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Committee for European Securities Regulators
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By on-line submission

2nd June 2010

Dear Sally

Consultation Paper: CESR Technical Advice to the European Commission in the Context of the MiFID Review – Equity Markets (Ref: CESR/10-394)

Thank you for the opportunity to provide comments in relation to CESR's work on aspects of MiFID relating to equity markets. We have set out below our views in relation to: pre-trade transparency; post-trade transparency and the consolidation of transparency information; and regulatory boundaries and requirements. We have provided in the Annex to this letter our responses to the question posed by CESR in the Consultation Paper. We would be happy to discuss our response in more detail with CESR or provide such data as may be required.

By way of background, BATS Trading Limited¹ ("BATS Europe") is based in the UK and is authorised and regulated by the UK Financial Services Authority ("FSA") as the operator of a Multilateral Trading Facility ("MTF").² BATS Europe operates an Integrated Book (for displayed orders and non-displayed Large in Scale orders), a Dark Book (for non-displayed orders that match at an externally generated reference price) and an Order Routing Facility so that orders which are not filled on the BATS Europe order books may be routed to other execution venues.

BATS Europe is supportive of the underlying positive impact of competition and free choice on innovation and efficiency. We believe that MiFID has been successful in promoting competition, which has resulted in increased efficiency and reduced costs in many areas for market users. We are,

¹ BATS Trading Limited is a fully owned subsidiary of BATS Global Markets Inc. Owners of BATS Global Markets Inc include affiliates of Citigroup, Credit Suisse, Deutsche Bank, GETCO, JPMorgan, Lime Brokerage, Morgan Stanley, Merrill Lynch and Wedbush.

² BATS Europe launched its market for the trading of pan-European equity securities on 31st October 2008 and regularly matches more than 10% of the notional value traded in FTSE 100 securities and 5-7% of other major European indices.

therefore, generally supportive of CESR's overall reinforcement of the underlying principles of MiFID and its efforts to ensure that its aims are met.

The responses to CESR's *Call for Evidence on the impact of MiFID on secondary markets functioning* (November 2008)³ ("November 2008 Call for Evidence") raised a number of issues, including concerns based on anecdotal evidence, and we are supportive of CESR's efforts to conduct fact finding in relation to those concerns to ensure that it is able to make an evidence-based assessment on the functioning of MiFID and where further regulatory intervention is necessary.

We consider that it is important to differentiate between where the aims of MiFID have not been achieved, but could be through consistent supervisory efforts across Member States and the enforcement of existing requirements, and where there is a clear market failure that will not be resolved by market forces alone. In the case of the latter, we believe that where regulatory intervention is proposed it should be both necessary and that the benefits of such intervention will outweigh the costs.

In our view, it is not clear from the evidence gathered by CESR and presented in the Consultation Paper that regulatory intervention has been proposed in areas where there is evidence of market failure, that the proposed regulatory intervention would further the aims of MiFID, or that the benefits to the market would outweigh the costs. In particular, we would point to the evidence collated by CESR with respect to the use of the pre-trade transparency waivers by Regulated Markets (RMs) and MTFs (collectively referred to hereafter as "organised markets") and the volume of business transacted in broker crossing systems. By contrast, we would note the high costs of transparency information where market and competitive forces have thus far been unsuccessful in significantly reducing costs. As a result we consider the latter to be an area where there may be a market failure and where regulatory intervention could deliver clear benefits to market users.

Pre-trade transparency for RM/MTFs

We agree with CESR that pre-trade transparency has an important role to play in promoting the efficiency of the price formation process and in mitigating the potential negative impact of market fragmentation.⁴ Whilst we are supportive of CESR's aims to ensure a high level of transparency, **we strongly disagree with the approach proposed by CESR in the Consultation Paper with respect to the pre-trade transparency waivers; both in terms of the substance of the proposals and the basis on which further regulatory intervention has been judged necessary.**

The evidence gathered by CESR demonstrates that the proportion of trading that takes place on organised markets in comparison with OTC is split approximately 65%/35%. The evidence also shows that whilst there have been significant shifts in market share between predominately "lit" (that is, pre-

³ Ref CESR/08-872

⁴ Ref CESR/09-355: Report on the Impact of MiFID on equity secondary markets functioning (10th June 2009)



trade transparent) RMs and new entrant MTFs, the overall proportion of business conducted on organised markets in comparison with OTC has remained relatively static. In addition, the evidence shows that whilst organised markets have availed themselves of the pre-trade transparency waivers, the vast proportion of business conducted on these venues is pre-trade transparent (circa 90%)⁵ and there is no evidence to show that this figure is significantly declining.

In our view, the data collected by CESR demonstrates that there is no evidence of market failure. Nor that regulatory intervention is necessary or that it would deliver net benefits. Therefore, we do not support proposals in the Consultation Paper that would impose further restrictions or conditions on the use of the pre-trade transparency waivers.

There is clearly a balance to be struck between mandated universal transparency (a public good and the creation of a liquid, efficient market) and the ability to waive the requirement for pre-trade transparency. The current waivers contemplate that there are a number of legitimate reasons why pre-trade transparency may be waived, including: to minimise market impact for large orders (and to effectively safeguard the provision of risk capital); for orders that are price taking; and where it facilitates the achievement of best execution (either through functionality offered by an organised market or in a bilaterally negotiated transaction).

We consider that it is important to not consider the impact of the current approach to pre-trade transparency in isolation. Transparency is a means to achieve regulatory aims and whilst a high degree of transparency clearly brings benefits to the market by ensuring more efficient pricing and centralising access to liquidity, we would contend that an overly restrictive approach may actually undermine these aims. We also consider that it is important to consider restrictions placed on how and where orders can be executed in the context of the MiFID “best execution obligation”.⁶

As a matter of principle, we believe that market participants should have choice in where they execute orders, whether on an organised market or OTC, to suit their individual requirements and those of their clients. The pre-trade transparency waivers effectively allow market participants to bring certain business onto organised markets where it would have otherwise taken place OTC. It must be noted that this activity would not be pre-trade transparent whether taking place OTC or on an organised market. It should also be recognised that whilst non pre-trade transparent liquidity does not contribute to price formation from a pre-trade point of view it does contribute valuable post-trade information (to the extent that the last traded price makes a significant contribution to subsequent pre-trade information), thus contributing to the overall efficiency of the market.

⁵ This figure is significantly higher if trading data from one jurisdiction is removed with respect to the LIS pre-trade transparency waiver and from one jurisdiction with respect to Negotiated transaction waiver.

⁶ Article 21 of the Level 1 Directive: investment firms must “take all reasonable steps to obtain, when executing orders, the best possible result for their clients taking into account price, costs, speed, likelihood of execution and settlement, size, nature or any other consideration relevant to the execution of the order”.



We would contend that the current restrictive approach to the use by organised markets of the pre-trade transparency waivers is resulting in business that could otherwise take place on organised markets being conducted OTC.⁷ This results in liquidity being fragmented further and potentially held at different points along the trading chain rather than being available for execution on an organised market (whether pre-trade transparent or not). As an example, current regulation with respect to the reference price pre-trade transparency waiver has effectively mandated the creation of a separate pool of liquidity by organised markets wishing to offer this service with no interaction with the displayed order book of the same organised market. This structural inefficiency denies investment firms the opportunity of providing best execution to their clients since non pre-trade transparent liquidity cannot interact readily with pre-trade transparent liquidity. We would contend that this is an unintended and unwanted consequence of the current restrictive interpretation of the waiver.

Similarly, only permitting non pre-trade transparent liquidity to execute at the mid-point under the reference price pre-trade transparency waiver rather than anywhere in the spread of a reference bid-offer undermines the competitiveness of organised markets. Allowing RMs and MTFs to provide services that are attractive to market participants that currently use OTC facilities would encourage the migration of OTC activity to organised markets.

We have set out in the Annex to this letter our detailed views in relation to each of the MiFID pre-trade transparency waivers and would be happy to provide any further detail or data that CESR may require.

We would urge CESR to consider further the effects of the current approach to the pre-trade transparency waivers. In particular, to ensure that CESR's advice to the Commission with respect to further regulatory intervention is based on clear evidence of clear market failure, the sub-optimal implementation of pre-trade transparency waivers created by their current interpretation, and that any proposals would better achieve MiFID's aims. We would contend that the current approach and the proposals for further restrictions have the opposite effect.

Post-trade transparency and consolidation of transparency information

We agree with CESR that post-trade transparency information plays a vital role in ensuring the efficiency of price formation, assisting in the operation of the best execution obligation and mitigating the potential adverse impact of market fragmentation. We fully support CESR's efforts to improve the quality of OTC trade data and to eliminate the current barriers to the consolidation of transparency

⁷ Whilst it is important to take into consideration the structural differences between the US and European equity markets, we would note that the use of non-displayed liquidity is considerably less constrained in the US and that there is no evidence of detriment to the orderliness or efficiency of the market. We would also note that the percentage of business conducted on US organised market is higher, which tends to suggest that organised markets are a more attractive place to trade. We would contend that this is indicative of the greater flexibility in the type of business permitted on organised markets.



information from multiple sources, including organised markets and OTC. As part of CESR's dialogue with market participants on the impact of MiFID, we understand that a number of examples have been provided of poor quality data (duplicate reports, error in terms, etc) and there are instances of supervisory differences in the interpretation and enforcement of the current requirements.

We consider that the multipronged approach is sensible and we appreciate the efforts taken by CESR to involve market practitioners (through the Joint CESR/Industry Working Group) to address identified issues and in the development of standards. Whilst it is possible that existing initiatives by market participants to promote greater standardisation in post-trade transparency information may have succeeded without regulatory intervention, we would agree that the proposed approach has benefits in terms of ensuring consistency across Members States and also addresses issues unlikely to be resolved by market forces alone. For example, through the introduction of Approved Publication Arrangement (APA) regime, which – in conjunction with further guidance on reporting – should resolve a number of the issues relating to duplicate post-trade transparency information and concerns relating to quality.

The introduction the APA regime appears to be a key step in addressing a number of concerns relating to post-trade transparency information. We are encouraged that the regime proposed encompasses the benefits of competition and free choice of APA, within a regulatory framework designed to address clear issues. That said, **we believe that the success of the proposed APA regime in addressing the concerns that CESR has set out will depend on a commitment by national regulators to effectively supervise these entities both at the point of approval and ongoing, and to take steps where necessary to ensure consistent, high standards and compliance with the requirements.** It would appear that ESMA has a role to play in ensuring supervisory convergence.

With respect to the permissible post-trade delays, whilst there are clear benefits to price formation in ensuring timely post-trade disclosure of trading activity, we appreciate concerns expressed by a number of market participants about the potential negative impact of reducing certain thresholds and the introduction of an end of day reporting requirement. As noted earlier in this response, we believe that transparency is an important tool to achieve regulatory aims. However, **CESR should carefully weigh whether the benefits of the earlier publication of data outweigh any additional costs associated with risk positions that could be created and which would likely be passed on to the end investor.**

With respect to CESR's proposals in relation to the Mandatory Consolidated Tape (MCT), we appreciate the benefits that could be garnered in creating a single, reliable, cost effective source of data. However, we would be concerned about creating a monopoly provider and potentially losing the efficiency benefits of a competitive model (including with respect to innovation, quality of service and pricing competition). We would also highlight the current deficiencies in the US consolidated system and the significant costs that would be incurred by market participants in creating an MCT.

With the exception of costs in obtaining transparency information (and costs and restrictions associated with both consolidating and distributing that data), we believe that CESR's various proposals to improve

the quality of data, ease search costs and facilitate consolidation should mitigate a number of issues without the need for the MCT. Provided CESR's proposals results in clear, comprehensive requirements that are enforced by regulators, we believe that the introduction of the MCT would not be proportionate at this stage. However, **given the importance of accurate and consolidated transparency information, we would suggest that the success of any new proposals is kept under review with a view to pursuing an MCT should regulatory efforts and market forces be unsuccessful.**

Whilst we consider that CESR has made a number of sensible proposals to address certain issues relating to the quality and timeliness of post-trade transparency information, and the consolidation of transparency information, we are concerned that there are no direct measures aimed at reducing the cost of real-time transparency information. We would agree that reducing search costs and easing the consolidation of data from multiple sources (through the introduction of the APA regime and of common standards) should have downward pressure on costs. However, **we are concerned that the issue of real-time data costs will not be resolved by market forces alone.**

Whilst there has been some downward pressure on headline trading or transaction fees, there has not been a significant reduction in the fees charged by major European exchanges for data (or, indeed, other ancillary charges). As CESR notes, the cost of obtaining a complete pre- and post-trade picture of trading in Europe is approximately €450 per user per month in comparison with the cost of a complete picture of post-trade transparency information in the US of US\$70 (around €50) per user per month. We believe that the direct charges levied by the incumbent European exchanges are still significantly higher than that which would have been established in a truly competitive, non-constrained environment. It is also worth noting that a number of new entrant MTFs have made their data available in real-time free of charge. This would tend to suggest that, despite the significant decrease in market share for many of the incumbent European exchanges since the implementation of MiFID, they still wield dominant market power.

New entrant trading venues have for the most part attempted to remove barriers to access. For example, BATS Europe does not charge membership or access fees, has an open competitive connectivity model (from which it generates no profit) to ensure low costs, and charges no fees for real-time pre- and post-trade transparency information. However, the current bundling of fees (so that subsets of data cannot be purchased at reasonable rates) and the heterogeneity of market centres effectively allows the creation of silos and the continuation of monopolistic behaviour. As a consequence, the current disproportionately high costs of obtaining a complete and consolidated picture of trading activity results in a dislocation between professional trading firms (who can bear the current costs) and other investors (including institutional and retail) to whom the cost to access information is prohibitive. These high costs adversely impact the ability of these trading firms and investors to realise the benefits of the emerging competitive trading environment.⁸

⁸ See also recent study by the European Capital Markets Institute (EMCI): *The MiFID Metamorphosis* (May 2010): <http://www.ceps.eu/book/mifid-metamorphosis>



Whilst CESR's proposals go some way to address these concerns **we would urge CESR to consider the matter of real-time data costs further, including whether regulatory intervention with respect to real-time data costs would resolve this issue and provide significant benefits to market participants.**

Regulatory boundaries and requirements

We fully support CESR's proposals to ensure a level playing field between RMs and MTFs, and agree that Market Operators and Investment Firms should be subject to the same requirements when conducting the same activities, including the operation of an MTF. We would, however, note that we consider this to be largely an issue of perception rather than substance.

Some responses to CESR's November 2008 Call for Evidence raised concerns about an unlevel playing field and the possibility of regulatory arbitrage. As a UK FSA authorised firm, BATS Europe is currently subject to a number of requirements relating to the areas discussed by CESR in the Consultation Paper. These include: the FSA Principles, including Principle 3 (Management and control) and Principle 8 (Conflicts of interest)⁹; the detailed systems and controls requirements in the FSA Sourcebook *Senior Management Arrangements, Systems and Controls* (SYSC)¹⁰; and the detailed prudential requirements in the FSA *Prudential Sourcebook for Banks, Building Societies and Investment Firms* (BIPRU)¹¹.

As a result, we believe that we already comply with the requirements proposed by CESR and, as such, we would not incur any additional burden or costs. We would also note comments made by the FSA's in its recent publication *The FSA's markets regulatory agenda*¹² that: "we [the FSA] supervise the most important MTFs to the same standards as Recognised Investment Exchanges (i.e. Regulated Market operators)".

Where operating an RM (that is, a primary market for securities admitted to trading on an RM), it is clearly appropriate that Market Operators should be subject to specific requirements applicable to this different type of activity. Whilst we think that it would be useful to re-visit the Prospectus Directive in light of MiFID, we would note that a number of the major European exchanges have established (or acquired) MTFs to enable them to offer market trading in pan-European secondary securities in competition with the new entrant MTFs. Therefore, Market Operators should be able to and currently do compete on a level playing field with investment firm MTFs for secondary market trading.

⁹ <http://fsahandbook.info/FSA/html/handbook/PRIN/2/1>

¹⁰ <http://fsahandbook.info/FSA/html/handbook/SYSC> - including provisions relating to: governance arrangements; the identification and management of risks; the identification and management of conflicts of interest; and systems, resources and procedures to ensure continuity and regularity in the performance of regulated activities.

¹¹ <http://fsahandbook.info/FSA/html/handbook/BIPRU>

¹² UK FSA: *The FSA's markets regulatory agenda* (May 2010): <http://www.fsa.gov.uk/pubs/other/markets.pdf>



Further comments

Whilst not the subject of this Consultation Paper, we think that it is important not to consider the impact of MiFID in isolation. With respect to the reduction of frictional costs and any increase in the level of trading on organised markets¹³ (or indeed the migration of trading activity from the OTC space), we would point to the barriers posed by current high costs associated with clearing and settlement¹⁴. We would also note the recent moves by a number of major European exchanges to move towards a vertical silo model. Despite efforts, such as the Code of Conduct, **it would appear that initiatives such as Central Counterparty interoperability (which BATS Europe has made considerable efforts to support) would benefit from strong support from the regulators.**

Yours sincerely

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BATS ... Making Markets Better

¹³ The February 2010 report on MiFID by Pierre Fleuriot highlights the difference in trading velocity between the US and Europe despite the efforts of MiFID (see page 22), and also notes the significantly higher clearing and settlement costs (see page 38): <http://www.eifr.eu/files/file4315653.pdf>

¹⁴ See, for example, recent study conducted by Oxera:
<http://www.oxera.com/cmsDocuments/Reports/Costs%20of%20securities%20trading%20and%20post-trading%20April%202010.pdf>

Annex

2. Transparency

- *Question 1: Do you support the generic approach described above?*
- *Question 2: Do you have any other general comments on the MiFID pre-trade transparency regime?*

We agree with CESR that pre-trade transparency has an important role to play in promoting the efficiency of the price formation process and in mitigating the potential negative impact of market fragmentation. Whilst we agree that there should be an overarching transparency requirement for trading on organised markets, we do not agree with the limited circumstances in which CESR proposes permitting derogation from this requirement. The data set out by CESR clearly demonstrates that there is no market failure with respect to the current level of transparency (and, indeed, transparency trends).

There is clearly a balance to be struck between mandated universal transparency (a public good and the creation of a liquid, efficient market) and the ability to waive the requirement for pre-trade transparency. The current waivers contemplate that there are a number of legitimate reasons why pre-trade transparency may be waived, including: to minimise market impact for large orders (and to effectively safeguard the provision of risk capital); for orders that are price taking; and where it facilitates the achievement of best execution (either through functionality offered by an organised market or in a bilaterally negotiated transaction).

Transparency is a means to achieve regulatory aims. Whilst a high degree of transparency clearly brings benefits to the market by ensuring more efficient pricing and centralising access to liquidity, we would contend that an overly restrictive approach to use of the pre-trade transparency waivers by organised markets may actually undermine these aims. In particular, by restricting the ability of organised markets to offer innovative solutions that would result in lower costs for market users and that would increase the efficiency of the price formation process.

We also consider that the current approach has resulted in a greater number of distinct and separate pools of liquidity by effectively restricting the types of non-displayed orders that can interact with displayed orders. For example, when offering non-displayed order types pegged to a reference price within the spread, the current interpretation of the reference price pre-trade transparency waiver effectively required us to create a separate pool of liquidity with no interaction between the Integrated Book (predominantly pre-trade transparent) and reference price system. There is no evidence that such interaction would undermine MiFID's pre-trade transparency principles, nor have a detrimental effect on price formation. Rather, investors may be able to benefit from greater certainty of execution by interacting with a deeper pool of liquidity in addition to the possibility of price improvement. It is difficult to argue that the current situation is the best outcome for investors or that it best preserves the principles in MiFID since the current approach artificially separated two pools of liquidity that would logically be able to interact to optimise best execution for customers.

We would urge CESR to consider further the effects of the current approach to the pre-trade transparency waivers. In particular, to ensure that CESR’s advice to the Commission with respect to further regulatory intervention is based on clear evidence of clear market failure, the sub-optimal implementation of pre-trade transparency waivers created by their current interpretation, and that any proposals would achieve better achieve MiFID’s aims. We would contend that the current approach and the proposals for further restrictions have the opposite effect.

In the Consultation Paper, CESR proposes moving from a “principles-based” to “rules-based” approach with respect to the pre-trade transparency waivers. Whilst we appreciate the efforts by CESR to ensure consistent interpretation of the waivers through the current “approval” process, this process is rather cumbersome and lengthy. A rules-based regime would have the benefit of providing greater consistency and legal certainty. That said, by hard coding the current waivers into rules, there is a risk that the rules would be inflexible, in particular with respect to future innovation and changes to trading behaviour. On balance, we would be minded to support a rules-based regime but would **urge CESR to ensure that the rules are drafted in such a way to ensure provide certainty but retain sufficient flexibility to allow for further innovation.**

- *Question 3: Do you consider that the current calibration for large in scale orders is appropriate (Option 1)? Please provide reasoning for your view.*
- *Question 4: Do you consider that the current calibration for large in scale orders should be changed? If so, please provide a specific proposal in terms of reduction of minimum order sizes and articulate the rationale for your proposal.*

As noted by CESR in the Consultation Paper, the LIS pre-trade transparency waiver is used relatively little, particularly when trading from one jurisdiction is excluded. We believe that this is indicative of the way in which trading has evolved and the way in which best execution may be achieved in a fragmented market. We would also suggest that given the current implementation and the calibration of the thresholds, the LIS pre-trade transparency waiver is not serving the purpose for which it was intended.

In particular, we would note that brokers have developed sophisticated tools to efficiently execute orders by sourcing liquidity across multiple execution venues and/or OTC. Whilst there is clearly still a need for a block trade regime, we consider that markets participants should not be forced to trade large orders in a single block on one venue in order to make use of a pre-trade transparency waiver when such large parent orders may be more efficiently executed by being split into multiple smaller child orders that are sent to multiple venues.

To this extent, we believe that whilst market participants have developed ways in which to effectively and efficiently execute orders in a fragmented trading environment, regulation is constraining their ability to use these solutions, particularly when using organised markets.

CESR's Technical Advice on Possible Implementing Measures of the Directive 2004/39/EC on Markets in Financial Instruments (April 2005) ("CESR's 2005 Technical Advice") noted that "a waiver should be available for all trades once they surpass a size at which mandatory public exposure of the interest in trading might, taking account of market conditions, make the costs of executing higher than would be the case if the transaction could be negotiate privately". One solution to ensure that the LIS pre-trade transparency waiver is used more effectively and does not fetter the ability of a firm to achieve the best possible result would be to place the obligation on the firm originating the large order rather than on the trading venue. For example, through a requirement that all child orders should be able to be linked back to the parent order regardless of where the child order was traded.

Should CESR decide that the current implementation of the LIS pre-trade transparency waiver be retained (that is, through the use of thresholds applied at the trading venue level), **we would strongly urge CESR to significantly reduce the thresholds to take into account the nature of trading on organised markets in the post-MiFID environment (including average order sizes, average trade sizes and the fact that liquidity will by its nature be fragmented in a competitive trading environment to the extent that the market impact of an individual order has increased)**. We would also note that the extreme market volatility experienced during the financial crisis was not anticipated by the LIS threshold methodology, including the frequency with which the calculations are revised.

BATS Europe launched after the implementation of MiFID, therefore, we are unable to provide comparative figures relating to order and trade sizes on our market at the time when the LIS bands and thresholds were calibrated.¹⁵ However, we would note the interesting and useful work conducted by the London Stock Exchange Group in this regard and would **urge CESR to take this type of analysis into consideration when formulating its views**.

- *Question 5: Which scope of the large in scale waiver do you believe is more appropriate considering the overall rational for its application (i.e. Option 1 or 2)? Please provide reasoning for your views.*

We would be interested to understand the proportion of LIS orders that partially execute and where the remaining executed portion of the order, i.e. the "stub", falls below LIS. Given the small percentage of orders that currently qualify as LIS, we consider it unlikely that mandatory publication of stubs would result in a significant increase in transparency. We would also contend that, unless the LIS thresholds are significantly decreased, the mandatory pre-trade publication of stubs would disincentivise market participants further from using organised markets for LIS orders. **Therefore, we do not support the mandatory publication of below LIS stub orders.**

¹⁵ As a point of comparison, since our launch at the end of October 2008, the proportion of notional value conducted on BATS Europe as a result of LIS orders has typically ranged from 0.2% - 0.5%.



- *Question 6: Should the waiver be amended to include minimum thresholds for orders submitted to reference price systems? Please provide your rationale and, if appropriate, suggestions for minimum order thresholds.*
- *Question 7: Do you have other specific comments on the reference price waiver, or the clarifications suggested in Annex I?*

BATS Europe does not believe that there should be a minimum threshold on orders submitted under the reference price pre-trade transparency waiver. The minimum threshold should be a parameter that market participants, of their own choice, can set on an order. Setting a minimum threshold could have unintended consequences, including complications related to creating bands or stock level thresholds, which requires complex implementation, in addition to requiring regular review and revision of the thresholds.

In the Consultation Paper, CESR notes that reference price systems have gained in popularity and are increasingly being offered by new entrant MTFs. BATS Europe launched its Dark Book in August 2009 as a reference price system that only matches orders at the midpoint of the best bid and offer on the Primary Market (“PBBO”). We would note that the data gathered by CESR demonstrates that the overall level of trading under the reference price pre-trade transparency waiver is insignificant compared with overall trading volumes on organised markets. This is evident on our own market where volumes in our Dark Book have increased since launch but remain insignificant in comparison with volumes on our Integrated Book. We would also note that the increased level of trading in our Dark Book has not been to the detriment of the Integrated Book, where volumes have steadily increased. We would also note that there is no evidence that use of such systems is detrimental to the orderliness of the market or to the efficiency of the price formation process. Therefore, we do not agree that further restriction is warranted.

We should note that our strong preference would be to offer non-displayed orders in our Integrated Book rather than operating a separate system. To that extent, we would be able to offer functionality such that non-displayed orders could peg (midpoint or off-set) to a reference price (PBBO or consolidated European Best Bid and Offer – “EBBO”) and those orders could interact with other orders in the Integrated Book. This would enable us to operate a single pool of liquidity, thus increasing the likelihood of execution, rather than fragmenting liquidity in our own MTF.

In addition, interaction between displayed orders and non-displayed orders pegged to a reference price allows for the possibility of price improvement, to the benefit of end investors. For example, if a mid-point non-displayed resting order and an incoming regular, marketable order are able to interact, both benefit from the increased likelihood of execution (compared with a scenario where these two orders must be entered into separate systems and cannot interact) and both would achieve price improvement.



We consider that being able to offer a platform where both displayed and non-displayed orders are able to interact is consistent with the underlying principles of MiFID.¹⁶ In particular, with regard to promoting competition between trading venues and increasing the efficiency of the market by increasing the types of orders and liquidity that can interact with each other, thereby lowering transaction costs and allowing investors to obtain a better result. In order to give a degree of protection and certainty to those effectively taking risk by displaying their liquidity, we believe that where displayed and non-displayed liquidity interact, displayed liquidity should always maintain priority over non-displayed liquidity at the same price level.

We would urge CESR to consider – in light of the data gathered and the impact of the current approach in artificially fragmenting liquidity – re-casting the reference price pre-trade transparency waiver to allow for price improvement within the spread and to remove the requirement that the waiver can only be used by a separate system.

In Annex I to the Consultation Paper, CESR proposes clarifying the tests that the price referenced under the waiver should meet. The BATS Europe Dark Book currently uses the midpoint of the PBBO, although we would ideally use an EBBO as a reference price, as this would be more reflective of the fragmented trading environment where other venues contribute to price formation (we would also ideally allow price improvement within the spread rather than limiting executions to the midpoint). We would do not agree with CESR's proposals that use of the reference price pre-trade transparency system should be restricted to a separate system, in particular where there would hamper the ability of an organised market to use a price derived in part from its own displayed order book.

With respect to the use of an EBBO, we would contend that the current interpretation of the reference price pre-trade transparency waiver hampers our ability to do so; in particular, the concepts relating to “widely published” and “reliable reference price”. We currently collect and process data from other venues for internal purposes and the market share page on our website. To this extent, we could create an EBBO for use as the reference price in the Dark Book. However, we would note the high costs in obtaining such data and the often restrictive nature of the legal agreements, in particular with respect to use and redistribution. Therefore, without first addressing these issues, **we would contend that the clarifications suggested by CESR with regard to the publication of the reference price are not proportionate.**

Moreover, we would question whether it is necessary for market participants who are price taking to have access in advance to a real-time feed of the price reference data being used by the trading venue, particularly where all of the components of the reference price are readily available in real-time. Rather,

¹⁶ We would note that Recital 5 of the MiFID Regulation provides that: “[the] framework of rules [is] designed to *promote competition* between trading venues for execution services so as to increase investor choice, *encourage innovation*, *lower transaction costs*, and *increase the efficiency* of the price formation process on a pan-Community basis” (italics our emphasis).

it is important that the trading venue has a robust, transparent and reliable methodology for calculating and validating the reference price. We would also suggest that organised markets should provide details of the reference prices used at the point of execution.

CESR notes that “it would be very burdensome for market participants to have access to all components and calculate the EBBO themselves in order to establish the reference price at which they trade”¹⁷. We would argue that, where the trading venue has created an EBBO (which may not necessarily be published in real-time) through a robust, transparent and reliable methodology, the costs for market participants are effectively reduced.

- *Question 8: Do you have any specific comments on the waiver for negotiated trades?*

We agree with CESR’s assessment that the pre-trade transparency waiver for negotiated transactions should be retained. Trades under this waiver are negotiated privately by two counterparties but are brought onto an organised market, such that they can benefit from being “on market trades” (for example, subject to the rules of that market, centrally cleared, etc). We agree with CESR that there are circumstances where it is appropriate to waive pre-trade transparency to enable intermediaries to achieve best execution for their clients. For example, because a better quality of execution might be achieved outside the book (including whether order book cannot fill the whole order).

However, we disagree with the current interpretation of the negotiated transaction pre-trade transparency waiver, which is restricted to a single price (that of the market to which the negotiated transaction is reported). **We do not agree that it is appropriate to constrain the reference price to a single market but rather would contend that it would be more appropriate to permit a reference price based on an EBBO.** We believe that requiring reference to prices on a single market does not necessarily represent the best interests of investors (in contrast with the purpose of the waiver). We would also suggest that preventing the use of an EBBO is illogical considering it has been permitted in principle in relation to the reference price pre-trade transparency waiver.

In addition, we would argue that limiting the reference price to that generated on the market to which the trade is reported creates a quasi-concentration rule that may interfere with or bias competition, and which is not in keeping with the underlying principles of MiFID with respect to competition.

- *Question 9: Do you have any specific comments on the waiver for order management facilities, or the clarifications provided in Annex I?*

Whilst we would agree with a number of the clarifications proposed by CESR to ensure fairness with respect to interaction rules, we do not agree with the underlying approach taken by CESR in relation to the types of order management facilities that can be operated by organised markets.

¹⁷ Paragraph 9 of Annex I to the Consultation Paper.

CESR states in its 2005 Technical Advice that: “The pre-trade transparency obligation should be waivable for the information held in the facilities provided by RMs or MTFs for the management of orders such as “iceberg”-type orders, whereby only part of the order is visible, stop orders or close orders. The reason for this is that these are facilities provided by RMs or MTFs that *help intermediaries and their clients in executing their orders in the most efficient way*. CESR is of the opinion that the *provision of these facilities should be left to the discretion of RMs and MTFs.*” (italics our emphasis)

We do not agree with CESR’s proposals to further cement the requirement that an order management facility must encompass an element of pre-trade transparency (akin to an iceberg facility). Clearly any such functionality should be fair (for example, maintains priority for displayed orders and does not preference any one user with privileged information). However, **we are concerned that the proposals made by CESR will unnecessarily restrict the ability of organised markets to offer functionality that would help intermediaries and their clients execute orders in the most efficient way.** In particular, it is not clear what is achieved by preventing organised markets from offering facilities that replicate orders or combinations of orders that can currently be used by brokers but in a more efficient manner. We would argue that offering such functionality is precisely the intention of this waiver; however, the drafting of the waiver has effectively restricted its application to those facilities available at the time of drafting (iceberg facilities and stop orders).

Allowing organised markets to provide functionality that enables intermediaries to achieve best execution for their clients democratises its use by members of that trading facility. We would also suggest that allowing organised markets to offer functionality that would be attractive to their members in aiding them to more efficiently execute orders may attract more business onto organised markets.

As noted in our response to question 1, whilst allowing organised markets to offer such functionality may not result in an increase in the publication of pre-trade information (which would not be made pre-trade transparent in any event), it will result in immediate post-trade publication of any resulting trades. Attracting more liquidity to organised markets results in greater interaction of liquidity and therefore increases the likelihood of execution. In addition, post-trade information forms a vital part of price formation, thus contributing to an effective price formation process.

We would urge CESR re-cast the order management facility pre-trade transparency waiver such that it is not tied to iceberg or stop order functionality (including a “pending pre-trade disclosure” requirement) but rather is sufficiently flexible to allow organised markets to offer functionality that can aid their members to achieve more efficient execution of their orders.

- *Questions 10-16 relating to the regime for Systematic Internalisers (SIs)*

To the extent that CESR considers there is evidence to suggest that it is necessary to retain the SI regime, we would agree with CESR’s proposals to clarify the definition of SI and to ensure that the quoting obligations are meaningful. To the extent that CESR aims to create parity between organised

markets and SIs, we would argue that elements of the SI regime, including the ability to offer price improvement, should be available to organised markets.

2.1 Post-trade transparency

- *Question 17: Do you agree with this multi-pronged approach?*

We agree with CESR that post-trade transparency information plays a vital role in ensuring the efficiency of price formation, assisting in the operation of the best execution obligation and mitigating the potential adverse impact of market fragmentation. We fully support CESR's efforts to improve the quality of OTC trade data and to eliminate the current barriers to the consolidation of trade data from multiple sources, including organised markets and OTC. As part of CESR's dialogue with market participants on the impact of MiFID, we understand that a number of examples have been provided of poor quality data (duplicate reports, error in terms, etc) and there are instances of supervisory differences in the interpretation and enforcement of the current requirements.

We consider that the multipronged approach is sensible and we appreciate the efforts taken by CESR to involve market practitioners (through the Joint CESR/Industry Working Group) to address identified issues and in the development of standards. Whilst it is possible that existing initiatives by market participants to promote greater standardisation in post-trade transparency information may have succeeded without regulatory intervention, we would agree that the proposed approach has benefits in terms of ensuring consistency across Members States and also addresses issues unlikely to be resolved by market forces alone. For example, through the introduction of Approved Publication Arrangement (APA) regime, which – in conjunction with further guidance on reporting – should resolve a number of the issues relating to duplicate post-trade transparency information and concerns relating to quality.

- *Question 18: Do you agree with CESR's proposals outlined above to address concerns about real-time publication of post-trade transparency information? If not, please specify your reasons and include examples of situations where you may face difficulties fulfilling this proposed requirement.*
- *Question 19: In your view, would a 1-minute deadline lead to additional costs (e.g. in terms of systems and restructuring of processes within firms)? If so, please provide quantitative estimates of one-off and ongoing costs. What would be the impact on smaller firms?*

We would note that MiFID currently requires transactions to be published as close to real-time as possible, and that CESR has provided guidance that the three minute deadline should only be used in exceptional circumstances.

CESR notes that some responses to its November 2008 Call for Evidence suggested that some firms were routinely using the maximum delay. If CESR has evidence of this, either because of poor quality reporting systems or an attempt to gain any advantage by delaying the publication of post-trade



information, we believe that this should be a supervisory matter and that national regulators should enforce compliance with the current rule.

We agree that there are clear benefits in post-trade information being made available instantaneously, although we have no objection to information being published within a one minute deadline where the circumstances necessitate this delay. However, we do not believe that an amendment to the requirement will resolve what appears to be a supervisory issue.

- *Question 20: Do you support CESR proposal to maintain the existing deferred publication framework whereby delays for large trades are set out on the basis of the liquidity of the share and the size of the transaction?*
- *Question 21: Do you agree with the proposal to shorten delays for publication of trades that are large in scale? If not, please clarify whether you support certain proposed changes but not others, and explain why.*
- *Question 22: Should CESR consider other changes to the deferred publication thresholds so as to bring greater consistency between transaction thresholds across categories of shares? If so, what changes should be considered and for what reasons?*
- *Question 23: In your view, would i) a reduction of the deferred publication delays and ii) an increase in the intraday transaction size thresholds lead to additional costs (e.g. in ability to unwind large positions and systems costs)? If so, please provide quantitative estimates of one-off and ongoing costs.*

Given the importance of post-trade transparency information in ensuring an efficient price formation process and aiding the functioning of the best execution obligation, we agree that it is necessary to ensure that there is a comprehensive and clear framework to ensure publication of post-trade transparency information. Within this, it is important to ensure there is a mechanism to allow for the delayed publication of certain post-trade information to minimise market impact and to safeguard the continued provision of risk capital, such that investors receive the best possible result.

To this extent, we are supportive of CESR's proposal to maintain the existing deferred publication framework. Whilst there are clear benefits to price formation in ensuring timely post-trade disclosure of trading activity, we appreciate concerns expressed by a number of market participants about the potential negative impact of reducing certain thresholds and the introduction of an end of day reporting requirement.

As noted earlier in this response, we believe that transparency is an important tool to achieve regulatory aims. However, CESR should carefully weigh whether the benefits of the earlier publication of data outweigh any additional costs associated with risk positions that could be created and which would likely be passed on to the end investor.



BATS Europe publishes all trades conducted on its MTF instantaneously and does not operate an OTC trade reporting facility. Therefore, we will be interested in the views of the operators of trade reporting facilities, and sell side and buy side firms, who are best placed to respond to CESR's specific proposals on deferred publication thresholds and delays.

3. Application of transparency obligations for equity-like instruments

- *Question 24: Do you agree with the CESR proposal to apply transparency requirements to each of the following (as defined above):*
 - *DRs (whether or not the underlying financial instrument is an EEA share);*
 - *ETFs (whether or not the underlying is an EEA share);*
 - *ETFs where the underlying is a fixed income instrument;*
 - *ETCs; and*
 - *Certificates*

If you do not agree with this proposal for all or some of the instruments listed above, please articulate reasons.

We are supportive of CESR's proposals to create a transparency regime for equity-like instruments that trade in a similar way to shares.

We would note that ETF volumes in European are significantly lower than those in the US. We would be interested to see whether a clearer, pan-European transparency regime results in greater activity in these types of instruments.

- *Question 25: If transparency requirements were applied, would it be appropriate to use the same MiFID equity transparency regime for each of the 'equity-like' financial instruments (e.g. pre- and post-trade, timing of publication, information to be published, etc.). If not, what specific aspect(s) of the MiFID equity transparency regime would need to be modified and for what reasons?*

As noted in our responses to questions 1-9, we consider that there are significant inefficiencies in the current pre-trade transparency regime for shares. We would also note that a number of organised markets currently offer trading in equity-like instruments (such as ETFs) with more flexibility in the types and size of orders that can be non-displayed. In the case of BATS Europe, this has not resulted in an overwhelming preference for non-displayed orders, nor has there been any negative impact on price formation.

Therefore, **we would urge CESR to craft a pre-trade transparency regime that addresses the concerns we have expressed in relation to the current regime for shares.** Similarly, we would highlight the concerns about the quality of post-trade transparency information, and the consolidation and cost of transparency information. Whilst CESR's proposals in relation the post-trade transparency regime for

shares should go a long way to address the current issues, as noted in our response to question 31, we do not believe CESR's proposals will resolve the issues relating to real-time costs.

Question 26: In your view, should the MiFID transparency requirements be applied to other "equity-like" financial instruments or to hybrid instruments (e.g. Spanish participaciones preferentes)? If so, please specify which instruments and provide a rationale for your view.

We do not currently offer trading in these types of instruments and will be interested in the views of market participants.

4. Consolidation of transparency information

- *Question 27: Do you support the proposed requirements/guidance (described in this section and in Annex IV) for APAs? If not, what changes would you make to the proposed approach?*
- *Question 28: In your view, should the MiFID obligation to make transparency information public in a way that facilitates the consolidation with data from other sources be amended? If so, what changes would you make to the requirement?*
- *Question 29: In your view, would the approach described above contribute significantly to the development of a European consolidated tape?*

We are supportive of CESR's proposals to require investment firms to publish their trade reports through an APA. The majority of concerns (including relating to duplicate reporting and uncorrected errors in terms) have related to post-trade transparency information. We believe that reducing search costs and improving the quality of post-trade information will ease the consolidation of data from multiple sources. Similarly, we agree that greater standardisation will facilitate the consolidation of data from organised markets and the new APAs.

The introduction of the APA regime appears to be a key step in addressing a number of concerns relating to post-trade transparency information. We are encouraged that the regime proposed encompasses the benefits of competition and free choice of APA, within a regulatory framework designed to address clear issues. That said, **we believe that the success of the proposed APA regime in addressing the concerns that CESR has set out will depend on a commitment by national regulators to effectively supervise these entities both at the point of approval and ongoing, and to take steps where necessary to ensure consistent, high standards and compliance with the requirements.** It would appear that ESMA has a role to play in ensuring supervisory convergence.

- *Question 30: In your view, what would be the benefits of multiple approved publication arrangements compared to the current situation post-MiFID and compared to an EU mandated consolidated tape (as described under 4.1.2 below)?*



We believe that a number of CESR's proposals will aid the consolidation of European trade data, including proposals relating to: standards; clarity on reporting requirements; and the mandatory use of APAs for OTC trade reporting.

The Joint CESR/Industry Working Group has an important role to play with respect to the first two elements. We welcome the opportunity to contribute to these discussions, and to build upon initiatives with which we have been involved to promote harmonisation and standardisation (for example, the Uniform MTF symbology work and efforts to harmonise pan-European tick size regimes).

With respect to APAs, we believe that these form an important part of facilitating a consolidated tape (whether created by market forces or a mandatory regulatory solution). As noted in our response to questions 27-29, we believe that the success of the APA regime will depend on the consistent application of high standards and willingness by regulators to enforce those standards.

- *Question 31: Do you believe that MiFID provisions regarding cost of market data need to be amended?*
- *Question 32: In your view, should publication arrangements be required to make pre- and post-trade information available separately (and not make the purchase of one conditional upon the purchase of the other)? Please provide reasons for your response.*
- *Question 33: In your view, should publication arrangements be required to make post-trade transparency information available free of charge after a delay of 15 minutes? Please provide reasons for your response.*

We are supportive of CESR's suggestions that charges for pre- and post-trade transparency information should be unbundled and that all organised markets and APAs should make post-trade transparency information available free of charge after a delay of a maximum of fifteen minutes.

Pre- and post-trade information should be made available separately since their utilisation could be quite different. The manipulation of the vast amount of real-time pre-trade information requires significantly more technical resources and capabilities than post-trade information. As well as being more expensive to process, bundled pre- and post-trade information is also likely to be more expensive to acquire. **The unbundled pre- and post-traded information should also be made available by organised markets in a more granular form, for example, FTSE 100 separately from the FTSE 250.**

Whilst we consider that CESR has made a number of sensible proposals to address certain issues relating to the quality and timeliness of post-trade transparency information, and the consolidation of transparency information, we are concerned that there are no direct measures aimed at reducing the cost of real-time transparency information. We would agree that reducing search costs and easing the consolidation of data from multiple sources (through the introduction of the APA regime and of common standards) should have downward pressure on costs. However, we are concerned that the issue of real-time data costs will not be resolved by market forces alone.



Whilst there has been some downward pressure on headline trading or transaction fees, there has not been a significant reduction in the fees charged by major European exchanges for data (or, indeed, other ancillary charges). As CESR notes the cost of obtaining a complete pre- and post-trade picture of trading in Europe is approximately €450 per user per month in comparison with the cost of a complete picture of post-trade transparency information in the US of US\$70 (around €50) per user per month. We believe that the direct charges levied by the incumbent European exchanges are still significantly higher than that which would have been established in a truly competitive, non-constrained environment. It is also worth noting that a number of new entrant MTFs have made their data available in real-time free of charge. This would tend to suggest that, despite the significant decrease in market share for many of the incumbent European exchanges since the implementation of MiFID, they still wield dominant market power.

New entrant trading venues have for the most part attempted to remove barriers to access. For example, BATS Europe does not charge membership or access fees, has an open competitive connectivity model (from which it generates no profit) to ensure low costs, and charges no fees for real-time pre- and post-trade transparency information. However, the current bundling of fees (so that subsets of data cannot be purchased at reasonable rates) and the heterogeneity of market centres effectively allows the creation of silos and the continuation of monopolistic behaviour. As a consequence, the current disproportionately high costs of obtaining a complete and consolidated picture of trading activity results in a dislocation between professional trading firms (who can bear the current costs) and other investors (including institutional and retail) to whom the cost to access information is prohibitive. These high costs adversely impact the ability of these trading firms and investors to realise the benefits of the emerging competitive trading environment.¹⁸

Whilst CESR's proposals go some way to address these concerns **we would urge CESR to consider the matter of real-time data costs further, including whether regulatory intervention with respect to real-time data costs would resolve this issue and provide significant benefits to market participants.**

- *Question 34: Do you support the proposal to require RMs, MTFs and OTC reporting arrangements (i.e. APAs) to provide information to competent authorities to allow them to prepare MiFID transparency calculations?*

This data is used as the basis for the MiFID transparency framework and, as trading volumes are fragmented across multiple organised markets and OTC, it is important that the calculations are an accurate reflection of the whole market. A number of the MTFs, including BATS Europe, provided data to contribute to the most recent MiFID transparency calculations and we are supportive of CESR's proposals to require organised markets and APAs to provide information to competent authorities for these purposes.

¹⁸ See also recent study by the European Capital Markets Institute (EMCI): *The MiFID Metamorphosis* (May 2010): <http://www.ceps.eu/book/mifid-metamorphosis>

- *Question 34: Do you support the proposed approach to a European mandatory consolidated tape?*
- *Question 35: If not, what changes would you suggest to the proposed approach?*
- *Question 36: In your view, what would be the benefits of a consolidated tape compared to the current situation post-MiFID and compared to multiple approved publication arrangements?*
- *Question 37: In your view, would providing trade reports to a MCT lead to additional costs? If so, please specify and where possible please provide quantitative estimates of one-off and ongoing costs.*

With respect to CESR's proposals in relation to the Mandatory Consolidated Tape (MCT), we appreciate the benefits in creating a single, reliable, cost effective source of data. However, we would be concerned about creating a monopoly provider and potentially losing the efficiency benefits of a competitive model (including with respect to innovation, quality of service and pricing competition). We would also highlight the current deficiencies in the US consolidated system and the significant costs that would be incurred by market participants in creating an MCT.

With the exception of costs in obtaining data (and costs and restrictions associated with both consolidating and distributing that data), we believe that CESR's various proposals to improve the quality of data, ease the costs of locating post-trade information and facilitate consolidation should mitigate a number of issues without the need for the MCT.

Consolidated tapes are technically available from information vendors today. It is the prohibitive cost and bundling of the underlying data that inhibits their commercial viability.

Provided CESR's proposals results in clear, comprehensive requirements that are enforced by regulators, we believe that the introduction of the MCT would not be proportionate at this stage. However, given the importance of accurate and consolidated transparency information, we would suggest that the success of any new proposals is kept under review with a view to pursuing an MCT should regulatory efforts and market forces be unsuccessful.

5. Regulatory boundaries and requirements

- *Question 38: Do you agree with this proposal? If not, please explain.*
- *Question 39: Do you consider that it would help addressing potential unlevel playing field across RMs and MTFs? Please elaborate.*
- *Question 40: In your view, what would be the benefits of the proposals with respect to organisational requirements for investment firms and market operators operating an MTF?*
- *Question 41: In your view, do the proposals lead to additional costs for investment firms and market operators operating an MTF? If so, please specify and where possible please provide quantitative estimates of one-off and ongoing costs.*



We fully support CESR's proposals to ensure a level playing field between RMs and MTFs, and agree that both Market Operators and Investment Firms should be subject to the same requirements when conducting the same activities, including the operation of an MTF. We would, however, note that we consider this to be largely an issue of perception rather than substance.

Some responses to CESR's November 2008 Call for Evidence raised concerns about an unlevel playing field and the possibility of regulatory arbitrage. As a UK FSA authorised firm, BATS Europe is currently subject to a number of requirements relating to the areas discussed by CESR in the Consultation Paper. These include: the FSA Principles, including Principle 3 (Management and control) and Principle 8 (Conflicts of interest)¹⁹; the detailed systems and controls requirements in the FSA Sourcebook *Senior Management Arrangements, Systems and Controls* (SYSC)²⁰; and the detailed prudential requirements in the FSA *Prudential Sourcebook for Banks, Building Societies and Investment Firms* (BIPRU)²¹.

As a result, we believe that we already comply with the requirements proposed by CESR and, as such, we would not incur any additional burden or costs. We would also note comments made by the FSA's in its recent publication *The FSA's markets regulatory agenda*²² that: "we [the FSA] supervise the most important MTFs to the same standards as Recognised Investment Exchanges (i.e. Regulated Market operators)".

Where operating an RM (that is, a primary market for securities admitted to trading on an RM), it is clearly appropriate that Market Operators should be subject to specific requirements applicable to this different type of activity. Whilst we think that it would be useful to re-visit the Prospectus Directive in light of MiFID, we would note that a number of the major European exchanges have established (or acquired) MTFs to enable them to offer pan-European secondary market trading in competition with the new entrant MTFs. Therefore, Market Operators should be able to and currently do compete on a level playing field with investment firm MTFs for secondary market trading.

- *Question 42: Do you agree to introduce the definition of broker internal crossing process used for the fact finding into MiFID in order to attach additional requirements to crossing processes? If not what should be captured, and how should that be defined?*
- *Question 43: Do you agree with the proposed bespoke requirements? If not, what alternative requirements or methods would you suggest?*

¹⁹ <http://fsahandbook.info/FSA/html/handbook/PRIN/2/1>

²⁰ <http://fsahandbook.info/FSA/html/handbook/SYSC> - including provisions relating to: governance arrangements; the identification and management of risks; the identification and management of conflicts of interest; and systems, resources and procedures to ensure continuity and regularity in the performance of regulated activities.

²¹ <http://fsahandbook.info/FSA/html/handbook/BIPRU>

²² UK FSA: *The FSA's markets regulatory agenda* (May 2010): <http://www.fsa.gov.uk/pubs/other/markets.pdf>

- *Question 44: Do you agree with setting a limit on the amount of client business that can be executed by investment firms' crossing systems/processes before requiring investment firms to establish an MTF for the execution of client orders ('crossing systems/processes becoming an MTF)?*
- *What should be the basis for determining the threshold above which an investment firm's crossing system/process would be required to become an MTF? For example, should the threshold be expressed as a percentage of total European trading or other measures? Please articulate rationale for your response.*
- *In your view, should linkages with other investment firms' broker crossing systems/processes be taken into account in determining whether an investment firm has reached the threshold above which the crossing system/process would need to become an MTF? If so, please provide a rationale, also on linking methods which should be taken into account.*
- *Question 45: In your view, do the proposed requirements for investment firms operating crossing systems/processes lead to additional costs? If so, please specify and where possible please provide quantitative estimates of one-off and ongoing costs.*

A number of responses to CESR's November 2008 Call for Evidence highlighted concerns regarding the level of business conducted by investment firms operating internal crossing systems (also referred to as Broker Crossing Systems). We appreciate the efforts made by CESR to collect data with respect to this type of activity to ensure that it is able to fully assess the extent of business conducted in Broker Crossing Systems.

Where operating the same activities as organised markets, as a matter of principle, we believe that market operators and investment firms should be subject to the same requirements; where a broker wishes to operate an MTF, it should be subject to the same requirements. That said, we believe that, in many cases, Broker Crossing Systems have a substantively different business model from organised markets and that they fulfil a different function. Therefore, **in such cases, we do not believe that Broker Crossing Systems should be subject to the same requirements, nor that they should be forced to amend their business model to that of an organised market.** We would also note that Broker Crossing Systems currently operate under a regulatory framework that includes requirements relating to best execution, the identification and management of conflicts of interest, post-trade transparency obligations and the reporting of suspicious transactions to regulators.

We do not believe that a threshold for investment firms would be viable since such thresholds suffer from definitional, continued relevance and monitoring problems, with the added challenge of the organisation complexity of many investment firms.

We can appreciate the benefits for regulators if investment firms operating Broker Crossing Systems notify their regulators and provide information on the functionality operated. However, **we believe that CESR needs to carefully consider whether the benefits of mandating real-time identification of trading activity will outweigh the negative impact that could be had on the ability of market participants to trade in size without adverse market impact and to the provision of risk capital.**



If CESR addresses the issues that have been raised in relation to the pre-trade transparency waivers, including as set out in our response to questions 1-7, this would resolve a number of the complaints relating to a level regulatory playing field. In particular, this would ensure that organised markets can remain competitive and attractive places to trade, whilst recognising the different function fulfilled by Broker Crossing Systems.

We believe that – provided the market is orderly and fair – market participants should have choice in where and how to trade such that they achieve the best possible result. We do not consider that an outcome, which results in regulation preventing the operation of functionality that is useful for investors and helps them to achieve the best possible result, where there is no clear market failure would be desirable.

6. MiFID options and exemptions

We have limited our response to this section of the Consultation Paper to question 46.

- *Question 46: Do you think that replacing the waivers with legal exemptions (automatically applicable across Europe) would provide benefits or drawbacks? Please elaborate.*

CESR proposes moving from a “principles-based” to “rules-based” approach with respect to the pre-trade transparency waivers. Whilst we appreciate the efforts by CESR to ensure consistent interpretation of the waivers through the current “approval” process, this process is rather cumbersome and lengthy. A rules-based regime would have the benefit of providing greater consistency and legal certainty. That said, by hard coding the current waivers into rules, there is a risk that the rules would be inflexible, in particular with respect to future innovation and changes to trading behaviour. On balance, **we would be minded to support a rules-based regime but would urge CESR to ensure that the rules are drafted in such a way to ensure provide certainty but retain sufficient flexibility to allow for further innovation.**