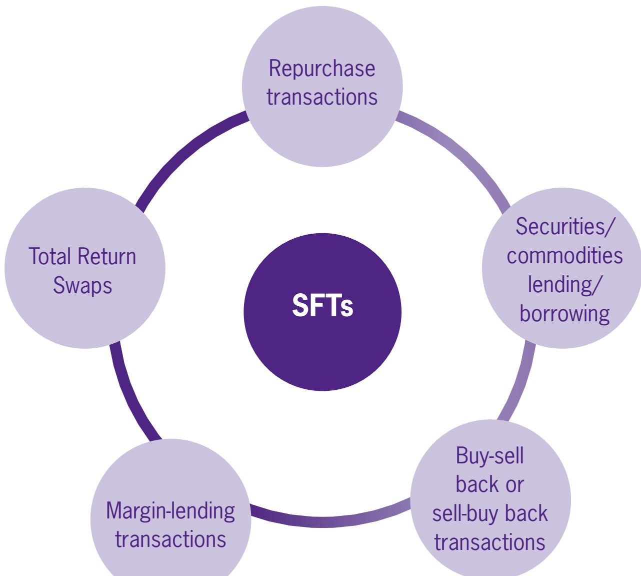
It has recently been clarified by the European Securities and Markets Association (ESMA) that the information requiring disclosure under the SFTR should be included in the next annual or semi-annual report to be published after 13 January 2017.

Where in the annual report should the required disclosures be included?

The SFTR does not require these disclosures to be included within the audited financial statements in the annual report. Management may therefore consider including such disclosures within an unaudited section of the annual report.

What is an SFT?

The SFTR highlights the following transaction types as SFTs:



A number of industry participants have raised a query as to whether the definition of a TRS included in the SFTR could be interpreted to include Contract For Differences (CFDs). Our current understanding is that CFDs will not be in scope of the SFTR however, clarification has been sought from ESMA on this matter.

What needs to be disclosed?

Section A of the annex to the SFTR sets out the following disclosure requirements in annual and semi-annual reports. Some of the disclosures are partially covered through existing accounting frameworks or other regulatory requirements, however there are a number of new disclosure requirements.

Global data
- the amount of securities and commodities on loan as a proportion of total lendable assets defined as excluding cash and cash equivalents; and
- the amount of assets engaged in each type of SFTs and TRSs expressed as an absolute amount (in the collective investment undertakings currency) and as a proportion of the collective investment undertakings Assets Under Management (AUM).

Concentration data
- ten largest collateral issuers across all SFTs and TRSs (break down of volumes of the collateral securities and commodities received per issuer's name); and
- top ten counter-parties of each type of SFTs and TRSs separately (name of counter-party and gross volume of outstanding transactions).

Aggregate transaction data for each SFT and TRS according to new categories
- type and quality of collateral;
- maturity tenor of the collateral broken down in the following maturity buckets: less than one day, one day to one week, one week to one month, one to three months, three months to one year, above one year and open maturity;
- currency of the collateral;
- maturity tenor of the SFTs and TRSs broken down in the following maturity buckets: less than one day, one day to one week, one week to one month, one to three months, three months to one year, above one year, open transactions;
- country in which the counter-parties are established; and
- settlement and clearing (e.g. tri-party, central counter-party, bilateral).

Data on reuse of collateral
- share of collateral received that is reused, compared to the maximum amount specified in the prospectus or in the disclosure to investors; and
- cash collateral reinvestment returns to the collective investment undertaking.

Safekeeping of collateral received as part of SFTs and TRSs
- number and names of custodians and the amount of collateral assets safe-kept by each of the custodians.

Safekeeping of collateral granted as part of SFTs and TRSs
- the proportion of collateral held in segregated accounts, in pooled accounts or in any other accounts.

Data on return and cost of each type of SFTs and TRS
- broken down between the collective investment undertaking, the manager of the collective investment undertaking and third parties (e.g. agent lender) in absolute terms and as a percentage of overall returns generated by that type of SFTs and TRSs.

How we see it

SFTR is yet another piece of regulation for the asset management industry to consider. Internal processes should be put in place early to clearly define and consider:
- what will be categorised as a SFT?
- who's responsibility is it to produce the required disclosure data?
- can the required data be easily retrieved and collated?
- where will the data be disclosed in the annual and semi-annual report?
- judgements applied in the calculation process and interpretation of key terms.

Significant input from all service providers to the fund will be necessary to ensure the disclosure requirements laid out under the SFTR are being adhered to. As a result, the impact of the SFTR to the annual and semi-annual reports should not be under-estimated.

Contact

If you have any questions regarding SFTR please contact a member of our team at grantthorntonam@ie.gt.com

24-26 City Quay, Dublin 2, D02 NY19

Offices in Dublin, Belfast, Cork, Galway, Kildare, Limerick and Longford.

@GrantThorntonIE www.grantthornton.ie