

Market Watch

Markets Division: Newsletter on Market Conduct and Transaction Reporting Issues

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Finalised guidance for reporting of transactions on Turquoise Derivatives

As notified in Market Watch 40, on 1 May 2011, EDX London, a Recognised Investment Exchange (RIE), was integrated into Turquoise Global Holdings Limited ('Turquoise'), forming Turquoise Derivatives, which is operated as a Multilateral Trading Facility (MTF).

Previously, firms reported transactions admitted to trading on EDX as on-exchange transactions. Under the current rules, transactions for derivative instruments admitted to trading on Turquoise Derivatives are technically OTC derivatives.

However, to avoid firms having to make systems changes to comply with the current rules, we proposed to allow firms to either report as OTC derivatives or to continue to report as on-exchange transactions as if they were derivatives admitted to trading on a regulated market. Transactions are reported as on-exchange transactions by populating the instrument identifier with the relevant International Securities Identification Number (ISIN) of the derivative and the trading venue with the Turquoise Market Identifier Code (MIC).

As this proposal represented a change to the current rules the FSA was required to consult on this.

The consultation was published on the guidance section of its website:

www.fsa.gov.uk/Pages/Library/Policy/guidance_consultations/index.shtml and closed on 22 September 2011.

There were no responses that raised any objections or requested any clarification to the proposed guidance. The guidance has therefore been made with immediate effect and firms now have the choice of reporting as on-exchange derivatives or as OTC derivative transactions. We believe it would be easier both for firms and the FSA to report using an ISIN.

Finalised guidance for reporting of transactions on derivative markets where reference data is not available

In Market Watch 40 we published finalised guidance for reporting of transactions in derivatives conducted through clearing platforms of derivative markets (ISIN or Aii) where the reference data is available to the FSA and the Authorised Reporting Mechanisms (ARMs). We also gave firms notice of our intention to propose new guidance for firms reporting derivative transactions conducted through clearing

platforms of derivative markets where the reference data for those transactions is not made available to the FSA and ARMs.¹

The FSA and ARMs rely on the provision of instrument reference data relating to the transactions conducted through clearing platforms of derivative markets in order to validate the accuracy of the transaction reports. Typically, this reference data is provided by the regulated derivative exchange concerned.

We consulted on proposed guidance that would require firms to report these particular transactions where the reference data is not available using the equivalent ISIN for ISIN derivative markets or Aii exchange product code for Aii derivative markets of the standardised derivative contracts (order book contracts).

The guidance proposed that when reporting transactions in derivatives conducted through clearing platforms of an Aii derivative market where the reference data for these transactions is not made available to the FSA and the ARMs, the Aii code for these transactions should contain the following components:

- the Exchange Product Code of the standardised derivative contracts (order book contracts); and
- the remaining Aii fields (derivative type, put/call identifier, maturity date, strike price and the ISO 10383 Market Identifier Code (MIC)) should be populated as per the flex derivative contract traded.

When reporting transactions in derivatives conducted through clearing platforms of an ISIN market where the reference data for these transactions is not available, the ISIN of the standardised derivative contracts (order book contracts) should be transaction reported.

It was proposed that the guidance would become effective as of 31 March 2012.

The consultation was published on the guidance section of its website: www.fsa.gov.uk/Pages/Library/Policy/guidance_consultations/index.shtml and closed on 6 October 2011.

There were no responses that raised any objections or requested any clarification to the proposed guidance. The guidance has therefore been made with an effective date of 31 March 2012.

Prior to 31 March 2012, firms are not required to report transactions in derivatives conducted through clearing platforms of derivative markets where reference data is not available to the FSA and ARMs.

However, where firms choose to report these transactions they may do so in a number of ways:

- (i) using the equivalent ISIN for ISIN derivative markets or Aii code for Aii derivative markets of the standardised derivative contracts (order book contracts);
- (ii) using the ISIN for ISIN derivative markets or Aii code for Aii derivative markets which is issued by the clearing platform to the parties to the trade but is not part of the reference data available to the FSA and to the ARMs. These trades will be rejected by the FSA and/or ARMs and the FSA does not require them to be re-submitted; or
- (iii) as an OTC derivative transaction.

1 Currently Eurex does not provide Aii codes for the flex derivative contracts to the FSA and ARMs. The FSA is endeavouring to establish a solution for this particular set of instruments.

The complete guidance in respect of reporting transactions in derivatives conducted through clearing platforms of derivative markets is as follows:

Reporting transactions in derivatives conducted through clearing platforms of derivative markets (ISIN or Aii)

This guidance applies to all transactions in derivatives conducted through clearing platforms of derivative markets (ISIN or Aii) within the EEA, regardless of whether those derivatives are fungible or differ in any characteristics from an exchange standardised instrument.

This guidance applies to transaction reports submitted to the FSA. Other competent authorities may have different requirements.

These derivatives are on-exchange instruments traded off order book and should be reported accordingly, as set out below.

Where reference data is made available to the FSA and ARMs

(a) ISIN derivative markets (eg flex options on the Turquoise Derivatives)²

When a transaction in a derivative instrument is conducted through the clearing platform of an ISIN derivative market that is a regulated market, the transaction should be reported as an ISIN transaction.³

This guidance will be effective from 31 March 2012. Firms, may, however, elect to report transactions in derivatives conducted through clearing platforms of an ISIN derivative market prior to this date.

Example of a transaction on Turquoise Derivatives reported as an ISIN transaction

- FI100 12 2011 5300 Equity Index Call Option on the Turquoise Derivatives.
- The firm should report this using the ISIN code (GB00D62KYB69). The exchange venue will be TRQD. The counterparty will be the exchange CCP.

Where the transaction is conducted on behalf of a client, the 'client side' transaction report must include the MIC of the derivative exchange in the venue field.

(b) Aii derivative markets (e.g. BClear)

Firms are not required to report transactions in derivatives conducted through clearing platforms of an Aii derivative market until 31 March 2012. From this date, firms are expected to report these transactions as shown in the examples below.

Example of fungible contracts (contracts that mirror standardised contracts on order book)

- Buy 10 Vodafone Dec 2011 160 Calls through BClear (NYSE Liffe).
- The firm should report this transaction using the Aii code. The counterparty will be the exchange CCP.

² As per the confirmation in this Market Watch, firms can continue to report transactions executed in derivatives admitted to trading on Turquoise Derivatives as if they were derivatives admitted to trading on a regulated market, by identifying the derivative with the relevant ISIN code. Hence, Turquoise Derivatives is used here as an example of an ISIN derivative market.

³ Transactions in derivatives admitted to trading on Turquoise Derivatives may be reported as an ISIN transaction or as an OTC derivative transaction.

- The Aii code for this transaction will contain the following components: Instrument Identification 'VOD' (Exchange Product Code of Vodafone), Quantity 10, Strike Price 1.60, Expiry Date 16 Dec 2011, Derivative Type: 'O', Put/Call Indicator 'C', Venue Identification 'XLIF'.

Example of non-fungible contracts (contracts that do not mirror standardised contracts on order book)

- Buy 10 Vodafone Nov 2011 166 Calls through BClear (NYSE Liffe).
- The firm should report this transaction using the Aii code. The counterparty will be the exchange CCP.
- The Aii code for this transaction will contain the following components: Instrument Identification 'VOU'⁴ (Exchange Product Code of Vodafone), Quantity 10, Strike Price 1.66, Expiry Date 18 Nov 2011, Derivative Type: 'O', Put/Call Indicator 'C', Venue Identification 'XLIF'.

Where the transaction is conducted on behalf of a client, the 'client side' transaction report must include the MIC of the derivative exchange in the venue field.

Firms may, however, elect to report transactions on fungible and non-fungible derivatives conducted through clearing platforms of Aii derivative markets as OTC derivative transactions prior to the implementation date (31 March 2012).

Example of reporting as OTC derivative transaction prior to 31 March 2012

- Buy 10 Vodafone Dec 2011 160 Calls through BClear (NYSE Liffe).
- The firm should report using the Venue Identification Code (MIC) of 'XXXX', and the counterparty will be the actual counterparty to the transaction.
- Other components of the report will include: Underlying Instrument Identification 'GB00B16GWD56' (ISIN of Vodafone), Instrument Type 'A' (Equity), Quantity 10, Strike Price 1.60, Expiry Date 16 Dec 2011, Derivative Type: 'O', Put/Call Indicator 'C'.

Where reference data is not available to the FSA and the ARMs

The FSA and ARMs rely on the provision of instrument reference data relating to the transactions conducted through clearing platforms of derivative markets in order to validate the accuracy of the transaction reports. Typically, this reference data is provided by the regulated derivative exchange concerned.

However, in some circumstances the FSA and the ARMs are unable to obtain reference data from derivatives markets on their flex derivatives contracts (eg currently Eurex does not provide Aii codes for the flex derivative contracts).

In circumstances where this reference data is not made available to the FSA and ARMs, firms will be required to report these transactions using the equivalent ISIN for ISIN derivative markets or the Aii exchange product code for Aii derivative markets of the standardised derivative contracts (order book contracts).

4 In this example, an American option, cash settled.

When reporting transactions in derivatives conducted through clearing platforms of an Aii derivative market where the reference data for these transactions is not made available to the FSA and the ARMs, the Aii code for these transactions should contain the following components:

- the Exchange Product Code of the standardised derivative contracts (order book contracts); and
- the remaining Aii fields (derivative type, put/call identifier, maturity date, strike price and the MIC) should be populated as per the flex derivative contract traded.

When reporting transactions in derivatives conducted through clearing platforms of an ISIN market where the reference data for these transactions is not available, the ISIN of the standardised derivative contracts (order book contracts) should be transaction reported.

This guidance will be effective from 31 March 2012.

Prior to 31 March 2012, firms are not required to report transactions in derivatives conducted through clearing platforms of derivative markets where reference data is not available to the FSA and ARMs.

However, where firms choose to report these transactions they may do so in a number of ways:

- (i) using the equivalent ISIN for ISIN derivative markets or Aii code for Aii derivative markets of the standardised derivative contracts (order book contracts); or
- (ii) using the ISIN for ISIN derivative markets or Aii code for Aii derivative markets which is issued by the clearing platform to the parties to the trade but is not part of the reference data available to the FSA and to the ARMs. These trades will be rejected by the FSA and/or ARMs and the FSA does not require them to be re-submitted; or
- (iii) as an OTC derivative transaction.

Contact details

This newsletter is produced regularly by the Market Conduct and Transaction Monitoring teams in our Markets Division. If you would like to receive this newsletter by email, or have any comments on it, please contact: market.watch@fsa.gov.uk

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