Finance for Europe

Association for Financial Markets in Europe

Consultation Response

HM Treasury Wholesale Markets Review Consultation

(l) September 2021

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on **HM Treasury's Wholesale Markets Review consultation**. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

Chapter 2 – Trading Venues

1. Where do you think the regulatory perimeter for trading venues needs to be clarified?

AFME members agree that the current market structure for trading venues is generally sound. We recommend the avoidance of any significant changes to the existing regulatory perimeter for trading venues.

2. Do you think it would be more appropriate for changes to be made to the definition of a multilateral system in legislation, or for the application of the existing definition to be clarified through FCA guidance?

AFME supports HMT's approach with regard to the definition of a multilateral system. We do not believe that changes to the definition are required, recognising that an unnecessarily narrow definition would constrain trading activity, to the detriment of UK market structure. We agree that certainty regarding regulatory status will allow firms to compete effectively and fairly with one another, and therefore we believe it would be helpful for the regulator to provide guidance concerning high touch trading activity.

In this regard, we support comparable trading systems being defined and regulated in a consistent manner, however, it is important that differing types of trading activity, which are inappropriate for the definition of multilateral system, are not captured. In particular, high touch trading activity (typically conducted via voice broking) should be excluded from the definition. This activity contrasts heavily with multilateral platforms (e.g. continuous lit order book systems) and instead consist of a bespoke service provided to clients who typically trade in larger sizes.

AFME therefore suggests that FCA provides guidance which clarifies that the definition of multilateral system excludes transactions that are arranged in a non-automated manner.

By contrast we do not believe that further guidance is required regarding technology providers because we feel, subject to the assessment below, that these systems fall outside of the current definition. AFME members note that under the current regime provisions are made for the operation of diverse software and communications platforms such as EMS, OMS, chat, voice, RFQ, bulletin boards and so on which are not acting in a multilateral fashion. AFME members support healthy competition and diversity in financial markets and utilise a variety of platforms/utilities to provide and access liquidity for the benefit of their end clients. Technological advances and market structure innovation has delivered improved outcomes the users of and participants in European capital markets.

A key characteristic of the definition of multilateral is that of many to many interaction. The interaction in software is on a bilateral basis, as in any EMS or OMS, which routes trades bilaterally. Aggregation of bilateral indications (with no multilateral interaction) is still communication on a bilateral basis and thus does not require authorisation as a multilateral facility.

It should be the design of the system, the role the technology provider assumes, their involvement and responsibilities in the day-to-day operation, the type of protocols and interactions between participants within them that should be evaluated rather than superficial similarities with incumbent/legacy trading venues.

We also believe that it is important to distinguish between (i) systems that allow multiple third parties to interact in a system, and (ii) systems that allow for multiple bilateral interactions with existing relationships (where each bilateral interaction cannot interact with each other). The former are true multilateral systems while the latter are a collection of bilateral relationships with no multilateral aspects.

In addition, any facility where there is no genuine trade execution taking place in the system (see MiFIR Recital 8) and which does not have any involvement on how and where the trade might take place, should not be forced to become a trading venue. In this sense, we agree with ESMA which stated in its Q&A on market structure topics (Question 7), "the fundamental characteristic of a trading venue is to execute transactions".

Furthermore, we agree with HMT that that changes to the definition or unnecessary guidance for these systems would insert further barriers to entry and stifle innovation in this sector. Therefore, we believe that, ultimately, this should be a matter of supervision and enforcement rather than further legislative change. We recommend that the FCA engages with technology providers and works to ensure they have the correct permissions in place.

3. Should the current restrictions on matched principal trading by an MTF be retained?

AFME is supportive of proposals to permit matched principal trading by an MTF. AFME members do not see any benefit to a scenario where an investment firm is required to establish a separate entity in order to execute client orders in a matched principal capacity on its own MTF. This provides a cost-effective approach whilst maintaining the robust requirements set out under Article 18(4), MiFID II which requires that *"investment firms and market operators operating an MTF or an OTF have arrangements to identify clearly and manage the potential adverse consequences of any conflict of interest between the interest of the MTF, the OTF, their owners or the investment firm or market operator operating the MTF or OTF and the sound functioning of the MTF or OTF"*[1].

4. Should the current restrictions on the operation of an SI within the same legal entity of an OTF be retained?

AFME is supportive of the proposal to allow an investment firm to operate an SI and an OTF within the same legal entity. If conflicts of interest should arise, sufficient provisions exist already within MiFID for handling such matters appropriately.

[1] Article 18(4), MiFID II

5. **If you answered no to question 4:**

   Should new rules and disclosures be introduced to address the specific conflicts that MTFs and OTFs would be exposed to when providing MPT or operating an SI?

MTFs and OTFs are already subject to appropriate rules and disclosures as set out within the FCA Handbook[2]. Moreover, Article 18(4), MiFID II sets out a clear expectation that *"investment firms and market operators operating an MTF or an OTF have arrangements to identify clearly and manage the potential adverse consequences of any conflict of interest between the interest of the MTF, the OTF, their owners or the investment firm or market operator operating the MTF or OTF and the sound functioning of the MTF or OTF"*[3].

AFME does not consider that additional regulation on the management of specific conflicts would be necessary or helpful.

6. **Do you think that OTFs should be allowed to execute transactions in packages involving derivatives and equities under their rules and systems?**

AFME supports the proposal to allow OTFs to be allowed to execute transactions in packages involving derivatives and equities.

7. **What would be the risks and benefits of allowing this approach?**

AFME members agree with HMT's assessment that the restriction of the ability of OTFs to execute these trades achieves no meaningful regulatory objective and has instead introduced unnecessary complexity.

Allowing the execution of packages involving derivatives and equities under the rules and systems of an OTF avoids the unnecessary situation where separate legs of package transactions are executed across different trading mechanisms in an unnecessarily complex manner, for example where a swap or derivative is executed on an OTF with an underlying cash equity product executed elsewhere.

8. **Do you agree that the existing regulatory requirements for disclosure at admission to trading (for MTFs and SME Growth Markets) are disproportionate for small-sized issuers?**

No AFME response.

9. **What principles and/or types of information should be considered when developing requirements for disclosure at issuance to ensure requirements are proportionate?**

No AFME response.

10. **How far should these be determined by the venue operator versus regulation, and what other features may provide proportionate assurances around the quality of issuers admitted to a venue (e.g. role of advisors in process)?**

No AFME response.

[2] FCA Handbook, MAR 5, 5A and 5AA

[3] Article 18(4), MiFID II

11. Would the creation of a new category of trading venue be an appropriate means to facilitate access to public markets for very small firms? What size of firms would be appropriate for a new trading venue?

No AFME response.

12. If you answered no to question 11: Would the facilitation of the creation of new market segments be a more suitable intervention?

No AFME response.

13. If you answered yes to question 11 or 12: What should the market cap of companies that can trade on the new trading venue and/or segment be?

No AFME response.

14. Do you believe intermittent rather than continuous trading would increase liquidity?

No AFME response.

15. Do you think that additional measures, such as new funds structure are needed to stimulate institutional investors to invest in SMEs?

No AFME response.

16. What, if any, further forms of investor protection do you deem appropriate for this proposed new category of trading venue?

No AFME response.

17. Do you believe that regulatory or industry guidance about how venues should operate and what they should communicate during an outage would be useful?

Continuation of trading

During outages at incumbent exchanges, trading should continue on the alternative available MTFs. However, incumbent exchanges have proven to be to be a single point of failure largely due to the inefficient and inconsistent handling of such outages.

The current shortcomings in the industry surrounding communication and expectation are what primarily inhibit resilience. These should be the areas of focus. Because the expectations of how an outage will play out (and the way that other participants will respond) are usually unclear, the natural response is to 'wait and watch'. This is particularly so where the length of an outage could range from a few minutes to the rest of the day. The result is a self-fulfilling expectation that trading will halt entirely during a primary market trading outage.

To break this self-fulfilling expectation, we believe that industry participants across the board should adopt Communicate-First principles to identify and respond to outages effectively. Within this, we would emphasise that an agreed minimum time between notification of a venue re-opening and actually re-opening is a crucial element of influencing participant's behaviour.

Whilst FIA-EPTA and AFME members view the intraday price formation process as being distributed between available venues, primary market call-auctions are a clear exception during which price-formation is temporarily centralised. Currently, when a primary market re-starts following an outage, it is standard procedure to re-start the market with a call auction. At this point a majority of market participants will want to realign their trading activities with that call auction. Whilst there is no order-protection rule in the UK, many sizeable participants acting for clients will nevertheless implement similar routing decisions 'de-facto' to meet investor protection requirements. Absent a specific technical status to broadcast that a primary market is not functioning, any decision to disregard data from the primary market must be made, and reversed, manually. For this reason, venues which have suffered an outage should open in a manner which avoids dependency on the primary opening and causes minimal disruption to trading.

We believe this requires three principal developments:

- Development of outage playbooks by venues.
- Development of a central venue status communications platform that allows market participants to view in one place the *published* status of relevant trading venues, and, crucially, to communicate anonymously about the *observed* health of the venues.
- Development of minimum standards for outage communication channels from venues to participants once an outage is identified. This should be as standardised as possible and can potentially also utilise the envisioned central status platform.

Regulatory guidance around allowed participation by participants in the communications platform and expected timelines for venues to implement minimum outage communications standards can be useful to support the swift and consistent adoption by all relevant parties.

Policymakers and regulators should also consider further market structure reforms that minimise single points of failure and lessen dependencies on any one exchange. Secondary trading venues that can handle material trading volumes and critical functions including closing auctions, as well as independent sources of consolidated market data, can further promote market resiliency and stability.

Outage playbook

FIA-EPTA and AFME members agree that industry should work, together with the UK authorities, to formulate a playbook which will ensure the resilience of equities markets during major outages.

We believe this playbook should encompass a number of components and principles:

- Accurate and timely identification of outages by participants and trading venues.
- An orderly halt to trading on the affected venue halt and redirection of trading to alternate venues.
- Reliable and standardised broadcast of details surrounding the outage, order status, planned resolution and re-opening by the trading venue
- A minimum time between participants being notified of a venue re-opening and trading on that venue re-commencing.

- Orderly restart of the affected trading venue and resumption of trading, with specific scenarios dependent upon the timing and nature of the outage.

Continuation of trading requires simply improved process and communications, not any adoption of specific alternative opening trading phases; though in the case of the closing auction and settlement price determination the problem requires more consideration to ensure consistent adoption across the industry of a mechanism to deliver realistic prices.

Central venue status communications platform

AFME and FIA-EPTA propose that a central venue status communications platform be developed as an industry-wide initiative. Good communications from trading venues are heavily reliant on a venue to be first aware that it is experiencing technical difficulties and to be incentivised to notify participants. In practice, market participants are often the first to notice issues with connectivity, market data, or order flow at a venue. Presently, there is no standardised and commercially secure way in which participants can communicate amongst themselves to alert others of potential outages and identify if the issue is internal to the participant's systems or a broad venue issue. To solve this, AFME and FIA-EPTA consider that a secure venue status communications platform could provide a centralised tool to more identify outages quickly and to maintain continuity of trading.

This platform should be simple and secure in its design and we envision a step-wise, iterative approach to its development. In the future, such a platform could form a valuable single central hub whereby any participants or other stakeholders could obtain information about the health of trading venues. However, to get to that state would be a large project and in some ways parallel or duplicate efforts and tools that trading venues already maintain. Therefore we propose beginning with a simple platform with the goal of offering market participants a multilateral place to communicate anonymously about trading venue issues and health, and only after its proven adoption, possibly expanding its function.

The platform should have the following features:

- Secure and validated; users should be bona-fide participants, venues, or relevant stakeholders in a place to offer actual insight into venue health
- Monitorable by regulators; to ensure no market abuse occurs
- Anonymous to each other; users should not need to balance any reputational issues against open communication
- Multi-lateral; all users should be able to view and participate in the discussions
- Simple to implement; ideally leveraging existing widely adopted industry communications platforms
- Built with an awareness of the potential broader functions in the future

As stated earlier, we believe that a simple communications platform can allow market participants and venues to far more rapidly and efficiently identify outages or technical failures at trading venues. Following this identification, trading venues would take up the responsibility for communicating information about the outage, order book/execution status, and planned resolution. To keep the platform initially simple to implement, we envision this second stage of communication to occur through existing venue channels, subject to minimum standards as described below. That said, we do believe that with time, the envisioned communications platform can potentially become a central point of venue communication.

Minimum standards for venue outage communication

AFME and FIA-EPTA have both previously put out some proposals for minimum standards of communication that we would like to see adopted by trading venues across the industry. We still believe that the adoption of these standards would go a long way toward improving the resilience of (EU/UK) markets in an outage situation. Regulatory guidance around expected participation and timelines can be useful to support the swift and consistent adoption by all relevant parties of the standards developed jointly.
We propose the following minimum standards:

Pre-established procedures

- A crisis management team should be established at each trading venue. This crisis management team would be responsible for communications around outages to all stakeholders as well as maintaining the venue's crisis playbook.
- All trading venues should develop and publish a playbook for what will occur if or when an outage takes place.
    - The playbook should clearly identify the mechanisms and locations (websites, protocols) for dissemination of information to stakeholders regarding the outage.
    - It should be clear what information these channels will include and in what format.
    - In addition, there should be protocols for identifying, diagnosing and resolving issues and halting and restarting trading including a minimum notification time.
    - Playbooks should outline different scenarios in which exchanges will or will not re-open and establish clear procedures for re-opening.
    - Trading venues should also define a procedure to determine the market closing price in the event where the market cannot reopen.

During the outage

- Trading venues must be proactive and clear in their communications, giving stakeholders as much detail as is known, as soon as it is known, without speculation.
- Ideally, communications regarding market status should also be in a machine-readable format, available on exchange connectivity and market data protocols, so that trading systems can automatically incorporate these notifications into their procedures, where relevant.
- All communication regarding the ongoing health of a venue's trading system and details about possible outages should also be made publicly available to all interested parties and hosted in a central location, for instance on a defined webpage.
- These communications should be updated on a fixed schedule, for instance every 15 minutes, giving a status update, even if the update is "no update".

Status of orders

- At a minimum, any market statuses, instrument prices, outstanding order statuses, and trade feeds published by trading venues on their execution or market data feeds must be accurate and consistent during an outage, and not lead participants to believe the venue is operating in a normal state. A special outage or closed status can aid this.
- This market data notification regarding status is essential for the market to know without doubt that there is a technical issue on the market, which can in turn trigger participants' automatic redundancy plans and allow participants to decide whether or not to continue trading elsewhere.
- Trading venues should make public the specific time stamps at the point at which orders were cleared and/or rejected and which trades were considered valid. This should be done as soon as is feasible.

Reopening

- Any planned re-opening times should be published on this central location. Re-opening times should be communicated clearly to the market at least 20 minutes prior to opening and re-open on a "round" time increment (e.g., [on the hour or half hour]).
- Trading venues should consult with participants on whether to re-open to ensure there are no outstanding issues which might be further exacerbated by the market re-open.
- When a venue restarts it should open in a manner which avoids dependency on the primary opening and causes minimal disruption to trading.

After an outage

- Trading venues should provide all stakeholders and members with a comprehensive post-mortem analysis and follow-up points after any major incident, which should include disclosure of the root cause and the steps taken to rectify and prevent recurrence.
- Outages will happen. Venues should be judged on how well they handle those outages.

18. Do you have views on a fail-safe mechanism to ensure that the market has access to the key closing benchmarks during an outage in a primary exchange? What role do you see UK authorities playing to deliver this?

Yes, AFME and FIA-EPTA believe that the industry (participants and venues) and regulators should continue to work together to ensure that there is always a closing-price generating auction that the majority if not all market participants can access for both trading and settlement as well as utilize for benchmark calculation and derivatives settlement where relevant.

We do not yet have a clear view on whether this should occur on a secondary venue or an alternative 'failsafe' channel within the primary venue, although depending on the link of the failsafe channel at the primary venue, a separate channel will be preferred. We welcome further discussion amongst industry stakeholders and venues on the matter to come to a concrete proposal.

Regulators can play a role in ensuring that individual business interests can be transcended in the name of better systemic resilience by participating in and facilitating this dialog. Furthermore, regulators can aid the discussion by setting expectations for timelines of both agreement and implementation of the agreed mechanism by the industry at large. Following implementation regulators should also play a role by ensuring that the mechanism as agreed remains functional and operative.

UK authorities could therefore make provisions that require primary markets to recognise, as the official closing reference price, an industry agreed alternate closing reference price in the event that a market outage has prevented the establishment of a closing reference price in the usual manner.

19. What other steps do you think UK authorities could take to ensure market resiliency in the event of an outage?

AFME and FIA-EPTA propose the removal or amendment of Article 15(2), RTS 7 which refers to exchanges' requirement to "*ensure that trading can be resumed* ***within or close to two hours*** *of a disruptive incident*". This is counterproductive as it creates an incentive to resume trading at an arbitrary point in time even if there are still system issues while in the interim discouraging shifting continuous trading to an alternative venue. It is also ignoring the nature of outages which dictate that a venue will be unable to control whether it can resume orderly trading within that timeframe.

Proposed regulatory changes for reference prices:

Certain changes introduced by MiFID II have increased the likelihood that trading will not migrate to other venues where the "main" market (i.e. the market where the instrument is admitted to trading) is not operating. These concentrate financial markets' reliance on individual venues (exacerbating or contributing to disorderly markets), inhibit investors' ability to manage their investments and prevent the migration of activity to other markets (where it could safely otherwise take place in an orderly manner):

A) We believe that the definition of the most relevant market in terms of liquidity (Article 4, RTS 1) should be amended and its use reviewed. This definition is important as it currently drives the reference price for the reference price waiver, provides a reference price for SI quoting (Article 10 RTS 1) and is relied on for the material market definition to determine the venue that communicates announcements on trading halts (Article 1 RTS 12).

B) In calculating the most relevant market in terms of liquidity, the opening and closing auction turnover should be excluded from the calculation (as are other forms of trading such as negotiated and large in scale transactions). These are quasi monopolistic trading phases which do not take place on other venues and so decrease the likelihood that a market other than the main market will be the most relevant market. It prevents like-for-like comparison of the continuous trading phase (that happens on multiple markets).

C) There is no reason that reference price waiver (Art 4(1)(a) of MiFIR) should rely on the most relevant market in terms of liquidity. Such reliance increases dependencies in the market and prevents the orderly migration of trading. It should revert to a definition similar to the one that existed in MiFID I (e.g. a price that is "widely published and is regarded generally by market participants as a reliable reference price").

D) SIs should be able to formulate their quotes on the basis of prices other than that most relevant market where that market is not in operation. An amendment should be made to Article 10 of RTS 1 to permit this (e.g. by adding "unless the most relevant market in terms of liquidity is not operating or not operating in an orderly fashion, in which cases the SI may use other reference prices that it determines reflect prevailing market conditions").]

Chapter 3 – Systematic Internalisers (Sis)

20. Do you agree that the definition for SIs should be based on qualitative criteria?

AFME is supportive of having a qualitative definition for SIs, however it is important that the regime retains a standardised mechanism which ensures that investment firms that execute client orders on an organised, frequent, systematic and substantial basis continue to register as SIs. We therefore recommend that HMT adopts the MiFID I definition of systematic internaliser which is "an investment firm which, an organised, frequent and systematic basis, deals on own account by executing client orders outside a regulated market or MTF".

If further guidance is required concerning the criteria of the SI definition this should be outlined in the FCA handbook as guidance.

From a fixed income perspective, AFME members note that the SI regime has not transferred well to non-equity instruments such as cash bonds given the vast differences in the trading profiles of equity and non-equity instruments. Nevertheless, FI members agree that the construct of the SI regime should be maintained given the correlation to the MIFID reporting requirements however the regime should be reworked in line with the removal/revision of some of the other pre-trade transparency requirements for fixed income instruments.

Please see our response to Question 24 regarding our proposal for a separate designation for reporting purposes only.

21. If you answered no to question 20: Do you think the definition should be amended in another way?

Please see AFME's response to Question 20.

22. If you answered yes to question 20: Do you think that regulatory guidance should be used to support the definition in legislation?

AFME members suggest that the FCA monitors the outcomes from the new approach and if additional guidance is deemed necessary, AFME and its members would welcome the opportunity to engage with the FCA. We expect that this guidance is most likely to be required for edge cases and in any event, AFME members expect that the opt-in option will remain.

23. Do you currently opt-in to the SI regime?

Many AFME members opt into the SI regime. Irrespective of whether they meet the current threshold requirement, one of the main reasons for opting in is to assist with and facilitate clients' MiFID II post-trade reporting.

24. Should SIs be determined at entity level instead of on an instrument by instrument basis, for reporting purposes?

AFME agrees with HMT's observation that where SIs are determined at an instrument by instrument level for some transactions this can create uncertainty about who should report the trade. It is important that it should be clear that designation of SIs at any level for reporting purposes should be clarified as being only for this service and should be distinct from transferring other regulatory obligations for firms that are acting in an SI capacity. AFME supports the concept outlined in HMT's consultation, however we propose that a firm should be a designated reporting entity separately to being determined an SI for a specific instrument or by entity. With respect to the level of the designation, AFME notes that firms vary in size and scale and it may not be viable for smaller firms to be designated for reporting in all asset classes and therefore an asset class/sub-asset class rather than entity level designation may be considered by HMT to be a more proportionate approach. Additionally for equities, we believe that for the purposes of pre-trade transparency, firms should be able to opt-in on an instrument by instrument level.

This approach would require the FCA to keep the list of designated entities to which clients could refer to understand which party would report, and where neither party is a designated reporter then the seller would report. AFME believes that this approach and the FCA's central maintenance of this registry would be enormously valuable to the market. However, if the FCA has concerns with regard to administering this registry then we would be happy to explore other options such as a standard setting body or a voluntary provider. The designated reporting entity approach has the advantage that firms determined or opted in as SIs will be only those firms acting as SIs where the business model and service provision fits the definition.

With respect to a designated reporting entity, AFME believes that third country firms who are regulated and who are able to provide investment services within the UK should be able to opt in both as an SI and a designated reporting entity

25. What would be the risks and benefits of adopting such an approach?

Identifying reporting responsibility at instrument level is excessively complex for all involved. Moving up to an asset class or sub-asset class basis would provide greater clarity for buy-side firms (who will find it easier to identify who will be reporting) and allow sell-side firms to shoulder reporting responsibility in the asset classes for which it makes sense for them to do so. For bigger firms, this may be every asset class, and having the ability to opt in allows such firms to obtain all the benefits of entity-level reporting entity identification while also allowing smaller or more specialised firms to report in a way that is more appropriate to their size or business activities. The same reasoning applies to SI identification.

As stated in our response to Q24, by removing the link between SI status and post-trade transparency, the designated reporting entity approach provides the benefit that firms determined or opted in as SIs will be only those firms acting as SIs where the business model and service provision fits the definition.

26. Do you agree with the government's proposal to allow SIs to execute at the midpoint for all trades, provided the executed price is within the SI's quoted price?

AFME supports HMT's desire to promote SI's ability to offer best execution to their clients through the provision of execution at mid-point at any size. Execution at mid-point is a globally accepted execution mechanism. The UK and EU are alone in applying a requirement for brokers to execute at a round tick and preference on counterparty over another when determining the execution price. In other jurisdictions, firms are able to offer price improvement, benefitting the end client, by executing at the mid-point. This is particularly valuable for investors seeking to execute in larger sizes.

The purpose of the tick size regime is to ensure orderly and transparent trading takes place on trading venues through promoting the effective formation of prices on displayed order books. It also helps to maintain a reasonable depth of liquidity whilst allowing spreads to fluctuate. The tick size regime's relevance is principally to order book driven markets which are pre-trade transparent (e.g. on venues that accept orders with a specified limit price), and to alternative trading mechanisms that are comparable/competitive to such order book driven markets. For bilateral trading, especially above SMS, the tick size regime has no relevance and does not serve to help or protect investors in any way, in fact it works to their detriment by limiting SIs ability to offer execution at mid-point which, in other jurisdictions, provides a fair and effective way of providing price improvement

With the aim of allowing end investors to benefit from price improvement and to ensure a fair application across any type of trading venue, AFME recommends the following approach for both trading venues and SIs:

- for all sizes of order, mid-point should remain a valid execution price, permitted to trade at a half tick, both on trading venues and SIs
- trades that are above Large in Scale (LIS) or that are non-price forming should not be subject to the tick size regime;

This would guarantee that SIs are able to provide meaningful price improvement in trades of significant size (i.e. above SMS but below LIS) without having to risk information leakage by advertising sizeable trading interest through their quotes.

AFME is concerned by the proposal to limit the provision of mid-point to trades that are not larger than the SI's quoted size given that public SI quotes drive the risk provision to an SI's clients. The proposal set out by HMT would introduce a scenario where, in order to execute at midpoint, SIs would expected to provide public quotes in significant sizes which could be hit repeatedly by other market participants. Such a requirement introduces high levels of risk which could not be justified and would ultimately result in firms being unable to execute at midpoint for large trades.

This would lead to a system where firms would be able to execute at midpoint for small trades (e.g. £5,000) but would be unable to do so for larger trades below LIS (e.g. £500,000). The net effect of this would be that investors only receive the benefits of price improvement for smaller trades but not in larger sizes where the benefit would be greater. Please see the table below which demonstrates the implications of HMT's proposal:

Trade size	Is there a risk of SIs' public quotes being hit multiple times in sizes beyond their risk appetite?	Trade size below LIS for liquid stocks?	Are SIs practically capable to provide midpoint execution?
£5,000	No	Yes	Yes
£500,000	Yes	Yes	No

For the avoidance of doubt, there should be no restriction in size relating to when firms are permitted to execute at mid-point. AFME believes that there are other ways to encourage the SI quotes, please see our response to Question 27 for more detail.

27. Do you think any other changes are needed to increase the effectiveness of the SI regime?

The effectiveness of the SI regime is of utmost importance for the trading of both equities and non-equities instruments.

For equity markets, on the basis that the SMS remains at current levels and subject to further in-depth analysis before being proposed, AFME members would be supportive of increasing the minimum quoting size to 100% of SMS for shares as this broadly represents the average trade size of business executed on trading venues, meaning SIs can control their risk and continue to use the top of book as the benchmark to quote and reflect prevailing market conditions.

AFME members stress that such a proposal can only be acceptable if the SMS continues to be a fair representation of the average traded value for the stocks.

From a fixed income perspective, based on the adoption of the designated reporting proposal outlined in our response to Q24, AFME and its members do not consider that any other changes are needed to increase the effectiveness of the SI regime.

AFME members note that the SI regime was originally introduced for equity instruments only under MiFID I to ensure more transparency was available regarding the trading of equity instruments traded outside the perimeter of an exchange, given exchange trading is the predominant mode of trading for equity instruments, for this reason the SI regime links directly to the STO for equities. The SI regime was extended to non-equity asset classes under MiFID II. Within Fixed income, given the bespoke nature of each instrument, bonds predominantly trade OTC. Furthermore, there is no link between the SI regime and the DTO for derivatives. Essentially, for non-equity asset classes such as fixed income, their bilateral trading activities have remained consistent since the introduction of MiFID II, the SI regime is merely a new name that has been given to some investment firms when trading bilaterally above a certain level. Given the current post-trade reporting waterfall, a large majority of firms have decided to opt in/identify themselves as SIs in order to assist their clients with post-trade reporting requirements, even if they do not strictly fall under the definition and the trading thresholds. Consequently, these firms are then subject to the pre-trade rules, an unwelcome consequence of the MiFID II regime.

In summary AFME fixed income members conclude that the SI regime has not transferred well to non-equity instruments such as cash bonds, given the vast differences in the trading profiles of equity and non-equity instruments.

Chapter 4 – Equity Markets

28. Do you think that the DVC should be deleted?

Yes.

Having a diversity of execution mechanisms within UK equity market structure is vital to facilitating varying sets of investment strategies and objectives. Different types of liquidity existing within the same broader eco-system is a sign of a healthy market. On this point, we refer to the FCA Occasional Paper 17/29, "Aggregate Market Quality Implications of Dark Trading" which asserts that *"since the trades executed in the dark are based on reference prices determined on the lit exchanges, the overall market's price discovery process is more efficient for each stock traded simultaneously in the dark and lit venues*". We also note the Paper's conclusion that trading quality is "*furthered by the existence of dark pools operating alongside lit exchanges. It is important that policy makers take care not to eliminate the market quality benefits of dark trading by arbitrarily imposing uniform dark trading restrictions for all stock sizes".*

AFME does not believe that enforcing increased lit trading necessarily improves price formation and, conversely, may impact the ability for firms to provide best execution for their clients. For these reasons, AFME has consistently called for the removal of the DVC which has resulted in no beneficial outcomes for end-investors and has resulted in unhelpful complexity in equity market structure.

UK and EU markets are alone in applying a volume-based constraint on dark trading making them a global outlier. Investors utilising dark pools do so with the objective of reducing market impact and therefore implicit cost. This in turn contributes to achieving better execution performance for the end investor.

For these reasons, we support the deletion of the DVC and agree that this approach will significantly reduce operational complexity in markets, lower compliance costs and increase stability and predictability in the trading of equity instruments.

AFME is also supportive of the proposal that the FCA continues to monitor the level of dark trading in UK markets. We support the notion that price formation needs to be protected and believe that the FCA should be able to intervene in extraordinary circumstances where it can be proved that the level of dark trading is undermining the price formation process.

29. Do you think alternative incentives are needed to encourage lit trading?

AFME members value the role of the lit order book and there is no desire to see non-exchange flow to represent the majority of execution within equities markets. However, we urge HMT to recognise the benefits to end investors brought about through the existence of a variety of execution choices. Diversity in trading choices supports positive outcomes for end-users and is a feature of a mature market structure. It is vital to recognise appropriately the important role played by SIs providing liquidity on risk. This risk intermediation is an absolutely essential part of a healthy investment ecosystem. SIs act as a 'shock absorber' for end-users by limiting price impacts of client positions. It is important to preserve such risk provision as part of the UK's market eco-system.

In accordance with the best execution rules set out within MiFID II, achieving the best price possible for clients is the key factor which determines where sell-side firms decide where to route orders. AFME members always take a data driven approach when considering which execution platforms offer the optimal execution conditions for an order.

AFME does not believe that there is any need for regulatory intervention and we don't support the introduction of any rules which have a bias towards one particular type of trading. Instead, we recommend that UK authorities review of the existing market structure with a view to judging whether the broader system can be deliver better outcomes for end investors (for example via the changes suggested in Question 30).

30. Should reference price systems be able to match orders at the midpoint within the current bid and offer of any UK or non-UK trading venue that offers the best bid or offer, to aid best execution?

Yes.

AFME agrees with HMT's proposal and believes that being able to reference any trading venue that offers the best bid or offer will aid best execution. This will ensure that the price being used will be a reflection of the best execution conditions based on the nature of the order. However, in order to provide reference price systems with greater capacity to determine the best possible bid or offer, they should be able to reference multiple venues at once.

This approach will also lay the groundwork for a solution to primary market outages (please see our response to Q.19). Allowing reference price systems to reference any trading venue will prevent the existing scenario where trading venues operating under a reference price waiver must reference the primary market. Although this change alone will not provide an adequate solution to market outage scenarios, it is a necessary step towards ensuring that trading in UK equity markets can continue in the event of a market outage.

31. Do you consider SIs quotes useful?

AFME's response to question 31 represents an equities view only. Please refer to our response to question 52 and 53 within Chapter 5 of this CP which contain our views on the use of SI quotes within bond markets. Under the current system, the incentive to be a systematic internaliser in equities has been driven by the requirements of the STO and the post trade transparency regime which have both led to firms opting in as a systematic internalisers for a wide array of instruments, many of which they might not actively trade. As a result of the proposals set out within the Wholesale Market Review consultation (particularly the removal of the STO and the application of a qualitative definition for SIs), we would expect firms to opt-in for as an SI for a more specific set of instruments which they actively trade. This should have a positive effect on the utility of the quotes being provided by SIs.

In our response to Question 27, we consider how SI quotes could be made more useful. In our response to this question, we state that on the basis that the SMS remains at current levels and subject to further in-depth analysis before being proposed, AFME members would be supportive of increasing the minimum quoting size to 100% of SMS for shares as this broadly represents the average trade size of business executed on trading venues, meaning SIs can control their risk and continue to use the top of book as the benchmark to quote and reflect prevailing market conditions. However, we would like to emphasise that such a decision should only be taken on the basis of in-depth, data driven analysis which fully considers impacts to UK market structure.

AFME members stress that such a proposal can only be acceptable if the SMS continues to be a fair representation of the average traded value for the stocks.

32. Do you think that the ability of SIs to execute clients' orders at midpoint would incentivise SIs to provide meaningful quotes?

Yes.

Permitting SIs to quote and execute at mid-point will result in more meaningful pre-trade transparency which represents a positive outcome for investors who also stand to benefit from price improvement.

For the reasons discussed in our response Q26, we do not agree with HMT's proposal to limit SI's ability to execute at mid-point to trades that are not larger than the SI's quoted size. AFME believes that there are other ways to encourage SI quotes, please see our response to Question 27 for more detail.

33. If you answered yes to question 32. What incentives could UK authorities introduce to encourage you to report more trades, while maintaining fair competition with market operators?

AFME does not support the notion of conducting a like for like comparison between trading venues and SIs (as in paragraph 4.15 of HMT's consultation).

AFME members value the price formation and price discovery provided by lit venues and do not wish to see that undermined. However, it is important to recognise that investors, including institutional asset managers, require a range of liquidity solutions to help meet their investment objectives. These include the execution of orders on trading venues, but also the ability for clients to gain the benefit of systematic internalisers' higher risk tolerance or balance sheet. An example of this is where an asset manager is looking to execute in large size with urgency. This liquidity may not be immediately available on trading venues. AFME members may take the risk from these clients providing certainty of execution to them and managing the subsequent market risk themselves.

In managing the market risk over an appropriate time horizon, AFME members will typically feed the risk into the market via multi-lateral trading venues. In this way, they bridge the asset manager's requirement to trade in large size and immediately, with the generally available supply of liquidity. As such SIs play a distinct and important role in bringing liquidity to the market.
Please refer to our response to Question 27 regarding ways in which to encourage SI quoting.

34. Do you think that the share trading obligation (STO) should be removed?

Yes.

AFME members believe the STO should be removed. It does not result in positive outcomes for end-users and increases complexity in market structure. Mitigating the unforeseen negative consequences of the STO has taken significant effort from UK officials, regulators and practitioners across the industry, for little benefit. The legislation has not cast the UK in a favourable light as a place in which to invest or raise capital.

We agree with UK authorities that the removal of the STO is necessary to ensure that UK based firms have the ability to execute trades on the venues where they will achieve optimal results for their clients. The STO stands as a direct barrier to firms being able to do so because it restricts trading in a way that is inappropriate, ineffective and not conducive to price formation or stability.

MiFID already ensures that multilateral trading cannot take place outside of a regulated market or a multilateral trading facilities. In addition, the SI regime and its qualifying thresholds ensure adequate supervision of firms that effect price forming transactions outside of trading venues. Additionally, the needs of firms to benchmark prices to the primary market for a given share drives trading to UK venues including the primary listing venue. Finally, the overall transparency regime for equity markets ensures visibility of both pre and post trade information.

AFME notes that removal of the STO may create some uncertainty with regard to the status of transactions currently exempted from the provision. AFME suggests that HMT makes clear that these trades continue to exempted from taking place on-venue including guaranteed VWAP transactions in particular, where VWAP price points rarely conclude on tick or at mid-point, and will therefore fall outside of the tick size regime.

35. Do you think that the requirements for algorithmic liquidity providers and trading venues to enter into binding market making agreements should be removed?

Yes.

AFME does not believe that UK authorities should favour any type of market activity. Where market participants decide to trade is a commercial decision that we do not consider as relevant for regulatory intervention.

36. What would be the impact of such a removal for you and/ or the market you operate in?

AFME members hope that the removal of the requirement for algorithmic liquidity providers and trading venues to enter into binding market making agreements will lead to more innovation relating to how liquidity can be provided in different circumstances.

37. Do you think the scope of the tick size regime needs to be recalibrated for overseas shares to ensure that firms can trade at the best prices in the UK?

Yes.

AFME supports proposals to recalibrate the tick size regime to allow trading venues to follow the tick sizes applicable in the relevant primary market of a share where that share does not have its primary market in the UK.

For dual listed shares, it is possible that there might be more than one tick size. HMT should ensure that MTFs are able to use any applicable tick sizes for these types of shares. This will ensure that trading venues are able to use the third country listed tick size for the third country line of the share.

38. Do you think trading venues are better placed to establish tick sizes for new shares until sufficiently robust data is available?

Yes. We agree that trading venues are well place to establish tick sizes for new shares ahead of robust data becoming available. However, we suggest that trading venue tick size determinations are submitted to the FCA to be compiled in an FCA database. This will help to ensure that tick sizes established by trading venues are appropriate whilst also ensuring that there is a single source for tick size data.

We take note of the current process undertaken by the FCA (as stated in its Statement on the Operation of the MiFID Markets Regime) where an initial estimate is applied and then updated after 6 weeks with a calculation for the first 4 weeks of trading in the UK. We believe that this is an appropriate approach.

39. What are the potential benefits and risks of delegating the setting of tick sizes, in general, to trading venues? What safeguards would be needed to avoid arbitrage issues?

AFME does not support the delegation of the setting of tick sizes, in general, to trading venues.

Previous experience demonstrates that trading venues in the UK and Europe have been unable to resist the temptation of competitively reducing tick sizes on their platforms in order to attract liquidity. When exchanges were previously entrusted with the setting of tick sizes, they openly admitted that this scenario led to a "race to the bottom" which led to "excessively granular tick sizes"[4]. Even after the introduction of the FESE tick size

[4] European exchanges finally agree tick size regime, https://www.finextra.com/pressarticle/28392/european-exchanges-finally-agree-tick-size-regime, 2009

table in 2009, exchanges were still incentivised to reduce tick sizes on their venue with certain exchanges choosing to go against the industry agreed protocol[5].

Trading venues are commercially driven enterprises which will seek to maximise profit through the attraction of liquidity. Although AFME can see a role for trading venues in establishing the appropriate tick size for new shares, we strongly oppose delegating the task of setting tick sizes on a permanent basis.

40. Are there any other parts of the equity regime that you think could be operated more effectively by the market, while upholding high standards?

AFME believes that there are several areas where the UK equity regime could be improved. We have detailed our recommendations below:

Treatment of non-price forming/technical trades:

a) Give ups

AFME believes that post-trade data quality could be significantly improved by recognising that the inclusion of non-price forming technical trades (which do not include portfolio trades and benchmark trades that should be appropriately flagged) damages the tape.

The existing RTS1 definition of give-in/ups does not accord with how most give-ups are structured in the equities market in practice. Thus, the industry is not considering equities give-ups being exempt from post-trade transparency. While ESMA tried to address the shortcomings through the 2019 ESMA Q&A on RFMD trades, this meant that transactions that should have been excluded by the give up definition are in fact reported (as XOFF with the TNCP flag). ESMA is also, separately, proposing to remove the TNCP flag within its consultation on RTS 1 and RTS 2, without specifying how equities give-ups should be reported. If implemented, this will lead to firms reporting give-ups as price forming transactions, which is not correct.

Most give ups and give ins in the equities market, do not involve a 'client trade' that is passed to another investment firm for the purpose of post-trade processing (though this may happen in other scenarios – e.g. in the futures and options markets).

Equities clients that have a prime broker relationships keep all their transactions with one or more prime brokers (PBs). However, they may not rely on their PBs for all executions. Instead, an Executing Broker (EB) is sent a request for market data, and following such a request, the EB undertakes a series of own account risk trades (which are reported to the tape by the venue or EB as they take place). The EB then offers (or, in other words, gives up) the own account trade or trades, usually on a net basis and often at the end of the day, to the client's PB. The PB then holds the position (for example as a custodian for the client) or enters into a swap with them (and uses the position as the hedge). Since the price forming trades were reported already when they happened (by the venue or EB, as applicable), there is no value in printing the (non-price forming) give-up between the EB and the PB to the tape.

[5] Euronext sparks outrage with tick size reduction, https://www.ft.com/content/97f0deb0-2ad1-11e0-a2f3-00144feab49a, 2011

We therefore propose that HMT retain and enhance the give-up definition in Article 1 of RTS 1 (in line with the Q&A) and that the reference to it in Article 13(c) of RTS 1 is retained. We propose that it is enhanced as follows so that it is capable of capturing most give-ups in the equities markets:

'give-up transaction' or 'give-in transaction' means a transaction where:

i) an investment firm passes a client trade to, or receives a client trade from, another investment firm for the purpose of post-trade processing<u>; or</u>

ii) <u>following a request for market data, an investment firm passes a risk trade to, or receives a risk trade from, another investment firm or third country financial institution.</u>

b) Inter-affiliate trades for the purpose of risk management

In relation to inter-affiliate trades, we do not believe that trades that occur for the purpose of intra-group risk management should be published to the tape and that they should be excluded under Article 2, Article 6 and Article 13 of RTS 1 (see our response to Q3). This is because the activity that these trades represent is to balance risk between group entities. It does not represent activity that could or would have been entered into with any other party and is not relevant when considering overall liquidity in a stock. On that basis, it is, as FIX suggest, intra-group housekeeping activity, and publication of it would give a misleading view of available liquidity in a particular instrument. We also do not believe that these transactions should be restructured (or otherwise flagged) as BENC or PORT transactions as ESMA suggest in their recent consultation on RTS 1 and RTS 2. To keep the tape clean, the BENC and PORT flags should only be used for benchmark and portfolio activity that represents addressable liquidity.

We would like to make clear that whilst our view is that these types of transactions (a and b) should be not be reported for the purposes of post-trade transparency, we believe that investment firms should be required to report these transactions in accordance with their obligations set out under Article 26, MiFIR.

c) Trades brought on a venue for clearing purposes

Some trade venues offer a service of counterparties being able to settle otherwise bi-lateral trades via CCP. The mechanics of such process requires the trade to be settled to be brought in on the trade venue, after which it will be submitted by the venue to CCP. AFME strongly believes that these trades should be specifically flagged or not included for the purpose of post trade transparency so that they can be easily removed when attempting to identify addressable liquidity. These trades are composed of an aggregated positions resulting from an earlier market activity that will already have been subject to post trade transparency rules and trade reported as a result.

<u>High touch trading:</u>

We agree that certainty regarding regulatory status will allow firms to compete effectively and fairly with one another, and therefore we believe it would be helpful for the regulator to provide guidance concerning high touch trading activity. .

In this regard, we support comparable trading systems being defined and regulated in a consistent manner, however, it is important that differing types of trading activity, which are inappropriate for the definition of multilateral system, are not captured. In particular, high touch trading activity (typically conducted via voice broking) should be excluded from the definition. This activity contrasts heavily with multilateral platforms (e.g. continuous lit order book systems) and instead consist of a bespoke service provided to clients who typically trade in larger sizes.

Transaction reporting:

Currently, firms dealing on own account are required to flag their position using the short sell indicator flag. Unfortunately, this system has not worked well in practice as firms are unable to convey their actual trading intent and instead can only show the position of individual trades.

AFME recommends that FCA consults on this issue and stands ready to assist in finding an appropriate solution.

Equity indices:

AFME believes HMT should consider mandating that equity index compilers use alternate price sources in cases where their default pricing sources are unavailable.

Interoperability:

Separately, AFME recommends that HMT explore the option of mandating that UK trading venues offer full interoperability for clearing. By obliging CCPs to interconnect, HMT would assist market participants to reduce costs through netting as cross margining trades taking place across different trading venues. We note that the London Stock Exchange have voiced their support for both open access and interoperability (LSEG - "Open Access: Myth Busting).

Chapter 5 – Fixed Income and Derivatives Market

41. Do you agree that the scope of the DTO should be revised to bring it in line with the scope of the CO following the changes introduced by the EMIR REFIT? What risks/ benefits do you see with this approach?

Please revert to ISDA response.

42. Do you think that all post-trade risk reduction services should be exempt from the DTO?

Please revert to ISDA response.

43. If you answered yes to question 42:

a) Do you think that there should also be an aligned exemption from the EMIR clearing obligation for trades resulting from post-trade risk reduction services?

Please revert to ISDA response.

b) What conditions do you think should be met for the exemption to be applicable?

Please revert to ISDA response.

44. Do you think the FCA should be given the power to modify or suspend the DTO quickly under certain circumstances, on a permanent rather than temporary basis?

Please revert to ISDA response.

45. Do you think that the current transparency requirements support price formation and open, competitive and fair markets? Please separate your answers by fixed income (please treat sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (please distinguish between OTC and exchange-traded derivatives (ETDs) where relevant).

AFME members welcome HMT's acknowledgement and consideration of different bond types throughout section 5 of this CP, which focuses on the transparency regime for fixed income and derivative markets.

MiFID II/ MiFIR is one of the most significant pieces of financial regulation ever implemented and incorporates the widest scope of products and asset classes in the world within its transparency regime. With regards to pre-trade transparency requirements within bond markets (including sovereign bonds, high yield bonds and investment grade bonds), consistent observations conclude that this information is not used , instead market participants prefer to utilize consistently updated market data streams for the purposes of price discovery. One of the main reasons for the lack of appetite for pre-trade transparency data is because the application of pre-trade transparency data does not lend itself well to bond markets, Bond trading is not an order book driven market but typically employs a request for quote (RFQ) model, whereby buyside clients send a query to multiple dealers simultaneously, Given the bespoke nature of fixed income instruments this makes it challenging for pre-trade quotes to be generalised or relied upon as a guide price.

In terms of post-trade transparency data, AFME members have observed that MiFID II transparency reporting requirements have significantly increased the amount of post-trade transparency data available to investors and market participants in non-equity asset classes, a vantagepoint supported by ESMA whom estimated that 279 entities reported non-equity data to FITRS in 2018, 156 entities reported non-equity data for the EU 27 in the same time period[6]. However, currently, the usability of this post-trade data to support price formation and open competitive and fair markets is restricted as the data is dispersed across many different entities and is published in different formats by APAs and Trading Venues which is not always published in a machine-readable way. The current fragmentation of data between APAs, along with a lack of standardisation in terms of format and accessibility is obscuring the amount of post-trade transparency information available to the market and making it challenging for market participants to obtain a consolidated view. Thus, the development of a consolidated tape for bond instruments will resolve these fragmented data issues and significantly increase and improve the usability of the current transparency data within fixed income markets.

Furthermore, for bonds AFME members consider that post-trade transparency data is beneficial in assisting price formation, but this process is not dependent on MiFID II pre-trade transparency data being published.

46. Do you think that using ToTV is a useful criterion for determining the scope of transparency requirements for non-equity instruments, and in particular OTC derivatives? Please separate your answers by fixed income (please treat sovereign bonds, high-yield bonds and investment grade

[6] Please see ESMA's Consultation paper MiFID II/MIFIR report on the transparency regime for non-equity instruments and the DTO published 10th March 2020 https://www.esma.europa.eu/sites/default/files/library/esma70-156-2189_cp_review_report_transparency_non-equity_tod.pdf (pg 60, Paragraph 168)

bonds separately) and derivatives (please distinguish between exchange treaded and OTC derivatives).

AFME members consider Traded on a Trading Venue (ToTV) to be the ultimate superset criterion for instruments traded. However, AFME members do not consider the ToTV criteria to be useful for determining the scope of the transparency requirements for non-equity instruments, in particular sovereign and investment grade bonds. As the criteria is an exceptionally broad concept resulting in a large degree of ambiguity throughout the industry and between market stakeholders. In order for ToTV to be used to determine the scope of the transparency requirements for bonds, this scope needs to be simplified and limited to a sub-set of truly liquid bonds. This would enable the FCA to develop a transparency regime that offers usability, validity and reliability. Once the regime is in operation for this sub-set of bonds, the FCA can then monitor, evaluate and then extend the scope to a wider set of instruments.

47. If you answered no to question 46: Do you think the concept of ToTV should be removed for OTC derivatives, and the scope of the transparency regime determined on the basis of whether the instrument is cleared? If so, what definition of 'cleared' should be used?

No AFME response.

48. Do you think there is another option to determine the scope of the fixed income and derivatives transparency regime? Please separate your answers by fixed income (please treat sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (please distinguish between exchange traded and OTC derivatives).

Yes. AFME members support a redesign of the post-trade transparency regime for fixed income markets, given the current liquidity calculations are extremely complex and lack validity. AFME members propose completely remodelling the existing transparency regime to result in better quality/ non ambiguous data.

AFME members consider that there are two different types of structures that could be put into place when constructing a transparency regime for bonds either:

1) Apply a tight transparency regime to a limited small scope of instruments (e.g. limit scope to certain maturity bands of on the run bonds). All the instruments within scope would be classified as liquid meaning no calibrations would be required. All other instruments will be subject to appropriate deferrals Or;
2) Define a wider scope of instruments within the transparency regime, however this will require appropriately defined liquidity calibrations to identify the relevant instruments . Examples as to how the liquidity calculations could be redefined include: Focusing on outstanding notational instead of total universe/number of bonds or focusing on issuance size filtering via maturity to ensure easily accessible data. It is important to note however, that volume masking alone for large sized trades will lead to information leakage by displaying a real-time price that clearly deviates from mid, so carefully calculated/accurate thresholds are essential. All other instruments will be subject to appropriate deferrals.

AFME members note that in order to develop a transparency regime for bonds that provides validity and simplification the scope of the regime will require compromise. Each of the regimes outlined above offer true validity but require different modifications.

Prior to any changes in the scope of the transparency regime for bonds being proposed, AFME urges HMT to engage further with the industry to ensure any future regime is workable for fixed income markets.

49. What instruments do you think should be in scope of the fixed income and derivatives transparency regime? Please consider fixed income (please treat sovereign bonds, high-yield bonds and investment-grade bonds separately) ETCs, ETNs, structured finance products, emission allowances and derivatives (please distinguish between exchange traded and OTC derivatives).

Following on from our response to Q48, AFME suggest the following alternative options for determining the scope of the transparency regime for bonds:

- Limit the scope to EU issued Govt bonds with a minimum issuance size and outstanding amounts.
- Limit the scope to Investment Grade Corporate bonds with a minimum issuance size and outstanding amounts
- Focus on outstanding notational instead of total universe/number of bonds
- Issuance size , all new issues over a specified threshold to be classed as liquid for a period of 30 days;
- Filter on bond maturity

AFME members also propose that structured notes should not be in scope of any consolidated tape built for fixed income instruments.

50. What changes do you think are needed to enable liquidity calculations to work effectively? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds) and derivatives (ETDs and OTC derivatives).

Currently, the calibration of bonds by sub-asset classes is extremely broad, applying the same SSTI and LIS thresholds to bonds based solely on instrument type, with little consideration given to the liquidity profile and characteristics of individual instruments. For example, there is currently the same level of transparency (SSTI/LIS thresholds) for a German 10yr bund that trades very frequently and in size, as there is for a sub-section of bonds (for example Slovakian government bonds) that are significantly less liquid. However, this issue is not limited to the sub asset class of sovereign bonds only but is relevant to all bond types/sub-asset classes. If the transparency regime for bonds, particularly different classes of bonds is not better designed, this could have inadvertent consequences that could impact the functioning of some less liquid debt markets.

Given the complexity and depth of the analysis required in order to develop effective liquidity calculations for fixed income bonds, AFME suggests that the FCA develop a market structure working group comprised of sell-side, buy-side and other relevant market participants in order to develop a workable methodology.

51. Do you think it would be preferable to move away from regular liquidity calculations towards a mix of qualitative and quantitative criteria? For example, on a sectoral basis? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment grade bonds separately) and derivatives (ETDs and OTC derivatives).

Yes. AFME members are supportive of HMT's proposal to move away from regular liquidity calculations in favour of a qualitative and quantitative criteria. The current liquidity calculations outlined under MiFIR/MiFID II are complex and do not accurately measure or capture true liquidity within the market.

AFME recommends that any quantitative criteria proposed is not backwards looking, as this does not provide a true reflection of the liquidity profile of the bonds captured. We would also encourage HMT to utilise up to date third party data for the purpose of post-trade transparency.

If HMT are yet to establish the criteria for their proposal, AFME members strongly urge HMT to work with the industry to define the parameters of the qualitative and quantitative criteria to ensure any new process accurately captures and reflects true liquidity within the market.

52. How do you currently use pre-trade transparency? Is pre-trade information on bonds and derivatives valuable? Please differentiate between fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives), and each trading method (for example RFQ, and order book).

The consistent feedback AFME members have received from their clients since the implementation of MiFID II is that buyside firms do not use MiFID II pre-trade transparency information, preferring to utilize consistently updated market data streams for the purpose of price discovery. A reason for buyside clients lack of appetite for pre-trade transparency data is because the application of pre-trade transparency does not lend itself well to bond markets, which are not order book driven markets but typically employ a Request for Quote (RFQ) model, whereby buyside clients send a query to multiple dealers simultaneously given the bespoke nature of fixed income instruments this makes it challenging for pre-trade quotes to be generalised or relied on as a guide price.

AFME members agree with HMT's goal to simplify the pre-trade transparency regime as much as possible. We strongly encourage HMT to go a step further and consider removing in its entirety the pre-trade regime for non-equity instruments.

53. Is there a case for removing MiFID II pre-trade transparency requirements for any asset class? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

Yes. AFME in its capacity as a bond trading association and its members strongly believe that pre-trade transparency requirements should be removed for all bonds. With regards to derivatives AFME refers HMT to the responses of other trade associations such as ISDA.

As noted in our response to Q52 (above) and Q84 (below) no firms within the industry use MiFID II pre-trade transparency information, preferring to utilize consistently updated market data streams for the purpose of price discovery.

Furthermore, given the nature of bond instruments the fixed income market is predominantly an institutional market with a buy to hold investor base meaning that different types of market participants (including hedge funds, ETF providers and retail investors) wishing to invest in the bond market will have access to indicative pricing information via the workflow/trading system they chose to execute their trade through, however this data is not defined as MiFID pre-trade transparency data but provides the service that clients require in terms of pre-trade information.

54. If you answered yes to question 53:

Do you think that RFQ, bilateral negotiations and indications of interest provide sufficient information for markets to function effectively? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

Yes. Within fixed income markets (including sovereign bonds, high-yield, and investment-grade bonds) AFME members support the continued use of different workflows including RFQ, bilateral negotiation, axes and indications of interest and consider that such practises provide sufficient information enabling fixed income markets to operate effectively. AFME members warn against mandating certain types of workflows, this could lead to significant inefficiencies in the functioning of the market and potentially reduce liquidity and widen bid-offer spreads.

AFME members stress the importance for the industry to embrace a variety of different workflows and trading modalities in order to allow the market to grow, adapt and drive innovation. This ensures the enablement and development of new solutions that facilitate clients technical access to market , whilst ensuring the continued transaction of fixed income instruments through recognised regulated services such as investment firms

55. How do you use pre-trade quotes streamed by SIs? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

As previously outlined AFME members do not use pre-trade transparency data (for a more detailed explanation see our response to Qs 52 and Q53).

56. For SIs, what impact do you think removing pre-trade transparency requirements would have on your business? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

In their capacity as SIs AFME members conclude that removing pre-trade transparency requirements for fixed income instruments (sovereign bonds, high-yield bonds, and investment grade bonds) would have little to no impact on SIs current business. AFME members note the availability of MiFIR SI pre-trade transparency data has not created demand for such information. Market participants continue to use consistently updated market data streams for the purposes of price discovery, together with axes and runs published by dealers. Nevertheless, Investment Firms in their capacity as SIs have committed to abiding by their pre-trade transparency obligations, but note the information is rarely requested or viewed by clients meaning the benefit of producing such information has no positive impact on or for the industry (buy or sell side) . As the bespoke nature of each quote/information request sent to an SI, including the characteristics of the instrument and the relationship between SI and client, make it challenging for pre-trade quotes to be generalised or relied on as a guide price, as a result this might impact on a client's appetite for SI pre-trade transparency information. Removing the pre-trade transparency requirements for SIs would reduce costs and enable better pricing for clients.

57. Do you have any other comments on the pre-trade transparency regime?

AFME members support the removal of pre-trade transparency requirements.

58. How do you currently use deferrals? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment grade bonds separately) and derivatives (ETDs and OTC derivatives).

The degree to which individual AFME member firms apply the deferrals framework is dependent on the firm's location and/or that of their APA. There is resounding consensus amongst all AFME members that a robust deferrals regime is necessary under the current transparency regime. However, AFME members consider that if the transparency regime were to be redesigned and the scope of the regime applied to a limited and tighter scope of truly liquid instruments, this could potentially lessen the need for deferrals resulting in a vastly modified and simplified deferrals regime.

AFME members note that deferrals were introduced for bonds under MiFID II because when the proposal to extend the transparency regime beyond equity instruments to include within scope non-equity asset classes including fixed income, it was acknowledged that unlike many other non-equity asset classes, cash bonds are predominantly traded in an OTC capacity, meaning firms offer access to their balance sheet and transfer risk. It was recognised that real time transparency could expose committed liquidity providers to undue risk, especially when trading in illiquid instruments or transactions above a certain size, given the longer time frames to unwind the trade or hedge. This remains the most important factor to be taken into account when thinking about redesigning the transparency regime in the UK. MiFID II, while being a complex regime, has been carefully calibrated and we should ensure that any redesign continues to take into consideration the benefits of more real-time reporting vs. the potential negative impact on market liquidity.

AFME members believe that for a transparency regime to be most efficient both the liquidity profile of the instrument and the size of the transaction will need to be taken into consideration.

59. Which asset classes should deferrals apply to? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

AFME in its capacity as a Bond Association reiterates that deferrals should apply to all bond classes including sovereign bonds, high yield bonds, investment grade bonds and those bonds classified as 'others'. Different deferral types are applied to different types of bonds depending on their classification and the size of the trade. there is less concern over the deferral regime for truly liquid bonds such as those bonds considered as benchmark bonds (e.g. German Bunds) A well calibrated deferral regime is essential for those bonds that are considered highly volatile such as high-yield bonds which can turnover large monthly volumes but trade relatively infrequently.

Furthermore, the liquidity profiles of bonds within the same sub-asset class can vary significantly, for example under the current transparency regime all sovereign bonds are subject to the same transparency requirements despite significant differences in the level of trading between these bonds e.g. some EU sovereign bonds trade often and in volume, whereas other EM bonds are significantly less liquid, which could have inadvertent consequences that could impact the functioning of some less liquid debt markets, particularly when moving to stage 3 and 4 of the liquidity parameters for bonds.

60. Do you agree that the deferral regime would benefit from being simplified?

AFME members do see benefit in simplifying the deferral regime. Currently the deferral regime is considered complex given the variety of deferral options available under MiFIR/MiFID II which are employed at the discretion of the NCA, within this means different NCA's within the EU apply different deferral regimes. AFME members do not necessarily agree that the optimal way to achieve simplification is through reducing the length of the deferral period available but that simplification can be achieved by coalescing on the amount of protection available . Therefore, AFME members support the continuation of the 4-week volume omission and the two day deferral period for price information, and includes the retention of the supplementary deferral provisions outlined under article 11 3 (b), 11 3 (c) and 11 (3) (d) of MiFIR, which allows the aggregation of trades.

AFME members also see the benefit in the concept of having one post-trade size threshold for deferrals. AFME members support the deletion of the post-trade SSTI threshold and the maintenance of the of the LIS threshold provide that the LIS threshold is revised down to the existing post-trade SSTI threshold of 80% and analyses is undertaken to ensure any re-calibration of the threshold does not result in any undue risk to the market.

61. What do you think the optimum deferral length is? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

AFME members note that in order to opine on the optimum deferral length for fixed income cash bonds, this requires confirmation of the instruments within scope of the U.K post-trade transparency regime for bonds.

As it stands under the current regime, AFME members support the continuation of the current deferral regime applied by the FCA in the UK, which comprises of 4 weeks for volume omission and the two day deferral period for price information. AFME members consider this regime to be optimal as it allows liquidity providers to continue to take on risk on their balance sheet without exposing them to undue risk. On average, for corporate bonds, liquidity providers keep positions on their balance sheets between 12 days and 15 days. however the range for which an SI owns an illiquid bond varies significantly, with some instruments listed on a firms balance sheets for any period of time ranging from 12 days up to a full calendar year, meaning firms need time to exit such positions. Such a deferral should be applied to less liquid instruments and large transactions.

62. What are your views on the government's proposal to delete the SSTI, package order, and EFP deferrals? Do you think it would lead to more meaningful transparency? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

In principle AFME supports the notion of only having one post-trade size threshold for deferrals, provided it is set at an appropriate level where there is not a significant jump in the level of transparency. This size level should be discussed and further consulted on with the industry. If HMT are planning to keep the current calculation method, then the LIS threshold should be revised down to the existing post-trade SSTI 80 percentile.

AFME remains available to work with HMT and the wider industry to further explore the possibility of simplifying the transparency regime and the post-trade size thresholds for deferrals. Any alterations to the current regime should only be considered after an adequate cost benefit analysis is executed to ensure the protection of committed liquidity providers form any undue risk. Any decision made after such cost-benefit analysis with market participants should be implemented cautiously via a phased-in approach, as the MiFID II/R transparency regime for non-equity instruments incorporates a vast array of different asset classes and product types.

63. Do you think volume masking and/or aggregation helps to encourage real time publication? Please separate your answers by fixed income (sovereign bonds, high-yield bonds and investment-grade bonds separately) and derivatives (ETDs and OTC derivatives).

AFME members remind HMT that whilst volume masking and aggregation are not mutually exclusive, by definition they do not lend themselves to real-time publication of trade data. Tools such as volume masking and aggregation of trade data exist to limit any unnecessary identification of sensitive inventory information which if made available could have adverse effects on the market, exposing committed liquidity providers who take on risk on balance sheet to facilitate client transactions to undue risk, especially when trading in illiquid instruments or transactions above a certain size.

Furthermore, volume masking and aggregation are not mutually exclusive in terms of implementation as outlined below:

	Pros	**Cons**
Aggregation	Protects liquidity on a trade by trade basis, protects pricing of individual trades that are large in size. Enables large trades to be made publicly available but not on an individual basis.	For small size trades, does not assist with the formation of transparency on an individual trade basis.
Volume Masking	Enables individual pricing formation to be disseminated publicly in real-time.	Lacks protection for large trades, as there is a deviation from mid price which enables identification of large trades.

As demonstrated by the table above, both aggregation and volume masking play a different function within the market for different trade types. Potentially both tools could be used together if the right transparency regime is calibrated.

AFME remains available to assist HMT if required to develop an appropriately calibrated transparency regime for bonds.

64. What are the risks and benefits of allowing trading venues to calculate LIS thresholds for ETD post-trade reporting?

Please revert to ISDA response.

Chapter 6 – Commodity Market

65. Do you think that the scope of the 'commodity derivatives' regime should be narrowed to derivatives that are based on physical commodities?

GFMA's commodities working group will be responding to this question.

66. Do you think that financial instruments which refer to commodities as a pricing element but are securities in their legal form, should be removed from the regime?

GFMA's commodities working group will be responding to this question.

67. Do you think economically equivalent OTC commodity derivative contracts should be removed from the commodity derivatives regime?

GFMA's commodities working group will be responding to this question.

68. Are there any other instruments that you think should be deleted from the commodity derivatives regime?

GFMA's commodities working group will be responding to this question.

69. What would be the risks and benefits of transferring responsibility for position limits from the FCA to trading venues?

GFMA's commodities working group will be responding to this question.

70. Under this model, what specific factors do you think should be addressed in the framework of requirements that UK authorities would provide for trading venues?

GFMA's commodities working group will be responding to this question.

71. Do you think that the scope of contracts that are automatically subject to position limits should be limited? If yes, do you think that it should be limited to contracts that are critical or significant, which includes those that are physically settled, and agricultural?

GFMA's commodities working group will be responding to this question.

72. Do you think that the UK commodity derivatives regime should allow position limits exemptions for liquidity providers?

GFMA's commodities working group will be responding to this question.

73. Do you think that the UK commodity derivatives regime should introduce a 'pass through' hedging exemption to enable investment firms to support a wider range of hedging practices?

GFMA's commodities working group will be responding to this question.

74. Do you think any other activities should be exempt from the regime?

GFMA's commodities working group will be responding to this question.

75. Are there areas of the UK's position reporting regime which could be improved?

GFMA's commodities working group will be responding to this question.

76. Do you think that the AAT should revert to a qualitative assessment of the activities performed by a market participant?

GFMA's commodities working group will be responding to this question.

77. Do you think that the basis of the AAT should be expected activity, rather than historic activity?

GFMA's commodities working group will be responding to this question.

78. Do you agree that the annual notification requirement should be abolished?

GFMA's commodities working group will be responding to this question.

79. Does the continued existence of the separate OMP and EMP regimes for commodity derivative market participants serve any meaningful purpose?

GFMA's commodities working group will be responding to this question.

80. Do you think that the OMP and EMP regimes should be removed as particular regulatory statuses from the UK's regulatory perimeter?

GFMA's commodities working group will be responding to this question.

81. Do you think any changes would need to be made to the MiFID II regime, if the OMP and EMP regimes are removed as particular regulatory statuses?

GFMA's commodities working group will be responding to this question.

Chapter 7 – Market Data

82. Do you agree that the government should take action to encourage the development of a CT? If you answered yes to question 82:

AFME members agree that the government should take action to encourage the development of a CT. We believe that the provision of an appropriately constructed CT could democratise access for all investors, regardless of resources or sophistication, with a comprehensive and standardised view of equities and fixed income trading environments. An appropriately constructed CT should also reduce the cost of display data and reduce complexity relating to market data licences. However, the design of the CT raises many challenges, which must be addressed ahead of any regulation or guidance being drafted to ensure that a high quality data source is built.

We agree with HMT that contribution by trading venues and APAs to the CT should be mandatory. This should act as a natural driver to ensuring maximum coverage in both equities and fixed income markets. However, AFME members are very concerned that, should venues be required to provide data to CTPs on terms that are significantly more competitive than for other consumers, there is a high risk that data providers could simply make up for any perceived shortfall by charging higher fees to direct consumers of the data. This should be prohibited and we would like to stress that the benefits of CT should not be diluted by unjust and aggressive pricing strategies being utilised by exchanges who hold a dominant position when selling market data.

Mandatory contribution is also required in order to ensure that a CT remains a viable commercial enterprise for CTPs. Without this approach, the need to consume data from a large number of trading venues and APAs required in order to develop a CT, will mean that a CTP could expect to pay considerable sums to maintain multiple data feeds and the right to distribute them. The CTP would need to pass costs on to end users to be commercially viable, however, consuming a high price consolidated tape in addition to potentially also consuming other market data generally, could be prohibitive for some consumers. The result of these circumstances is that despite the appetite for a CT, costs to consumers could limit the number of firms consuming CT data and therefore reduce the commercial incentive for the emergence of a CTP.

Additionally, we caution that the solution to this problem is not to impose mandatory consumption of a CT as in many cases this would mean investment firms would be forced to pay for both direct data feeds and CT data (essentially paying for the same data twice). Instead, the focus should be on reducing the cost of market data provided by incumbent exchanges who currently hold a position of significant market power from a pricing perspective.

AFME believes that a single CTP would be best placed to meet the requirements of market data consumers while also ensuring that a balanced governance structure can be applied. We are concerned that allowing multiple CTPs carries the risk that a high number of CTPs, which, if coupled with the proposal to reduce the coverage ratios, could lead to multiple CTPs with potentially different or overlapping product scopes which may defeat the purpose of having a truly consolidated view of the market and increase costs to consumers. To avoid this scenario, potential CTPs should compete in a tender process which establishes which firm will operate as a CTP for a set period. Having a single CTP will help to apply an appropriate governance structure which ensures that requirements of both consumers and providers are adequately reflected while ensuring that a commercially viable CTP model can exist.

Finally, AFME encourages HMT to coordinate with the EU and Switzerland with the aim of providing a pan-European consolidated tape which would maximise the benefits of a CT by ensuring a single consolidated source of data as opposed to separate CTs which cover the same instruments. We acknowledge that coordination with the EU could be complicated by the development of its own CT and if this is the case, AFME would still support coordination with Switzerland to develop a UK/Swiss CT. In order to ensure the possibility the future harmonisation of different CTs across multiple jurisdictions, AFME strongly recommends that HMT mandates the use of common data standards developed by FIX Protocol.

83. Do you think a fixed income tape should be prioritised?

AFME supports the simultaneous development of both a fixed income and equity CT. We believe that this approach does not require significant additional resource, however provides an opportunity for the UK government to maximise benefits of the CT across as wide scope of instruments, thereby improving investing conditions for a broader scope of investors in a short timeframe.

AFME forecasts that a fixed income CT may take longer to enact. In this context, AFME members recommend applying a phased approach within the class of cash bonds.

84. Do you think that it would be beneficial for a fixed income CT to include post-trade data only, or would there be value in a tape covering pre-trade data too?

A CT for fixed income should focus purely on capturing post-trade data for bonds only. As noted in our response to Q83, such a CT will assist with centralising the vast amount of post-trade data that is already public but currently not always published in a consistent, standardised, usable, or easily accessible format by Trading Venues and APAs.

Within fixed income markets there is little demand from buyside clients for pre-trade transparency information, as buyside firms continue to use consistently updated market data streams for the purpose of price discovery. Furthermore, the application of pre-trade transparency does not lend itself well to non-equity markets such as bonds.

As bond markets are not order book driven markets but typically employ a Request for Quote (RFQ) model, where the buyside sends a query to multiple dealers simultaneously given the bespoke nature of fixed income instruments, this makes it challenging for pre-trade quotes to be generalised or relied on as a guide price, as a result this might impact on a client's appetite for MiFID pre-trade transparency information.

AFME and its members reiterate that MiFID II post-trade transparency reporting requirements have produced a significant amount of post-trade data. However this information is currently published in different formats by APAs and Trading Venues and is not always published in a machine-readable way. The current fragmentation of data between APAs, along with a lack of standardisation in terms of format and accessibility is obscuring the amount of post-trade transparency information available to the market. The development of a fixed income tape will assist with centralising the vast amount of post-trade data that is already publicly available but not easy to access. This effectively means the development of a fixed income CT will ensure that post-trade transparency data for bonds is usable for the first time since the implementation of MiFID II.

AFME members stress that any CT developed for bonds must preserve the delicate balance between transparency and liquidity without causing committed liquidity providers undue risk. Therefore it is essential that the UK maintains the current MiFID II/ R option of 4 week volume omission and two day deferral period for price information regime already in operation, such that trades which benefit from deferred publication are not published on the tape until after the deferral period has expired. As outlined in our response to Q58, MiFID II introduced deferrals because it was recognised that real time transparency can expose committed liquidity providers to undue risks, especially when trading in illiquid instruments or transactions above a certain size, given the longer timeframes to unwind the trade or hedge.

85. Is there any value in a delayed data CT for fixed income markets?

AFME members highlight that delayed data is useful particularly in the context of market analysis.

Fixed income markets are different to equities markets and as a result there is less demand for instantaneous data. There are also functions within the bond market that utilize "backward looking" delayed data, such functions include transaction cost analysis, compliance functions, market abuse surveillance and general portfolio evaluation etc. which go beyond price formation and do not require access to real-time pricing. To conclude, AFME members support the delivery of a delayed data feed.

86. Is it valuable for an equity CT to include pre- and post-trade data?

For equities, a CT should include both pre-trade (three levels of price and size) and post-trade data. Ideally these would be developed in parallel. However if the inclusion of pre-trade data is not possible or would unreasonably delay the development of a CT for equities, AFME would support the introduction of a post-trade tape as a first phase.

For ETFs, it should be for post-trade data only as only a small amount of volume is traded on exchange the majority of ETFs are executed on request for quote (RFQ) execution venues.

A post trade tape should not include transactions which are technical (subject to conditions other than current market price) such as give-ups or inter-affiliate trades for the purpose of risk transfers. These are not considered 'addressable' by investors and rarely provide material information to them.

We believe it is more important to make sure that post-trade data clearly represents the differences between types of transactions (addressable, price-forming vs. technical in nature). It is paramount not only to actual price formation but also essential in running functions such as algorithm calibration, risk management and trade surveillance. AFME asserts that flags on transactions reported to the CT and consequently to APAs by trading venues should be granular enough to allow market participants to distinguish addressable versus non-addressable liquidity. We think this would lead to overall improved data quality and accordingly more refined transparency calculations. AFME members believe that non-price-forming activity (e.g. give-up/give-in trades) should not be included in transparency calculations (e.g. liquid market, SMS).

87. Is there any value in a delayed data CT for equity markets?

No, a delayed or EOD tape would only provide for a limited ex-post view of best execution and some post-trade data analytics but would not generate any benefits of democratising a standardised, comprehensive intra-day view across all executions venues in order to make this liquidity visible and available to all investors, regardless of sophistication or resources – it provides no incentive for venues or certain participants to provide more varied (at point of transaction) connectivity and liquidity (other than just to the primary market) to the retail market.

88. Should the government amend legislation to enable a market-led private sector CT to develop, or do you think UK authorities should be actively involved in creating a CT?

AFME does not have a preference as to whether a CT should be a public or private utility, provided it delivers on the core features of providing high quality data which is easily accessible, affordable for users and subject to appropriate governance structures. In either scenario, we believe that HMT and FCA should have a significant role to play in setting the appropriate framework and governance structure of a CTP. This will be important to ensure that the operation of a CT remains a commercially attractive option while also ensuring that the CT results in benefits to the consumers of market data.

Regardless of whether HMT opts for a public or a private solution, AFME believes that a single CTP would be best placed to meet the requirements of market data consumers while also ensuring that a balanced governance structure can be applied. We are concerned that allowing multiple CTPs carries the risk that a high number of CTPs will emerge due to the potential to consume market data for free. To avoid this scenario, potential CTPs should compete in a tender process which establishes which firm will operate as a CTP for a set period. Having a single CTP will help to apply an appropriate governance structure which ensures that requirements of both consumers and providers are adequately reflected while ensuring that a commercially viable CTP model can exist.

89. What are the legislative barriers for a private sector-led CT to emerge? Do you agree with the legislative changes identified above? Are there additional changes that UK authorities should be considering?

Please see AFME's response to Question 82.

90. Do you see any risks with removing the obligation for CTs to provide data for free after 15 minutes?

AFME does not support the removal of the obligation for CTs to provide data for free after 15 minutes. This latency profile of this market data contrasts significantly with a real-time CT which would provide a lower cost alternative to display data, currently provided by exchanges and data platforms. The ability for firms and retail investors to use this data, free of charge, to analyse market trends or conditions has been valuable for a wide variety of entities, regardless of scale or size. To remove this requirement *would go against the notion of democratising market data which should remain* a key goal for HMT.

Demand for data currently exists for latency at human eye or near real-time, but unfortunately this data remains incredibly expensive. Development of the CT would drive demand for its use for this latency between real-time and 15 minutes where this could be consumed at a lower affordable cost. Additionally, under AFME's proposal that data through the CT should also be consumed free of usage restrictions and licences, use cases of CT data would likely penetrate further into market data consumers' business functions and demand for the CT would support its viability.

91. What are the potential advantages and disadvantages of multiple private-sector CTs for each asset class?

AFME does not have a strong view on whether HMT should pursue a public or a private CT. However. we believe that it is important that a single CTP is selected per asset class in order to meet the requirements of market data consumers while also ensuring that a balanced governance structure can be applied. We are concerned that allowing multiple CTPs carries the risk that a high number of CTPs will emerge due to the potential to consume market data for free. To avoid this scenario, potential CTPs should compete in a tender process which establishes which firm will operate as a CTP for a set period.

92. Do you have any suggestions on further areas that UK authorities should be considering when making changes to market data, especially in relation to requirements that are set out in legislation?

AFME considers that the rising cost of market data represent a material challenge to the effective functioning of markets. We agree with the FCA's statement that "MiFID reforms have also opened up trading venues to greater competition. Trading venues that see their margins squeezed on trading activities could exploit any market power they have in relation to the supply of trading data to increase data prices, reduce quality and innovation". In our view, this has been the case and has had a detrimental impact on markets and, more importantly, end investors. AFME would like to emphasise that market data costs should be standardised for all market data consumers regardless of the type o user. Costs should be based upon the nature of the service and not the user.

For further detail on AFME's position in relation to market data, we refer HMT to our response to the FCA Call for Input. We look forward to engaging with the FCA once its Feedback Statement is published later this year. Finally, we note that ESMA has published guidelines on MiFID II/MiFIR obligations on market data. AFME welcomes the publication of these guidelines as a positive step towards addressing the ongoing issue of rising market data costs. We encourage HMT and FCA to seek a harmonised which sets out minimum requirements for entities that charge fees for market data.

Chapter 8 - Reporting

93. Where do the current regulatory reporting regimes for wholesale markets contain duplicative reporting requirements?

AFME provided examples of duplicative reporting requirements on reasoning to the response to Q40.

94. Is intervention needed to mitigate against duplicative reporting for firms undertaking SFTs with members of the European System of Central Banks?

No AFME response.

95. Do you think the 10% loss reporting rules for portfolios and contingent liability transactions offer effective investor protection? If not, how do you think the rules in this area should be revised?

AFME members consider that the 10% loss reporting rules for portfolios does not provide for effective investor protection. The loss reporting notification could cause investors to be alarmed and react hastily. This may adversely impact investor confidence in investing in capital markets more generally.

AFME supports UK Finance's response to this question.

96. Do you think electronic communication should become the default means of communication for disclosures and reporting to retail clients, and, if so, what protections are needed for retail clients around such a change?

While this is foremostly a matter for retail firms to consider with respect to retail clients, AFME suggests that retail clients could be provided with a choice to opt in to paper disclosures but there should be consideration as to whether the volumes of disclosures currently required by MiFID II and other product specific legislation (e.g. PRIIPS) is effective and Treasury should assess whether retail clients read and use these disclosures in practice.

AFME members report that the majority of wholesale clients prefer receiving information in non-paper format and therefore fully support a phase-out of paper-based information in order to reflect this. In addition, AFME members note that the phasing-out of paper-based information would reduce waste and support the sustainable finance agenda.

AFME members suggest that the regime be amended so that, when information must be provided (including when that information should be in a durable medium), the provision of such information by means of electronic communications shall become the norm and default option.

However, the digital transition to electronic format could turn out to be problematic for those retail clients which have so far relied on paper-based communications due to, for example, (1) age (2) hindered access to technology (3) lack of digital literacy. For these reasons, retail customers should still retain the possibility to receive pre-contractual documentation in paper upon request.

We expect that most documents will be distributed in electronic format. However, retaining the ability to provide documents in paper format if a client so requests will be important to ensure appropriate client information, for example for those who do not have access to electronic devices.

In order to achieve this goal, we would recommend that the Treasury consider amending Article 14 of

the PRIIPs Regulation so as to make the electronic format the default option for providing a KID – whilst also maintaining retail clients' ability to opt to receive a KID on paper format, if they so desire.

In addition, the practical experience of our members is that, in some cases, even existing and new professional clients do not elect to receive electronic communication (e.g. they do not provide the firm with an email address and/or have not switched on the functionality that would allow them receive electronic communications). It is therefore important that firms can continue to provide paper documents to both professional and retail clients, as well as eligible counterparties, so that clients who have proactively elected to receive paper documents as well as clients - including professional clients - who have not provided the firm necessary information, such as an email address, can continue to receive appropriate information about financial services and instruments provided to them.

We believe that the proposed approach could strike the right balance between the need to recognize the existence of increasing consumer demand for and use of online services on the one hand, and the need to recognize that not all investors have access to digital devices (or indeed want to receive electronic disclosures) on the other.

97. Are there any other changes to the conduct rules in the MiFID delegated regulation that you think could be made to reduce costs whilst continuing to offer meaningful investor protection?

AFME proposes a broader review of client reports, disclosures and consents for Professional Clients/Eligible Counterparties (ECPs). Members generally find that the following client reports, disclosures and consents for Professional Clients/ECPs are burdensome and create delays in dealing with clients without providing information that clients find useful:

i. Prior express consent.

The requirements to obtain prior express consent to non-publication of unexecuted client limit orders and execution of orders outside a trading venue are unnecessary when dealing with professional and eligible counterparties as these actions are well understood.

ii. Risk disclosures.

The risk disclosures that firms provide to clients are very lengthy (in printed form they can run to more than 10 pages) and cover risks that are well understood in the professional market. Firms understand that clients generally do not read these risk disclosures and so they are a document that can be expensive to create and maintain but which is not used by firms or clients. Risks in a bespoke or structured product that may be less well understood, will be described in appropriate detail in the documentation for that product.

iii. Post-execution reports.

Post-execution reports required by Article 59 of Delegated Regulation (EU) 2017/565 (Reporting obligations in respect of execution of orders other than for portfolio management) are cumbersome and unnecessary. Firms typically agree with their clients the data that should be included in post-execution reports based on the data that the client needs to receive and the format in which the client needs it. In some cases the data provided in Article 59 reports can conflict with client requests and cause issues with trade matching.

AFME members recommend removing the above obligations for firms when dealing with professional clients and ECPs. However should HMT consider that the consents regarding execution of trades should remain, we recommend these be consents that are capable of being deemed provided (in the absence of express disagreement) where a client sends a trade instruction following receipt of the consent request. AFME members recommend a similar approach to the consent that firms are required to obtain in relation to their execution policy, i.e. client consent should be deemed given (in the absence of express disagreement) when the client first places an order or sends a request for quote following receipt.

98. Do you think other changes are needed to ensure that the reporting regime correctly balances investor protection and transparency?

Please see our recommendations in our response to Q97 above.

99. Have you experienced any issues with the utilisation of ISINs as identifiers?

Please revert to ISDA response.

100. Do you have any suggestions on how the use of identifiers could be improved?

Please revert to ISDA response.

Chapter 9 – Cross Cutting Issues

101. What further steps can UK authorities take to enable firms to take advantage of technological innovation in capital markets?

We believe there are three steps that UK authorities can take to enable firms to take advantage of technological innovation. These are:

1) Review existing legislation and provide guidance on the application of rules where needed,
2) Ensure the regulatory framework remains technology-neutral and adaptable to change, and
3) Promote ongoing collaboration with the industry to keep pace with technological developments.

Technological innovation can benefit capital market participants by reducing costs, increasing efficiency, and enhancing resilience and transparency. UK authorities must ensure the regulatory framework is fit for purpose in the context of increased digitisation and technological innovation in capital markets, maintaining investor protection, market integrity and financial stability. We welcome the recent measures announced by UK authorities and look forward to providing input and participating as they are developed in collaboration with the industry.

Specifically for DLT, we note that the current regulatory framework for this technological innovation is built around existing financial market infrastructures (e.g. bilateral instead of multilateral relationships). Requiring DLT activities to replicate existing market structures limits innovation (e.g. increased process automation and streamlining of the capital markets value-chain). UK authorities should consider how to adapt existing regulations to reflect better how market participants interact in a decentralised DLT environment and how roles, responsibilities, and obligations should apply in this context. UK authorities should consider a range of policy options, including:

1) Providing guidance on the interpretation of existing rule-sets in a DLT context,
2) Creating a framework within which firms can test DLT products,
3) Making rule changes as soon as possible, taking into account the need for global consistency, and providing further clarity as future obstacles are identified, and
4) Taking an agile and flexible approach to the application of markets rules (e.g. considering the reallocation of responsibilities).

We recommend that UK authorities undertake a cost-benefit analysis to determine any approach for testing DLT solutions (e.g. resourcing, implementation costs, scalability). This analysis should include engagement with the industry to ensure that the approach is practical, efficient, and can bring value to capital markets. For more detail please see AFME response to HMT consultation and call for evidence on the UK regulatory approach to crypto-assets and stable coins p 13-15 (link).

102. What further steps can UK authorities take to support the wholesale markets sector as we move towards a low carbon economy?

AFME welcomes the UK government's continued commitments to tackling climate change. We agree that the financial services sector and capital markets play an important role in supporting the transition to net zero. In order for capital markets to perform this role effectively, it is important that there is clarity and consistency of classification of environmentally sustainable investments and that an appropriate corporate sustainability reporting framework is put in place, enabling investors to effectively and efficiently allocate capital in support of the transition.

We encourage the government to continue to prioritise work in this area including the development of the UK Green Taxonomy and introduction of mandatory TCFD-aligned reporting. We welcome the establishment of the Green Technical Advisory Group and progress in establishing a UK Green Taxonomy. The UK should build upon and reflect on the experiences from the work done on the EU Taxonomy Regulation when considering the granularity of screening criteria and reporting requirements, and also taking into account the Global Guiding Principles for Developing Climate Finance Taxonomies recently published by GFMA and BCG, together with ongoing work by the International Platform on Sustainable Finance on a Common Ground Taxonomy to minimize fragmentation and support global capital markets. As highlighted in the GFMA report, differing approaches can be particularly challenging for a diversified entity that operates across multiple countries, sectors, subsectors, global investors, and credit institutions to navigate, thereby impeding the rapid scaling of investment needed to achieve climate goals. Capital markets participants would particularly benefit from a clear roadmap for the transition to a low carbon economy, offering guidelines to design and assess credible and effective strategies for key sectors of the economy.

We welcome the progress on HM Treasury's Roadmap towards mandatory climate-related disclosures. Sustainability information is a key enabler of the financial sector's role in mobilising capital to support the green transition, and the FCA's work on enhancing climate-related disclosures can benefit investment decision-making as well as market integrity. We encourage authorities to, over time, strengthen the requirements, establish a roadmap for assurance of the disclosures and leverage new digital technologies to facilitate collection and access to sustainability information.[7]

We also strongly encourage HM Treasury to continue to seek progress at the international level to maximise consistency of approaches to taxonomies and reporting standards. We welcome the UK government's recent commitments to press for global action and building international standards in green finance and encourage the UK government to cooperate with international partners on the development of international standards, for example though the work of IOSCO and the IFRS Foundation. International cooperation is key to the development of a coherent regulatory framework to support the wholesale markets sector and achieve the 2050 goals.

103. How do companies harness retail investment whilst ensuring investor protection?

This seems an appropriate opportunity to modernise some of the exemptions from the Financial Promotions Order (FPO), which we believe would allow increased choice for high net worth individuals and family offices receiving wealth management services in the UK (and thus help the UK increase its importance as a wealth management hub) while at the same time giving companies that seek financing on the UK markets better access to investors (thus increasing the attractiveness of the UK for start-ups and growth companies).

We note that the FCA has published a new strategy[8] aimed at giving consumers the confidence to invest, supported by a high-quality, affordable advice market, which should lead to fewer people being scammed or persuaded to invest in products too risky for their needs.

104. How do companies take advantage of the globalisation of information to reach investors?

Please see our answer to Q105.

105. Is there a role for UK authorities to play to facilitate retail access to capital markets, while continuing to offer high standards of investor protection?

We believe efficient and well-developed capital markets are essential to meeting the financing and risk management needs of UK citizens, enterprises and public authorities. Importantly, well-functioning capital markets strengthen UK competitiveness and prospects for economic growth and job creation.

[7] Please see AFME response to FCA consultation on climate-related disclosures and ESG topics in capital markets, https://www.afme.eu/Portals/0/DispatchFeaturedImages/AFME%20response%20to%20FCA%20consultation%20on%20climate%20disclosures%20and%20ESG%20topics.pdf"

[8] https://www.fca.org.uk/news/press-releases/fca-sets-out-plan-tackle-investment-harm

Whilst it is a laudable aim to facilitate retail access to capital markets, it should be noted that direct retail participation it is not the preeminent mechanism. Rather, the usual mechanism for retail investors to access financial products and services is through indirect participation via intermediaries. One advantage of indirect investment, in addition to professional input into the investment choices of investors, is helpful diversification in market structure and participation which can lead to improved financial stability.

Thus, it is important to recognise that regulatory reforms of the wholesale banking sector, such as envisaged by the Wholesale Markets Review, will significantly impact outcomes for retail investors. Ultimately, costs are passed onto end investors who interact with financial markets through investments, pension funds and savings. When considering outcomes for end investors it is critical to consider the impacts of regulatory reforms to wholesale markets, which will be transferred to the retail investor in turn.

We understand that the section on retail investors (paragraphs 9.8 – 9.11) is aimed primarily at exploring ways for retail investors, in the UK and elsewhere, to invest in UK companies (rather than ensuring that UK retail investors have access to global capital markets). Assuming this is correct, AFME members note that it will be key for UK Government to have strong international cooperation and relationships with legislators and regulators in other jurisdictions to facilitate UK corporates and their advisers promoting those UK companies and their issuances in other jurisdictions.

AFME notes a point of potential concern around the drive to increase direct retail participation in capital markets brings, which necessarily brings with it a risk of loss of capital for those investors. If the political will is to increase the willingness of the average individual in our society to invest in those markets it has to be done in a way that highlights to those investors that the investor risks losing some or all of his/her capital; financial institutions that provide brokerage services cannot be expected to provide an insurance policy or to provide a backstop to pay out for those losses in cases where the financial institution did not mis-sell the financial instrument.

AFME represents the wholesale banking sector, which serves the end investors, and would like to engage in dialogue with the UK authorities on the interconnectedness of retail investment and wholesale financial markets to ensure best results for retail investors, UK companies and the UK as a whole.

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