

European Banking Authority  
DEFENSE 4 – EUROPLAZA  
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92927 Paris La Défense CEDEX

3<sup>rd</sup> October 2019

**Re: Consultation Paper on draft Regulatory Technical Standards (RTS) on criteria for assessing risk factors modellability under the Internal Model Approach (IMA)**

Dear Sirs,

Refinitiv welcome the opportunity to comment on the EBA's Consultation Paper for Draft Regulatory Technical Standards on Criteria for assessing the modellability of risk factors under the Internal Model Approach under Article 325be(3) of Regulation (EU) No 575/2013 (Capital Requirements Regulation 2 - CRR2), published on 27 June 2019.

Refinitiv is one of the world's largest providers of financial markets data and infrastructure, serving over 40,000 institutions in over 190 countries. It provides leading data and insights, trading platforms, and open data and technology platforms that connect a thriving global financial markets community - driving performance in trading, investment, wealth management, regulatory compliance, market data management, enterprise risk and fighting financial crime.

Refinitiv are working with a group of banks and market infrastructure providers with the aim of providing "real" price observation data via an industry solution. Our feedback on this consultation paper focuses on the availability of "real" price observation data in relation to questions 1-6 for which we would like to make the below remarks.

We recommend the EBA to adopt technical standards that are consistent with market convention and do not unduly inhibit the provision of "real" price observation data.

For a committed quote to be considered as a verifiable price, Refinitiv urge the EBA to adopt Option 1a as requiring committed quotes to have both a firm bid and an offer is in contradiction with existing convention. In many bond and derivative markets, particularly those based on a request for quote trading protocol, firm quotes consist of only a bid or an offer. Where such quotes are made public under MiFID II, the major European transparency initiative, the obligation for pre-trade transparency does not mandate quotes to have both a bid and an offer. Furthermore, Refinitiv's analysis of 240K+ bond and derivative quotes highlight that all the quotes are single sided – only a bid or an offer. Given the limited alternative sources, adopting Option 1b could lead to a near 100% reduction in the availability of committed quote data available for RFET.

Refinitiv question whether a formal definition of "non-negligible volume of a transaction or quote, as compared to usual transaction sizes for the bank, reflective of normal market conditions" aids effective

risk management and is in the best interest of market participants as well as the end consumer. We caution against implementing explicit limits to define non-negligible volume due to the material challenges associated with such a calibration.

Regarding the definition of “unreasonably large bid-offer spread as compared to usual bid-offer spreads, reflective of normal market conditions” we also question whether a formal definition is required due to the challenges in specifying an accurate definition as well as the lack of such a requirement in the global BCBS standard.

Finally, Refinitiv would like to highlight the importance for financial institutions to be able to readily access and adopt data from third party providers as an input to their modellability assessment. We believe the existing requirements for annual independent audit, provision of evidence of the transaction or committed quote to competent authorities upon request and the requirements for a committed quote to be a legal obligation risks hindering sufficient access to “real” price observations. Refinitiv propose that these risks could be mitigated by 1) limiting the scope and granularity of the annual independent audit; 2) ensuring the requirement to provide evidence of the transaction or committed quote to competent authorities upon request is not used excessively; and 3) aligning the definition of committed quotes to market convention. Sufficient access to “real” price observation should support an efficient market that doesn’t systematically misclassify risk factors as non-modellable and where smaller institutions or new entrants do not face undue barriers to entry due to limited access to data.

Yours faithfully,



John Mason

Head of Pricing and Reference Data

**Q1. Do you agree that a committed quote, to be considered verifiable, should be required to have both a firm bid and offer price? If you think that solely a bid or offer price should be sufficient please provide a convincing rationale.**

No. Refinitiv disagree that for a committed quote to be considered verifiable it should be required to have both a firm bid and offer price. Refinitiv support option 1a (as outlined on page 32 of the consultation paper). For many OTC markets (particularly those that are less liquid), it is convention for firm quotes to be either a bid or an offer. In addition, under MiFID II there is no obligation for two sided quotes to be published. Finally, Refinitiv believe such a requirement is inconsistent with the BCBS (Basel Committee on Banking Supervision) 2019 Minimum capital requirements for market risk and the associated FAQs, which do not stipulate this requirement on committed quotes. Mandating committed quotes to include a bid and an offer price to be considered verifiable unduly limits their availability to the point where the data is no longer a fair and accurate reflection of the liquidity in the market and such the technical requirement is inconsistent with the policy objective.

Many traditional OTC markets, including corporate bonds, trade using a request for quote (RFQ) protocol. Under these systems a customer submits a request for quote by specifying key characteristics such as the instrument, size they wish to trade, buy vs. sell and the dealers they want the RFQ to be submitted to. Given the customer specifies whether they are seeking to buy or sell the instrument, dealers respond to this RFQ by providing a single-sided quote. Once the dealer has submitted their quote, the client is able to accept the best price and execute the trade. A similar workflow is adopted in voice trades that are executed bilaterally. At no point in the workflow is a two-sided committed quote made available to the client, the market or the public.

It should be noted that single-sided committed quotes are not limited to RFQ markets. Major exchanges support single-sided quotes from a functionality perspective and Refinitiv find evidence of these quotes being used in instruments such as index options trading on Eurex, where only a firm bid or an offer is available. In addition, single sided quotes are common place in select FX NDF markets where liquidity is limited.

In 2018, MiFID II extended pre- (and post-) trade transparency in European equity markets to bond and derivative markets. Delegated Regulation (EU) 2017/583 of 14 July 2016 Article 2 specifies that trading venues are required to “*make public the range of bid and offer prices and the depth of trading interest at those prices*”. The information to be made public depends on the type of system adopted by the trading venue (see Annex I of the regulation for further details on the information to be made public under each of the six systems). Under a request for quote trading system the regulation specifies “All submitted quotes in response to a request for quote may be published”. This includes quotes which are composed of only a bid or an offer.

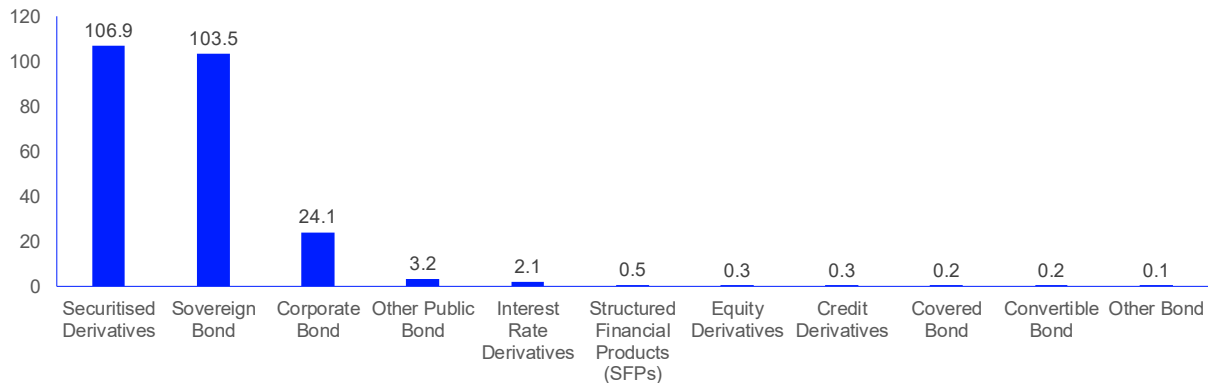
Finally, Refinitiv have reviewed the BCBS Minimum capital requirements for market risk (with FAQs) published in February 2019. On review of these updated requirements Refinitiv find no reference to committed quotes requiring a firm bid and offer price.

**Q2. Please provide an estimation of the impact of requiring solely a firm bid or offer price compared to requiring both. Please provide this impact e.g. in terms of number of non-modellable risk factors, stress scenario risk measure charge or number of eligible committed quotes for different risk factors/ risk factor categories.**

Requiring committed quotes to have both a firm bid and offer significantly reduces the quantity of quote data eligible for inclusion in the risk factor eligibility test. Refinitiv estimate that for many bond and derivative markets this requirement could lead to a near 100% reduction in the quantity of quote data available for RFET.

Currently in traditional OTC markets, committed quote data is rarely available in the public domain. One exception to this is MiFID II, a major European regulatory initiative, under which select executable quotes are made public. The scope of quotes made public under MiFID II is restricted to those in markets considered to be liquid and activity considered not to be large in scale compared with the normal market size. To estimate the impact of requiring committed quotes to have both a firm bid and offer Refinitiv analysed a sample of 240K+ MiFID II quotes published by major APAs (Approved Publication Arrangements) and trading venues during the week commencing 17 June 2019 (see Chart 1).

**Chart 1: MiFID II bond and derivative quotes by product**  
Number of quotes (#000s), 17-21 June 2019

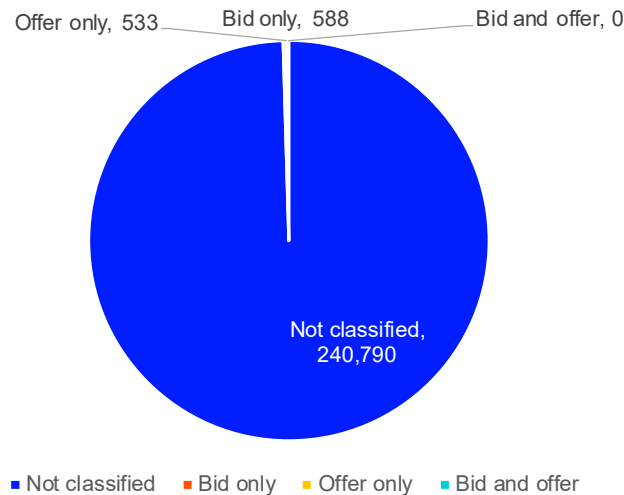


Source: Various MiFID II APAs and trading venues, Refinitiv analysis

Of the quotes analysed by Refinitiv, only 0.2% of the quotes specified which side the quote related to – whether it was a bid or an offer. None of these quotes included both bid and offer details. Refinitiv further analysed whether single sided bid or offer quotes were published in the same instrument at the same time and found no conclusive evidence that two sided quotes are being reported as simultaneous single-sided bid and offer quotes.

**Chart 2: MiFID II bond and derivative quotes by quote type**

Number of quotes (#000s), 17-21 June 2019



Source: Various MiFID II APAs and trading venues, Refinitiv analysis

Mandating committed quotes to include a bid and offer would likely render all (or nearly all) MiFID II quote data for bond and derivative markets ineligible for the risk factor eligibility test. Given the lack of other data publicly available in these markets today, such a definition would in effect reduce the availability of a quote for bond and derivative markets by near 100%.

**Q3. How would you define and check for a “non-negligible volume of a transaction or quote, as compared to usual transaction sizes for the bank, reflective of normal market conditions” for the purpose of assessing the validity of a price observation?**

Refinitiv question whether a formal definition for “non-negligible volume of a transaction or quote, as compared to usual transaction sizes for the bank, reflective of normal market conditions” aids effective risk management and is in the best interest of market participants as well as the end consumer. We caution against implementing explicit limits to define non-negligible volume due to the material challenges associated with such a calibration. If a formal definition must be introduced, Refinitiv recommend institutions should be able to classify committed quotes and trades conducted by financial institutions or those collected from market infrastructure (such as trading venues and CCPs) providers to be classified as of non-negligible volume.

Refinitiv note that it is operationally not feasible to implement explicit volume-based limits either at industry or firm level to define a non-negligible volume. The framework would need to take into account factors such as product type and market structure (e.g. electronic markets typically trade in smaller sizes than voice markets). In addition, it requires a high level of transparency that risks hindering the

efficient functioning of the market. If such a framework was miscalibrated, it could lead to insufficient “real” price observations compared to true market activity and result in risk factors being inappropriately classified as non-modellable. This risks unnecessarily high capital charges and could discourage trading activity which could have benefitted the market and /or end consumer. It is not feasible to implement volume-based limits at industry level as for many markets that banks need to source “real” price observation data there is currently no complete and accurate transparency initiatives from which to calibrate such a framework. In addition, the introduction of such transparency in OTC markets could negatively impact the efficient market function. It is also not possible to calibrate such a framework at firm level as in illiquid markets the provision of volume information on third party trades and committed quotes could negatively impact the provision of liquidity.

If further clarity is required Refinitiv recommend institutions should be able to classify committed quotes and trades conducted by financial institutions or over market infrastructure (such as trading venues and CCPs) to be classified as of non-negligible volume. Such trading activity is already governed by regulations which ensures the fair and efficient functioning of capital markets and therefore should be consistent with the policy objective of the risk factor eligibility test.

**Q4. How would you define and check for an “unreasonably large bid-offer spread as compared to usual bid-offer spreads, reflective of normal market conditions” for the purpose of assessing the validity of a price observation obtained from a committed quote? In your response, please provide a detailed reasoning.**

Refinitiv question whether a definition and check for “unreasonably large bid-offer spread as compared to usual bid-offer spreads, reflective of normal market conditions” is required, since:

- A) Specifying an accurate definition of “unreasonably large” can be challenging due to highly different characteristics observed in different instruments and markets; as well as variation over time
- B) Refinitiv find no requirement in the BCBS 2019 Minimum capital requirements for market risk and the associated FAQs that committed quotes require a firm bid and offer price and thus implicitly does not mandate checks for an unreasonably large bid-offer spread

If a definition and check are required, single sided quotes (i.e. either bids or offers) should be exempt since it is not possible to calculate a bid-offer spread. Refinitiv also note that many of these instruments are illiquid so it is not possible to accurately estimate the bid for committed offer quotes nor the offer for committed bid quotes. For markets where convention is to provide committed quotes with both a bid and offer, Refinitiv would like to highlight that the size of the spread can differ significantly depending on the liquidity available in the market. Less liquid markets tend to have wider bid-offer spreads. Given the correlation between illiquidity and bid-offer spread and reliance on quote data, Refinitiv recommend the EBA retain sufficiently flexible guidance on “unreasonably large bid-offer spread as compared to usual bid-offer spreads, reflective of normal market conditions”.

**Q5. Do you see any problems with requiring that institutions are allowed to use data from external data providers as input to the modellability assessment only where the external data**

**providers are regularly subject to an independent audit (independent of whether the price is shared with the institution or not)? If so, please describe them thoroughly (i.e. for which data providers and the reasons for it).**

It is essential for institutions to be allowed to use data from external data providers as an input to their modellability assessment for there to be an efficient market where smaller institutions or new entrants do not face undue barriers to entry.

Under the current market structure, exchange traded markets are subject to high levels of pre- and post-trade trade transparency meaning that executed trades and committed quotes are widely available where activity is taking place. However, in OTC markets there is very limited availability of verifiable prices that can be used for the risk factor eligibility test. The opaque and fragmented nature of these markets means that without efficient consolidation and distribution of trade and committed quote data, institutions will inaccurately classify modellable risk factor as NMRFs which could result in excessive NMRFs. Smaller banks and new entrants are disadvantaged vs. larger banks and incumbents as in opaque markets they have fewer observations based on internal data. This could reduce their likelihood of passing RFET and hence require them to hold more capital, which could act as an unfair barrier to entry.

**Q6. Do you have any proposals on additional specifications that could be included in the legal text in order to ensure that verifiable prices provided by third-party vendors meet the requirements of this Regulation?**

No. Refinitiv do not propose any additional specifications to ensure verifiable prices provided by third party vendors meet the requirements of this regulation.

Refinitiv note that the requirements for an annual independent audit and provision of evidence of the transaction or committed quote to competent authorities upon request already place a significantly higher burden on vendors than those requirements associated with traditional delivery of market and reference data, which can be used in other elements of FRTB. We are concerned that these requirements in conjunction with the already narrow scope of data that's eligible for inclusion in the risk factor eligibility test risk significantly increasing the cost of third-party vendor "real" price observation data and hindering its availability. As mentioned in our response to Q5 this could lead to excess NMRFs and act as an unfair barrier to entry.

Refinitiv propose that these risks could be mitigated through a pragmatic implementation approach to the requirements for third-party vendors as well as alignment between the definition of committed quotes and market convention. Limiting the scope and granularity of the annual independent audit, as well as ensuring there isn't excessive adoption of the requirement to provide evidence of trades and quotes to competent authorities would ensure sufficient data quality without unduly increasing cost. Mandating committed quotes to be a legal obligation to buy and sell the corresponding financial instrument at that price if requested is not fully consistent with convention in many OTC markets. Revising this requirement to include those quotes where there is an obligation under market convention

to buy or sell the corresponding financial instrument at that price if requested would more closely align the definition with market convention and avoid unduly restricting the availability of data.