# Virtu Financial Europe Response to ESMA Consultation Paper on the Guidelines on the MiFID II/MiFIR obligations on market data (ESMA70-156-2477, the "CP")

#### Introduction

Virtu Financial Europe (collectively **''Virtu''** or **''we''**) is a group of investment firms authorised in both the EU and UK. Virtu undertakes a range of MiFID activities including market making, proprietary trading, brokerage services, acting as a systematic internaliser and operating POSIT MTF. Virtu welcomes ESMA's efforts to critically examine and open for public discussion the critical issue of market data fees.  We broadly welcome the draft guidelines contained in this consultation paper.  We have provided further commentary under specific questions to outline where the guidelines could be enhanced to ensure they meet the objectives set out in MiFID II/MiFIR and the ESMA Report on Market Data (ESMA70-156-1606).

Importantly, ESMA has not given any substantial consideration to the related issue of connectivity costs which are often a large and overlooked component of market data charges.  Virtu is concerned that market data providers may increase the connectivity charges to subscribers in order to offset any loss of revenue as a result of these new guidelines.  We address this point further at Q26.

Virtu also notes that, for real and substantive change to unfair market data practices to be realised, National Competent Authorities need to ensure proper enforcement of these guidelines and the European Commission needs to progress the Level 1 changes proposed in the Report on Market Data.

**Question 1: What are your views on covering in the Guidelines also market data providers offering market data free of charge for the requirements not explicitly exempted in the Level 2 requirements?**

These guidelines should not apply to providers who do not charge for market data.  To do so would unfairly add to the cost of market data provision without the provider receiving any compensation from subscribers. Further, in applying such provisions to providers who do not charge for market data, ESMA may disincentiveise the free provision of market data by such providers, leading to a situation where more charges associated with market data are generated. This stands contrary to the intention of the requirements which is to reduce market data costs for consumers of market data.

To our knowledge, no issues have been raised by subscribers of such data providers and thus they should not be the target of supervisory focus.

#### Question 2: Do you agree with Guideline 1? If not, please justify.

#### We agree with the intention and spirit of draft Guideline 1 as it calls for increased granularity and transparency into the costs of producing and disseminating market data. We also note the submission of the European Principal Traders Association ("EPTA") which gives a detailed assessment into the actual costs to a trading venue of producing market data.

#### To further strengthen the aims of this guideline, we believe NCAs should be required to audit these methodologies on an annual basis. This would establish a benchmark for costs which the annual review could then be evaluated against. Having such a benchmark for assessment would appear to be necessary in light of the fact that the law already requires that market data be provided on a reasonable commercial basis, (as noted in paragraph 17 of the consultation paper), but compliance with such requirements has been difficult to determine without such a benchmark.

**Question 3: Do you think ESMA should clarify other aspects of the accounting methodologies for setting up the fees of market data? If yes, please explain.**

We do not agree with the statement at paragraph 19 which reads:

considering the different operating models and cost structures of market data providers these guidelines do not harmonise the cost accounting methods but rather require market data providers to have a clear and documented methodology for setting the price of market data.

We urge ESMA to be as prescriptive as possible with regard to the accounting methodologies related to the cost of producing and disseminating market data. Without clearly defined standards it is likely that methodologies employed by market data providers will be as many and varied as their fee schedules are today, which would defeat the purpose of the needed enhanced transparency. This runs contrary to the intention of comparability and transparency to facilitate assessment of the reasonable costs basis across a range of market data providers.

We believe that adopting a common format will be crucial in examining the issue across a variety of market data providers and propose that the model follows the one put forth by the Investors Exchange (IEX).[[1]](#footnote-1)

While all market data providers vary, the hardware and software components used in the provision of market data, whether by venues or vendors, are adequately mapped to this model. Exceptions should only be permitted with the publication of an adequate explanation as to how the model does not hold for a market data provider.

Furthermore, prior to obtaining cost models from market data providers, it would be helpful if ESMA and the European Commission clarified many grey areas within the Level 1 and 2 texts including, but not limited to, amortization standards, and most particularly the appropriate sharing of joint costs such as thresholds for allocating costs to employees who do not exclusively work in market data, costs for software (licensing) and hardware (servers, networking equipment, circuits, and data centre costs).

We believe that only uniformity in the model will facilitate the aims of comparability and assessment of compliance with the reasonable costs basis provisions.

#### Question 4: With regard to Guideline 2, do you think placing the burden of proof, with respect to non-compliance with the terms of the market data agreement, on data providers can address the issue? Please provide any other comments you may have on Guideline 2.

We agree with the spirit of draft Guideline 2, but believe it needs to go further.  While placing the burden of proof on the data provider will go some way towards addressing the issue, others remain.

Virtu believes that market data policies and audit practices should be structured to encourage and support compliance rather than to penalize non-compliance for the financial benefit of the market data provider. It is important to ensure that the appropriate usage based fees are applied equally to all customers. There are, however, several key changes which can be made to improve the audit process for both customers and market data providers.

Foremost among the changes would be to limit the audit look-back period to two years. With changes to key personnel oftentimes it can be extremely difficult to illustrate decommissioned entitlements systems and reproduce usage reports especially when looking back over an extended period.  Indeed, several exchanges in Europe have an unlimited lookback period.  Excessively long look-back periods are further exacerbated by interest and penalty fees and only serve to make audits contentious with the auditor incentivised to find problems.

Another issue that often arises is the new interpretation of deliberately vaguely drafted contract/licence provisions. We suggest that if a contractual provision in an audit is concluded to encompass an additional service for which a charge is applied by the provider they need to show that it was applicable at the outset of the agreement. That is, the market data provider needs to demonstrate that the charge was in existence and applicable when the agreement was signed as opposed to a new 'service' created during the life of the agreement.

Where problems or issues with compliance are identified by an auditor there is no independent arbiter of their findings.  Often in our experience we and others in the market are penalised for perceived infringements identified during an audit but which cannot be challenged to an independent authority.  We suggest that NCAs and/or ESMA may have a role to play here.

**Question 5: Do you consider that auditing practices may contribute to higher costs of market data? Please explain and provide practical examples of auditing practices that you consider problematic in this context. Such examples can be provided on a confidential basis via a separate submission to ESMA.**

We feel that market data costs are unnecessarily driven higher in audits owing to expansive policy (i.e. the potential access standard) and third party auditors who are compensated on a percent recovered basis.

Under the potential access standard, a display user is considered fee-liable if they potentially had the ability to access market data from that exchange, regardless of whether or not they had actually used the data. Under this policy, if a developer had created a display application that integrated market data from a variety of exchanges but had neglected to implement permissions, an auditor could cite all employees of the firm as having “potential access” and the financial consequences can be devastating.

Even if the firm had usage data showing that only several users had actually accessed each market and the rest of the firm had not, under audit, the firm could be liable for a multi-million-dollar costs finding. Virtu believes that this standard unnecessarily increases the cost of market data for participants and that ESMA should consider requiring exchanges to implement an **actual** rather than **potential** usage standard with the burden on the exchange to demonstrate actual usage.

Virtu also believes that third party auditors compensated on a percent recovery basis are overly incentivized to audit aggressively and intrusively with interpretation of market data usage agreements often diverging from that intended, or even provided by the data licensor. We would encourage ESMA to investigate these arrangements and believe Guideline 13 should explicitly require market data providers to engage external audit only upon a fixed fee model.

**Question 6: Do you agree with Guideline 3? If not, please justify, by indicating which parts of the Guideline you do not agree with and the relevant reasons.**

Virtu fully endorses draft Guideline 3 on the need for market data providers to introduce clear client categories. As highlighted by ESMA in the consultation paper accompanying the draft Guidelines, customers often find it challenging to determine which client category that they belong to, severely hampering their ability to anticipate the fees, terms and conditions applicable to them. To further strengthen the guideline ESMA should prescribe the criteria used by market data providers to determine client categories on the basis of objective and easily verifiable criteria so as to enable customers to estimate the conditions that will apply to them.

We also share ESMA’s assessment that customers should not be charged more than once for the same data based on use cases. The duplication of fees in this manner is a common tactic used by market data providers and dramatically increases the cost of market data for end-users. Such practice clearly contravenes the requirement that data costs be based on the cost of producing and disseminating the data.

**Question 7: Do you agree with the approach taken in Guideline 4? If not, please justify, also by providing arguments for the adoption of a different approach.**

Virtu fully agrees with draft Guideline 4. The customers of market data providers require certainty in terms of their categorisation for the purposes of market data fees, terms and conditions. A situation wherein the market data provider can charge multiple fees for market data based on different use cases or a client potentially belonging to more than one category is grossly unfair toward the customer and potentially creates inconsistencies in how different clients are treated. Some customers may fall into multiple categories but may take in the market data feed one time.  We can see an argument whereby a customer may be charged an additional amount for a separate use case, but customers cannot and should not be charged for each use case **and**category.

**Question 8: Do you agree with Guideline 5? If not, please justify.**

In principle, Virtu agrees with draft Guideline 5 instructing market data providers to ensure the same technical arrangements for customers belonging to the same category. However, we recognise that there may be significant practical barriers to ensuring the same level of latency and connectivity for a customer base that may be widely dispersed geographically. As a result, any discrepancies in latency or connectivity should be justified by the market data provider based on technical constraints and the capacities of their customers.

**Question 10: Do you agree on the interpretation of the per user model provided by Guideline 6? If not, please justify and include in your answer any different interpretation you may have of the per user model and supporting grounds.**

Yes, Virtu agrees with the interpretation of the per user model provided by draft Guideline 6. Where currently investment firms may be charged, for instance, for 3 “devices” for the same end user this will result, as was expected with the introduction of MiFID II, in a 66% saving in market data fees. Currently a number of regulated markets offer unit of count netting for display data but have a cap with regards to the number of devices that each user can use. Although this translates in a lower charge in comparison to the un-netted model, it is still resulting in multiple billing per user. This guideline will provide the clarity to market data providers to ensure that users are only charged once for display data and is expected to result in substantial savings for impacted subscribers.

In addition, Virtu is aware of exchanges approaching our clients who subscribe to our execution management systems with issues around data licensing.  The exchange informs the client that they need a non-display data license to use our EMS **despite**the EMS operator already paying c. £80,000 p.a. for the non-display data license. That is, **exchanges are trying to charge our client for market data that we have already paid for use by our EMS.**

In one example of this, when the auditor of the relevant exchange was challenged by Virtu (as EMS provider) and the subscribing client, the exchange stated that ‘use of an execution management system constitutes the need for a non-display data license by each subscriber to the EMS.’  The EMS operator already pays the license for the non-display data and thus this results in duplicate charging by the exchange. The EMS subscribers should not be required to also pay the license. There is no additional cost incurred by the exchange in this scenario upon which they could base the proposed fee to the EMS subscriber.

This is a further example of unfair charging practices by dominant exchanges and should be enumerated as an example of poor behaviour in the guideline above.

**Question 11: Do you agree with Guideline 7? If not, please justify. In your opinion, are there any other additional conditions that need to be met by the customer in order to permit the application of the per user model or do you consider the conditions listed in Guideline 7 sufficient to this aim? Please include in your answer the main obstacles you see in the adoption of the per user model, if any, and comments or suggestions you may have to encourage its application.**

Yes, Virtu agrees with draft Guideline 7 and do not believe that there are any other conditions that should need to be met by the customer in order to permit the application of the per user model. Subscribers should be able to correctly identify the number of active users who have access to the data, through facilities such as market data entitlement control systems, and report the exact number to market data providers. However, we are concerned that market data providers may use this guideline as a delaying tactic by introducing exhaustive measures in order for a customer to be able to prove that they can correctly identify the number of active users.  We further address this issue at Question 13.

**Question 12: Do you agree with Guideline 8? If not, please justify also by indicating what are the elements making the adoption of the per user model disproportionate and the reasons hampering their disclosure.**

Yes, Virtu agrees with draft Guideline 8 but would like to highlight that it is expected that all market data providers will be able to offer the per user model and that this would be an extremely unusual case. The majority of EU regulated markets already offer PPU (Per Physical User) programs, also known as netting programs, the issue experienced by market data subscribers is that these RMs make it extremely hard to be accepted into these programs.

**Question 13: Do you think ESMA should clarify other elements of the obligation to provide market data on a per user fees basis? If yes, please explain.**

We believe that ESMA should provide guidance to market data providers with regards to the turnaround time from the point at which a client requests entry onto a per user model and acceptance onto that model. At present one of the main barriers to entry into these programs is the length of time of the approval process. For example, our trade association members have experienced that it has taken up to two years to be accepted onto a program with what has been seen by some as delaying tactics, such as lack of communication during the process, to minimise the number of members availing of the program.  Given draft Guideline 7, it seems reasonable for a market data provider to be required to provide a written response to a client within three or six months with full reasons set out in the response if approval is denied.

**Question 14: Do you agree with Guideline 9? If not, please justify.**

We agree with draft Guideline 9.  Market data providers should make the data available to purchase separately from additional services and should not condition the purchase of market data upon additional services.

**Question 16: Do you agree with Guideline 10 that market data providers should use a standardised publication format to publish the RCB information? If not, please justify.**

We agree with draft Guideline 10 that market data providers should publish RCB information in a standardised format.

**Question 18: Do you agree with the proposed definitions in Guideline 11? In particular, do they capture all relevant market uses and market participants? If not, please explain.**

We agree with the proposed definitions as set out in draft Guideline 11.

**Question 20: Do you agree with Guideline 12? If not, please justify.**

We do not agree with the second part of draft Guideline 12.   Market data providers should be held to a very high level of transparency, including disclosing to the public the actual level of the margin in the fees for market data.  Such a measure is proportional given the oligopoly which exists amongst market data providers.

**Question 22: Do you agree with Guideline 13? If not, please justify.**

This guideline should also include limits relating to the application of fees retroactively, limits to the frequency of auditing and limits to how far back audits may look as discussed above.

**Question 23: Which elements for post- and pre-trade data publication should be required? In particular, are flags a useful element of the publication? Should there be any differences between the different types of trading systems? Is the first best bid and offer sufficient for the purpose of delayed pre-trade data publication?**

Flags are a crucial element of the market data publication and should be maintained.

**Post-Trade**

For post-trade data the price, volume, transaction, published time, institution ID and venue ID flags are all critical elements of the data which should be maintained.  There should no be no difference between the different types of trading system.

**Pre-Trade**

For pre-trade data it is important to consider the impact on users if they were required to move their systems to using delayed data.  Pre-trade data is often used for aiding compliance queries and best execution examinations amongst other uses. For most of these use cases the Level 1 (first best bid and offer) data would not be sufficient. Level 1 data does not provide a depth of information necessary to fulfil these use case obligations.

As a compromise, it may be sufficient if there was an amalgamation of the first 5 levels of data.  This would cover most use cases without being overly burdensome on the data provider.

A further suggestion is to make the delayed data available in the same format and via the same infrastructure as the live data, just delayed by 15 minutes. That way we could also ensure consistency, accuracy and format of data.

As to the question of operational challenges in having to store sufficient pre-trade data, we envisage that exchanges are already storing that data for compliance and reporting reasons so do not consider it too onerous.

**Question 24: Which use cases of post- and pre-trade delayed data are relevant to you as a data user? What format of data provision is necessary for these use cases, and especially for pre-trade delayed data?**

Market Data are used throughout the value chain of securities business from research, trading, advice, portfolio management to securities administration and custody. For example, securities services in banks, investment firms or asset managers provide services to institutional investor in various areas such as Net Asset Value (NAV) computation, compliance checks, clients & regulatory reporting, fund administration and custody to name a few all of which require the production of all kinds of reports. In the exchange space, delayed market data from other trading venues is being used for offering various market models to customers, for brokers to implement the Best Execution, for regulatory supervision, to operate regulatory reporting services, or for index calculations.

We would like to see the data available both real-time delayed (delayed data available in the same format and via the same infrastructure as the live data, just delayed by 15 minutes) and available to download for up to one week after creation.

**Question 25: Do you agree with the definitions of data-distribution and value-added services provided in Guideline 16? Please explain.**

We agree with the definitions set out in Guideline 16.

Data redistribution generally is understood as the process of moving data replicates from one data site to other sites or distributing from one party to another without altering the data. The redistribution, or just distribution, fee is paid to the exchange when market data, display or non-display, is delivered to a system, person, or business other than the one that initially purchased the data. Most commonly, redistribution fees are incurred when a broker shows market data to a client or a vendor sells the market data information to a third party. Depending on factors like what exchange the data is from, what data provider is used, and if it is display or non-display data, the cost of redistribution can vary. Redistribution fees are paid whenever market data is redistributed. The definition of the business practice is therefore accurate.

#### ****Question 26: Do you have any further comment or suggestion on the draft Guidelines? Please explain.****

#### **As noted in the introduction, ESMA should give due consideration to the charging of ‘connectivity fees’ by market data providers. Market participants must often pay these fees in order to connect to exchanges. Some commentators believe, including Virtu, that these may be increased without cause in the future to offset any losses from market data revenues.**

#### **Similar transparency rules should be applied to connectivity fees as are proposed for regular market data fees to allow for clear demarcation between different fees applied to market data subscribers.**

#### **Virtu would be happy to engage further with ESMA on this topic if necessary.**

1. “The Cost of Exchange Services” (https://iextrading.com/docs/The%20Cost%20of%20Exchange%20Services.pdf) [↑](#footnote-ref-1)