Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012 (Text with EEA relevance)

REGULATION (EU) 2015/2365 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

of 25 November 2015

on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Central Bank[(1)],

Having regard to the opinion of the European Economic and Social Committee[(2)],

Having regard to the opinion of the Committee of Regions[(3)]

Acting in accordance with the ordinary legislative procedure[(4)],

Whereas:

(1) The global financial crisis that emerged in 2007-2008 has revealed excessive speculative activities, important regulatory gaps, ineffective supervision, opaque markets and overly complex products in the financial system. The Union has adopted a range of measures in order to render the banking system more solid and more stable, including strengthening capital requirements, rules on improved governance and supervision and resolution regimes, and to ensure that the financial system fulfils its role in directing capital towards the financing of the real economy. Progress made on the establishment of the banking union is also decisive in this context. However, the crisis has also highlighted the need to improve transparency and monitoring not only in the traditional banking sector but also in areas where bank-like credit intermediation known as ‘shadow banking’, takes place, the scale of which is alarming, having already been estimated to amount to close to half of the regulated banking system. Any shortcomings with regard to those activities, which are similar to those carried out by credit institutions, have the potential to affect the rest of the financial sector.

(2) In the context of its work to curb shadow banking, the Financial Stability Board (FSB) and the European Systemic Risk Board (ESRB) established by Regulation (EU) No

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1092/2010 of the European Parliament and of the Council[5] have identified the risks posed by securities financing transactions (SFTs). SFTs allow the build-up of leverage, pro-cyclicality and interconnectedness in the financial markets. In particular, a lack of transparency in the use of SFTs has prevented regulators and supervisors as well as investors from correctly assessing and monitoring the respective bank-like risks and level of interconnectedness in the financial system in the period preceding and during the financial crisis. Against this background, on 29 August 2013, the FSB adopted the policy framework entitled 'Strengthening Oversight and Regulation of Shadow Banking' ('FSB Policy Framework') for addressing shadow banking risks in securities lending and repos, which was endorsed in September 2013 by the G20 Leaders.

(3) On 14 October 2014, the FSB published a regulatory framework for haircuts on non-centrally cleared SFTs. In the absence of clearing, such operations raise major risks if they are not properly collateralised. While enhancing transparency in the reuse of client assets would be a first step towards facilitating counterparties' capacity to analyse and prevent risks, the FSB is due to complete its work, by 2016, on a set of recommendations on haircuts on non-centrally cleared SFTs to prevent excessive leveraging and mitigate concentration risk and default risk.

(4) On 19 March 2012, the Commission published a Green Paper on Shadow Banking. Based on the extensive feedback received and taking into account international developments, the Commission issued, on 4 September 2013, a communication to the Council and the European Parliament entitled 'Shadow Banking — Addressing New Sources of Risk in the Financial sector'. The Communication stressed that the complex and opaque nature of SFTs makes it difficult to identify counterparties and monitor risk concentration and also leads to the build-up of excessive leverage in the financial system.

(5) A high-level expert group chaired by Erkki Liikanen adopted a report on reforming the structure of the Union banking sector in October 2012. It considered, among other things, the interaction between the traditional and the shadow banking systems. The report recognised the risks of shadow banking activities such as high leverage and pro-cyclicality, and it called for a reduction of the interconnectedness between banks and the shadow banking system, which had been a source of contagion in a system-wide banking crisis. The report also suggested certain structural measures to deal with remaining weaknesses in the Union banking sector.

(6) Structural reforms of the Union banking system are dealt with in a proposal for a regulation of the European Parliament and of the Council on structural measures improving the resilience of EU credit institutions. However, imposing structural measures on banks could result in certain activities being shifted to less-regulated areas such as the shadow banking sector. That proposal should therefore be accompanied by the binding transparency and reporting requirements for SFTs laid down in this Regulation. Thus, the transparency rules laid down in this Regulation complement that proposal.

(7) This Regulation responds to the need to enhance the transparency of securities financing markets and thus of the financial system. In order to ensure equivalent conditions of

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competition and international convergence, this Regulation follows the FSB Policy Framework. It creates a Union framework under which details of SFTs can be efficiently reported to trade repositories and information on SFTs and total return swaps is disclosed to investors in collective investment undertakings. The definition of SFT in this Regulation does not include derivative contracts as defined in Regulation (EU) No 648/2012 of the European Parliament and of the Council[(6)]. However, it includes transactions that are commonly referred to as liquidity swaps and collateral swaps, which do not fall under the definition of derivative contracts in Regulation (EU) No 648/2012. The need for international convergence is reinforced by the probability that, following structural reform of the Union banking sector, activities that are currently exercised by traditional banks might migrate to the shadow banking sector and encompass financial and non-financial entities. Therefore, even less transparency may arise for regulators and supervisors in respect of those activities, preventing them from obtaining a proper overview of the risks linked to SFTs. This would only aggravate already well established links between the regulated and the shadow banking sectors in particular markets.

(8) The evolution of market practices and technological developments enable market participants to use transactions other than SFTs as a source of funding, for liquidity and collateral management, as a yield-enhancement strategy, to cover short sales or for dividend tax arbitrage. Such transactions could have an equivalent economic effect and pose risks similar to SFTs, including pro-cyclicality brought about by fluctuating asset values and volatility; maturity or liquidity transformation stemming from financing long-term or illiquid assets through short-term or liquid assets; and financial contagion arising from interconnectedness of chains of transactions involving collateral reuse.

(9) In order to respond to the issues raised by the FSB Policy Framework and the developments envisaged following structural reform of the Union banking sector, Member States are likely to adopt divergent national measures which could create obstacles to the smooth functioning of the internal market and be to the detriment of market participants and financial stability. In addition, the lack of harmonised transparency rules makes it difficult for national authorities to compare the micro-level data stemming from different Member States and thus to understand the real risks individual market participants pose to the system. It is therefore necessary to prevent such distortions and obstacles from arising in the Union. Consequently, the appropriate legal basis for this Regulation is Article 114 of the Treaty on the Functioning of the European Union (TFEU), as interpreted in accordance with the consistent case-law of the Court of Justice of the European Union.

(10) The new rules on transparency should therefore provide for the reporting of details regarding SFTs concluded by all market participants, whether they are financial or non-financial entities, including the composition of the collateral, whether the collateral is available for reuse or has been reused, the substitution of collateral at the end of the day and the haircuts applied. In order to minimise additional operational costs for market participants, the new rules and standards should build on pre-existing infrastructures, operational processes and formats which have been introduced with regard to reporting derivative contracts to trade repositories. In that context, the European Supervisory

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Authority (European Securities and Markets Authority) ('ESMA') established by Regulation (EU) No 1095/2010 of the European Parliament and of the Council[7] should, to the extent feasible and relevant, minimise overlaps and avoid inconsistencies between the technical standards adopted pursuant to this Regulation and those adopted pursuant to Article 9 of Regulation (EU) No 648/2012. The legal framework laid down by this Regulation should, to the extent possible, be the same as that of Regulation (EU) No 648/2012 in respect of the reporting of derivative contracts to trade repositories registered for that purpose. This should also enable trade repositories registered or recognised in accordance with that Regulation to fulfil the repository function assigned by this Regulation, if they comply with certain additional criteria, subject to completion of a simplified registration process.

(11) In order to ensure consistency and effectiveness of ESMA's powers to impose penalties, the market participants that fall within the scope of this Regulation should, by reference to Regulation (EU) No 648/2012, be subject to the provisions regarding ESMA's powers as laid down in that Regulation as specified, in respect of the rules of procedure, by the delegated acts adopted pursuant to Article 64(7) of that Regulation.

(12) Transactions with members of the European System of Central Banks (ESCB) should be exempted from the obligation to report SFTs to trade repositories. However, in order to ensure that regulators and supervisors obtain a proper overview of the risks linked to SFTs concluded by the entities they regulate or supervise, the relevant authorities and the members of the ESCB should cooperate closely. Such cooperation should enable regulators and supervisors to fulfil their respective responsibilities and mandates. Such cooperation should be confidential, and conditional on a justified request from the relevant competent authorities, and should only be provided with a view to enabling those authorities to fulfil their respective responsibilities having due regard to the principles and requirements of the independence of central banks and the performance by them of their functions as monetary authorities, including the performance of monetary, foreign exchange and financial stability policy operations which members of the ESCB are legally empowered to pursue. The members of the ESCB should be able to refuse to provide information where the transactions are entered into by them in the performance of their functions as monetary authorities. They should notify the requesting authority of any such refusal together with the justification therefor.

(13) Information on the risks inherent in securities financing markets should be centrally stored, and easily and directly accessible by, inter alia, ESMA, the European Supervisory Authority (European Banking Authority) ('EBA') established by Regulation (EU) No 1093/2010 of the European Parliament and of the Council[8], the European Supervisory Authority (European Insurance and Occupational Pensions Authority) ('EIOPA') established by Regulation (EU) No 1094/2010 of the European Parliament and of the Council[9], the relevant competent authorities, the ESRB and the relevant central banks of the ESCB, including the European Central Bank (ECB) in carrying out its tasks within a single supervisory mechanism under Council Regulation (EU) No 1024/2013[10], for the purpose of identification and monitoring of financial stability risks entailed by shadow banking activities of regulated and non-regulated entities. ESMA should take into consideration the technical standards adopted pursuant

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to Article 81 of Regulation (EU) No 648/2012 regulating trade repositories for derivative contracts and the future development of those technical standards when drawing up or proposing to revise the regulatory technical standards provided for in this Regulation. ESMA should also aim to ensure that the relevant competent authorities, the ESRB and the relevant central banks of the ESCB, including the ECB, have direct and immediate access to the information necessary to perform their duties, including to define and implement monetary policy and to perform oversight of financial market infrastructures. In order to ensure this, ESMA should set out the terms and conditions for access to such information in draft regulatory technical standards.

(14) It is necessary to introduce provisions on the exchange of information between competent authorities and to strengthen the duties of assistance and cooperation which they owe each other. Due to increasing cross-border activity, competent authorities should provide each other with the relevant information for the exercise of their functions in order to ensure the effective enforcement of this Regulation, including in situations where infringements or suspected infringements may be of concern to authorities in two or more Member States. In the exchange of information, strict professional secrecy is needed to ensure the smooth transmission of that information and the protection of particular rights. Without prejudice to national criminal or tax law, the competent authorities, ESMA, bodies or natural or legal persons other than the competent authorities, which receive confidential information, should use it only in the performance of their duties and for the exercise of their functions. However, this should not prevent the exercise, in accordance with national law, of the functions of national bodies responsible for the prevention, investigation or correction of cases of maladministration.

(15) SFTs are used extensively by managers of collective investment undertakings for efficient portfolio management. Such use can have a significant impact on the performance of those collective investment undertakings. SFTs can be used either to fulfil investment objectives or to enhance returns. Managers also make use of total return swaps which have effects equivalent to SFTs. SFTs and total return swaps are extensively used by managers of collective investment undertakings to get exposure to certain strategies or to enhance their returns. The use of SFTs and total return swaps could increase the general risk profile of the collective investment undertaking whereas their use is not properly disclosed to investors. It is crucial to ensure that investors in such collective investment undertakings are able to make informed choices and to assess the overall risk and reward profile of collective investment undertakings. When assessing SFTs and total return swaps, the collective investment undertaking should consider the substance of the transaction in addition to its legal form.

(16) Investments made on the basis of incomplete or inaccurate information as regards a collective investment undertaking’s investment strategy can result in significant investor losses. It is therefore essential that collective investment undertakings disclose all relevant detailed information linked to their use of SFTs and total return swaps. In addition, full transparency is especially relevant in the area of collective investment undertakings as the entirety of assets that are subject to SFTs and total return swaps are not owned by the managers of collective investment undertakings but by their investors.