MONITORING THE QUALITY OF TRANSACTION REPORTS RECEIVED UNDER ARTICLE 26 OF MIFIR

This press release relates to the obligation for credit institutions and investment firms to report transactions in financial instruments as set out in Article 26 of MiFIR. It informs on the number of reporting entities as well as the number of reports received by the CSSF in 2019 and aims more particularly to inform all reporting entities on the quality and completeness campaigns that the CSSF conducted during the years 2018 and 2019 as well as to announce the topics that will be the subject of dedicated campaigns during the year 2020.

In this press release, references to a specific “Field” refer to the fields in Table 2 of Annex I of Commission Delegated Regulation (EU) 2017/590 (“RTS 22”).

Entities within the scope of the transaction reporting obligation

In accordance with Article 1(2) of MiFIR, the obligation to report transactions in financial instruments to the CSSF applies to credit institutions and investment firms incorporated under Luxembourg law as well as to branches of third country firms authorised in Luxembourg (together referred to hereunder as “Investment Firms”).

As of 1 January 2020, the CSSF has registered 128 Investment Firms that submit transaction reports to the CSSF either directly or via an approved reporting mechanism (“ARM”). During 2019, 22,221,230 reports (including cancellations and corrections) have been submitted by the aforementioned Investment Firms to the CSSF via the system set up to this end.

1. Main observations and recommendations issued in 2018 and 2019

Since the entry into force on 3 January 2018 of the new reporting format under MiFIR, the CSSF is monitoring the quality of the transaction reporting data. During the last two years, the CSSF not only carried out the standardised quality tests developed together with the other competent authorities and ESMA, but also conducted a series of data completeness and quality enhancement campaigns with a focus on the different topics listed below.

Entities in scope

Before the entry into force of MiFIR in January 2018, all Investment Firms were asked to inform the CSSF whether or not they are subject to the transaction reporting obligation under Article 26 of MiFIR as provided for in Circular CSSF 17/674. Since the new rules came into force, every new Investment Firm is asked to inform the CSSF whether it is required to report transactions under Article 26 of MiFIR or not.

In 2019, the CSSF added an additional validation rule to its reporting system that rejects reports citing executing entities that did not notify the CSSF before submitting their first transaction reports. Before the implementation of this rule, the CSSF received transaction reports from various ARMs citing as executing entities Investment Firms that had, however, informed the CSSF that they were not subject to the transaction reporting obligation of Article 26 of MiFIR. In this context, the CSSF noted that several concerned Investment Firms did not differentiate between the possibility of transmission as offered by Article 4 of RTS 22 and the outsourcing of their reporting obligation or that there were misunderstandings between the receiving entity and the entity transmitting the order. Ultimately, the Investment Firms listed as executing entities were not aware that the CSSF received reports in their name and had to review the agreements they had with their counterparties.

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Given that several of these cases of misunderstanding were linked to receiving entities located in third countries, the CSSF wants to highlight that the transmission possibility provided by Article 4 of RTS 22 is only
given on condition that the receiving entity is itself subject to Article 26 of MiFIR and that it is therefore not possible to make use of this possibility if the receiving entity is located in a third country i.e. in a country which is not part of the European Economic Area.

Completeness of reporting

Towards the end of 2018, Investment Firms that had notified the CSSF that they are subject to transaction reporting requirements were provided with a global overview on the number of accepted and not cancelled transaction reports received by the CSSF on their behalf. They were asked to verify that those figures are consistent with the number of transaction reports that they have submitted to the CSSF, and to rectify the situation by back-reporting missing transaction reports if necessary.

In this context, the CSSF wants to remind, regardless of the mechanism chosen to report transactions, that Investment Firms need to ensure that they have access to the data that is transmitted on their behalf to the CSSF as well as to the feedback files generated by the CSSF in order to be able to solve any problems that may arise. This access to the relevant data is important considering that ultimately the Investment Firm, whether alone or together with an ARM, is responsible for the transaction reports citing itself as executing entity.

In this context, it should be noted that Article 15 of RTS 22 requires that the methods and arrangements by which transaction reports are generated and submitted by Investment Firms shall include among others:

- mechanisms for identifying errors and omissions within transaction reports;
- precautionary measures to enable the timely resumption of reporting in the case of a failure of the reporting system;
- mechanisms for identifying unreported transactions.

The CSSF noticed that in some cases, it took Investment Firms a long time to compare the data made available to them by the CSSF with their own databases. In this context, the CSSF would like to stress that Investment Firms are required to ensure an impeccable follow-up of their transaction reports and that, in the context of a new similar campaign, Investment Firms shall be able to respond to the CSSF’s requests within the required timeframe.

Missing LEI codes

According to Article 26(6) of MiFIR and RTS 22, legal entities mentioned in the transaction reports must be identified with their respective Legal Entity Identifier ("LEI"). In order to inform reporting entities of this requirement, following two press releases were issued:

- 12/10/2017 Mandatory use of legal entity identifier (LEI) under MiFID II/MiFIR and EMIR
- 26/11/2017 MiFID II/MiFIR: Mandatory LEI for transaction reporting

To support a smooth implementation of the LEI requirements under MiFIR, ESMA allowed for a temporary period of six months during which Investment Firms were permitted to provide a service triggering the obligation to submit a transaction report to clients from whom they did not previously obtain an LEI code, provided that before the provision of the service the Investment Firm obtained the necessary documentation from the client to apply for an LEI code on his behalf.

In this context, the CSSF has implemented validation rules controlling the validity of the LEI codes provided in the transaction reports submitted by the Investment Firms. As a result, for transactions executed after 3 July 2018, transaction reports containing LEI codes that are not valid on the trade date are systematically and automatically rejected by the CSSF systems.

For this reason, Investment Firms were asked to put in place measures to prevent that transactions may be executed for any legal entities not possessing a valid LEI code. Even if the number of rejections in relation to incorrect LEI codes has constantly decreased, the CSSF reminds Investment Firms that they are not allowed to execute a reportable transaction on behalf of a legal entity not possessing a valid LEI since they will in such case not be able to fulfil their reporting obligation and thus fail to comply with the requirements of Article 26 of MiFIR.
UTC (Coordinated Universal Time)

In the context of data quality tests performed on transaction reports, the CSSF identified that in several transaction reports the time indicated in field 28 “Trading date time” was the local time instead of UTC. Investment Firms have been informed that, within the framework of the transaction reporting obligation, dates and times shall always be reported in UTC.

Execution of a transaction on a trading venue (Field 36 “Venue”)

In April 2019, the CSSF carried out a test to ensure that field 36 “Venue” (“Field 36”) was correctly populated in all the transaction reports submitted to the CSSF.

This review has shown that several Investment Firms have sent inaccurate transaction reports mentioning a trading venue (regulated market, MTF, OTF) in Field 36, where they could not be considered as having executed the transactions on a trading venue i.e. as direct market facing entity. Section 5.4. of the ESMA Guidelines on transaction reporting (ESMA/2016/1452), transposed into the Luxembourg regulatory framework via Circular CSSF 17/674, provides more guidance regarding the entry of Field 36, in particular as to when a transaction should be considered to be executed on a trading venue and when the MIC code of the venue should be included in the transaction reports. The same section also states that in case the Investment Firm is not the direct market facing entity, it is not regarded as executing on a trading venue for the purposes of transaction reporting. It is further specified that where the transaction was executed on a trading venue, with a systematic internaliser (“SI”) or on an organised trading platform outside of the Union, Field 36 of the market side report should be populated with the MIC code of the venue, trading platform or SI. All other reports in the transaction chain should be populated with ‘XOFF’.

Given the direct relationship between Field 36 and field 3 “Trading venue transaction identification code”, Investment Firms were also reminded that transaction reports in which Field 36 cites a trading venue (regulated market, MTF, OTF) shall include the trading venue transaction identification code in case it has been disseminated to them by the trading venue operator.

2. Prospects for the 2020 campaign

The quality campaign for the year 2020 will follow an approach similar to the one of the preceding two years. In order to continuously enhance the quality of transaction reports submitted to it, the CSSF will continue to perform the quality tests as defined by ESMA, check the general quality of the reports submitted by certain selected entities and put a particular focus on the specific points listed below.

Trading capacity (Field 29)

As set out in RTS 22, there are three different trading capacities that may be reported: “dealing on own account”, “matched principal” and “any other capacity”. The reported trading capacity should reflect the capacity in which the Investment Firm actually traded and should be consistent with the rest of the information in the Investment Firm’s transaction report. In particular:

- Where an Investment Firm is “dealing on own account” (DEAL), it shall be reported as the executing entity in field 4 “Executing entity identification code” (“Field 4”) in the transaction report and shall be either reported as the buyer or seller. In return, where an Investment Firm is dealing in a “matched principal trading” capacity (MTCH) or in an “any other trading capacity” (AOTC), it shall be reported as the executing entity in Field 4 in the transaction report and shall not be reported as the buyer or seller.

- Where an Investment Firm is “dealing on own account” or on a “matched principal trading capacity”, field 25 “Transmission of order indicator” should be populated with ‘false’.

The CSSF will contact the Investment Firms whose transaction reports are not in line with the aforementioned requirements.
Transmission of an order pursuant to Article 4 of RTS 22

Following Article 3(2) of RTS 22 an Investment Firm shall not be deemed to have executed a transaction where it has transmitted an order in accordance with Article 4 of RTS 22 and is therefore no longer obliged to submit a transaction report under Article 26 of MiFIR. The conditions to be met for transmitting orders pursuant to Article 4 of RTS 22 are outlined in the first paragraph, points (a) – (c) of the said Article.

For the review, special focus will be put on Investment Firms who declared to transmit orders pursuant to Article 4 of RTS 22, but whose Legal Entity Identifier (“LEI”) can be found within the buyer or seller field (field 7 or 16 respectively) of another Investment Firm’s transaction reports. The CSSF will contact these Investment Firms that have argued on the basis of Articles 3 and 4 of RTS 22 that they no longer have to submit transaction reports themselves and require them to provide a copy of the transmission agreements duly signed between themselves and the receiving entities as well as a sample of transactions for which this possibility of transmission has been claimed. On the basis of these samples, it will be verified whether the receiving entities submit correct transaction reports to the CSSF.

Late reporting

Pursuant to Article 26(1) of MiFIR, Investment Firms shall submit transaction reports to the CSSF as soon as possible and no later than the close of the working day following the transaction execution day. In order to further reduce late transaction reporting, and taking into account that the IT systems set up under MiFIR should be stabilised two years after their implementation, the CSSF will require submissions that meet the deadlines set by MiFIR.

Partial executions

In a transaction chain, without transmission, the way in which Investment Firms that are not direct market facing report transactions depends on how their counterparty confirms the executions. In case direct market facing entities decide to report all partial executions in “matched principal” or “any other capacity” trading capacity, they are required to confirm them in the same way to their counterparties which must therefore also submit transaction reports for each partial execution. If on the other hand market facing entities group the partial executions by passing them through their own accounts and reporting to their competent authority on the one hand all the partial executions and on the other hand the grouped transaction, all citing as trading capacity “DEAL”, the Investment Firm representing the next link in this transaction chain will only have to report the grouped execution which has been confirmed to it by its counterparty.

If Investment Firms do not respect this logic, authorities cannot reconstruct the transaction chains and determine the final buyer and seller behind a specific execution. Investment Firms that receive the details of the partial executions as well as a total confirmation of their orders will be asked to clarify this point with their counterparties in order to know what information is to be declared within the framework of Article 26 of MiFIR.

3. Monitoring to be ensured

For some of the 2018 and 2019 campaigns documented above, only a limited number of Investment Firms were contacted. Therefore, the CSSF asks all Investment Firms to review without delay whether their systems are in compliance with the points raised in Section 1 above. If in that context an Investment Firm notices that its reporting system does not comply with one of these points, it shall contact the CSSF as soon as possible in order to define a reasonable timeframe to bring its system into compliance. As far as the points announced for 2020 are concerned, the CSSF strongly encourages Investment Firms to review straight away whether their systems comply with the rules and to notify the CSSF without delay if any errors are detected. Such a proactive approach by Investment Firms will be considered as a positive element in the assessment of each individual case and in the decision of the enforcement actions that may be taken by the CSSF.

Luxembourg, 12 February 2020