

Transaction Reporting Forum

10am-12pm 3 April 2009

1. Data quality

Principally, we use transaction reports to detect and investigate suspected market abuse – insider trading and market manipulation – in support of our statutory objectives of maintaining confidence in financial markets and reducing financial crime. To accomplish this, we rely on the quality of data submitted by the firms. So firms must meet specified standards when reporting transactions to us.

To ensure accuracy and completeness of the data, firms must have appropriate systems and controls to enable them to comply with their regulatory obligations. Moreover, the transaction reporting arrangements within firms should include periodical reviews of transaction reports. So to help firms check their transaction reports have been successfully submitted to us, we encourage firms to request a sample of transaction reports by using the web form available at www.fsa.gov.uk/pages/Doing/Regulated>Returns/mtr/managing/request/index.shtml.

Using this facility as part of the review process will enable firms to compare the transaction reports we receive with the reports they send from their own systems. This exercise should also involve checking the accuracy of the individual data elements included in the transaction reports and their compliance with the guidance issued. If firms identify any errors or failures they should tell us immediately.

For further information on transaction reporting requirements, please see our newsletter, Market Watch Issue No.29 available at <http://www.fsa.gov.uk/pages/Doing/Regulated>Returns/mtr/resources/index.shtml> and all the relevant information available on the relevant part of our website: <http://www.fsa.gov.uk/Pages/Doing/Regulated>Returns/mtr/index.shtml>.

2. Transaction reporting rules and guidelines

The proposed changes to the transaction reporting rules (contained in chapter 5 of CP08/16: Quarterly consultation (No 18) and handbook notice 85) principally affect OTC derivative instruments and were derived following agreements with industry working groups. The major change is a relaxation of the requirements to report OTC derivatives with multiple underlying instruments such as indices or baskets. However, CDSs on single name debt issuers remain firmly in scope.

We do not derive much benefit from reports on OTC index and basket derivatives and we hope that removing this burden will benefit firms. However, in return, we expect firms to improve the quality of transaction reporting and to ensure they have adequate monitoring of this area for abuse and submit STRs as necessary.

In addition to this concession, we are adding three new instrument types.

Firms told us that there are some OTC derivatives that simply cannot be shoehorned into the transaction report, – for example chooser options that have attributes of both put and call options. Since they cannot be accommodated by the traditional option derivative type, we had to create a new type called ‘Complex’. However, this new category must not be treated like a bucket category – it can only be used for truly complex derivatives. We will expect firms to discuss these with us or through one of the industry working groups.

The other two new derivative types are:

- spreadbet on option on an equity, and
- CFD on an option on an equity.

These categories only affect retail firms and have been agreed with the Spreadbetting Association.

Transaction reporting of the new derivatives types will take effect at the same time as reporting of Aii instruments which is expected in late September 2009, but we have already stated that we would not take action against firms that immediately ceased reporting OTC index/basket derivatives (see MarketWatch 29).

We are drafting a new version of the Transaction Reporting User Pack (TRUP). The first version was published before the implementation of MiFID. The new version will contain guidelines on the reporting of transactions in on exchange derivatives and guidelines on how to use the new derivative type classifications etc. We are currently reviewing scenarios drafted by a sub group of the OTC derivatives working group that relate to transactions in on exchange derivatives. We will use this to complete the relevant section of the TRUP.

3. AII project

We have seven Approved Reporting Mechanisms (“ARM”); Xtrakter, TRS, Credit Suisse, London Stock Exchange, Omgeo, Euroclear, and Virt-X/SWX. Of the seven listed ARMs we can confirm that four ARMs are intending to collect and submit AII Transaction Reports; Xtrakter, TRS, Credit Suisse, and London Stock Exchange. These ARMs and Omgeo have also confirmed that they will collect and submit OTC complex derivative types K, Q, and Y (OTC KQY).

We are working with each of the ARMs to prepare for implementation, currently focusing on preparation for the upcoming AII and OTC KQY industry testing phase. The key objective of industry testing is to validate that AII and OTC KQY transaction reports can be successfully submitted from the industry to the ARMs and through to us for processing.

We scheduled a testing seminar with the ARMs on Wednesday 1 April but due to the G20 Summit the meeting was postponed until Wednesday 8 April. The purpose of the seminar was to walk through and agree the Industry Test Approach and Plan with the ARMs. We now expect your member ARM will be in a better position to provide you with clarity regarding your participation in industry testing.

We have formed an Aii implementation working group supported by the BBA and the FOA. The aim of this group is to provide a forum in which we and the industry can monitor the preparations for Aii implementation and highlight areas where further clarity is needed. Through this forum we will shortly be issuing a brief survey to firms, ARMs and system vendors to assess their degree of readiness for Aii implementation. This will help us to finalise the implementation deadline and to assess the number of transaction reports we are likely to receive.

If you have any further questions please see our website where we have published a list of frequently asked questions, direct your queries to your member ARM, who will answer your question directly or contact us for further clarification

4. European developments in transaction reporting

CESR Tech

The CESR Tech Group was formed to determine and implement the technical solutions required to facilitate CESR Directives – notably MiFID.

One major success of CESR Tech was the delivery of the Transaction Reporting Exchange Mechanism (TREM) within budget and on time. This allows competent authorities (CAs) within the EEA to route transaction reports to other CAs as required by MiFID – ie to the home state authority of a branch and to the relevant competent authority for any particular instrument.

CESR Tech is also responsible for agreeing many of the standards used for many of the reporting fields such as BICs and ISINs and for negotiations with the industry on new standards such as the Aii code.

CESR TREM User Group

Since November, MiFID has required us to send certain transaction reports to other EEA competent authorities via CESR's Transaction Reporting Exchange Mechanism (TREM). Where the reporting firm is a branch of a non-UK EEA firm we send the transaction report to the home competent authority. Where we are not the most relevant CA for the financial instrument that is the subject of the transaction report we send the transaction report to the most relevant CA. Each month the CESR TREM User Group meet to discuss data quality issues related to the exchange of transaction reports. The other CAs also use transaction reports for market abuse monitoring so accurate reporting is also key to them.

The work of this group is continuing – in particular, the group is designing metrics to measure the quality of data being exchanged through the TREM.

CESR Tech and instrument reference data

Another project CESR Tech is currently undertaking is the exchange of reference data between authorities. As you are aware, many of the reference data items associated with an instrument ISIN are not collected through a transaction report. We currently collect this data from a data vendor. From now on, all CAs will be responsible for collecting reference data for MiFID instruments from the exchanges they supervise. So we are currently arranging to receive this data on an ongoing basis from the LSE, EDX, Liffe and PLUS Markets.

This reference data will then be sent to CESR, who will then rationalise the data sent by all the CAs and send a consolidated file of reference data covering all exchanges within CESR to every CA. This will allow every CA to understand the transaction reports they receive and enable them to correctly route reports to the relevant competent authorities rather than rely on the current proxy. CESR aims to go live with this project by mid-June 2009.

CESR Tech OTC derivatives working group

We have gone beyond the MiFID transaction reporting requirements by including reports of transactions in OTC derivatives whose value was dependent upon an instrument admitted to trading on a regulated or prescribed market. These OTC derivatives are caught within the Market Abuse Regime and the attractions of these instruments can be demonstrated by the fact that they often feature in our market abuse investigations. So it would be irresponsible of us not to collect transaction reports for these instruments. Many of the other CESR CAs have now also realised the risks to the integrity of their markets presented by the use of OTC derivatives. As a result, three other CAs already collect OTC derivatives transaction reports and many other CAs intend to start collecting them.

We have championed the collection of OTC transaction reports within CESR and has prompted CESR Tech to set up a working group to design a mechanism to exchange these reports based on the same principles of relevant competent authority and home competent authority that govern the exchange of MiFID transaction reports.

CESR launched a Call for Evidence to collect views on the standards that may be required for identify every OTC derivative issue and to classify each derivative type. While we are very keen to help the detection of market abuse across Europe through the exchange of OTC derivative transaction reports, we remain mindful of the need to prevent additional costs to the UK industry by any change to the standards. While CESR is keen to promote international standards, we are optimistic that our work in the CESR Tech groups will enable us to exchange OTC derivative reports with minimal impact on our firms.

The exchange of OTC derivative transaction reports by CAs will begin on a voluntary basis. Around half of the CESR CAs want to be included in the first phase of the project which is expected to go live some time in 2010.

Review of the scope of the MiFID transaction reporting requirement

In May 2007, CESR published level three guidance on MiFID transaction reporting. Part of this guidance attempted to determine a harmonised definition of execution of a transaction for transaction reporting purposes. Many compromises had to be made to achieve an agreement between the CAs and the resultant guidance did not meet its aim of helping create harmonised transaction reporting rules across CESR. So a new Call for Evidence on the definition of a transaction was launched and the MiFID Markets Sub Group was tasked with producing a consultation paper with new guidance. As well as agreeing on the definition of execution of a transaction, the group will also attempt to agree on standardising the requirements for counterparty and client identifiers and may address associated issues such as whether portfolio managers are required to transaction report.

The group still has some difficulties in reaching agreements on these issues due to the divergence of market practices across CESR. Also, CAs that have implemented client identifiers do not wish to lose the advantage this affords them in detecting market abuse whilst some CAs that have not implemented client identifiers are deeply concerned about the costs involved in implementing them. The group is making progress, but still has some difficult discussions ahead.

MiFid Article 57

MIFID provides that a competent authority of one Member State may request the cooperation of the competent authority in another Member State in a supervisory activity or for an investigation (see Article 57 – Art 57). This also provides that in the case of investment firms that are remote members of a regulated market, the competent authority of the regulated market may choose to address the firms directly, in which event the requesting authority should inform the competent authority of the home Member State of the remote member.

Our approach to Art 57, outlined in our Policy Statement PS07/2 was that its discretionary power related only to remote members of regulated markets and only to matters concerning the supervision of those markets. Our view at that time was that the competent authority of the regulated market may not approach the remote members of that market for the purpose of the general supervision of those members.

We have since changed our approach following a consensus view reached by the CESR Chairs that the scope of direct approaches to remote members under Art 57 extends to both the supervision of regulated markets and to market abuse enquiries. In light of the decision of the CESR Chairs, we now encourage firms operating as remote members to comply with direct requests by the relevant competent authorities

Some firms have expressed concerns regarding the processing of direct requests from overseas authorities. We have proposed to the BBA and to CESR-Pol the adoption of a common format to data requests, which would facilitate the making of, and handling of, requests.

We are also aware that some firms have concerns that their client confidentiality obligations prevent them from providing client information unless required by law to do so. In practical terms, this means that some firms are unwilling to respond to direct requests, although they are willing to provide the information to us to pass on to the overseas regulators, subject to the exercise of our statutory powers under FSMA. We are continuing to act as an intermediary between the firms and the overseas regulators to resolve this issue.

5. BBA (Presentation by Ross Barrett – Policy Director of Capital Markets at BBA)

- BBA / Xtrakter are lead trade association liaising with us on transaction reporting.
- Very successful outcome on MiFID switch-over as a result of coordinated FSA-industry discussions considering complications and short-time span.
- Continuing dialogue over AII – FSA has done good work.
- BBA leads three working groups:
 - Industry Transaction Reporting Working Group;
 - TRUP Working Group; and
 - Complex Derivatives Working Group.
- TRUP WG
 - Addition of very helpful explanatory guidance.
- Complex Derivatives WG:
 - carve out of multiple underlyings;
 - addition of instrument types; and
 - avoidance of unnecessary cost.