ICMA
European Repo and Collateral Council

ESMA review of SFTR Level 3: ICMA comments

October 2022

	Issue that can be addressed in the Validation Rules (VR) and/or Q&As
	Issue that requires changes beyond VR and/or Q&As

1. General issues:

#	Issue	Description	ICMA Recommendation
1	**Reconciliation window after maturity or termination date**	• The RTS on trade repositories require these entities to recycle unreconciled reports back into the daily reconciliation process until 30 days after the *Maturity Date* or *Termination Date* of a transaction. • However, reconciliation is performed against the Trade State Report and these cannot be modified, updated or corrected after the end of the *Maturity Date* or *Termination Date* plus 1 business day. This means that unreconciled reports at the trade repository cannot be corrected retrospectively in order to achieve reconciliation and the 30-day recycling period serves no useful purpose.	The maturity-date-plus-one deadline should be abolished, by modifying the Validation Rules for fields 2.3 (Event Date) and 2.14 (Maturity Date) accordingly.
2	**Historic corrections**	• Because of the maturity-date-plus-one deadline for reporting, it is not possible to correct past Trade State Reports once the deadline has passed. The procedure proposed by ESMA in Q&A6 does not work as it only updates the latest Trade State Report and the Daily Activity Report. • This rule also prevents the extension of maturity dates in the event of fails under current rules where	The maturity-date-plus-one deadline should be abolished by modifying the Validation Rules for fields 2.3 (Event Date) and 2.14 (Maturity Date) accordingly. This change would not entirely solve the issue. We will submit a separate note/query to elaborate on the issue and request clarification.

		they discovered more than one day after the maturity date.	

3	**Failed settlement**	• The SFTR reporting framework does not provide for the reporting of delivery failures. ICMA proposed, on the basis that SFTR reports should reflect the contractual reality of transactions, that delivery failures should be ignored as, in the case of repo, failure to deliver does not delay the start of a contract and the accrual of interest, nor does it delay the cessation of interest accrual at maturity. This is in contrast to securities lending, where the accrual of fees and rebate interest does not start until delivery and continues until redelivery.
		• However, ESMA belatedly decided that fails on the repurchase leg of a repo should result in the maturity date being rolled forward to reflect the continuation of exposure and, where the reporting window was missed, by creating imaginary repos for reporting purposes. This guidance was provided in the form of Q&As, But in the case of repo, this approach is misleading as regards contractual maturity, profit-and-loss and the nature of the exposure between the parties.
		• The extension of the maturity date and creation of imaginary repos forces a divergence between firms' reporting and their books and records. It also disrupts the automated STP linkage between booking systems and reporting systems on the one hand, and settlement systems on the other, as instructions are usually automatically generated by booking systems.
			• The approach should be clarified in Q&As.
			• Neither L1 nor L2 texts include any reference to the reporting of fails. The Guidelines provide ambiguous guidance for the reporting of the repurchase leg:
			  ○ On the one hand, the underlying logic in table 6 (e.g. row 46) and also the reporting logic for 'partial returns' (para 96) indicates that settlement fails are not meant to impact reporting on the repurchase leg of a repo.
			  ○ On the other hand, section 4.9.5 (in particular paragraph 115) on SFT terminations seems to contradict this approach, indicating that in case of a settlement fail on the repurchase leg parties are expected to modify the maturity date.
			• Given the contradictory guidance in the Guidelines, we believe that the issue can be addressed in Q&As. We suggest that the current Q&A guidance is updated/modified to provide for a differentiated treatment of repos and securities lending, in line with the economic and legal structure of the transactions. For repo this would mean reporting on a contractual basis.

		Instructions generated by a fail have to be suppressed. This is challenging. • The T+1 reporting requirement makes it very difficult, if not impossible, for parties to implement the proposed reporting of fails, as they are usually not known until very late in the day or next day. If the reporting deadline is missed, imaginary new repos have to be reported. This will present a false picture of turnover. • Reporting settlement fails is also impracticable for CCP-cleared repos, as a failed net delivery of securities cannot be meaningfully attributed to any of the underlying gross repo deliveries. In September 2020, ESMA informally acknowledged this and suggested that CCP-cleared CCPs would be exempt from the fail reporting rule. However, this concession fragments the application of the rule for reporting failed settlement and weakens the case for continuing to apply this rule to other types of repo, not least repos which are bilaterally netted. • The rules for reporting fails have evolved piecemeal because they were not originally envisaged as reportable and involve huge effort which is not justified by the incidence of fails, particularly given that margining will continue during a fail, so the risk revealed will be minimal. In other words, there is a skewed cost/benefit ratio.	
5	**Correcting COLU reports where collateralization is against net exposure**	• If it is necessary for one party to correct a COLU report, ESMA's Guidelines (p.32, Table 6, row 55) specify that this unilateral change should be made using a CORR report. However, this guidance cannot always be followed because *Table 1, field 9, Counterparty Side and Table 2, field 1, Unique Transaction Identifier*, are mandatory fields in CORR	ESMA should implement its proposal to allow separate reporting of loan and collateral data for CORR reports.

		reports but cannot be correctly filled in where *Table 2, field 73, Collateralization of Net Exposure* = TRUE, as field 1.9 and 2.1 apply to individual repos and, in a net collateralized portfolio of repos, a party may be the buyer in some transactions and the seller in others. • In the last iteration of the VRs (general information), ESMA proposed to allow separate reporting of loan and collateral data but this was not implemented.	
6	**Correcting loan data for an SFT that is part of a portfolio which is collateralized against net exposure**	• Under the latest version of the Validation Rules, a CORR report of loan data for an SFT which is part of a portfolio that is collateralized against its net exposure would have to include field 2.75 (Type of Collateral Component) and thus several subsequent fields describing the collateral in detail. This would be burdensome and unnecessary as the reported collateral would apply to the whole portfolio of SFTs rather than just the SFT being corrected. In addition, there is no rationale for reporting the collateral of an SFT when correcting only loan data. • It would not be possible for ESMA to restrict this rule to SFTs that are collateralized at transaction level as most SFTs now have 2.73 (Collateralization of Net Exposure) = TRUE.	The Validation Rules should be revised to allow CORR reports to exclude collateral data either when correcting SFTs in a portfolio collateralized against the net exposure and/or when only loan data is being corrected. This may require amendments to the ESMA Guidelines.
7	**Reporting the Collateral Basket Identifier for GC financing facility trades using multiple collateral baskets with their own ISINs**	• If a party executes more than one repo on the same day on a GC financing facility in more than one collateral basket, each of which has their own ISIN, the resulting COLU reports, which will have the same LEIs and the same Master Agreement Type, will result in later reports over-writing the basket ISINs of earlier reports in field 2.96.	ESMA should implement its proposal to allow separate reporting of loan and collateral data but this was not implemented in the last iteration of the Validation Rules.

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8	**Overwriting of COLU reports of agency repos managed by different agent lenders and tri-party agents due to inadequate primary key**	• This is a problem shared with securities lending but which is not as significant for repo.
		• Problems arise where more than one COLU report is made on the same day, which happens where counterparties delegate reporting to multiple agent lenders or tri-party agents. TRs use the latest COLU report to populate the Trade State Report and overwrite the previous COLU report because the primary key for distinguishing reports of collateral against a net exposure is the combination of LEIs and Master Agreement Type. Transactions between the same parties will have the same agreement, so the TRs ignore that fact that different reports are for different transactions.
			• The ISLA SFTR WG has proposed three options in which the following fields --- Branch of Reporting Counterparty (1.7); Branch of Other Counterparty (1.8); Tri-party Agent (1.14); Agent Lender (1.18); and Collateral Basket Identifier (2.96) --- would be:
			  ○ added to the primary key for distinguishing COLU reports;
			  ○ made repeatable fields for a security;
			  ○ added to the primary key in the case of fields 1.7 and 18 but made repeatable at the level of the security for all the other fields.

9	**Currencies for collateral fields**	• Field 2.85 (Currency of Collateral Nominal Amount) is matchable from go-live; field 2.86 (Price Currency) is matchable from G+33; but both are optional. • Fields 2.85 and 2.86 are optional but the XML schema requires them for fields 2.83 (Collateral Quantity and Nominal Amount) and 2.88 (Collateral Market Value). • Fields 2.85 and 2.86 are often not being reported. • Fields 2.85 and 2.86 are one of the most common causes of mismatches.	• The Validation Rules and the schema should align.

10	**Reconciliation breaks due to asynchronous COLU reports**	• Because reports are reconciled on the basis of the reporting date and not the Event Date, if party A sends a COLU report for a transaction or net exposure on S and party B sends a COLU report for the same transaction or net exposure on S+1, the two will not be reconciled by the TR. • For example, if parties A and B are sending updates to the collateral balance as at close of business on Monday, but A sends a COLU on Monday (S) and B sends the corresponding COLU on Tuesday (S+1), the TR will seek to reconcile A's COLU for Monday with the COLU that B sent on Monday reporting the collateral balance on Friday because it receives those reports on the same day. The fact that the Event Dates are different is ignored. • ESMA's guidance is that reporting parties should agree to align reporting dates. This impractical in a high-volume, complex and automated market.	• COLU reports need to be assimilated by TRs using Event Date. This will presumably require changes beyond the scope of the current updates.
11	**Event Date for re-use reporting**	• ESMA has accepted that the Event Date for collateral update and CCP margin update reports should measure the party's balances of collateral on the basis of <u>expected</u> settlement (ie ignoring failed deliveries and assuming perfect settlement). • However, in the Guidelines (table 5, p.26, para 116), ESMA specified that collateral re-use update reports should measure the party's balances of collateral on the basis of <u>actual</u> settlement (reflecting failed deliveries). ESMA says that re-use can only be made of actual balances. This is not correct, as parties plan re-use on the basis of expected balances. There has been no explanation of why re-use balances are being treated differently from other collateral balances. • Calculation based on actual balances is very difficult within the reporting deadline and a switch to	ESMA should re-align the reporting of collateral re-use with that for collateral updates and margin updates so that all balances of collateral should be reported on the basis of <u>expected</u> settlement. The Guidelines should be amended accordingly.

		expected balances would make little or no practical difference to a number that is anyway of limited value where it has to be estimated.	

2. Field-specific issues

#	Issue	Description	ICMA Recommendation
12	**Agent Lender** (field 1.18)	• This field is being used in repo for fund managers lending cash on behalf of client funds, which makes the field less informative.	• Field 1.18 should be limited to securities lending. All agent and arrangers in repo should therefore report in field 1.15 (Broker). • As part of the broader review, the name of field 1.15 could then be changed to be more generic.
13	**RTN** (field 2.2)	• If a repo is submitted to a *CCP* which clears by "open offer", then according to ESMA's draft Final Report of March 2017, no prior repo is assumed to exist and so there is no *RTN*. • However, the Validation Rules make the reporting of an *RTN* conditional on *Table 2, field 5, Cleared* = TRUE, with no exemption for repos cleared by open offer. Accordingly, despite the draft Final Report, parties have to report an *RTN* for all cleared repos, including those cleared by open offer.	ESMA should clarify which rule is to be followed when reporting. The Validation Rules are simplest and therefore to be preferred.
14	**Minimum Notice Period** (field 2.16)	• There is confusion over the definition of the notice period for extendible repos. • In the absence of guidance, some parties argue that this period should be the interval between the extension option date and the original maturity date. However, this would provide no additional information to that already provided by field 2.17 (Earliest Call-Back Date) and field 2.14 (Maturity Date). • ICMA has recommended that this field should be the interval between the option date and the new (optional) maturity date.	ESMA is asked to confirm that the notice period for an extendible is the interval between the effective notice date and the extended maturity date. Confirmation could be provided in the form of a Q&A.

15	**DBV Indicator** (field 2.19)	• DBV is a tri-party service, so this field is redundant. • In addition, if the field is retained, it needs to be clarified whether this field and field 1.14 are both filled in.	Make field 2.19 blank in the Validation Rules and consider deleting the field as part of the broader review.
16	**Spread** (field 2.32)	This field does not allow fractions of a basis point, which are found in CCP-cleared repos. ICMA provided a rounding convention as best practice.	ESMA should provide for decimal places in field 2.32. This has been enabled in the base XML schema.
17	**Adjusted Rate** (field 2.35) and **Rate Date** (field 2.36)	• These fields serve little purpose, now being limited to report pre-agreed repo rate changes, which are not common.	Make fields 2.35 and 2.36 blank in the Validation Rules, and consider deleting as part of the broader review.
18	**Security or Commodity Price** (field 2.49) and **Price Currency** (field 2.50)	• These fields are used to report the price of a buy/sell-back but are not correct. Most buy/sell-backs are now priced in terms of the repo rate. • Field 2.50 can only be used for equity collateral.	Replace fields 2.49 and 2.50 as the default for the reporting of buy/sell-backs with fields 2.23 (Fixed Rate) and 2.24 (Day Count Convention).
19	**Collateralization of Net Exposure** (field 2.73)	• This field was originally intended to identify whether collateral was being provided for an individual repo (to which the collateral would be linked by the UTI of the repo) or for a portfolio of repos (to which the collateral will be linked by the LEIs of the parties and the Master Agreement Type). • Most repos are collateralized individually. The few exceptions include GC financing facility repos and tri-party repos managed by JP Morgan. However, variation margins are usually calculated against net exposure. • In the absence of any provision in SFTR or by ESMA for the reporting of variation margin on bilaterally-cleared repos, ICMA proposed that such margin should be reported by a special collateral update report for the variation margin on a portfolio of non-	ESMA should abolish the requirement to report 2.73 = TRUE just because variation margin is against net exposure. This should only be required where net exposure is the actual contractual situation for initial collateral. Q&A 3 should be amended accordingly.

		cleared repos under the same master agreement (2.73 = TRUE), while the repos would be individually reported (2.73 = FALSE). • Confusion was created at a late stage in the implementation of SFTR by ESMA's guidance, initially in the GL but subsequently clarified in Q&As, that, if margin was calculated against the net exposure of a portfolio of repos, then all repos in that portfolio should be reported as being collateralized on a net exposure basis, even if the initial collateral was allocated to individual transactions. ESMA has offered no rationale. Their proposal means that the collateralization of most repos will be fundamentally misrepresented and field 2.73 would be largely redundant, since it would apply to most repos. • The current rule has been problematic in that only one COLU report with 2.73 = TRUE will be accepted by the trade repository for the same reporting parties and master agreement (fields 1.3, 1.11 and 2.9). If a party sends a COLU report for each repo for which 2.73 = TRUE and for variation margin, later reports would over-write earlier reports. The trade repositories have solved this problem by using the presence of a UTI in a COLU report as a signal not to allow over-writing. However, there are instances where several COLU reports, each with 2.73 = TRUE but without UTIs (which are optional for COLUs), will be sent. These will still over-write each other. For example, in the case of multi-manager funds, each manager may calculate variation margin against a separate net exposure and give or take margin separately to/from the same counterparty under the same master agreement.	

20	**Value Date of Collateral** (field 2.74)	This field was designed for the reporting of the pre-payment of collateral for securities loans. Collateral is not pre-paid in repo.	Make this field N/A for repo in the Validation Rules.
21	**Haircut or Margin** (2.89)	This field is the source of many reporting errors because both the name and definition can be confusing.	• The name of this field should be Haircut. • The definition should make it clear, perhaps by the use of a formula, what is meant by a haircut. • This would require a change to the RTS. However, in the meantime, the conditional validations in the Validation Rules could be used to clarify the definition.
22	**Collateral quality (field 2.90) and Collateral type (field 2.94)**	These fields could have multiple applicable responses depending on the source of the information. This currently results in many matching breaks. In addition, 'NOTR' for collateral quality contradicts the ESMA guidance to use firms' internal assessments (ESMA Guidelines, para 279).	ESMA should provide further guidance on the criteria to use for identifying collateral quality and collateral type when faced with mismatches. This may require changes to the ESMA Guidelines.
23	**Jurisdiction of the Issuer** (field 2.92)	The definition of this field is ambiguous.	Clarify whether the jurisdiction is that of incorporation or of the head office.
24	**Level** (2.99)	• It is not possible to meet the conditions for position reporting of CCP-cleared repo.	The Validation Rules should specify that this field should always be reported as TCTN.