

ADVICE TO ESMA

Mandate for a peer review into the collection and use of Suspicious Transaction and Order Reports under the Market Abuse Regulation as a source of information in the context of market abuse investigations (ESMA42-111-4772)

I. Executive summary

1. The SMSG supports the review both regarding the collection and use of suspicious transaction and order reports (STORs) under the Market Abuse Regulation (MAR). STORs are key in mitigating market abuse and uphold market integrity and following their introduction in 2003, evidence and assessment of the use of STOR is needed.
2. In particular, it would be beneficial to obtain more information on the collection of STORs and reporting by stakeholders, including any differences between the classes of financial instruments and between NCAs and local stakeholders (investment firms, stock exchanges, trading venues, proprietary traders, other supervisory bodies, asset management companies and industry bodies as defined in the Mandate, further referred to as stakeholders). Also increased transparency on the use of STORs, such as enforcement or non-enforcement decisions by NCAs, would be important. In addition, harmonization could be increased in relation to the forms, and the information requested, as well as the NCA's processes for managing the reports. As proposed, it would be beneficial to ask market stakeholders for input.

II. Background

3. On 18 December 2018, ESMA received a mandate for a peer review into the collection and use of suspicious transaction and order reports under the market abuse regulation as a source of information in the context of market abuse investigations. In the present advice, the SMSG provides input on this peer review.

III. Comments

Quality and adequacy of STORs – effective supervision to ensure that NCAs are receiving timely, meaningful and comprehensive STOR

4. The Mandate notes that the Assessment Group “may” seek input and engagement from stakeholders. As the STORs reporting is related to several stakeholders, the SMSG recommends that a questionnaire should be developed and distributed to stakeholders to get a better overview of the usage of STORs reporting. This would improve the information gathering process as well as the quality of the review. In addition, this could provide a tool for self-assessment by the reporting stakeholders and raise awareness in the market.
5. Regulators have expressed concerns that some firms adopt an overly cautious approach to submitting STORs and firms have been advised to reflect on the reasons why they do not submit more STORs. Under-reporting of STORs may happen for example because firms may require a particularly high burden of proof that market abuse has taken place before they make a submission. ESMA should seek to determine whether this approach exist in the various jurisdictions. In this context, it would be interesting to compare the balance in the various jurisdictions between recorded submissions to the NCAs and cases where the suspicions were deemed not reasonable.
6. As proposed, the review should include all NCAs in order to get a complete overview of the usage of STORs in EU. On-site inspection should then be established for an adequate number of NCAs, representative for the capital markets in the EU.
7. The reporting methods should be fully harmonized between the NCAs, in order to allow for increased ability to coordinate the process for reporting entities as well as for the NCAs. This would further enhance supervisory convergence at European level.
8. The NCAs usage of STOR could be monitored by asking for figures about:
 - a) Frequency at which the NCA produces an analysis of trends in STORs reporting;
 - b) Frequency at which the NCA audits the STORs reporting compliance of its investment firms;
 - c) Whether such audits include all asset-classes, and how such compliance audits differ across each asset-class;
 - d) Whether the NCA has issued compliance-related sanctions in the context of STORs reporting, and if so what were the reasons for the sanctions;
 - e) Whether STORs reporting has led to requests for information issued to other NCAs or to 3rd-country supervisors, and whether such requests were successful;
 - f) Whether the NCA has received requests for information from other NCAs or from 3rd-country supervisors in the context of STORs supervision;

- g) Whether the NCA has identified a bias towards reporting insider dealing rather than market manipulation and, in case such bias has been identified, what the reasons are of the bias identified by the NCA;
- h) How many STORs the NCA receives per asset-class per annum, in absolute terms and in proportion to the market size; and
- i) How many successful enforcement actions the NCA has brought as a result of STORs reporting.

Substantive analysis and use of STOR

- 9. When analyzing the number of STORs and how they are managed within the NCA, it would be useful to also assess the resources of, and procedures utilized by, the NCA.
- 10. It would also be relevant to review enforcement criteria and, as this is closely related, the issue of contrasting the criteria applied by different NCAs when evaluating the difference between an entity failing to declare a STORs and an entity being considered as committing market abuse itself. When an entity fails to declare a STOR, this does not necessarily mean that that entity is intending to abuse the market, but in some cases an NCA may consider this to be the case. The distinction between both cases should be clear: i.e. failing to declare a STORs and committing market abuse.
- 11. With algorithmic trading, it may be more difficult to identify how results are derived and this may impede the identification of suspicious transactions. It would be relevant in ESMA's review to explore the manner in which NCAs and stakeholders deal with this issue.
- 12. The report following the peer-review should include clarification on what is market-based manipulation and what are suspicious trades.

Cross-border cooperation

- 13. To provide valuable conclusions it would be appropriate to cover an adequate number of NCAs for on-site visits, representative for the capital markets in the EU.
- 14. For achieving the goal set out in point 5 above (seeking adequate information from stakeholders), apart from the on-site meetings with NCAs, the peer-review team could also organize a series of meetings with relevant stakeholders in the same Member States. This would lead to a more balanced result of the peer review, combining information gathered not only from the NCAs, but also from stakeholders.

Other

- 15. Insights from earlier reviews such as from UK FCA and AMF, should be used as appropriate. For example, there seems to be a high proportion of STORs related to equities rather

than other asset classes including fixed income and commodities. Within that asset class (equities), the FCA has also identified a bias towards reporting insider dealing rather than market manipulation. ESMA should determine whether such pronounced biases are replicated in other jurisdictions and should seek to identify the root causes.

16. It would also be of interest to get insights into any problems which might have been encountered as a result of the use of third-party providers for post-trade surveillance.
17. It would be interesting to estimate the efficiency of the usage of STORs with a cost and benefit analysis on both the stakeholder side and the NCA side.

This advice will be published on the Securities and Markets Stakeholder Group section of ESMA's website.

Adopted on 25 March 2019

[signed]

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