

**OICV-IOSCO CONSULTATION REPORT**  
**Technological Challenges to Effective  
Market Surveillance  
Issues and Regulatory Tools**  
**Comments by AMAFI**

Association française des marchés financiers (AMAFI) has more than 120 members representing over 10,000 professionals who operate in the cash and derivatives markets for equities, fixed-income products and commodities. Nearly one-third of the members are subsidiaries or branches of non-French institutions.

AMAFI welcomes the opportunity to comment on the Consultation Report (hereafter referred as to the "Report" on "*Technological Challenges to Effective Market Surveillance Issues and Regulatory Tools*" issued by the International Organization of Securities Commissions.

Before answering the questions of the "Report", AMAFI would like to emphasise some general comments.

## **I) GENERAL COMMENTS**

AMAFI welcomes IOSCOs' initiative to assess effective market surveillance. We agree with the three objectives (protection of investors, ensuring that markets are fair, efficient and transparent, reducing systemic risk) identified by IOSCO as being the main objectives of securities regulation.

Effective surveillance of markets currently constitutes an important issue to restore confidence in the markets. These have indeed been challenged by many stakeholders, in particular issuers and investors since the 2008 financial crisis coupled with the technical and regulatory changes.

AMAFI considers however that an effective surveillance of markets relies on three levels: supervisory bodies, trading venues and market participants. The "Report" is mainly focussed on the first level and does not take into account the two other pillars. AMAFI suggest IOSCO to carry out further work on these questions. Indeed, it would be very useful to have a common framework on the respective duties of each layer of the ladder. Given that some of the questions raised by the report concern much more regulators themselves than market participants.

It cannot be denied that the evolution of technologies, especially the development of high frequency trading raises new issues regarding the ability of market regulators to fulfil their functions. Anyway there is no evidence that the nature of market "malpractices" has evolved fundamentally because of technological changes. The main difficulty market regulators have to deal with is linked to their capacity to collect and analyse an increasingly amount of data and information in a more and more fragmented environment (technological and legal).

AMAFI fully agrees with the high level recommendations proposed by IOSCO.

## II) IOSCO recommendations and questions

AMAFI members mainly carry out investment services within the EU. As a whole, the EU market can be considered as a “local market” because of the harmonisation of the rules. But there are still “cross boarder issues” given the fact that the harmonisation of the supervision has not been achieved yet. The responses to the IOSCO ‘questions must be read in that perspective.

### 1. Regulatory Capabilities

*Market Authorities should have the organizational and technical capabilities to monitor effectively the Trading Venues they supervise, including the ability to identify market abuse and trading that may impact the fairness and orderliness of Trading Venues.*

- 1. What regulatory capabilities are, in general, needed in order for Market Authorities to survey for and detect market abuse that occurs on a cross-asset and cross-market basis? How can such abuse be best detected and combated?**

As stated in the general comments, the detection of market abuse should also rely on trading venues and market members. Concerning specifically Market Authorities, within one single jurisdiction, the supervision should be done by one single regulator on a cross-asset and cross-market basis. This is more efficient for both Market Authorities and the financial industry.

- 2. Do you think existing systems (e.g., audit trail systems) in your jurisdiction monitor effectively electronic trading (both cross-market and cross-asset), i.e., are they able to ensure the fair and orderly functioning of Trading Venues and to promote market integrity? Please explain and describe any enhancements that you believe are necessary. Are the necessary resources for effective systems available?**

First we would like to stress that the issues (fair and orderly functioning of trading venues, market integrity) concern all type of trading and not only electronic trading.

In the EU, the ongoing revision of MIFID and MAR regulation are aimed to put in place an actual cross-asset and cross-market supervision by modifying the current regulatory loopholes.

In France progress has been made in this area in the supervision of derivatives activities since the 2008 financial crisis, especially concerning transaction reporting which has been extended to OTC derivatives .

Concerning more specifically electronic trading, it must be noticed that ESMA has issued in February 2012 guidelines on “Systems and controls in an automated trading environment for trading platforms, investment firms and competent authorities”. The guidelines adopted by all European Authorities in may 2012 provide in the EU a common and useful framework for competent authorities, investment firms and market operators.

**3. To be able to perform effectively market surveillance, to what extent should Market Authorities have the ability to reconstruct and analyse order books? Why or why not?**

To perform effectively market surveillance, in particular to detect market manipulations such as “quote stuffing”, “momentum ignition” or “layering and spoofing”, it is crucial that Market Authorities have the ability to analyze order books. But to be efficient, the order book shall comprise at least all the trading venues where a given securities is listed. If the analysis is only carried out order book by order book, market manipulations are almost impossible to detect and to prove.

## **2. Review of Surveillance Capabilities**

*Market Authorities should regularly review and update as appropriate their surveillance capabilities, including systems, tools and surveillance staff skills, particularly with respect to technological advances.*

**4. Do you think that developments in technology have impacted Market Authorities' ability to monitor markets? If so, how?**

If we consider the French and European experience, the fragmentation of liquidity within European jurisdictions since the implementation of MIFID in 2007, has had an impact on the capacity of the French regulator to assess market manipulations. It is linked to the fact that the authority does not have access to the order book of trading venues which are outside its jurisdiction. MIFID 2 regulation should solve this problem.

**5. Are there specific developments that have impacted this ability more than others? If so, which ones?**

As stated above, fragmentation of liquidity is probably the most difficult issue the AMF has to deal with. AMF does not have access to all order books and cooperation between regulators is not optimum.

**6. To what extent have you identified instances of market abuse or possible market abuse, including inappropriate activity that could (or has) lead to disorderly markets, which you feel is directly related to the misuse of automated trading technology? Please provide details. For example: Do you believe your jurisdiction has experienced market infrastructure disruptions caused by automated trading, including HFT/algorithm use, that have caused network traffic or processing to exceed the capacity of Trading Venues, key market information providers or large market participants? If so, please describe.**

We have not identified or experienced any noticeable market infrastructure disruption due to automated trading in our jurisdiction.

**7. Have there been any developments other than technology that have impacted Market Authorities' ability to monitor the markets? Please provide details.**

See our answer question 5

### 3. Access to Data

*Within their jurisdiction, the relevant Market Authority(ies) should individually or collectively have the capability to access data in a way that enables them to conduct effective surveillance.*

- 8. To what extent do you think that a Central Reporting Point is necessary within a domestic market in order to conduct surveillance effectively, particularly across markets and/or assets? In other words, to what extent would the development of audit trail systems that are able to consolidate pre- and post-trade data across Trading Venues within a domestic market be beneficial? Please explain your answer.**
- a. To the degree that you advocate a Central Reporting Point, what kind of data would be needed for your respective surveillance tasks, e.g., order data/transactions data, both? What are the impediments to introducing these systems? What are the benefits?**
  - b. What are the potential costs associated with the establishment of a Central Reporting Point?**

We really believe that centralization of information is crucial within a domestic market, domestic market being the EU in Europe. This is more efficient and less costly for both regulators and the industry. For instance, since the implementation of MiFID, authorities have adopted different approaches concerning transaction reporting. This implies, for firms which carry out investment services within EU, duplication of reporting, different IT developments, complex internal organizations and regulatory risks.

Two types of Central Reporting Points are to be distinguished. The first one is the reporting of transaction on a cross-market and cross-assets basis. The second one is related to post trade transparency in a context of fragmentation of liquidity. There is a need for supervisory purposes but also for market stakeholders (investment firms, issuers, investors) to have a single data base where all the transactions are stored in a properly manner. Given that, AMAFI deeply regrets that the current draft of MiFID 2 regulation does not ensure the setting up of a single and complete database. Central reporting system and post trade system are not necessary located in the same entity.

There is no doubt that Central Reporting Points are less costly than multiple systems. First it ensures homogeneity in terms of information, data and format while multiple systems necessarily cause heterogeneity. Then it is cheaper to implement and update one single system rather than implementing and updating various systems. The economies of scale of a single system largely compensate the transfers of multiple systems towards one single.

- 9. Are there alternatives to a Central Reporting Point that can achieve the same end? Please explain.**

AMAFI considers that Central Reporting Point should be promoted. Alternatives are more costly and less efficient.

## 4. Customer Identification

*Market Authorities (individually or collectively) should have the capability to associate the customer and market participant with each order and transaction.*

### **10. To what extent should market surveillance systems or audit trails require the provision of customer identifiers? What are the impediments to providing customer identifiers in audit trail data?**

There is no doubt that Market Authorities should have the capacity to associate the customer with each order and transaction. The question is to assess whether including customer identifiers in the reporting system is workable and more efficient than the current practice in France (investment firms provide such information on request).

AMAFI understands that the availability of client IDs could be an improvement for competent authorities from a market abuse point of view. However, for it to be the case, AMAFI considers that such identification is currently not practicable for two main reasons:

- Harmonisation of client identifiers. There is currently no unique way to identify clients (and citizens for the same token) across the world. The implementation of the Legal Entity Identifier (LEI) could partially solve the problem but only for clients that are financial entities and not all clients.
- Confidentiality of the information. Is there in each Member State a legal base to authorise the transmission of client information cross-border?. This question could be quite prominent in several Member States and not least in France where there is a banking secrecy principle entrenched in the legal framework under which firms operate.

Even if a common client identifier is created, developing new systems to take orders and secure data is likely to result in very high costs, not accessible to all securities firms. Even then, as client data are eventually spread throughout the chain of intermediaries, the risk of data leak is increased.

## 5. Format

*Market Authorities should require that data required for market surveillance be reported to the requisite Market Authority for use and storage in a usable format.*

### **11. What regulatory steps, if any, should Market Authorities take in order to help ensure that any data reported to them for use and storage is in a usable format?**

In the EU the current situation is not satisfactory because of the lack of harmonization of reference and format data. The Market Authorities should develop in liaison with the industries common standards.

### **12. To what extent are you concerned about the ability of Market Authorities to reconstruct and analyze order book(s) in the correct sequence? What tools are necessary to do so?**

See question 3 above.

## 6. Data Protection

*Market Authorities should establish and maintain appropriate confidential safeguards to protect surveillance data that is reported to them.*

### **13. To what extent are current confidentiality provisions sufficient? If not, how can they be strengthened?**

It is crucial to ensure that the persons notifying suspicious transactions to a competent authority are protected from any harm and their liability should not be engaged as a result. Market Authorities shall ensure that competent authorities do not disclose to any person the identity of the person having notified these transactions, if disclosure would, or would be likely to harm the person having notified the transactions.

### **14. To what extent should Market Authorities be able to obtain surveillance data from other Market Authorities, whether inside or outside their jurisdiction, relating to securities trading, including the identity of customers? What issues are raised? Please explain your answer.**

See questions 3 and 10 above.

## 7. Synchronization of Business Clocks

*Market Authorities should consider requiring Trading Venues and their participants within their jurisdiction to synchronize, consistent with industry standards, the business clocks they use to record the date and time of any reportable event.*

### **15. To what extent do you think there would be value in requiring Trading Venues and market participants to attach a synchronized time-stamp to their orders reflecting when that order was sent?**

A synchronized time stamp is necessary in order to put in place a post-trade data base and to monitor order books. To reach this goal, the various order books should be required to be synchronized on a millisecond basis.



Contact:

Emmanuel de Fournoux – Director of Market Infrastructures, [edefournoux@amafi.fr](mailto:edefournoux@amafi.fr) +331 53 83 00 70