MiFID II - Transaction Reporting

Transaction reporting is an important part of the existing MiFID framework and is also integral to regulators' ability to monitor market abuse in capital markets. In essence, transaction reporting is the mechanism by which investment firms provide reports to regulators, containing trade details of each transaction they execute, no later than close of business the following day. Transaction reporting under MiFID I was primarily an issue for sell-side firms, such as brokers and dealers, who report transactions for their clients.

Regulators across Europe have focused on the quality of transaction reporting to varying degrees with both the Central Bank of Ireland and the UK's Financial Conduct Authority, being among the most active in this regard. This is evidenced by the substantial number of enforcement actions that have been taken for transaction reporting infringements. The significance of these fines and the number of entities sanctioned for erroneous or incomplete transaction reports, demonstrates both the complexity and the regulatory risk associated with transaction reporting.

It is interesting therefore that industry commentators have referred to the transaction reporting requirements under MiFID as a "walk in the park" compared to the upcoming requirements under Article 26 of MiFIR and delegated regulation 4733 of 14 July 2016 (RTS 22). Under the new framework, the scope of transaction reporting has broadened considerably. There are four main reasons for this:

Transaction reporting will now also become the responsibility of the counterparty who initiates the transaction, typically buy-side firms, as under MiFIR all investment firms have responsibility for ensuring transaction reporting information for their firm is accurate.

Firms can no longer simply rely on a broker or trading venue to complete transaction reporting on their behalf without having adequate oversight of these arrangements. Also branches of third country firms will have to submit transaction reports to the regulator which authorised the branch.

	MiFID I	MIFID II
Reportable products	Equities and some equity exchange traded derivatives	Virtually all instruments traded on European venues, including non-EU derivative instruments that relate to an EU security or index
Venues	All products traded on European regulated markets (RMs) and organised trading facilities (OTFs)	All products traded on European RMs, OTFs and multilateral trading facilities (MTFs)
Data fields	24 data fields	65 data fields (new data required includes detailed data to identify buyer and seller including traders and decision makers, more detailed information on the traded instruments and a number of indicators that put a trade in a specific context such as the use of waivers or short selling)
Reportable transactions	Purchase and selling of instruments	Reportable transactions include increases and decreases of notional amounts and the exercise of options, warrants or convertibles

Impact on buy-side investment firms

Buy-side firms that currently do not conduct transaction reporting will need to consider how best they can meet the requirements under MiFID II.

- They can either report themselves if they have the capability to do so; or
- They can delegate the reporting to a relevant party once they have appropriate governance arrangements in place to oversee the activity. Many European regulators have made it abundantly clear that there will be no tolerance for poor quality transaction reports, whether the result of under-, over- or simply incorrect reporting. Against that background, it is probably not surprising that firms may be cautious about outsourcing transaction reporting to a third party provider.
- Buy side firms also have another way to report transactions under MiFID II – they can transmit their transactions to another investment firm who will then report the transactions on their behalf – so-called RTOs (Reception and Transmission of Orders). As the regulatory burden to report will be on the second investment firm, they will usually only take on this added risk for adequate compensation and so this option could prove to be a costly alternative for buy-side firms.

What if you already submit transaction reports?

Firms who are already submitting transaction reports will need to assess their current systems to see if they are "fit for purpose" for MiFID II, to establish if the additional data that must be reported can be readily obtained. The new data that must be reported includes:

- Flagging of particular types of trades such as short sells. This will require front-office traders to indicate the type of trade and the existence of a system able to capture that information and populate the relevant field on the executed transaction report;
- End client data: Legal Entity Provider (LEI) - if relevant - or the name and date of birth if a natural person; and
- Decision maker: LEI (if relevant) or the name and date of birth if a natural person.

Data Management – Protection and Security

As sensitive information concerning personal details of staff and clients will need to be transferred to regulators and potentially third party firms (depending on any outsourcing arrangements in place), investment firms will have to review local rules regarding data protection and data security as well as considering the new rules, coming into force on 25 May 2018, under the European General Data Protection Regulation (GDPR).

Given the various types of data that needs to be captured, stored and reported as part of transaction reporting requirements and record-keeping of orders, firms will need to consider end-to-end data needs and whether a centralised data repository is required.

Currently under MiFID I there are different national rules that may bring other types of financial instruments within the scope of transaction reporting, such as collective investment schemes. Firms operating in different jurisdictions will need to address any local variations, which may still exist after MiFID II comes into effect.

The requirements regarding transaction reporting are among the most complex within the entire MiFID II package not only because of the technical nature of the requirements but also because firms will have to put a powerful IT solution in place. This IT system will require seamless collaboration between regulatory and IT specialists as well as the firm's project management team to ensure compliance with the requirements from the outset. The first transaction report must be submitted to national regulators on 4 January 2018 by close of business – one working day after MiFID II actually comes into effect.

Non-standard data

The fundamental challenge of transaction reporting is data management. Data management issues are also integral to many of the other new requirements such as best execution or reporting of costs to clients. While the data for these requirements may prove difficult to access, it is prescriptively set out.

That, however, is not the case for target market information in the context of product governance requirements, which is non-standard and bespoke to each firm. Consequently firms are facing the additional challenge of having to compile and manage considerable amounts of non-standard data.

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Produced by: KPMG's Creative Services. Publication Date: 2017. (2526)