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Race to the Bottom for Market Data Reform

The UK and EU are trying to catch up with the US in building their respective Consolidated Tapes (CT). The US has no intention to slow down and wait for the Europeans in market data reforms. Yet, the US D.C. Circuit ruling in July 2022 weakens the already weak proposition of the SEC's governance requirements over the equity CT-Plan. The US decentralized competing model (DCM) of 2/3 Self-Regulatory Organizations (SROs) and 1/3 non-SROs representation in the operating committee cannot be executed. The SEC prescribed minimum terms and conditions (T&C) for CT-Plan Version 2 in replacing the non-SRO representation provisions are ineffective (see this). The SEC has until September 21, 2024, to determine whether to approve or disapprove it.

Improving the capabilities of the Financial Instruments Transparency System (FITRS) that hosts the results of the MiFID transparency calculations in the UK and EU has stirred up much debate. Various stakeholders (ICMA, AMF, ESMA, FCA) are conducting qualitative and quantitative assessments to decide the liquid classes of financial instruments, particularly for bonds. The industry is looking at the regulators to be the referee, while the regulators are asking the Data Expert Group (DEG) to propose recommendations. Liquidity is a highly subjective moot point. Learning from the US FINRA's TRACE recalibration to formulate a strategy to suit the issuers and the investors' appetites would help. Though, regulators should not be finessing the calibration.

Given the stages of development and current market structure differences for equity and non-equity markets, the definition of 'real time' for equity CT should NOT be the same for bonds. Doing so could be a detriment to the fixed income markets' liquidity. The US proposed rule to reduce the 15-minute FINRA's TRACE reporting timeframe to 1-minute is problematic. We cannot comprehend why the ESMA in the EU maybe going cheap while soliciting public comments that stated, *"in light of cost efficiency considerations, ESMA recognizes the potential benefits of establishing a single set of requirements applicable across the three asset classes. This approach would streamline compliance efforts for data contributors reporting to multiple CTPs across various asset classes, promoting operational efficiency and reducing administrative burdens."*

According to an empirical study, minimum requirements for the technical criteria are barriers to innovation. Potential bidders to become CT Providers (CTPs) in the UK and EU, or Competing Consolidators (CCs) in the US, would prioritize compliance over creativity. Its focus is on meeting regulatory requirements rather than exploring better ways to address problems (e.g. RTS-13 Article 10 incomplete or potentially erroneous information a.k.a. data quality issues + security and synchronization challenge amid aggregation distance/ location differential issues). Amazon Time Sync Service provides time synchronization over Network Time Protocols. It has an observed accuracy of around 400 microseconds. Yet, multicast is not readily available in the public cloud. It has security and other complex issues. Why not learn from the current practices of High Frequency Trading firms/ self-aggregators when pursuing sub-microsecond precision?

Ecosystem degradation happens when damage is inflicted on others. Such damage can be in form of delayed access to information by subscribers of the public SIPs / CTPs, while trading venues' (TVs) proprietary products (PPs) are unreasonably priced that optimally allow access to only by few elite players. It can also take the form of under developing the public SIP / CT feeds in favor of self-interest to promote PPs. Ecosystem degradation can also result in high barriers of entry, in which one must rely on certain tools (e.g., smart order routers, transaction cost analyzers, liquidity sourcing, outsourced execution services) to have a reasonable chance to survive in the market.

The UK is a few months ahead of the EU in consultation on improving markets' transparency. The FCA is *"prioritizing the benefits of immediacy of price publication over full disclosure of traded volume."* Fragmentation is inevitable under Brexit. Although the FCA's efforts in collaborating with the industry to hash out many details for what they want in the CTs is applaudable. We strongly disagree with LSEG's attempt to deter regulatory consideration of a market-wide request for a pre-trade equities CT (see this).

Putting it in layperson terms, the LSEG and NYSE studies are about 'queuing and wait time at the checkout counters'. We think slippage and other phenomena are related to the capabilities differences between lit Exchanges, Multilateral Trading Facilities (MTFs), Systematic Internalizers (SIs), and Single Dealer Platforms (SDPs). The relative AVAILABILITY and price difference of mass market products (e.g., CT) versus TVs' PPs and Approved Publication Arrangements' (APAs) value-added services (VAS) is key. If the Have-Nots are willing to commit their limited resources to compete with the Haves, they should be given affordable and comparable choices.

Transmission and Availability are two different things. It is worth rethinking whether data should be required to be sent to the CTP and the whole concept of *"Trade Reporting"*. Instead of "SEND", "OBTAIN" or read-only permission to "wiretap" data legally at its source is a better approach. Wiretapping is the fastest approach and would eliminate the intermediaries. In addition, it has the following advantages:

- Benefits of Consistency – the economy of scale for centralized data management, minimize data-in-motion for cybersecurity and privacy protection, data quality is no longer a problem because what being shared is fair to everyone, avoid conflicts/ arbitrations between multiple versions of truths.
- Prevents a single point of failure – when one intermediary is down, X # of Investment Firms (IFs)' data would be missing. While one IF's connection with CTP is down, the implication is far less. When the CTP is down, the experience will be consistent for everyone, rather than some having the information, and some do not.
- Values of Bespoke Model connecting to everyone – enable the direct administration and enforcement of rights and obligations, mass customization through the powerful infrastructure, no melding nor favoritism by intermediaries to distort or subjectively allocate incentives.

The *"same manner same method"* provision under the US SEC's Market Data Infrastructure Rule (MDIR) $\neq$ Collocation $\neq$ Latency Equalization $\neq$ Market Data Available SECURELY in SYNCHRONIZED TIME. The former SEC Chair Mary Jo White has stated the need to *"deemphasize speed as a key to trading success."* Time-lock encryption protects time sensitive information from being decrypted prematurely. It eliminates the problem of where the CT data center is located.

Who owns the data and who gets what should NOT be dictated by regulators NOR by a small group of people in a "governance committee". Rebate tiering and competitive pricing of different market centers are analogous to Private Clubs favoring collaboration / outsourced trading. CT or other financial infrastructures are meant for the long-term. Policy makers should consider TVs as different streaming platforms and recognize the noumenon of rebate incentives serves as royalty payments for the use of others' copyrighted material. Healthy development of the industry should NOT only focus on latency or the velocity factor, but also the 3 other aspects of the 4V's, namely: veracity, variety, and volume.

Regardless of the US, UK, or EU, dismissing related market structure issues and be short-sighted to do the bare minimum in "checking the box" for market data reform is indeed a race towards the bottom. It will NOT achieve the goal of *"affecting competitive pressures for existing sellers of market data, resulting in cheaper, higher quality and more accessible data for its users."* Market reform should be about the divergence between private and social costs to delineate rights and obligations appropriately, as well as addressing extraordinary market volatility (e.g., Berkshire, Knight Capital, LME, Flash Crashes, MEME stocks phenomenon, and other vulnerabilities), amid transition from latency to A.I. algo driven markets.

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Data Boiler is a Type C organization member of the European Commission's Data Expert Group. Between my patented inventions in signal processing, analytics, machine learning, etc. and the wealth of experience of my partner, Peter Martyn, we are about Market Reform, Governance, Risk, Compliance, and FinTech Innovations to create viable paths toward sustainable economic growth.