

Wednesday 19 April 2017

Directorate-General for Financial Stability, Financial Services and Capital Markets Union
European Commission
1049 Bruxelles/Brussel
Belgium

Dear Sirs,

Securities Financing Transactions Regulation (SFTR) – application to syndicated lending

I am writing to you on behalf of the Loan Market Association (LMA) to encourage the Commission to endorse the approach adopted by the European Securities and Markets Authority (ESMA) with respect to the application of the reporting requirements of the SFTR to the European syndicated loan market.

In its final report to the Commission on technical standards under the SFTR dated 31 March 2017 ESMA concluded that a purposive interpretation of the definition of "margin lending" in the SFTR means that the reporting requirements of the SFTR do not apply to transactions related to mergers and acquisitions, corporate restructuring, investing in infrastructure and other forms of syndicated corporate lending, due to their limited direct link with shadow banking. Rather, ESMA considers that, consistently with the Financial Stability Board (FSB) policy framework, the margin lending reporting obligation should only apply to prime brokerage margin lending.

The LMA strongly supports these conclusions and encourages the Commission to confirm this interpretation and to adopt the technical standards, with their recitals confirming this approach, in the form proposed by ESMA.

The Loan Market Association

The LMA has as its key objective improving liquidity, efficiency and transparency in the primary and secondary syndicated loan markets in Europe, the Middle East and Africa (EMEA). By establishing sound, widely accepted market practice, the LMA seeks to promote the syndicated loan as one of the key debt products available to borrowers across the region.

As the authoritative voice of the syndicated loan market in EMEA, the LMA works with lenders, law firms, borrowers and regulators to educate the market about the benefits of the syndicated loan product, and to remove barriers to entry for new participants.

Since the establishment of the LMA in 1996, our membership has grown steadily and now stands at over 600 organisations covering 55 nationalities, comprising commercial and investment banks, institutional investors, law firms, service providers and rating agencies.

The SFTR – margin lending

The SFTR defines securities financing transactions (SFTs) to include "margin lending", defined as follows:

"a transaction in which a counterparty extends credit in connection with the purchase, carrying or trading of securities, but not including other loans that are secured by collateral in the form of securities."

We wrote to Verena Ross of ESMA on 30 November 2016 (copied to then Commissioner Lord Hill) expressing the LMA's concern about the potential application of the definition of margin lending and therefore the reporting requirements in the SFTR to a wide range of syndicated lending transactions with corporate borrowers, including loans relating to the financing or refinancing of infrastructure and asset transactions, mergers and acquisitions (M&A) and corporate reorganisations, even though these transactions have little in common with the kinds of bilateral margin loans that were intended to be reported under the SFTR. We urged ESMA – in conjunction with the European Commission - to provide guidance interpreting the SFTR in a way that makes clear that the reporting requirements do not apply to these kinds of transactions. We also pointed out that including syndicated loans of the kind discussed above within the SFTR reporting framework would present a number of challenges which would need to be addressed in the regulatory technical standards (RTS) under the SFTR.

The LMA also responded to ESMA's consultation on the technical standards under the SFTR and reiterated our concerns in our response to Question 27 of that consultation.

ESMA's final report

In the light of these comments we welcomed the conclusions reached in ESMA's final report. ESMA discusses the scope of the definition of margin lending in section 4.2.4.4 of its report and in Section 19.2.3 of Annex XII – Cost benefit analysis (page 337). In particular, ESMA states that:

185. The consultations revealed that many different types of transactions might be captured in the scope of the "margin lending" definition. However, ESMA is of the view that most of these transactions only bear a limited relationship to SFTs and shadow banking. Expanding the scope of reporting to capture such transactions could undermine the purpose of the regulation by collecting large amounts of irrelevant information.

186. The SFTR recital highlights that the Regulation "follows the FSB Policy Framework (...) under which details of SFTs can be efficiently reported". The November 2015 FSB standards for SFT data collection, developed as part of the FSB policy framework, "only focus on margin lending provided to non-retail clients". Therefore, loans to retail clients, including Lombard loans and other forms of private banking, should be exempted from the reporting obligation.

187. Moreover, it has come to ESMA's attention that the "margin lending" SFTR definition may also capture other forms of lending to non-retail clients, including the financing of non-financial corporate clients. While non-financial entities remain within the SFTR scope, transactions related to mergers and acquisitions, corporate

restructuring, investing in infrastructure and other forms of syndicated corporate lending should be exempted from the reporting obligation, due to their limited direct link with shadow banking.

188. Therefore, ESMA is of the view that, consistently with the FSB, the margin lending reporting obligation should only apply to prime brokerage margin lending, i.e. cash lending from prime brokers to their clients against collateral as part of a prime brokerage agreement. The features of prime brokerage margin lending are further described below.

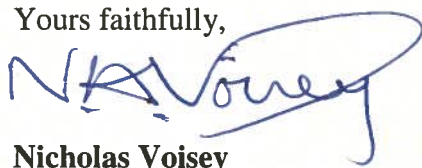
This interpretation of the SFTR is reflected in recital 1 to the draft regulatory technical standard on reporting (page 256 of the final report):

(1) The purpose of Regulation (EU) 2015/2365 is to provide transparency of SFTs. SFTs cover purely financial transactions, the purpose of which is trading of securities, and which are related to liquidity or maturity transformation, functioning of the financial markets and systemic risk. Although a textual interpretation of “margin lending transactions” could cover transactions related to M&A, corporate restructuring or investing in infrastructure, etc., a purposive interpretation of that definition argues against considering those transactions as “margin lending transactions” within the meaning of the SFTR. This is demonstrated by the stated purpose of the Regulation (EU) 2015/2365 in the recitals and by the choice of transactions that are listed as SFTs. Indeed, expanding the scope of reporting of “margin lending transactions” could undermine the purpose of the regulation by collecting an enormous amount of irrelevant information.

As already mentioned, the LMA strongly supports ESMA's conclusions and encourages the Commission to confirm this interpretation and to adopt the technical standards, with their recitals confirming this approach, in the form proposed by ESMA.

Should you have any additional questions or wish to discuss this further, please do not hesitate to contact me by email at Nicholas.Voisey@lma.eu.com or on +44 (0)20 7006 5364.

Yours faithfully,

A handwritten signature in blue ink, appearing to read 'N. Voisey', with a large, sweeping flourish extending from the end of the name.

Nicholas Voisey
Managing Director
Loan Market Association