

Mind the gap!

Peter Moss, CEO of the SmartStream Reference Data Utility (RDU), takes a look at the gap in the MiFID II regulatory reporting framework filled by the Systematic Internaliser Registry, an industry collaboration between a group of APAs and the SmartStream RDU. As well as bringing clarity to the industry in this area, he believes the registry potentially offers buy-side firms commercial advantage through the data it generates.

MiFID II has consumed the financial industry for the last two years. Its introduction has resulted in the generation of a vast amount of new data and this information – which has been created through twenty-eight national regulators and by several hundred registered institutions – is now flowing through the markets.

At the heart of MiFID II, which came into force on January 3rd 2018, lay the desire of regulators to inject greater transparency, notably in the fixed income and OTC derivatives markets. To achieve this end, financial authorities focused on the part played by systematic internalisers (SIs), imposing new pre-trade, post-trade and transaction reporting obligations on this group of firms.

Registering as an SI was, initially, voluntary but from September 1st 2018 it became mandatory for qualifying firms dealing in equities and fixed income. In these areas, financial institutions trading a volume of an instrument or a group of instruments in excess of a limit set by ESMA must now act as a systematic internaliser in that instrument or group of instruments. A breathing space has been given to the OTC derivatives markets, with regulators allowing the voluntary opt-in period for SIs to run until March 1st 2019.

The incoming rules have caught a large number of firms in their net. Prior to September 1st, roughly seventy-five companies had chosen to become SIs. Currently, more than one hundred and thirty firms are signed up with ESMA, although

at the moment perhaps some ninety of these are operating as SIs. By the middle of next year, as many as one hundred and fifty financial institutions are likely to have registered as SIs.

Problematically for the financial sector, the SI regime contained a gap at its core – one which it fell to the industry to fill. MiFID II transparency rules determine that where a counterparty to a deal is an SI in the instrument being traded the SI has the reporting obligation. This leaves firms facing a tricky question – how do they know whether a counterparty is a systematic internaliser or not? Herein lies the difficulty for, while ESMA set up a register of SIs, it did not provide a listing of the instruments for which SIs offer their services.

And the difficulties did not stop there. With no central database of instrument-level listings set up by regulators, Approved Publication Arrangements (APAs), which are responsible for managing trade reporting on behalf of the market, could not operate effectively – it was impossible for APAs to report accurately if they could not understand precisely which companies were acting as systematic internalisers for which instruments.

Stepping into the breach came a group of seven APAs and the SmartStream RDU, which worked in collaboration to create the Systematic Internaliser Registry. The registry is a centralised repository which captures, stores and distributes a listing of SIs and their associated financial instruments.

The SI registry operates by gathering data, on a



“MiFID II transparency rules determine that where a counterparty to a deal is an SI in the instrument being traded the SI has the reporting obligation. This leaves firms facing a tricky question – how do they know whether a counterparty is a systematic internaliser or not?”

Peter Moss, SmartStream

daily basis, from the APAs and their SI customers. Systematic internalisers are able to contribute information in three different formats – ISIN, Issuer, and COFIA. Typically, instrument classification determines which format is most appropriate.

The RDU aggregates this input and, importantly, also validates it, thereby ensuring a high standard of accuracy. The cleaned, consolidated data is then distributed to participating APAs and SIs for use in their regulatory reporting mechanisms. The information can also be made available to other market participants. Distribution takes place via file – either by delta file or in the form of a master file which contains all the active records contributed by SIs – or by API request service. The API, which can be tapped into on demand, is particularly useful for firms which simply wish to access data relevant to specific securities of interest.

At present, the registry collects data from over ninety SIs – a group which constitutes almost all of the larger brokers across Europe. The registry is open to all APAs and SIs and operates on a “give to get” basis, encouraging the broadest possible participation. It offers a reliable, accurate set of listings at a granular, instrument and instrument class level, enabling APAs to report correctly on behalf of SIs, and allowing trading counterparties to identify where they have MiFID II reporting obligations. The registry has brought a much-needed dose of clarity to the industry in this area, and now plays an essential role in supporting the day-to-day process of trading in Europe.

Turning more specifically to the buy-side – the registry gives buy-side participants the ability to understand whether they are required to report or not, and can also potentially help them achieve more cost-effective regulatory compliance. For example, by carefully selecting SIs with which to trade, it may be possible for a buy-side firm to avoid the obligation to trade report.

Importantly, the registry creates a clear picture of who is trading what – in fixed income and OTC it shows which brokers deal in particular instruments – improving the buy-side’s understanding of the markets in which they are doing business. It is a good indicator of best execution capability and points to where liquidity can be found, making it a valuable tool for broker selection, especially in less mainstream products.

Finally, it is worth keeping in mind that the SI Registry is built on very solid foundations – The SmartStream Reference Data Utility (RDU). Set up by the industry, the RDU offers a complete set of reference data for MiFID II compliance purposes, full global coverage of securities reference data for futures and options, and a managed security master service that dramatically simplifies enterprise data management strategy. ■

The SmartStream Reference Data Utility (RDU) is a managed service that delivers complete, accurate and timely reference data for use in critical regulatory reporting, trade processing and risk management operations, dramatically simplifying and reducing unnecessary costs for financial institutions.

The RDU acts as a processing agent for its participants selected data sources; sourcing, validating and cross-referencing data using market best practises so that these processes do not need to be duplicated in every financial institution. An experienced global team, who operate under the compliance frameworks of their customers, deliver data that is fit-for-purpose, consistent and in a format that is specific to the financial institutions’ needs.