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With Emir refit set to finally land in the EU the buy-side should expect some direct impact on trading strategies, say experts

With the EU's Emir refit implementation set to come into force on 29 April, The TRADE looks into what should be front of mind for trading entities and the importance of adopting a 'right first time' mentality to avoid potential repercussions.

By Claudia Preece

As the European Market Infrastructure Regulation (EMIR) refit introduces significant technical modifications, buy-side entities should expect important strategic and operational adjustments as legacy systems and previously established reporting practices could struggle to handle the regulatory shift, experts tell The TRADE.

The Emir refit comprises key changes to the Emir reporting regime which are geared at raising data quality and increasing transparency across the derivatives market in order to ensure increased financial stability.

The change is set to come into force on 29 April in the EU before the UK follows suit with their own implementation, fixed for later this year on 30 September.

The incoming refit is set to have a much broader scope than the original Emir mandate, with implementation across the derivatives trading market covering both OTC and listed derivatives, with the potential for a "ripple effect" to other areas.

Keeping regulators on side

As market players seek to stay on top of the changes, it is important to note that failure is seemingly not an option as regulators continue to be far more technologically knowledgeable than in times gone by. Now, key industry experts, data scientists, and policy makers are increasingly working together to ensure that as rules are introduced, they cover the even the most granular aspects.

Speaking to The TRADE earlier this year, Thomas Steimann, chief executive of SIX's Regis-TR, made clear the importance of market players approaching the refit from the point of view of an enhancement to, rather than a new, regulation. Due to this, regulators are set to be less forgiving, he explained, and unlikely to allow a 'grace period'.

Instead, firms will be expected to start off already at a run, performing their activities from the get-go.

Speaking to The TRADE, Steve Walsh, director of product and solutions at Duco agrees that regulators are set to take a firm stance: "Reporting parties will need to adopt a 'right first time' mentality and be in a position to incorporate and provide all of the required trade reporting attributes accurately […] there will be heavy scrutiny on the required infrastructure and the quality of static data."

"Firms should approach this as a T0 process requirement, trades with material issues will not only impact the accuracy of trade reporting but introduce discrepancies into trade and risk positions."

Eric Heleine head of the trading desk at Groupama Asset Management, tells The TRADE that from his perspective the effects of this for buy-side entities are two-fold. On the one hand, there is set to be increased operational efficiency, and therefore cost savings thanks to simplified reporting, however on the other comes the element of increasingly complicated clearing obligations.

"The new clearing obligations may necessitate a shift in trading strategies, particularly for entities that are now subject to or exempt from clearing, affecting liquidity and market access [it will] have a direct impact for the equities derivatives."

Specifically, the changes have the potential to influence hedging costs and strategies, as well as possibly affecting equity market liquidity and volatility, he adds.

Derivatives: A complex puzzle

Linda Coffman, executive vice president of SmartStream, responsible for overseeing the SmartStream reference data utility, tells The TRADE that one of the key drivers for the changes is the fact that derivatives are a less-understood asset class, and thus possess various intricacies.

"Given the complexities involved in defining and understanding the underlier of each derivative, the risk exposure is buried within the derivative and thus Emir continues to provide a mechanism to add more transparency within this asset class.

"[...] Access to all the data is probably one of the key challenges for the buy-side. Derivatives terms and conditions can be quite complex. Not many firms, buy- or sell-side, have previously had to consider many of the data points needed for Emir refit, such as delivery routes, and energy specific attributes."

The plan is to introduce 74 new data fields – which includes detailed information concerning counterparty data – understandably meaning that the firms in question are set to manage and report an increasingly complex set, and higher volume of, data.

Addressing the impact of the changes to data management and reporting requirements, Heleine explains: "Emir refit introduces technical modifications that demand significant strategic and operational adjustments from buy-side entities.

"The focus on simplifying reporting, adjusting clearing obligations, and enhancing risk management practices has direct consequences for trading strategies, operational efficiency, and compliance frameworks, particularly in the context of equity derivatives and with ripple effects across other asset classes."

So what is the real challenge? Speaking to The TRADE, Coffman explains that not only is it the number of attributes that firms must report, but also the format of those attributes.

They will now be required via an Extensible Markup Language (XML) format, as opposed to Comma-separated Values (CSV) formats, which a majority are more comfortable reporting in currently.

She further adds that "many firms are struggling with the concept of third-party equivalence when determining which transactions fall within the scope of Emir and there is [also] the reconciliation piece – which is challenging even for those delegating their reporting and are still responsible for gathering the necessary data."

To delegate or not to delegate

Though many firms have historically preferred to delegate their reporting, in particular those on the buy-side due to the huge number of attributes to be reported, there are pros and cons to either side.

Walsh asserts that there is a continual debate around the approaches: "Firm's self-reporting are testing their ability to provide the new and amended reporting attributes required by ESMA. Firms that delegate their reporting are locked in negotiations with their delegated reporting parties on delegated reporting agreements, those delegating want liability and those reporting on their behalf want indemnity!"

However, what is most important for industry players to bear in mind is the reality that whether delegating or managing internally, firms themselves are still the ones ultimately responsible for the accuracy of the information – meaning that the volume and detail of the information being 'delegated' out, will also need to be increasingly detailed.

"Global regulators want firms to independently validate their approaches. Marking your own homework is no longer accepted. Keeping your delegated reporting party honest and owning the responsibility of reporting is mandatory, challenging and questioning approaches to eligibility and obtaining the required information to offer ESMA comfort on data integrity at the TR's is imperative," says Walsh.

Chris Childs, managing director, head of repository and derivatives services at DTCC, spoke to The TRADE about the impact of this resourcing challenge for firms, highlighting that of the upmost importance for traders and the buy-side is the resilience of their technological solutions.

“Firms, especially smaller entities, may struggle to adapt to the new reporting formats and the increased number of reporting fields. The implication is the pressing need for enhanced reporting systems and processes to accurately capture and report the expanded data set.”

It is undeniably a tricky question to answer for many firms, with various school of thoughts having battled it out in the long lead up to the refit. Reporting infrastructure relies on eight to 20 systems for the required attributes, a significant onus.

In times gone by, firms have relied on labour intensive solutions and legacy systems, however, it is clear that regulators are keen for the market to develop as one in order to facilitate a more controlled environment with increased oversight.

“This is where investment in automation and technology infrastructure is more crucial than ever – these tools are essential for streamlining complex processes such as data mapping and tracing data lineage. Legacy systems and past reporting practices may hinder firms from successfully navigating the regulatory transition,” says Childs.