

The Markets in Financial Instruments Directive II (MiFID II) and Markets in Financial Instruments Regulation (MiFIR) impose a new framework for EU financial services that is hugely prescriptive in respect of how business can be conducted and adds significantly more layers of transaction reporting complexity.

The range and reach of new reporting obligations are a major headache for operations and compliance teams when precious internal resources – people and capital – are also focused on a host of market conduct rules affecting client servicing and fair and transparent trade execution that go beyond MiFID II, such as Market Abuse Regulation.

Transaction reporting compliance with MiFID II/MiFIR requires eligible firms to identify all transactions subject to new rules and to deploy an efficient process workflow to satisfy the obligation to report details of transactions to local regulators “as soon as possible” and no later than T+1. Regulators have indicated that they will take a very dim view of firms that fail to report in the prescribed manner at ‘go live’, with those that fail to comply facing severe financial penalties and reputational risk.

Although the new date for MiFID II/MiFIR compliance may seem a long way off, delaying action now in the hope that this headache will go away is not an option. In addition, the [EMIR Rewrite](#) is likely to come into force before MiFID II, with its own set of transaction reporting challenges. Furthermore, regulators are clear that they expect to see progress now by reporting firms in the implementation of appropriate processes to comply with new regulatory obligations at go live.

## Who needs to report under MiFID II/MiFIR?

It might be simpler to list who *doesn't* need to report. Firms that have been authorised solely as Alternative Investment Fund Managers (AIFMs) under the Alternative Investment Fund Managers Directive (AIFMD) and firms authorised as UCITS management companies under UCITS Directives fall outside of the scope of MiFID II when carrying out the activity of managing (or marketing) the funds for which they act. With few exceptions, however, MiFID II and MiFIR reporting obligations apply to [all investment firms](#) including:

- Investment managers providing advice and portfolio management to individual clients (e.g. managed accounts)
- Credit institutions
- Market operators, including any trading venues
- All financial counterparties under EMIR
- All non-financial counterparties falling under Article 10(1)(b) of EMIR
- Central Counterparties (CCPs) and persons with proprietary rights to benchmarks
- Third-country firms providing investment services or activities within the EU

MiFID reporting obligations extend beyond EU/EEA borders and apply to:

- Any derivative traded outside of the EU where the underlying instrument is traded on an EU trading venue must be reported.
- Any offshore firm giving execution instructions to an EU broker will have to provide a Legal Entity Identifier (LEI).
- Firms executing orders ‘offshore’ for dual listed instruments for an EU-based decision maker may have to provide an LEI to submit trade reports to the EU entity - and in a format compatible with that entity’s own transaction reporting process.

## What must be reported?

Not only do more parties have to report, they have to report more information about more transactions. MiFID II expands the range of financial instruments that have to be reported to pretty much **every tradeable instrument and derivative of an instrument** including:

- Financial instruments admitted to trading or traded on an EU trading venue and to all financial instruments where the underlying instrument is traded on a trading venue. “Trading venues” include Multilateral Trading Facilities (MTF) and Organised Trading Facilities (OTF), the likely home for OTC derivatives subject to the trading obligation.
- Financial instruments where the underlying instrument is traded on a trading venue. This essentially widens the scope to capture all OTC transactions in such instruments.
- Financial instruments where the underlying is an index or a basket composed of instruments traded on a trading venue. This means that just one component of either an index or basket will bring that financial instrument under the reporting obligation.

Furthermore, firms must provide details of any trade execution that changes a firm’s or its clients’ positions in a given product; MiFIR, MiFID II’s companion regulation, imposes additional and specific reporting obligations relating to equity execution quality and commodities positions.

### Snapshot – Validations and New Reportable Indicators

#### *Validations based on Trading Capacity*

- Executing entity can’t reappear as Buyer or Seller for AOTC or MTCH capacity
- Executing entity must appear as either Buyer or Seller for DEAL capacity
- Transmitting Firm ID can only be completed where capacity = AOTC

#### *New Reportable Indicators*

- Linked trade ID for legs of complex deals
- Short sale indicator where disclosed by ultimate seller
- Waiver flag for counterparty directly facing exchange
- Exchange trade reference for on-exchange counterparty
- Increase and reduction of position flag
- Transmission of order indicator

Retail derivatives firms are impacted significantly by new rules and will be consulting their lawyers to see if they need to become an **Organised Trading Facility (OTF) or Systematic Internaliser (SI)**. If either of these states applies, those firms will become subject to most of the rules applying to major regulated markets, including pre and post-trade transparency requirements, the obligation to apply ISIN references to all traded products and to supply reference data to regulators each day, as well as to report transactions by T+1 along with all other market participants. SIs will also need to ensure continuous, public, two-way pricing at all times, likely facilitated by an APA (Authorised Publication Arrangement).

### Snapshot - RTS 22 Article 15: Methods and Arrangements for Reporting Financial Transactions

#### *Regulated Requirements include:*

- Mechanisms for identifying errors and omissions
- Mechanisms to avoid duplicate reports
- Ensuring transaction reporting reflects all changes in position of firm and clients

#### *New emphasis on:*

- Reporting process testing
- Regular reconciliation (from front office re: timing, accuracy, completeness)

## Consolidation and disclosure of trading data under MiFIR

In the continuing quest for best execution and market transparency, MiFIR introduces new rules around timely public disclosure of transaction data. Data must be disseminated by one of three [authorised Data Reporting Service Provider \(DRSP\)](#) channels:

- **ARMs (Approved Reporting Mechanisms)** remain substantially the same in concept as those authorised by the FCA under MiFID I, although they pick up certain additional obligations and organisational requirements.
- **Consolidated Tape Providers (CTPs)** are self-explanatory (although to date no organisation has put itself forward to assume this particular mantle).
- **APAs** require most explanation and play a much more significant role than current Trade Data Monitors (TDMs), mainly because of the vastly increased number of products which will become trade-reportable. Every investment firm and Systematic Internaliser trading a bespoke product on its own books will have to appoint an APA to make trade details available in (quasi) real-time on a reasonable commercial basis (think of it like a regulated stock price ticker), make the information public (through the APA platform), and supply the data to authorised CTPs. (Although the identity of originating firms will not be made public, each trade will be given an individual reference by the APA to facilitate enquiries from firms and their regulators).

## Significantly greater reference data burden

A key element of MiFID II's focus on data quality is the breadth of reference data that firms will be obliged to obtain, maintain and use to report transactions.

- **LEI required before providing client services**  
It is no surprise that the **LEI**, which caused so much pain when it was introduced under EMIR, is reinforced under MiFIR as the standard for identifying corporate entities. What is new and explicit in MiFIR [Regulatory Technical Standards](#), however, is the requirement that "investment firms obtain clients' LEIs from clients before providing services which would trigger reporting obligations in respect of transactions effected on behalf of those clients" (RTS 22(13)). This may prove particularly troublesome for firms offering services to non-EEA clients that have been, to date, somewhat reluctant to provide them (LEIs).

### Snapshot - Migration to ISIN from Aii

- Simultaneous database changes for MiFIR and EMIR
- Determining non-EEA derivatives with underlying EEA listings
- Receipt and use of ESMA "golden list"
- Validation against prior day list per L3 – validating trades in new listings
- "Equivalence" rules for bilateral contracts to use traded ISINs

- **National/Individual person identifiers for investment decisions/trade execution**

The new requirement for additional identifiers (e.g. National Insurance Number in the UK) to identify individuals (natural persons) within transaction messages is also potentially problematic. As well as having to enhance client onboarding processes to collect customer identifiers (LEIs), investment firms must now also take a feed from internal HR systems to incorporate many (and different) national identifiers for individual employees identified as responsible for each investment decision/trade execution.

### Snapshot - National Identifiers

- Client and internal identifiers
- **CONCAT** construction for individuals only primary designation in 5 jurisdictions
- Plan to ensure data capture
  - Appropriate internal data capture/control
  - Secured data storage
  - Control model developed in-line with ESMA/FCA and legal requirements

- *Alternative Instrument Identifier (Aii) replaced by original ISIN standard*

The biggest surprise in terms of reference data has been the overhaul of product identifiers. The [Aii](#), which took four years to implement under MiFiD and was taken up subsequently by EMIR for exchange-traded derivatives, has been discarded in favour of the 'legacy' ISIN standard.

Instruments that don't have an ISIN in their own right, or are not listed in the 'official' [ESMA list](#) when it is published, will require up to 15 additional fields of description and categorisation to be associated with them, including a 'complete and accurate' [CFI code](#).

While the July 2015 update to ISO 10962 (Standard for CFI Codes) is a comprehensive categorisation of financial instruments, firms may still struggle to find 'complete and accurate' codes for new and/or bespoke products, like CFDs based on bond futures, for example, and commodity-based spread bets.

Similarly, while the 'underlying instrument' field for OTC derivatives must be populated with an ISIN value, not all instruments currently in scope as reportable will have a readily identifiable ISIN (e.g. CFDs on currency pairs listed currently on at least one MTF).

As such, reporting firms and trading venues have to resolve the conundrum of reporting on a myriad of (now) reportable transactions to comply with regulatory reporting timelines without knowing exactly how to report them - and in the absence, potentially, of 'complete and accurate' CFI codes and /or underlying ISIN values at the time they must be reported.

### Snapshot – ISIN and non-ISIN products

- Ability to obtain new ISINs for certain product classes in good time
- Potential for ISIN re-use to become common
- Potential for multiple ISINs for fungible products

#### *Non-ISIN products:*

- Is there an underlying product on the ESMA list (e.g. FX CFDs)?
- "Limbo" proposal for pending underlying validation response (7 days)
- Possible multiple underlying ISINs (e.g. basket trades)
- Determination of accurate and complete CFI code
- Complex field validation based on CFI code

**Given all of these challenges, it is hardly surprising that impending regulatory reporting obligations tax the imagination (and try the patience) of even the most experienced operations teams.**

### Avoid a regulatory reporting migraine – get it right first time

Understanding and managing the complexity of new reporting obligations under MiFiD II/MiFiR and with the proposed **EMIR Rewrite** and other evolving regulatory frameworks like [SFTR](#) thrown into the mix, presents an enormous challenge to all reporting firms and particularly those entities that find themselves subject for the first time to new regulatory reporting obligations.

Eligible firms must determine whether they have sufficient expertise to evaluate evolving reporting requirements effectively themselves and the right resources to expand or adapt internal systems and processes to deploy an effective and compliant solution to multi-regime, multi-jurisdiction transaction reporting obligations.

Alternatively, firms may choose to partner with an external service provider focused exclusively on understanding and managing the impact of regulatory change on transaction reporting processes, and to manage end-to-end reporting processes for multiple regulatory regimes and reporting destinations.

Abide Financial's **PROXIMITY** programme helps reporting parties to manage the challenge of MiFID II/MiFIR, EMIR Rewrite and other regulatory reporting obligations, combining a systematic and guided approach to meeting regulatory reporting timelines with an established, end-to-end implementation, technology, operations and compliance ecosystem.

In essence, we tell you what you need to do (to comply), do it for you (taking and transforming reportable trade data to meet all regulatory obligations), then tell you what we've done (tailored client reporting).

Clients benefit from a fully managed process that takes the pain – and effort - out of untangling the complex web of diverse (and changing) reporting requirements and mitigates the risk of reporting failure as new rules come in to effect.

### Why PROXIMITY?

- **Experience** – knowledge gained from extensive EMIR and MiFID I client onboarding
- **Expertise** – implementation of complex, multi regime reporting requirements
- **Efficiency** - optimised operational resources; reduced cost of compliance
- **Guidance** - managing operational, compliance and technology risk across reporting regimes
- **Infrastructure** – proven reporting environment and end-to-end processes

The starting point of every Abide engagement is a no-obligation consultation with a transaction reporting specialist and free 'regulatory health check'. Contact us now for an in depth conversation about preparing for MiFID II, EMIR and other regulatory reporting challenges.

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