COMMITTEE OF EUROPEAN SECURITIES REGULATORS

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CONSULTATION PAPER

CESR Technical Advice to the European Commission in the Context of the MiFID Review - Equity Markets

Deadline for contributions: CESR invites responses to this Consultation Paper by **31 May 2010**. All contributions should be submitted online via CESR's website under the heading 'Consultations' at www.cesr.eu. All contributions received will be published following the close of the call for evidence, unless the respondent requests its submission or any annex containing commercially sensitive information to be confidential.

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Executive Summary

The Markets in Financial Instruments Directive (MiFID) came into force on 1 November 2007. It introduced significant changes to the European regulatory framework for secondary markets. CESR initially assessed the impact of these changes in the first half of 2009 and published a report in June 2009. This report on 'impact of MiFID on equity secondary markets functioning' (Ref.:CESR/09-355) recommended further work to address some issues identified.

Following the publication of the report, CESR held a series of meetings with representatives from regulated markets (RM), multilateral trading facilities (MTFs), investment firms, buy-side firms and market data vendors and conducted a fact-finding to obtain information on dark trading taking place on RM, MTFs and investment firms' crossing processes. This Consultation Paper has been developed on the basis of CESR's continued work on the issues identified in the previous report. The consultation aims at assisting CESR to provide the European Commission (EC) with technical advice on the MiFID Review regarding equity markets by July 2010, so that the EC can report to the European Parliament and the Council on possible changes to MiFID.

The main topics addressed in this Consultation Paper are covered by the following headings:

Pre-trade transparency regime for RM/MTFs: Data from the fact-finding shows that more then 90 percent of trading on organised markets in Europe is pre-trade transparent. CESR recommends retaining the general requirement for pre-trade transparency on organised markets (RM/MTFs). However, exceptions to pre-trade transparency should continue to be allowed under certain circumstances. In order to provide greater clarity for regulators and market participants and facilitate continuous supervisory convergence, CESR seeks to move from a 'principle based approach' to waivers from pre-trade transparency to an approach that is more 'rule based'. As regards the scope and criteria for the waivers, CESR consults in Section 2.1.1 of the Consultation Paper on whether some of the waivers should be recast (i.e. thresholds for, and scope of, large in scale waiver, introduction of a minimum order size for the reference price waiver) and provides further clarifications on the interpretation of the waivers (Annex I).

Definition of and obligations for systematic internalisers: The recommendation of CESR in Section 2.1.2 of the Consultation Paper is to retain the systematic internaliser regime but revisit the definition of 'systematic internaliser' (SI) and related obligations to ensure a consistent understanding and implementation and to improve the value of information provided to the market.

Post-trade transparency regime: A key theme in this Consultation Paper is the recommendation of CESR for an improvement in the quality and timeliness of post-trade transparency and the ability to effectively consolidate information received from multiple European equity markets. It is therefore recommended in Section 2.2 to retain the current framework for post-trade transparency, but introduce formal measures to improve quality, shorten delays and reduce the complexity of the regime. More specifically, it is proposed to amend MiFID to embed additional standards for the publication of post-trade information (Annex II) and to provide further clarifications of the post-trade transparency obligations (Annex III). To finalise the proposed standards for post-trade transparency information and to further specify proposed amendments to improve the quality of OTC post-trade transparency data by July 2010, CESR suggests establishing a joint CESR/Industry Working Group immediately following the publication of this Consultation Paper.

Application of transparency obligations to equity-like instruments: CESR also recommends in Section 3 of the Consultation Paper to enhance the scope of transparency regime by applying transparency obligations to equity-like instruments admitted to trading on a RM, including depository receipts, exchange-traded funds, exchange-traded commodities and 'certificates'. These instruments are considered to be equity-like, since they are traded like shares and, from an economic point of view, equivalent to shares. CESR believes that there are benefits for investors stemming from a harmonised pan-European pre-and post-trade transparency regime for these instruments.

Regulatory framework for consolidation and cost of market data: CESR recognises that significant barriers to the consolidation of post-trade data remain and that without further regulatory intervention, market forces are unlikely to deliver an adequate and affordable pan-European consolidation of transparency information. Two possible approaches to achieve this goal are proposed for consultation in Section 4. One approach would retain the commercially-driven consolidation process but supplement the introduction of new standards to improve data quality and achieve greater consistency in trade publication practices by requiring investment firms to publish their trades through Approved Publication Arrangements (APAs). All APAs would be required to operate data publication arrangements to prescribed standards (Annex IV). The other approach would built on this APA regime but would require a single consolidated tape to offer market users a single point of access.

Regulatory boundaries and requirements: In Section 5 of the Consultation Paper, CESR addresses concerns about certain inconsistencies which may have impacted the level playing field. It is proposed to align the requirements which apply to RM and MTFs under MiFID, and to introduce tailored additional obligations for investment firm operating crossing systems/processes. CESR also consults on the possibility of requiring investment firms operating crossing systems/processes to set up MTFs for their crossing activity once they have reached a certain size on its own or in combination with other crossing systems/processes with which they have a private link.

MiFID options and discretions: In section 6 of the Consultation Paper some options and discretions relating to MiFID market provisions are identified and CESR consults on the desirability of eliminating certain options and discretions.

1. Introduction

1. The Markets in Financial Instruments Directive (MiFID), a major part of the European Union's Financial Services Action Plan (FSAP), came into effect on 1 November 2007. It introduced significant changes to the European regulatory framework, taking account of developments in financial services and markets since the Investment Services Directive (ISD), which it replaced, was implemented in 1995.

2. In November 2008, CESR published a Call for Evidence (Ref. CESR/08-872) on the impact of MiFID on secondary market trading in equities. In response, thirty-nine submissions (including four confidential submissions) and three confidential annexes were received from a range of European trade associations, regulated markets (RMs), multilateral trading facilities (MTFs), market data vendors, investment firms and other interested parties. CESR also organised a roundtable at the beginning of 2009 which attracted a broad range of market participants.

3. In June 2009, CESR published its report on the 'impact of MiFID on equity secondary markets functioning' (Ref. CESR/09-355). This report set out its findings and recommended further work to address issues identified. Following the publication of the report, CESR held a series of meetings with representatives from RMs, MTFs, investment firms and market data vendors. CESR also received further written representations from RMs, issuers, high frequency traders and market data vendors. Finally, CESR conducted a fact finding to obtain information on dark trading taking place on RMs, MTFs and investment banks' internal crossing processes.

4. In developing proposals for the Commission's MiFID review, it is important to keep in mind relevant changes in the operation of trading and market structure. Technological advance has continued to facilitate new developments in markets, an important example being the strong growth in algorithmic and high frequency trading. CESR will continue work on these micro-structural issues in parallel to the MiFID review. A Call for Evidence has been published in

this respect on 1 April 2010 for a one month call for comments. Where appropriate, CESR will incorporate the outcome of this work in its final advice to the Commission.

5. This consultation paper is organised as follows. Section 2 describes issues relating to the MiFID pre- and post-trade transparency regime and puts forward proposals aimed at addressing concerns raised following the implementation of MiFID including, in particular, lack of clarity of the MiFID pre-trade transparency waivers and quality of post-trade transparency information. Section 3 considers existing transparency of so-called 'equity-like' financial instruments and proposes to extend MiFID transparency obligations to such instruments. Section 4 considers remaining barriers to consolidation of transparency information and puts forward two possible approaches to promote consolidation. Section 5 assesses whether there is a case of re-aligning regulatory boundaries and requirements and puts forward proposals to better align requirements between RMs and MTFs and puts forward proposals for new requirements for investment firms' crossing processes. Section 6 identifies options and discretions in MiFID which relate to RMs, MTFs and SIs and where a more harmonised approach might be desirable. Finally, Section 7 summarises recommendations and outlines proposed next steps in the development of CESR advice to the European Commission on the review of MiFID provisions relating to equity markets.

6. This consultation paper forms one part of CESR's work on the MiFID Review, which will result in advice to the European Commission on a wide range of issues.

7. CESR invites comments from stakeholders on this consultation paper. Respondents can post their comments directly on the CESR's website (www.cesr.eu) in the section "Consultations". The consultation closes on 31 May 2010.

2. Transparency

8. A key objective of MiFID is 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-European basis. A high degree of transparency is an essential part of this framework, so as to ensure a level playing field between trading venues so that the price discovery mechanism in respect of particular shares is not impaired by the fragmentation of liquidity, and investors are not thereby penalised[1]. Transparency also facilitates the application of the best execution obligations.

9. In developing policy options for transparency, it has been assumed that the existing MiFID framework for competition and best execution obligations remain unchanged.

2.1 Pre-trade transparency

2.1.1 Organised trading platforms (RMs and MTFs)

10. MiFID introduced pre-trade transparency obligations for shares admitted to trading on a regulated market with the aim of providing the wider investing public with access to information on current opportunities to trade on a timely basis. Pre-trade transparency obligations were also devised as a way of mitigating the potential adverse impact of a fragmentation of markets and liquidity, ensuring a level-playing field between trading venues, promoting the efficiency of the overall price formation process on a pan-European basis and assisting an effective operation of best execution obligations[2].

[1] Article 5 of the MiFID Implementing Regulation

[2] The situation prior to MiFID is described by ESME, Fact finding regarding the developments of certain aspects of pre-trade transparency in equities under MiFID, p. 5et seq.

11. MiFID places the same pre-trade transparency obligations on both RMs and MTFs[3]. This regime requires RMs/MTFs to make public, on reasonable commercial terms, details of best bids and offers and the depth of trading interests at these prices.

12. MiFID also allows competent authorities to grant RM/MTF waivers[4] from pre-trade transparency obligations for certain types of orders and systems. There are four waivers from pre-trade transparency obligations, for:
    a. orders that are large in scale;
    b. reference price systems;
    c. systems which formalise negotiated transactions; and
    d. orders held in an order management facility

13. MiFID recognises that there are circumstances where exemptions from pre-trade transparency obligations are necessary. It explains that the waivers have been set out bearing in mind the need to ensure a high level of transparency and to ensure that liquidity on trading venues and elsewhere is not impaired as an unintended consequence of obligations to disclose transactions and thereby to make risk positions public.

14. The CESR fact finding shows that more than 90 per cent of trading on organised public markets in Europe is pre-trade transparent. The data indicates an increase in trading on organised public markets without pre-trade transparency in 2009, compared to 2008 from a quarterly average of 6.4 per cent of total EEA trading on organised public markets in 2008 to a quarterly average of 8.9 per cent in 2009 (see Table 1 below). The fact finding also indicates that the majority of trading without pre-trade transparency on organised markets takes place using the waivers for negotiated trades and for orders that are large in scale.

Table 1: Trading in EEA shares executed under MiFID pre-trade transparency waivers[5]

	2008				2009			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Trading under pre-trade waivers*	282.3	263.4	213.0	182.7	146.9	203.9	206.8	240.6
All Trading in EEA shares on RMs and MTFs*	4234.6	3804.1	3692.5	2912.7	1934.1	2227.8	2289.8	2442.5
Total as a % of all trading in EEA shares on RMs and MTFs	6.7%	6.9%	5.8%	6.3%	7.6%	9.2%	9.0%	9.8%

*Values are in bn Euros
Sources: (1) Value of trading on RMs and MTFs without pre-trade transparency: Member State competent authorities; (2) All trading in EEA shares on RMs and MTFs: Thomson Reuters

2.1.1.1 Waivers from pre-trade transparency

15. Post-MiFID, trading platforms have availed themselves of pre-trade transparency waivers and many have been innovative in developing proposals which they felt responded to user demands and were within the MiFID scope. However, there are some concerns that the regime does not

[3] See Articles 29(1) and 44(1) of MiFID. Pre-trade transparency obligations of systematic internalisers are laid down in Article 27 of MiFID and Articles 22 to 26 of the Commission Regulation (EC) No 1287/2006 of 10 August 2006 implementing Directive 2004/39/EC of the European Parliament and of the Council as regards record keeping obligations for investment firms, transaction reporting, market transparency, admission of financial instruments to trading, and defined terms for purpose of that Directive, OJ L 241, 2.9.2006, p.1 ("MiFID Implementing Regulation").
[4] See Articles 29(2) and 44(2) of MiFID and Articles 18 to 20 of the MiFID Implementing Regulation.
[5] These figures do not include trading under the waiver for order management facilities. This table and the table on the Large in Scale Waivers do not include information from the Estonian and Icelandic FSAs.

operate satisfactorily in a number of areas. There have been some interpretation issues on the scope of the waivers, which have resulted in practical difficulties. This lack of consistency and certainty is seen by trading platforms and their users as endangering the level playing field.

16. CESR has recognised that there are difficulties with the application of the waivers and has agreed to a number of initiatives. In April 2009, it launched a procedure whereby competent authorities submit proposals for the use of the waivers for discussion within CESR (the CESR waiver process). This process aims to achieve supervisory convergence and to ensure a consistent application of the waivers. The results of CESR's assessments of order types and order matching methodologies proposed by operators of RMs/MTFs are published on the CESR website in the document 'Waivers from Pre-Trade Transparency Obligations under the Markets in Financial Instruments Directive (MiFID)'[6].

17. More fundamentally, there has been substantial debate amongst regulators and market participants about the structure of the waivers. In particular, some participants contend that the waivers were designed in 2006 to match the market structure that existed at that time, but are less suited to the competitive and innovative market structure facilitated by the introduction of MiFID[7].

18. Many trading platforms and their users consider that the waivers are too narrow, do not provide for market developments, and are stifling innovation. It has also been suggested that it would be desirable to have a more dynamic transparency regime which responds to innovation and market developments. On the other hand, some other trading platforms and market participants consider that the use of waivers adversely affects the efficiency of the price formation process.

Proposal

19. CESR has considered carefully the most appropriate framework for pre-trade transparency in a post-MiFID environment and concluded that it would be desirable to:

- retain the generic requirement that all trading on organised markets (RMs/MTFs) must be pre-trade transparent;
- continue to allow exceptions to pre-trade transparency in certain circumstances. However, there is a question as to whether some of the waivers should be recast (further details on options for the waivers are set out below); and
- seek to move from a 'principle based' approach to waivers from pre-trade transparency to a 'rule based' approach where a more precise description of the waivers would provide greater clarity for market participants and competent authorities and facilitate continuous supervisory convergence with regard to waivers within CESR/ESMA, taking into account financial innovation.

Question 1: Do you support the generic approach described above?

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[6] Details of pre-trade transparency waivers are set out in Annex I. See also CESR/09-324 available at www.cesr.eu/popup2.php?id=5754.

[7] In its report 'Impact of MiFID on secondary markets functioning' CESR recognised that difficulties exist in interpreting the scope and purpose of the four types of pre-trade transparency waivers provided by MiFID, see paragraph 88 of CESR/09-355: "…there have been some significant interpretation issues, which have resulted in real practical difficulties: Many trading platforms and their users are of the view that the waivers are being interpreted too narrowly, are not keeping pace with market developments and are stifling innovation. There are divergent views within CESR membership on the scope of the waivers. This lack of consistency and certainty is seen by trading platforms and their users as endangering the level playing field. Many trading platforms contend that the gap between the average order size and the large-in-scale thresholds is too wide and that as a result trading participants do not get adequate protection from market impact when submitting transparent orders. This, it is claimed, has the effect of encouraging market participants to execute trades outside regulated markets and MTFs. Furthermore, it has been suggested that because the large-in-scale thresholds are only set once a year, it is particularly problematic in times of volatility like we are currently experiencing.

Question 2: Do you have any other general comments on the MiFID pre-trade transparency regime?

2.1.1.2 Large in scale waiver

Background

20. The large in scale (LIS) waiver is designed to protect large orders from adverse market impact. MiFID recognises that mandatory public exposure for large orders makes the costs of execution higher than if the transaction is not displayed publicly.

21. MiFID sets out order size thresholds (fixed amounts expressed in Euros) above which RMs and MTFs do not have to display orders submitted to their systems. There are 5 thresholds, one for each of the 5 liquidity bands into which shares are placed on the basis of their average daily order book turnover (ADT) over the previous calendar year.

22. In 2008, an average of 3.1% of trading on European RMs and MTFs took place using the LIS waiver. The percentage rose to 4.2% in 2009 (see Table 2 below). However, the whole of this increase, and approximately 75% of all trading using this waiver in 2009, is attributable to trading in one jurisdiction. Elsewhere, the waiver is used relatively little, accounting for only one per cent of overall trading.

Table 2: Trading in EEA shares executed under the large in scale waiver

	2008				**2009**			
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**
Trades under LIS waiver*	115.8	148.1	106.1	86.1	63.5	100.6	90.4	119.6
Total as a % of all trading in EEA shares on RMs and MTFs (Percentage excluding Member State that is the main user of waiver)	2.7% (1.0%)	3.9% (1.5%)	2.9% (0.9%)	3.0% (0.8%)	3.3% (0.7%)	4.5% (1.6%)	3.9% (0.9%)	4.9% (0.8%)

*Values are in bn Euros

Sources: (1) Value of trading on RMs and MTFs without pre-trade transparency: Member State competent authorities; (2) All trading in EEA shares on RMs and MTFs: Thomson Reuters

23. CESR continues to consider that a waiver from pre-trade transparency for orders that are large in scale is justified to allow investors to avoid market impact when executing large trades. However, CESR seeks views on options for the calibration of the thresholds for large in scale orders and clarifications on the scope of this waiver (see also clarifications in Annex I).

Large in scale – thresholds

24. Many trading platforms contend that the gap between the average order size and the LIS thresholds (set in 2006) is too wide and that as a result market participants do not get adequate protection from market impact when submitting orders. MiFID sets the threshold for large orders in the most liquid shares at €500 000, stepping down in stages to €50 000 for large orders in the least liquid shares. By comparison, the average trade size on the London Stock

Exchange was €22 266 in 2006 compared with €11 608 in 2008 and €9 923 in 2009[8]. These trading platforms hold that the thresholds for large orders should take into account changes in average trade size.

25. It is also claimed that the current regime has the effect of encouraging market participants to execute trades away from RMs and MTFs. However, this claim is not clearly evidenced by any corresponding increase in the overall percentage share of OTC trading.

26. The main question is whether the current thresholds under the LIS waiver are appropriate and strike a proper balance between the general benefit of transparency and necessary protection from adverse market impact. CESR recognises that factors other than current order sizes are relevant in assessing whether MiFID existing thresholds provide adequate protection for large orders. For instance, development of algorithmic trading and ability to trade shares on multiple platforms may need to be taken into account, as they may have rendered the execution of large orders more complex without necessarily affecting their market impact. As noted above, the volume of trading that occurs under the waiver has so far been relatively high in one Member State but very low elsewhere.

Options

27. Option 1: No change to the LIS thresholds (see Table 3 below).

Table 3: Option 1: Existing MiFID regime - orders large in scale compared with normal market size

Class in terms of average daily turnover (ADT) in €	**ADT < 500 000**	**500 000 ≤ ADT < 1 000 000**	**1 000 000 ≤ ADT < 25 000 000**	**25 000 000 ≤ ADT < 50 000 000**	**ADT ≥ 50 000 000**
Minimum size of order qualifying as large in scale (LIS) compared with normal market size	50 000	100 000	250 000	400 000	500 000

28. Option 2: Set thresholds so as to provide a moderate reduction in the minimum order size qualifying for the LIS waiver (e.g. reduction of the minimum order sizes for each liquidity band by 25%).

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?

Large in scale – treatment of residual orders ('stubs')

29. The current scope of the large in scale waiver for large orders that do not get fully executed is not clear. The specific situation that arises is where an initial large order satisfies the relevant LIS threshold but, when partially filled/executed, is reduced to a 'stub' that falls below the relevant threshold.

[8] London Stock Exchange website: www.londonstockexchange.com Factsheets and News. (NB: these figures are based on an exchange rate of 1 GBP = 1.15 EUR)

30. Some CESR members have allowed 'stubs' to retain the protection of the LIS waiver. Trading platforms in these jurisdictions are not required to cancel or display partially filled large orders that are below LIS thresholds.

31. While there are divergent views on this issue, CESR recognises the benefit of a consistent approach and for this to be clarified in MiFID. The question is therefore whether a 'stub' should be displayed if its residual size is below the relevant LIS threshold.

32. One possible policy option is to allow residual orders below the relevant LIS thresholds to remain dark. One of the arguments supporting this option is that it would facilitate an efficient order matching process. The other policy option is to require that residual orders below the relevant LIS thresholds be pre-trade transparent. One of the arguments supporting this option is that the rationale for the waiver to limit market impact for orders above a certain size does not necessarily hold for stubs which are smaller than the LIS threshold. Also, allowing residual orders below LIS thresholds to remain undisclosed would create an inconsistency with the transparency requirements for new orders of the same size.

Options

33. Option 1: Amend MiFID to clarify the application of the LIS waiver to stubs. This option would make it clear that partially executed LIS orders (stubs) continue to benefit from the waiver following partial execution.

34. Option 2: Amend MiFID to clarify that the LIS waiver does not apply to stubs. This option would require that LIS thresholds only apply to initial orders and not to residual orders that have been partially executed. Thus, the remaining stubs would have to be disclosed in the order book or cancelled.

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

2.1.1.3 Reference price waiver

Background

35. The reference price waiver is designed for passive price taking systems that match supply and demand without price discovery and at a fixed reference price (e.g. the opening or closing price, or at a reference price recorded at some other point during the day). Reference price systems were operated in some Member States prior to the implementation of MiFID. Post-MiFID the business of trading systems using this methodology has evolved, from satisfying demand for trading primarily in less liquid shares to trading in the most liquid part of the market, and from offering single venue reference price systems to offering trading referenced to consolidated/multiple venue prices (e.g. a reference price related to the European Best Bid and Offer).

36. The CESR fact finding shows that the volume of trading executed in reference price systems is currently lower than trading under the LIS waiver or the negotiated trade waiver. Only four European jurisdictions have granted the waiver, and trading under that waiver accounted for 0.1% of all trading in EEA shares on RMs/MTFs in 2008. Trading using this waiver has increased since 2008, but it remains a small proportion of total trading in EEA shares on organised public markets, accounting for 0.5% on average in 2009, and 0.9% in the 4th quarter (see Table 4 below).

Table 4: Trading in EEA shares executed under the reference price waiver

	2008				2009			
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**
Trading under reference price waiver*	3.1	3.5	3.3	3.8	5.1	7.7	12.9	21.0
Total as a % of all trading in EEA shares on RMs and MTFs	0.1%	0.1%	0.1%	0.1%	0.3%	0.3%	0.6%	0.9%

*Values are in bn Euros

Sources: (1) Value of trading on RMs and MTFs without pre-trade transparency: Member State competent authorities; (2) All trading in EEA shares on RMs and MTFs: Thomson Reuters

37. Post-MiFID, reference price systems have gained in popularity and, in particular, are provided by new entrant MTFs, although not exclusively. For some, it is their only trading model. Broadly, the policy rationale for the reference price waiver remains. However, market developments have moved beyond CESR's observation in its previous technical advice to the EC in April 2005. Non-disclosure by these systems is no longer primarily due to the concern that the publication of orders, especially in the less liquid shares for which the systems were most frequently used, would increase the incentive to manipulate the continuous market before the reference price was fixed.

38. Some concerns have been raised that reference price systems are being used to execute small orders and it has been suggested that this is inconsistent with the general intention of the waivers to provide protection against market impact. On the other hand, some market participants have expressed concerns that the reference price waiver is overly restrictive and provides little scope for market developments and innovation. They consider it would be beneficial to have more flexibility, allowing more scope for execution within the (visible) market spread.

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?

2.1.1.4 Negotiated trade waiver

Background

39. The waiver for negotiated trades provides an exemption from pre-trade transparency for transactions that are not accessible to other members of a RM or MTF other than the one(s) that have pre-negotiated the trade. The rationale for the waiver was - among others - to enable intermediaries to achieve best execution for their clients in cases where it would not be in the interest of the client to enter the order into the order book because a better quality of execution might be achieved outside the order book (e.g. when the order book cannot fill the whole order). The negotiated trade waiver is also needed in cases where it is not possible to trade certain orders through a central trading mechanism e.g. where an order book has a significant minimum order size, permits the trading of only round lots or imposes other standard conditions such as settlement that some types of orders cannot meet. Negotiated trades have traditionally also been used for principal transactions which are subject to conditions other than the current market price such as principal VWAP or portfolio trades.

40. Negotiated trades existed pre-MiFID in many Member States. The waiver is used post-MiFID

particularly by RMs.

41. In 2008, an average of 3.2% of trading on European RMs and MTFs took place using the negotiated trade waiver. There was an increase to an average of 4.2% of total EEA trading on RMs and MTFs in 2009 (see Table 5 below).

Table 5: Trading in EEA shares executed under Negotiated Trade Waiver

	2008				2009			
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**
Trades under negotiated trade waiver*	163.4	111.9	103.6	92.8	78.4	95.6	103.5	100.0
Total as a % of all trading in EEA shares on RMs and MTFs	3.9%	2.9%	2.8%	3.2%	4.1%	4.3%	4.5%	4.1%

*Values are in bn Euros
Sources: (1) Value of trading on RMs and MTFs without pre-trade transparency: Member State competent authorities; (2) All trading in EEA shares on RMs and MTFs: Thomson Reuters

42. Broadly, CESR is of the view that the existing waiver for negotiated trades should be retained. However, CESR recognises that further clarification on the scope of this waiver may be desirable.

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

2.1.1.5 Order management facility waiver

Background

43. This waiver provides an exemption from pre-trade transparency for orders held in an order management facility, 'pending their being disclosed to the market'. The rationale for this waiver is that order management facilities provided by RMs/MTFs help intermediaries and their clients in executing their orders in the most efficient way. CESR's view in the technical advice it provided to the Commission during the formulation of MiFID implementing measures was that the provision of these facilities should be left to the discretion of RMs and MTFs.

44. CESR did not conduct a fact finding exercise to gather data on the use of this waiver. Most (if not all) RMs make use of this waiver for iceberg, stop market and/or stop limit orders. Some MTFs have also introduced similar functionalities.

45. Some trading platforms have raised concerns that the waiver is overly restrictive, does not allow for innovation and prevents them from providing the same order types and functionalities as investment firms. They claim that this is creating an unlevel playing field.

46. One way to address level playing field concerns between investment firms and RMs/MTFs would be by 'levelling up' the disclosure requirements for investment firms. This would require all orders submitted by investment firms to RMs/MTFs to be publicly displayed. Among other things, this would result in investment firms not being allowed to submit market orders or other orders with a zero time in force (e.g. IOC, FOK).

47. Another way to address level playing field concerns between investment firms and RMs/MTFs would be by 'levelling down'. This means that RMs/MTFs would be permitted to offer the same functionality with their order management facilities as investment firms can arrange. This would allow purely dark orders (in price and size) to be managed by RMs/MTFs that would

never appear in the order book or be visible to market participants before execution.

48. This waiver was designed in 2006 to allow for the management of order types that existed at that time. Some CESR members consider that it is too prescriptive and does not provide scope for market operators to respond to competition by offering more efficient and innovative services. Other CESR members do not share the concerns expressed about a potential unlevel playing field between RM/MTF and investment firms as regards order management. They consider that investment firms and trading platforms do not run the same business and should not be expected to be subject to the same rules.

49. CESR considers that there may be some serious practical implications when seeking to address level playing field concerns in the use of this waiver. It may also be difficult to determine whether the benefits from 'levelling up' or 'levelling down' would outweigh any resultant negative impact on liquidity and the price formation process.

50. CESR therefore proposes that the existing waiver for order management facilities be retained, recognising that further clarification on its conditions may be desirable (see Annex I).

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

2.1.2 Systematic internaliser regime

Background

51. MiFID was the first EU directive to introduce the concept of specific regulation for systematic internalisation. Although the basic concept is applicable regardless of asset class, MiFID obligations attaching to SIs relate to the trading of shares. The core of these requirements, which are set out in Article 27 of the directive, is for SIs to publish firm quotes in shares that are classified as 'liquid' under MiFID when dealing in sizes up to standard market size.[9]

52. In the CESR Call for Evidence, questions were raised on the small number of investment firms currently classified as SIs and identified as such in the CESR MiFID database. To date, 10 investment firms have informed their home Member State regulators that they carry out systematic internalisation. CESR has no view on what should be the appropriate number of SIs in Europe. The number of SIs may just not be higher. Another possible reason may be difficulties with the practical application of the SI definition in various Member States. There are also issues regarding the way in which SIs have been fulfilling their quoting obligations.

Key issues:

- Whether or not the SI definition requires clarification.
- Whether or not the SI obligations should be recalibrated to ensure that they are meaningful and add value for market users.

53. MiFID Article 4(1)(7) defines a systematic internaliser as '*an investment firm which, on an organised, frequent and systematic basis, deals on own account by executing client orders outside a regulated market or MTF*'.

54. Article 21(1) of the MiFID Implementing Regulation sets up further criteria indicating under which conditions the activity of a systematic internaliser is to be considered as 'organised, frequent and systematic':

a) the activity has a material commercial role for the firm, and is carried out in accordance with non-discretionary rules and procedures;

[9] Standard market sizes are set out in the MiFID Implementing Regulation, Annex II, Table 3.

b) the activity is carried on by personnel, or by means of an automated technical system, assigned to that purpose, irrespective of whether those personnel or that system are used exclusively for that purpose;
c) the activity is available to clients on a regular or continuous basis.

55. At present, the main problems with the definition rest in Article 21(1)(a) of the MiFID Implementing Regulation. The reference to non-discretionary rules may provide scope for firms to decide that any discretion they exercise in determining whether or not to execute client orders against own account leaves them outside the scope of the definition. However, it should be noted that a firm should always use discretion when deciding whether or not to execute a client order against its own account as the firm has to meet best execution obligations. In addition, the non-discretionary element of a SI is a relevant component of the definition to avoid including ad hoc transactions that would not be systematic.

56. The materiality criteria also offer scope for firms and regulators to adopt different views as to whether a firm falls within or outside the definition. In expanding on Article 21(1)(a), Recital 15 of the Regulation states that: '*An activity should be considered as having a material commercial role for an investment firm if the activity is a significant source of revenue, or a significant source of cost. An assessment of significance for these purposes should, in every case, take into account the extent to which the activity is conducted or organised separately, the monetary value of the activity, and its comparative significance by reference both to the overall business of the firm and to its overall activity in the market for the share concerned in which the firm operates. It should be possible to consider an activity to be a significant source of revenue for a firm even if only one or two of the factors mentioned is relevant in a particular case*.' On this basis, firms have a degree of flexibility in assessing whether activity that could be considered as organised is material either in terms of monetary value of the activity or its significance in terms of the firm's overall activity or role in the market.

57. CESR considers it important that the criteria defining whether or not a firm falls within the SI regime should be as clear as possible.

Question 10: Do you consider the SI definition could be made clearer by:

i) removing the reference to non-discretionary rules and procedures in Article 21(1)(a) of the MiFID Implementing Regulation?

ii) providing quantitative thresholds of significance of the business for the market to determine what constitutes a 'material commercial role' for the firm under Article 21(1)(a) of the MiFID Implementing Regulation.

Please provide reasons to support your views.

Key issues – SI obligations

58. The present regime permits SIs to quote one-sided and in a size of only one share – a practice adopted by some but not all SIs. This means that many SIs are publishing quotes that tell the market little about the size of business they are prepared to take on. This information deficiency is accentuated by the fact that it is not possible for market users to assess the volumes and prices of trades conducted by individual SIs. This results from the MiFID Implementing Regulation exempting SIs from revealing their identity[10] in post-trade reports, provided they publish quarterly trading statistics. CESR is of the view that there is a strong case for making SI information more meaningful.

[10] MiFID requires SIs to publish all completed transactions and to identify themselves as the trading venue (e.g. through a BIC) unless they publish quarterly statistical information about their systematic internalisation business (in which case they can publish trades with the generic identifier of 'SI').

59. Currently, SIs are not allowed to offer price improvement for all orders up to customary retail size (currently set at €7,500) and all retail orders, regardless of size. The rationale for such restriction on price improvement is to provide for equal treatment of retail clients of systematic internalisers and for making quotes displayed meaningful. Whilst the constraints on price improvement were not identified as being problematic in the previous Call for Evidence, CESR is interested in understanding whether this particular aspect of the regime needs to be revisited.

Proposal

60. CESR proposes to amend the SI quoting obligations to make them more reflective of and useful to the type of business being undertaken. In particular, CESR proposes that:

- SIs be required to maintain two-side quotes;
- SIs be required to maintain a minimum quote size equivalent to 10% of the standard market size of any liquid share in which they are a systematic internaliser;
- the provision exempting SIs from identifying themselves in post-trade reports if they publish quarterly trading data be rescinded;

Question 11: Do you agree with the proposal that SIs should be required to maintain quotes in a size that better reflects the size of business they are prepared to undertake?

Question 12: Do you agree with the proposed minimum quote size? If you have a different suggestion, please set out your reasoning.

Question 13: Do you consider that removing the SI price improvement restrictions for orders up to retail size would be beneficial/not beneficial? Please provide reasons for your views.

Question 14: Do you agree with the proposal to require SIs to identify themselves where they publish post-trade information? Should they only identify themselves when dealing in shares for which they are acting as SIs up to standard market size (where they are subject to quoting obligations) or should all trades of SIs be identified?

Question 15: Have you experienced difficulties with the application of 'Standard Market Size' as defined in Table 3 of Annex II of the MiFID Implementing Regulation? If yes, please specify.

Question 16: Do you have any comments on other aspects of the SI regime?

2.2 Post-trade transparency

61. The MiFID post-trade transparency obligations apply to RMs, MTFs and investment firms and are intended to promote the efficiency of the overall price formation process, to assist the operation of the best execution obligation and to mitigate the potential adverse impact of market fragmentation. The information is also used, primarily by buy-side firms, to analyse the cost of transactions and to price portfolios.

62. MiFID broadened the post-trade transparency requirements across Europe most notably by requiring OTC trading to be transparent. However, whilst in some Member States MiFID introduced a higher level of post-trade transparency, in other Member States, as the MiFID deferred publication regime allowed for longer delays than were permissible pre-MiFID, transparency was reduced.

63. In their responses to the Call for Evidence and at CESR roundtables, many market participants expressed concerns about the effect of the fragmentation of post-trade

transparency information, especially in relation to OTC trading. In particular, concerns were expressed over the quality of post-trade information, the timing of publication of post-trade information and various barriers to consolidation of post-trade data.

64. As indicated in the June 2009 Report, CESR recognises the importance of having trade information of sufficient quality and is concerned about the deterioration which has followed MiFID implementation. CESR also recognises the need for timely post-trade transparency information. Proposals to improve the quality of transparency information and to reduce delays in the publication of data are outlined in Sections 2.2.1 and 2.2.2 respectively. Proposals to promote consolidation of transparency information are presented in Section 4 below.

2.2.1 Quality of post-trade information

65. In February 2007, CESR has published Level 3 guidelines and recommendations on publication and consolidation of MiFID market transparency data (Ref.: CESR/07-043) in order to facilitate the understanding of MiFID requirements and guard against a potential adverse impact of fragmentation of transparency information post MiFID.

66. However, many market participants, some of which were subject to an OTC post-trade transparency regime pre-MiFID, have noted that the quality of the transparency data has deteriorated significantly since MiFID was implemented in November 2007. These concerns were particularly pronounced in jurisdictions where all equity transparency information was previously published by the main RM. In those jurisdictions, the main RM not only consolidated equity data but monitored the quality and took appropriate remedial action as necessary.

67. According to market data vendors, investment firms do not always take the necessary steps to ensure that equity trade data is accurate and reliable, leading to a confusing picture of the OTC market. This contrasts with equity data from RMs and MTFs which is generally considered to be of high quality.

68. The importance of having trade information of sufficient quality is recognised and the deterioration which has followed MiFID implementation is considered to be concerning. CESR also recognises that there is not a single solution to improve the quality of data and that the problems raised reflect different issues, ranging from lack of clarity in the publication obligations to potential deficiencies in firms' compliance with their MiFID obligations.

Proposals:

69. To address the concerns relating to the quality of post-trade transparency information, CESR proposes to follow a multi-pronged approach, comprising the following elements:

    a. Amend MiFID to embed standards (list of proposed standards and consultation questions is provided in Annex II) for the publication of post-trade transparency information. These proposed standards are generally aimed at improving clarity, comparability and reliability of post-trade transparency and would cover matters such as condition codes for trade types and process for correcting erroneous post-trade reports.

    b. Amend MiFID to provide greater clarity i) in terms of what constitutes a single transaction for post-trade transparency purposes and ii) in terms of which investment firm shall make information related to OTC transactions public. CESR is also considering developing guidance to provide greater clarity about more complex trading scenarios; and

    c. Establish a joint CESR/Industry Working Group immediately following the publication of this CP to finalise the development of standards and clarification amendments by July 2010.

71. This proposed approach would be effective at addressing concerns over the quality of post-trade transparency information and enhancing the ability of competent authorities to monitor compliance and consider enforcement action as required.

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

2.2.2 Timing of publication of post-trade information

2.2.2.1 Real-time publication of transactions not eligible for delay

72. MiFID requires transactions to be published as close to real time as possible, but no later than 3 minutes after the trading time. Indeed, the 3 minute deadline should only be used in exceptional circumstances where the systems available do not allow for a publication in a shorter period of time. During CESR's Call for Evidence, it has been suggested that the quality of post-trade transparency information is negatively impacted because some investment firms routinely use the full 3 minutes to publish a transaction, rather than publishing a trade in real time and using the full 3 minutes on an exceptional basis.

73. CESR notes that in the US there is a requirement to publish information related to 'on exchange' transactions in real time and to publish information related to OTC transactions (which, in the US includes transactions executed on alternative trading systems (ATS) as close to real time as possible but no later than 90 seconds after the trade. The US Financial Industry Regulatory Authority (FINRA) is proposing to reduce the reporting deadline to 30 seconds from the trading time.

Proposal:

74. CESR proposes to improve the timeliness of post-trade transparency information by:

   i) amending MiFID obligation which requires RMs, MTFs and investment firms trading OTC to publish post-trade trade information in real time as follows: *transactions would need to be published as close to instantaneously as technically possible* , and

   ii) reducing the 3 minute deadline to 1 minute.

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?

2.2.2.2 Deferred publication regime

75. MiFID requires the European Commission to re-examine Table 4 of Annex II of the MiFID Implementing Regulation (deferred publication thresholds and delays). In CESR's Call for Evidence, market participants were asked whether MiFID categorisation of shares was appropriate for the deferred publication regime and whether the post-trade regime was working effectively.

76. Respondents to the Call for Evidence considered that delays were often too long to ensure adequate transparency and that, in some instances, investment firms seemed to avail

themselves of the maximum delay under MiFID even when the risks were already unwound. On the other hand, some respondents felt that the MiFID transparency regime was well calibrated and that there was no need for change. Some respondents also expressed the view that the post-trade transparency regime had not been in place for long enough and that it would be preferable to wait and see how the market evolved before considering amendments to the various parameters. When asked whether the categorisation of shares was appropriate, respondents expressed mixed views. Some respondents felt that the categorisation of shares was appropriate while others considered that it was not the case. In particular, some respondents questioned the appropriateness of the qualifying sizes for trades eligible for deferred publication.

77. CESR recognises that the existing deferred publication framework with four liquidity bands for shares based on their ADT has not been in place for a long time and no suggestion has been put forward for an alternative framework. However, CESR is of the view that there are grounds for re-calibration of the deferred publication thresholds and delays. In particular, whilst CESR recognises that there is potential for adverse market impact if market participants are not given enough time to unwind large trades before making these public, it considers that there is scope to shorten current MiFID delays which, in some cases, may extend to up to 3 days after a transaction has been executed. Such delays appear to be unnecessarily long, particularly considering that prior to the implementation of MiFID, delays for large trades did not extend beyond the end of the trading day in some jurisdictions. Such long delays also stand in sharp contrast with the US approach which requires real-time publication for 'on exchange' trades and publication in no later than 90 seconds for OTC trades.

Proposal

74. CESR proposes to maintain the existing deferred publication framework (Table 4 of Annex II of the MiFID Implementing Regulation) which currently encompasses four liquidity bands but to recalibrate delays and thresholds so as to:

i) shorten the delays so as to ensure that all transactions are published no later than the end of the trading day;

ii) shorten the intra-day delay of 180 minutes to 120 minutes; and

iii) raise all intra-day transaction size thresholds.

Specific suggestions for deferred publication thresholds and delays are outlined in the table below.

Table 7: Proposed deferred publication thresholds and delays

	Class of Shares in terms of average daily turnover (ADT)			
	ADT< EUR 100 000	**EUR 100 000 ≤ADT < EUR 1 000 000**	**EUR 1 000 000 ≤ADT < EUR 50 000 000**	**ADT ≥EUR 50 000 000**
	Minimum qualifying size of transaction for permitted delay			
60 minutes	EUR 15 000	Greater of 10% of ADT and EUR 30 000	Lower of 15% of ADT and EUR 5 000 000	Lower of 15% of ADT and EUR 10 000 000
120 minutes	EUR 30 000	Greater of 20% of ADT and EUR	Lower of 25% of ADT and EUR	Lower of 25% of ADT and EUR

		80 000	10 000 000	20 000 000
Until end of trading day	EUR 50 000	Greater of 30% of ADT and EUR 120 000	Lower of 35% of ADT and EUR 15 000 000	Lower of 35% of ADT and EUR 35 000 000

75. It is expected that, if implemented, these proposed changes would deliver greater post-trade transparency for all shares admitted to trading on EEA RMs. These proposed changes would also reduce the complexity of the deferred publication regime by cutting down the number of potential delays from six to three for certain categories of shares.

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.

3. Application of transparency obligations for equity-like instruments

76. At present, some Member States have applied MiFID transparency obligations to depositary receipts[11] (DRs) whilst others have not. When traded on organised trading platforms, DRs are typically subject to the trading platforms' rules governing transparency and, in many cases, trading platforms have implemented the same transparency obligations which apply to shares admitted to trading. Likewise, exchange traded funds[12] (ETFs), exchange-traded commodities[13] (ETCs) and 'certificates'[14] which are admitted to trading on RMs are typically subject to the same transparency regime as shares[15].

[11] Depositary receipts (DRs) are negotiable certificates that represent ownership of a given number of a company's shares and can be listed and traded independently from the underlying securities. DRs are typically traded in US dollars and issued by a depositary bank. Several forms of DRs can be listed and traded on EU RMs, including Global Depositary Receipts (GDRs) and American Depositary Receipts (ADRs).

[12] Exchange Traded Funds (ETFs) are open-ended funds which are admitted to trading on RMs and enable investors to gain exposure to equity and fixed income. ETFs trade just like shares.

[13] Exchange Traded Commodities (ETCs) are securities which are admitted to trading on RMs and enable investors to gain exposure to commodities and currencies without trading futures or taking physical delivery. ETCs trade just like shares.

[14] 'Certificates' are shares without voting rights attached, which provide a specific dividend that is paid before any dividends are paid to common shareholders, and which take precedence over common stock in the event of liquidation. In some Member States, such instruments are preference shares and are therefore already subject to MiFID transparency obligations,

[15] Some RMs have implemented a publication service for transactions in ETFs and ETCs executed OTC. In a separate initiative, some investment firms have voluntarily began to publish post-trade transparency information when trading ETFs OTC.

77. CESR has considered whether such 'equity-like' instruments should be subject to pan-European mandatory transparency obligations (i.e. pre and post-trade). In considering this question, CESR has decided not to focus on legal interpretation issues, recognising that because of specific legal characteristics, an instrument might fall within the MiFID definition of shares in one jurisdiction but not in another one ('certificates' being a case in point). Rather, CESR considered whether these instruments were, from an economic point of view, equivalent to shares and whether there would be benefits stemming from a harmonised pan-European transparency regime.

78. For instance, whilst the Net Asset Value (NAV) of a given ETF is often calculated at the end of the trading day using the closing price of the underlying securities and, in some cases, intraday NAV (iNAV) is also available, investors will typically not buy and sell ETFs at their NAV or iNAV on the secondary market. This is because the price of an ETF on organised trading platforms or OTC is affected by supply and demand forces. CESR considers that additional transparency might help investors make timely and informed investment decisions when buying/selling ETFs.

Proposal

79. CESR proposes to apply the MiFID transparency regime for the following equity-like financial instruments admitted to trading on a RM:

i) DRs (whether or not the underlying financial instrument is an EEA share);
ii) ETFs (whether or not the underlying is an EEA share or a fixed income instrument);
iii) ETCs; and
iv) Certificates

In practice, this would mean that the MiFID transparency obligations would apply whether the instrument is traded on RM, MTF or OTC[16].

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.

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?

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.

4. Consolidation of transparency information

80. Prior to the implementation of MiFID, in the vast majority of Member States, trading in shares

[16] In the case of DRs this may include distinctions depending upon whether the underlying financial instrument is an EEA share for the purpose of the market transparency calculations.

was concentrated on a RM. Alternatively, where trading was permissible away from a regulated market's system, it was typically reported to a RM (though this was not required in some Member States). These arrangements had the effect of concentrating trade information for each share in one, or a few, places providing market participants with a consolidated view of trading in a particular share. MiFID, on the other hand, has fostered the rise of new trading venues and introduced competition in trade publication services by giving investment firms, when trading as SIs or OTC, choice in where they publish their transparency information. As a result, data can now be available from a number of different sources, depending on where it is published. Fragmentation of transparency information, if not addressed properly, raises concerns because it could undermine the overarching transparency objective in MiFID, and may result in less transparent markets than was the case pre-MiFID. In order to achieve efficient price discovery and facilitate the achievement, and monitoring, of best execution, trade information published through different sources needs to be reliable and brought together in a way that allows for comparison between the prices prevailing on different trading venues.

81. With the implementation of MiFID there was an expectation that market forces would provide market participants with a way of accessing a consolidated set of data and a number of initiatives have been put in place with this aim. Since MiFID implementation many data vendors have been delivering consolidated data. However these services are not of a standard that fully satisfies market participants. Market participants believe that whilst some concerns exist in relation to the fragmentation of pre-trade information, regulators should focus first on barriers to consolidation of post-trade transparency information.

82. CESR is of the view that regulatory intervention (in addition to addressing issues surrounding the quality of transparency information) is necessary in order to facilitate consolidation. CESR agrees that the focus should be on post-trade transparency information as a priority.

4.1 Regulatory framework for consolidation

83. A recurring theme in the analysis of why consolidated data is not being delivered to the market to the standard it needs is the inadequate quality and consistency of the raw data itself, the inconsistencies in the way in which firms report it for publication, and the lack of any formal requirements to publish data through bodies with responsibilities for monitoring the publication processes.

84. CESR and market participants generally agree there is a need for an affordable consolidation of post-trade information but there are different views about how best to achieve it. Below are two possible approaches.

4.1.1. Multiple approved publication arrangements

85. The first option for improving the quality of data consolidation sets out to make the present, commercially–driven consolidation processes work better. It would supplement the introduction of new standards to improve data quality and achieve greater consistency in trade publication practices (as outlined in Section 2.2.1) by requiring investment firms to publish their trade reports through Approved Publication Arrangements (APAs). Under this proposal, competent authorities would approve entities wishing to act as an APA, and APAs would be required to operate data publication arrangements to prescribed standards. More details are set out below, addressing the standards that would be set for APAs and the adequacy of the present provisions for requiring publication arrangements to facilitate consolidation. This section also considers the issue of data costs under this approach.

Requirements for investment firms

86. Investment firms which execute transactions in shares[17] OTC would be required to make public the post-trade transparency information using an Approved Publication Arrangement (APA). An APA could be:

  a. a regulated market;

  b. Multilateral Trading Facility; or

  c. another organisation.

87. Investment firms would be allowed to use any APA in the EEA and may, if they wish, use more than one APA, although they would need to ensure that each transaction is not published more than once by a primary publication arrangement. As is currently the case, investment firms would be responsible for ensuring that post-trade data provided to an APA is reliable and monitored continuously for errors.

Requirements for APAs

88. An APA would need to be approved by its competent authority. Before approving an APA, competent authorities would need to ensure that the applicant meets the following criteria:

  a. It can ensure the security and confidentiality of the data received;

  b. It incorporates mechanisms for identifying errors in information to be made public;

  c. It is capable of publishing the information required under Article 27 of the MiFID implementing regulation[18] within the timeframe required under Article 28 of MiFID.

  d. It incorporates mechanisms for authenticating the source of information to be made public;

  e. It includes appropriate precautionary measures to enable the timely resumption of publication in the case of system failure;

  f. It can facilitate the consolidation of the data with similar data from other sources;

  g. It can make the information available to the public on a non-discriminatory commercial basis at a reasonable cost.

89. Additional guidance would be provided by CESR outlining more precisely how APAs would be expected to meet criteria/conditions set out above. Proposed guidelines are outlined in Annex IV for consultation and cover matters such as access, security, dissemination, identification of incomplete or potentially erroneous information, correction of post-trade data and monitoring.

90. In addition to having to demonstrate that they meet these requirements at the time of approval, APAs would be subject to ongoing monitoring by the competent authority in respect of continuing compliance.

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[17] Including shares admitted to trading on a RM as well as 'equity-like' instruments as per Section 3.

[18] Article 27 of the MiFID Implementing Regulation requires the following information to be made public:
(a) the details specified in points 2, 3, 6, 16, 17, 18, and 21 of Table 1 in Annex I of the MiFID Implementing Regulation;
(b) an indication that the exchange of shares is determined by factors other than the current market valuation of the share, where applicable;
(c) an indication that the trade was a negotiated trade, where applicable;
(d) any amendments to previously disclosed information, where applicable.

91. APAs would be required to provide access to post-trade information submitted by an investment firm upon request by the firm's competent authority. To meet this obligation, APAs would need to maintain post-trade information for 5 years after the APA has disseminated the post-trade transparency information to the public.

92. In addition, APAs would be required to provide ad hoc and periodic information (proposed guidance is provided in Annex IV) to an investment firm's competent authority relating to the quality of data provided by the investment firm.

93. It is also proposed that CESR maintain and publish a list of APAs. APAs would be required to provide CESR a list of investment firms using their facilities to publish trade reports and keep it up to date. This information would be available only for CESR members.

Consolidation of data with similar data from other sources

94. Article 32(b) of the MiFID implementing regulation requires that any arrangement to make information public must facilitate the consolidation of the data with similar data from other sources. Some market participants are of the view that the requirement to facilitate the consolidation of data is too general and is not resulting in effective consolidation of data and have therefore suggested that it should be amended. If this MiFID obligation were amended, then this would apply to RMs and MTFs as well as APAs.

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?

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)?

Cost of market data

95. MiFID currently requires that transparency information be made available to the public on a non-discriminatory basis at reasonable cost. Some European data vendors have recently cut their data prices significantly. However, concerns remain that the cost of real-time market data is restricting the availability of affordable consolidated European post-trade data. Market data providers have estimated that a total fee for a full data set of pre- and post trade data of all EU venues would cost about € 450 per user per month. In comparison, the cost of consolidated post-trade data in the US is US$ 70 (around €50) per user per month. CESR recognises that there are significant differences between the European and US market data regime (e.g. competitive model in Europe compared to a monopoly in the US, a much higher number of trading venues and shares traded in Europe).

96. One possible approach suggested by some market participants to reduce the total cost of consolidated post-trade data in Europe would be to require those selling data to provide pre- and post-trade transparency information separately and not make the purchase of one conditional upon the purchase of the other[19]. In addition, CESR suggests that publication

[19] There are currently different approaches in Europe: some trading venues disseminate pre-trade and post-trade transparency information separately whilst others disseminate the information as one single data stream.

arrangements should provide post-trade transparency information available free of charge after a delay of 15 minutes.

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.

MiFID transparency calculations

97. For the purposes of MiFID transparency calculations for each stock, competent authorities currently use data provided by the primary RM trading each stock (and in some instances, MTFs). Some market participants believe that in order to ensure the continued accuracy of these calculations, each competent authority should use all post-trade transparency data for each stock, including information from RMs, MTFs and OTC reporting arrangements (e.g. APAs under the approach for consolidation proposed above). In order to do this, each RM, MTF and OTC reporting arrangement would be required to provide data to the relevant competent authority for this purpose.

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?

4.1.2 EU mandatory consolidated tape

98. A second option would supplement the introduction of new standards to improve data quality and achieve greater consistency in trade publication practices (as outlined in section 2.2.1) by requiring that all trades be made available to and published on a single consolidated tape This would provide comprehensive consolidation and offer market users a single point of access to post trade information. This approach would be similar to that which has been adopted in the US, but the arrangements for a consolidated tape in the EEA would need to cater for the specific needs and practicalities of the EU marketplace. This option would require a more substantial implementation project than option 1 but would represent a more structured step along the road towards a more integrated pan-European market.

Main characteristics of the EU Mandatory Consolidated Tape

99. In order to facilitate implementation and limit costs to market participants subject to publication requirements, the Mandatory Consolidated Tape (MCT) would build on existing arrangements:

   a. Every RM, MTF and APA would be required to send trade reports to the MCT in the required format.

   b. RMs, MTFs and APAs would be required to send their trade reports to the MCT free of charge. RMs, MTFs and APAs would continue to be able to sell their data to any other interested party.

   c. The MCT could charge a fee to its subscribers for real-time trade reports. The MCT data would become free after 15 minutes (as proposed above in paragraph 96). The MCT would not be permitted to develop value-added products based on the aggregated data.

d. The MCT would be run as a not-for-profit entity. Any profit made beyond covering operating costs and required capital expenditure would be distributed to the RMs, MTFs and APAs that contributed to the MCT based on the number/volume of transactions.

e. The operator of the MCT would be selected by means of a call for tender.

f. The MCT would be regulated and supervised by ESMA

g. The MCT would need to meet certain standards covering but not limited to security, dissemination (i.e. publication of information), operating hours, resources, contact arrangements, transparency of charges, conflicts of interest, outsourcing and monitoring. The MCT would be responsible for the detection of possible multiple publication (same transaction being sent to more than one primary source).

h. The MCT would need to keep the published data available for at least a period of 5 years to assist in the MiFID transparency calculations.

i. The MCT would need to provide access to trade reports submitted by a particular investment firm to the investment firm's competent authority for a period of 5 years after the reporting of the trade. Under this approach, APAs would not need to provide an investment firm's competent authority with trade reports submitted by that investment firm.

j. The MCT would need to make its services available to any person wishing to subscribe to its data.

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.

5. Regulatory boundaries and requirements

5.1 Regulated markets vs. MTFs

Background

100. In response to the CESR Call for Evidence, RMs expressed concerns that they are faced with an unlevel playing field vis-à-vis MTFs. While the MiFID provisions governing RMs and MTFs are to a large extent similar, RMs are concerned that they are subject to more stringent – and costly – regulatory requirements than their MTF competitors. For example, MiFID allows different capital requirements for RMs and investment firms operating MTFs. Rules relating to admission to trading of financial instruments and the verification of issuer disclosure obligations apply only to RMs and, unlike MTFs, RMs wishing to trade an issuer's shares admitted to trading on another regulated market can do so only 18 months after the original admission and may do so only following publication of a summary note of the issuer's prospectus. In some Member States additional requirements on RMs that go beyond MiFID have been implemented. Whether these or other differences create an unlevel playing field was

not specifically mentioned in the responses to CESR.

101. However, a key difference between requirements for RMs and MTFs operated by investment firms, which may be a potential source of unlevel playing field is the concept of "proportionate approach[20]" for organisational requirements that apply to MTFs and the discretion that may be attached to such test of "proportionality" by competent authorities. In this regard, an extension of requirements for RM under Article 39(a) to (c) of MiFID to investment firms or market operators operating an MTF may provide more clarity that RM and MTFs should be subject to the same organisational requirements as regards the operation of their trading platform.

Proposals

102. Member States shall require that an investments firm or a market operator operating an MTF, in addition to the requirements laid down in Article 13:

a. have arrangements to identify clearly and manage the potential adverse consequences for the operation of the MTF or for its participants, of any conflict of interest between the interest of the MTF, its owners or its operator and the sound functioning of the MTF, and in particular where such conflict of interest might prove prejudicial to the accomplishment of any functions delegated to the MTF by the competent authority;

b. be adequately equipped to manage the risks to which it is exposed, to implement appropriate arrangements and systems to identify all significant risks to its operation and to put in place effective measures to mitigate this risks;

c. to have arrangements for the sound management of the technical operations of the system, including the establishment of effective contingency arrangements to cope with risks of systems disruptions.

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.

5.2 Investment firms operating internal crossing systems/processes

Background

103. A number of investment firms in the EU operate systems that match client order flow internally. Generally, these firms receive orders electronically, utilise algorithms to determine how they should best be executed (given a client's objectives) and then pass the business through an internal system that will attempt to find matches. Normally, algorithms slice larger 'parent' orders into smaller 'child' orders before they are sent for matching. Some systems match only client orders, while others (depending on client instructions/ permissions)

[20] Article 13(4) in MiFID says that an investment firm shall take reasonable steps to ensure continuity and regularity in the performance of investment services and activities. To this end the investment firm shall employ appropriate and proportionate systems, resources and procedures.

also provide matching between client orders and 'house' orders.

104. Investment firms operating these systems are subject to client-oriented conduct of business rules, including best execution, rather than the market-oriented rules designed for RMs and MTFs. They are required to provide post-trade transparency for OTC transactions in shares admitted to trading on a RM. Investment firms are also required to have arrangements in place for identifying conflicts of interest and to notify competent authorities when they suspect a transaction might constitute insider dealing or market manipulation.

105. There has been considerable debate over the past year about the nature and scale of business executed by broker dealers in their internal crossing systems/processes and the way it is regulated. It has been suggested that use of these systems is significant and that they have been increasing their share of trading, in part because the systems are not subject to the same levels of transparency as are required of RM and MTF systems.

106. To establish a factual context for considering these issues, CESR conducted a fact finding towards the end of 2009[21]. In total, 11 investment firms from four different jurisdictions provided data, though the data from several firms whose systems became operational during the period covers only the latter parts of the period

107. The data supplied indicates that the proportion of total EEA trading executed by large investment firms in these systems is very low, ranging from an average of 0.7% in 2008 to an average of 1.15% in 2009 (increasing to 1.4% in the last two quarters of 2009) (see Table 7 below).

Table 7: Trading executed in brokers' crossing processes/networks[22]

	2008				2009			
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	Q4
Value (in bn euros)	37.7	39.7	43.4	39.9	28.0	36.9	47.7	55.7
Crossing as a % of OTC Trading	1.5	1.2	2.0	3.0	2.4	2.1	4.4	4.0
Crossing as a % or total EEA trading	0.6	0.6	0.7	0.9	0.9	0.9	1.4	1.4

Sources: (1) Value of trading executed on brokers' crossing systems/processes: information collected from 11 European investment firms and aggregated by competent authorities; (2) Total value of OTC trading in EEA shares: Thomson Reuters; (3) Total trading in EEA shares: Thomson Reuters

108. A similar debate on dark trading has occurred in the US. In the US, dark pools are alternative trading systems (ATS) operated by broker dealers that do not provide their best-priced orders for inclusion in the public consolidated quotation data. Broadly, an ATS is required to file a notification with the SEC, provide quarterly reports and maintain records (including of transactions). There are approximately 32 dark pools in the US. They executed approximately 7.9% of trading volume in National Market System (NMS) stocks in the third quarter of 2009[23].

109. While it is important to note the differences between the regulatory regimes in the US and the

[21] For purposes of the fact finding, broker operated crossing systems/processes were defined as internal electronic matching systems operated by an investment firm that execute client orders against other client orders or house account orders. Information related to internal electronic systems used exclusively for systematic internalisation was excluded and only trades executed in crossing systems/processes where post-trade transparency information is published are included (i.e. internal transactions where a house account order matches against another house account order are excluded).

[22] It should be noted that the value of OTC trading published by Thomson Reuters and used here, and as a consequence the value of EEA trading published by Thomson Reuters, may be inflated due to multiple reporting of a single transaction.

[23] SEC Concept Release on Equity Market Structure (34-61358), 14 January 2010, SEC website: http://www.sec.gov/rules/concept/2010/34-61358.pdf

EU, the SEC's proposals on dark pools are relevant to CESR's consideration of broker crossing systems. In November 2009, the SEC put forward three specific proposals to address concerns related to dark pools[24]:

- The first proposal would require actionable Indications of Interest (IOIs) — which are similar to a typical buy or sell quote — to be treated like other quotes and to be subject to the same disclosure rules.
- The second proposal would lower the trading volume threshold above which any ATS disseminating a quote to more than one person must display its best-priced orders publicly (i.e. be more pre-trade transparent). Currently, if an ATS displays orders to more than one person, it must display its best-priced orders to the public when its trading volume for a stock is 5 percent or more. The proposal would lower that percentage to 0.25 percent for relevant ATSs (prospectively including dark pools that use actionable IOIs but not dark pools that remain wholly dark).
- The third proposal would create the same level of post-trade transparency for dark pools - and other ATSs - as for registered exchanges. Specifically, the proposal would amend existing rules to require real-time disclosure of the identity of the dark pool that executed the trade.

110. The SEC requested comments on these proposed rules by 22 February 2010.

111. Broker dealers consider that internal matching of client orders, whether manual or automated, is core to traditional brokerage activity. They view it as being only one of a range of means that they use to execute client business and as providing execution efficiency.

112. Some CESR members consider that the current legal framework does not support a requirement for investment firms to register their internal crossing networks as MTFs. In particular, these systems do not have participants in the way that a standalone MTF does. In some jurisdictions, some investment firms operating internal crossing systems have decided to operate an MTF but are having to modify their business models significantly to bring the new activity within the MTF definition.

Proposals:

113. CESR proposes to introduce bespoke requirements for investment firms operating crossing systems/processes (as defined in footnote 21). These would include:

- A requirement for investment firms operating such systems to notify their competent authority and provide a description of the system, including (at least) details on access to the system, the orders that may be matched in the system, the trading methodology, the arrangements for post-trade processing and trade publication;
- A requirement for competent authorities to place on the CESR website the name of any firm that has notified it that it operates a broker internal crossing system with the respective BIC code to identify the crossing system;
- A requirement for investment firms to add the identifier for its crossing system to their post-trade information for all transactions executed on such systems;
- In addition, investment firms that operate a broker internal crossing system would be

[24] SEC website: http://www.sec.gov/news/press/2009/2009-223.htm

brought within the scope of the MiFID Article 41(2). This would require a competent authority demanding the suspension or removal of a financial instrument from trading on a RM or MTF to make a similar demand to broker internal crossing system;

– CESR is also considering the adequacy of existing arrangements for monitoring obligations in the context of firms' requirements to report transactions that may constitute market abuse.

114. Impose a limit on the amount of client business that can be executed by investment firms' crossing processes/networks before the crossing system is required to become an MTF. This implies that, for instance, obligations such as pre-trade transparency and fair access would be applicable once internal crossing processes reached a certain percentage of the market (i.e. similar to the proposed US approach), either on its own or in combination with other crossing systems/processes with which they have a private link.

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?

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)?

a) 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.

b) 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.

6. MiFID options and discretions

115. CESR has done an internal mapping exercise of discretions within MiFID in order to identify areas where a more harmonised approach might be desirable. A reduction of options and discretions in the EU regulatory framework may remove key differences in national legislation and could generally contribute to the realisation of a single European rulebook which has been endorsed at a political level by the ECOFIN Council. Regarding some options and discretions which are related to the work on the MiFID Review on equity markets, CESR therefore wishes to take the opportunity to ask for the view of market participants on eliminating certain options or turn certain discretions into rules. A few other options and discretions granted to

competent authorities in the MiFID provisions might rather be addressed by further harmonisation of supervisory practices within the regular CESR Level 3 work if considered appropriate after internal discussion among CESR members[25].

a) Waiver of pre-trade transparency obligations

116. Articles 29(2) and 44(2) of MiFID and Articles 18 to 20 of the MiFID Implementing Regulation foresee discretion for Competent Authorities to waive the obligation for RMs and MTFs to provide for pre-trade transparency under Article 29(1) and 44(1) of MiFID based on market models or the type and size of orders.

117. Some of the waivers such as the order management facility waiver for Iceberg and stop orders in Article 18(2) of the MiFID Implementing Regulation are used in a wide variety of Members States while others, e.g. the reference price waiver, are used in a more limited number of countries. This does not necessarily point at a divergent application of the waiver but rather results from the fact that the business models of RMs and MTFs in the Member States vary. Furthermore, the practice of granting waivers varies in Member States. While in most jurisdictions, the waiver provisions in MiFID have been implemented in a way that requires approval of individual arrangements, either by individual decision or by approval of (amendments to) the rules of a RM or MTF, in other Member States there is no such requirement.

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

b) Determination of liquid shares

118. Article 22(1) of the MiFID Implementing Regulation specifies the conditions for determining liquid shares for the purposes of the SI-regime in Article 27. In particular, it sets the conditions which must be met before a share admitted to trading on a regulated market can be considered to have a liquid market. In order to be liquid, a share must be traded daily and have a free float of not less than EUR 500 million, and one of the following conditions must be satisfied:
    a. the average daily number of transactions must not be less than 500; or
    b. the average daily turnover for the share must not be less than EUR 2 million.

119. In respect of shares for which they are the most relevant market, Member States are permitted to specify by public notice *that both conditions are to apply*. Up to date, only a limited number of Member States have exercised this discretion.

120. Generally, the use of discretion by some Member States but not by others may lead to deviations in the determination of a liquid share and may thus influence the scope of application of the SI-regime under Article 27 of MiFID. CESR is therefore considering whether a deletion of this discretion is desirable. If it is considered desirable, the question arises as to what the future harmonised criteria for the definition of a liquid share should be: both criteria (a) and (b) or only one of the two criteria.

Questions 47: Which reasons may necessitate the application of both criteria?

Questions 48: Is a unique definition of liquid share for the purposes of Article 27 necessary?

[25] This covers the following discretions of competent authorities: to waive the obligation to make public limit orders that are large in scale compared with normal market size in Article 22(2), to authorise RMs and MTFs to defer publication of details of transactions based on their type or size in Articles 30(2) and 45(2) of MiFID and Article 28 of the MiFID Implementing Regulation,

Questions 49: If CESR were to propose a unique definition of 'liquid share' which of the options do you prefer?

- **a) apply condition a) and b) of the existing Article 22(1), or**
- **b) apply only condition a), or**
- **c) apply only condition b) of Article 22(1)?**

Please elaborate.

c) Immediate publication of a client limit order

121. The order handling rules under Article 22(2) of MiFID prescribe that investment firms have to take measures to facilitate the earliest possible execution of a client limit order in respect of shares admitted to trading on a regulated market, when the order is not immediately executed under prevailing market conditions. The firm is required to make public immediately that client limit order in a manner which is easily accessible to other market participants, unless the client expressly instructs otherwise.

122. MiFID creates discretion for Member States to decide that investment firms comply with this obligation by transmitting the client limit order to a regulated market and/or an MTF.

123. The vast majority of CESR members apply this discretion. In practice, clients also often expressly instruct their investment firms not to disclose the limit order immediately to the public as foreseen in MiFID. CESR is therefore considering to propose to the Commission within the MiFID Review to replace the discretion with a rule under Article 22(2) which allows investment firms across Europe to comply with the obligation to make the client limit order immediately public in an easily accessible manner to other market participants if the order is not executed immediately under prevailing market conditions, by transmitting the client limit order to a RM and/or MTF.

Questions 50: Is this discretion (for Member States to decide that investment firms comply with this obligation by transmitting the client limit order to a regulated market and/or an MTF) of any practical relevance? Do you experience difficulties with cross-border business due to a divergent use of this discretion in various Member States?

Question 51: Should the discretion granted to Member States in Article 22(2) to establish that the obligation to facilitate the earliest possible execution of an unexecuted limit order could be fulfilled by a transmission of the order to a RM and/or MTF be replaced with a rule?

d) Requirements for admission of units in a collective investment undertaking to trading on a RM

124. Article 36(2) of the MiFID Implementing Regulation grants discretion to Member States to provide that it is not a necessary precondition of the admission of units in collective investment undertakings to trading on a RM that the RM satisfy itself that the collective investment undertaking complies or has complied with registration, notification or other procedures which are a necessary preconditions for the marketing of collective investment undertakings in the jurisdiction of the RM.

125. CESR is considering whether this option should be retained since only few Member States have made use of this discretion to date. In particular, CESR members from those Member States consider that the admission of units in collective investment undertakings to trading on a RM in a Member State and the marketing of a collective investment undertaking in that Member State are two separate and distinct activities. They also believe that marketing of units of collective investment undertakings to domestic investors is adequately controlled by other investment fund and intermediary legislation, and that there is no evidence that operation of the discretion has raised any concerns. A deletion would entail that compliance

with local provisions for the marketing of units in a collective investment undertaking would be assessed by the RM before units can be admitted to trading on that RM.

Question 52: Should the option granted to Member States in Article 36(2) of the MiFID Implementing Regulation be deleted or retained? Please provide reasoning for your view.

7. Conclusions and next steps

126. The publication of this Consultation Paper marks the culmination of nearly 18 months of work by CESR, including a Call for Evidence, fact findings, roundtables with market participants, presentations by stakeholders and the publication of a report on the impact of MiFID on the functioning of equity secondary markets. The key conclusion reached by CESR is that there is no need for radical changes to the MiFID framework but that important changes are required to address areas in MiFID which are not working effectively.

127. In particular, CESR proposes changes which will significantly enhance transparency in equity markets. For instance, there are a number of proposals aimed at improving the quality of post-trade transparency information and reducing delays before the publication of transparency information. CESR proposes to establish a joint CESR/Industry Working Group immediately following the publication of this Consultation Paper to finalise the development of standards for post-trade transparency information and to further clarify proposed amendments to improve the quality of OTC post-trade transparency information by July 2010. CESR also proposes to enhance the scope of transparency by applying the MiFID transparency obligations to instruments such as depositary receipts, exchange-traded funds, exchange-traded commodities and certificates. Finally, in addition to addressing a number of policy questions surrounding the MiFID pre-trade transparency waivers and the regime which applies to systematic internalisers, CESR intends to recommend to the European Commission a number of clarifications on some elements of the waivers.

128. CESR recognises that significant barriers to consolidation remain and that without further regulatory intervention, market forces alone are unlikely to deliver an adequate and affordable pan-European consolidation of transparency information. Two possible approaches for the consolidation of post-trade transparency information are proposed for consultation. These approaches also encompass proposals to address some of the concerns raised relating to the cost of market data.

129. The proposals put forward in this Consultation Paper also seek to address certain inconsistencies which may have impacted the level playing field. For example, it is proposed to align the requirements which apply to RMs and MTFs, and introduce bespoke obligations for investment firms operating crossing systems/processes. The Consultation Paper also consults on the possibility of requiring investment firms operating crossing systems/processes to set up MTFs for their crossing systems/processes once they have reached a certain size.

130. In developing these proposals, CESR has been mindful of relevant changes in market structure. CESR will continue work on micro-structural issues (including algorithmic and high frequency trading) in parallel to this review. A Call for Evidence has been published in this respect on 1 April 2010 for a one month call for comments. Where appropriate, the outcome of this work will be incorporated in CESR's final advice to the Commission.

131. Interested parties are asked to respond to these proposals until 31 May 2010. Following the responses to this CP, CESR will issue a feedback statement in parallel to providing its final advice to the European Commission on the MiFID review.

<u>ANNEX I</u> – MIFID PRE-TRADE TRANSPARENCY WAIVERS-- PROPOSED CLARIFICATIONS

1. In addition to addressing the policy questions raised in Section 2.1.1 of this Consultation Paper, CESR intends to recommend clarification, along the lines set out below, of how, in its view, some elements of the pre-trade transparency waivers should be interpreted and applied. These recommendations will be given to the Commission, possibly with concrete suggestions for wording amendments, for consideration for incorporation in the MiFID review. In the interim, CESR may clarify all or some of these interpretational questions (even before the finalisation of the MiFID Review) in the waiver document published on the CESR website[26].

<u>Large in scale waiver</u>

2. CESR is of the opinion that in case of an (integrated) order-book providing interaction between dark and lit (visible) orders, lit orders must be given execution priority over dark orders with the same limit.

3. To prevent circumvention of the large in scale threshold, CESR will also clarify that modifications of the size or price of a dark LIS order before (partial) execution are expected to be considered by the trading platform as a cancellation of the previous order and the entering of a new one. Thus, the modified order will get a new time stamp. In the context of the LIS waiver, this is particularly important for a reduction of the order size below the large in scale threshold because in this case the modified order has to become transparent or be cancelled.

<u>Reference price waivers</u>

4. Discussions among CESR members and with market participants have demonstrated that the following additional clarifications seem to be necessary in the framework of the MiFID review, irrespective of potential amendments to the scope (discussed in Section 2.1.1.3).

'another system'

5. CESR is of the view that the wording "by <u>another</u> system" includes reference price systems that take a reference price from a system operated by the same RM or MTF. Otherwise, a regulated market which wants to operate an MTF where prices are derived from its own RM (e.g. mid point of the RM's open order book) would be commercially disadvantaged vis-à-vis operators of MTFs which have not established their own price formation system. The intention to treat all RMs and MTFs in an equal and non-discriminatory manner also underlines this reasoning. It therefore needs to be clarified that a reference price system has to be separate from the order book from which it derives prices and will therefore constitute "another system" even if both are operated by the same market operator or investment firm. This interpretation is also supported by Recital 6 of MiFID which clarifies that a 'system' could also be composed of a set of rules.

'widely published'

6. CESR also considers that the concepts of 'widely published' and 'reliable reference price' require greater clarification.

7. It could be argued that 'wide publication' requires accessibility free of charge. Since Article 44 of MiFID requires pre-trade information to be "made available to the public" but does not require the data to be made public free of charge, the interpretation of 'wide publication' of the reference price should however not be stricter, particularly if a reference price could also be

[26] See CESR/09-324 available at www.cesr.eu/popup2.php?id=5754.

derived from the current spread of an open order book.

8. A related question is how many market participants must have access to the reference price to consider it as "widely published". It may be argued that the reference price is only relevant for the trading participants of the reference price system and therefore only all trading participants in the reference price system must have access to the reference price. The question is particularly relevant for reference prices which are derived from more than one platform such as a customised EBBO. Since part of the rational of the waiver is that the price is already known to market participants up-front, it generally has to be possible for every market participant to have access to the reference price. It is therefore not sufficient to provide the reference price only to trading participants.

9. Furthermore, it needs to be clarified whether the reference price itself needs to be published or alternatively/additionally its components. Again, this issue arises when considering a reference to prices of multiple platforms. It is argued that in this case it is sufficient if the trading methodology and the components of a reference price (e.g. the best bids and offers of all markets included in a customised EBBO) are widely published because the EBBO can then be replicated. However, the fact that all components are published does not seem to deliver the same result as a publication of the EBBO since 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. An alternative wide publication of the components of the reference price therefore does not seem to be sufficient if the reference price is calculated across multiple trading venues[27]. Furthermore, CESR considers it necessary to clarify that in addition to the reference price also the components of a multi-platform reference price have to be widely published.

'reliable reference price'

10. The criterion that the reference price has to be reliable has previously been discussed by CESR members in the waiver process. The view was expressed that 'the EBBO' may not yet be widely known and therefore not (yet) generally regarded by market participants as 'reliable reference price', even if it is generated by a large data vendor. On the other hand, there seems to be no doubt that a reference price formed on a regulated market and the price information provided by primary regulated markets is generally accepted by market participants as a reliable reference price. This discussion has demonstrated the difficulty to assess whether market participants regard the reference price as reliable when granting the waiver.

11. Taking into account market developments and practical difficulties with the current requirement that market participants have to consider the reference price as sufficiently reliable, CESR is of the opinion that a sufficiently reliable reference price in the future design of the reference price waiver under MiFID should rather refer to a quality standard. The reference price should be trustworthy and the markets referred to should be sufficiently liquid. The methodology used for generating the reference price should be pre-defined and publicly available. The reference price system should be required to have a price validation mechanism to ensure the quality of the reference price on an ongoing basis. The judgement of the reliability should be made by the platform when using a certain reference price and ultimately the competent regulator

Order management facility waiver

12. The wording of the order management facility waiver sets only two quite generic criteria:

[27] In case of a reference to a VWAP which has to be calculated when the relevant time period of the VWAP has ended, a different view can however be taken regarding the necessity of a wide publication of the VWAP itself if it is calculated with reference to trades executed on RMs or MTFs which are obliged by transparency requirements.

- orders held in an order management facility maintained by the Regulated Market or the MTF
- pending the disclosure of these orders to the market.

13. When interpreting this waiver, it is necessary to also look at the historical intention of the legislator and the respective CESR advice, the taxonomy of all waivers and the purpose of the waiver.

    Clearly Iceberg orders and stop orders were originally intended to profit from this waiver. However, in practice some competent authorities have not felt that it is necessary to formally grant a waiver for stop (limit/market) orders because they are treated like a normal limit or market order once disclosed to the order book with exactly the same pre-trade transparency and there is nothing to manage once the order has been released to the order book. There is also no interaction of orders introduced in the open order book with the stop order resting in the order management facility. In any case, both interpretations do not come to different results: it is clear that a stop order does not have to be made pre-trade transparent before its introduction in the order book.

14. From the functioning of Iceberg orders and stop orders which were originally intended to be covered, also the following other general criteria for order management facility waivers could be derived:

a) Order has to rest in the order management system

15. When discussing various order types eligible for this waiver, a clear distinction between an order management system and an order book is required.

16. Resting in the order management system is not conceivable for FOK and IOC because they are never disclosed on the order book and are immediately cancelled if execution is not possible. Thus, this waiver does not apply to those order types.

17. However, it is not always clear where the line between an order management system and an order book has to be drawn. For example, in some methodologies for Iceberg orders, an incoming aggressive FOK can also ‘look’ at, and take account of, the order volume of the hidden Iceberg in order to determine whether it should be executed or rejected. However, if new peaks of an iceberg order do not get a new time stamp, the distinction between the order management system and the order book is blurred and the ‘borderline’ is crossed.

b) Trigger for release is always ‘execution’

18. The discussion of the traditional Iceberg orders and stop orders have shown that a ‘trigger’ of the disclosure from the order management facility always seems to be necessary. The next peak of an Iceberg order is triggered by the execution of the previous peak, a stop order by a previous execution above/below a certain price. However, it always has to be a ‘previous execution’ in the open order book. Since discretionary orders can also be triggered by an incoming order, they would not fulfil this criterion.

c) Disclosure

19. MiFID does not elaborate on the concept of ‘pending disclosure’. It therefore has to be interpreted what ‘pending disclosure’ encompasses. One interpretation would be that the orders must be displayed (i.e. ‘rest’) on the public order book when they are released. However, is an order that leaves the order management system and subsequently matches an opposite order in an instant (the proverbial ‘nano second’) considered to be ‘disclosed’? This is illustrated by a stop market order which – as soon as it is triggered – leaves the order management system and matches with an opposite order. To better describe today’s reality it

should be clarified that the order must at least be generally capable of being displayed in the order book. To recognise that most orders are immediately executed when they are released from the order management system, the requirement could also be described as 'pending release from the order management system' or 'pending execution'.

20. Apart from the general clarifications above, the following common features of Iceberg orders can be clarified as essential.

Essential features for iceberg orders:
- specified limit of the order
- visible limit of the peak
- specified overall volume
- specified peak size
- specification of peak size and overall volume when entering iceberg order
- time stamp for new peak

21. A fact finding by CESR has demonstrated that there are different additional specifications in existing iceberg orders. As regards the features that the limit of the peak has to be visible, CESR has already clarified in the waiver document (CESR/09-324) that it is also essential that there is no other hidden 'discretionary limit'. The 'disclosed' limit therefore has to correspond to the hidden limit of the limit order held in the order management facility.

22. Regarding the feature 'specified overall volume' a majority of systems for iceberg orders demand the specification of a minimum overall volume of the Iceberg order. One system also specifies a maximum overall volume. The amount of a minimum overall volume varies. Some operators apply different minimum volumes to different segments of the market (e.g. larger minimum thresholds for large caps or shares traded with a higher volume or average size). This additional specification may have historical reasons because the Iceberg order was meant to provide a facility to help intermediaries to execute orders in the most efficient way. This help is only necessary if the orders are too large to get immediate execution in the market and must be 'worked' in a longer period of time. It could therefore be argued that Iceberg orders are only eligible for quite large orders and it is essential to specify a certain minimum volume of an Iceberg order depending on the market segment of the specific share. On the other hand, it may also be argued that the market environment has changed and that it is up to the market participant for which volume he wants to have the Iceberg order functionality if there are no limits stipulated by the RM or MTF. In order to provide flexibility and not being overly prescriptive, CESR agrees that the specification of an overall volume should be left to RMs and MTFs if they regard it as necessary. In any case, market participants have to specify the volume of the Iceberg order when entering it into the order management system.

23. Regarding the feature 'minimum peak size' CESR members take the common view that a zero tip Iceberg effectively results in a hidden order. If this were allowed, a hidden order would be possible without the large in trade threshold for the large in scale waiver. However, concerns have also been raised that a minimum peak size of 1 is not in line with the original intention of an Iceberg order since it should help brokers to execute rather bigger orders. On the other hand, this may not be a commercially sensible peak size specification by market participants anyway so that the peaks will always be bigger in practice and therefore no regulatory concern arises. Thus, CESR does not see a need for clarification or regulatory intervention in this regard.

24. As regards the feature 'time stamp', CESR has already clarified that it does not consider an Iceberg order as MiFID compliant if all consecutive peaks receive the original time stamp of the moment when the Iceberg order was originally introduced. In principle, all new peaks introduced in the order book should be treated like new orders and get the time stamp of their

introduction in the order book. This should be clarified in MiFID[28].

[28] An exception may be possible in a specific situation where all visible orders and peaks of iceberg orders have been executed against an incoming aggressive order and only tranches of remaining Iceberg orders are left in the order management facility. In this situation, a platform may provide priority to all the tranches of an iceberg order with time priority over another iceberg order. This kind of a system has been subjectto the CESR waiver procedure.

ANNEX II – PROPOSED STANDARDS FOR POST-TRADE TRANSPARENCY

Reference data

1. Under MiFID[29], post-trade reports must –among others - identify the instrument (share), the price notation and the venue where the transaction took place. In addition, MiFID requires i) an instrument to be identified using a unique code; ii) the price notation to identify the currency in which the price is expressed; and iii) the unique harmonised identification code of a venue to be used. MiFID specifies the exact format for identifying a transaction executed outside the rules of a RM or MTF (i.e. the code 'OTC') but does not specify the unique code to identify an instrument, how to identify the currency or the unique code to be used to identify a venue. Although CESR has published Level 3 recommendations in February 2007 to promote the use of consistent formats, contents and protocols across the EEA, different identifications for instruments, price notations and venues are used in the marketplace.

2. To bring consolidation forward CESR proposes to require the use of International Standards Organisation (ISO) standard formats for post-trade transparency information (see Table 9 below). CESR recommends ISO standards because ISO is the international standard body and ISO standards are widely used within the EEA. Furthermore, these standards are used by competent authorities when sharing transaction report information with one another under Article 25 of MiFID.

Table 9 - Standards for reference data[30]

Transparency publication field	Standard
Instrument identification	ISO 6166 International Securities Identification Number (ISIN)
Price notation	ISO 4217 currency code
Venue identification	Where the venue is a regulated market or multilateral trading facility the ISO 10383 Market Identifier Code (MIC) Where the venue is a systematic internaliser or broker operated crossing network/process the ISO 9362 Bank Identifier Code (BIC);

3. The intention is to ensure that the financial instrument, price notation and venue are identified in a consistent way.

4. MiFID[31] requires the price notation to contain 'the currency in which the price is expressed'. The CESR Level 3 guidelines and recommendations on publication and consolidation of MiFID market transparency data (CESR/07-043) recommend using the ISO 4217 currency code to identify the price notation and using integer in cent units to identify the unit price (i.e. EUR 2.00 would be identified as 200 Euro cents).

5. However, the ISO 4217 currency codes identify the major (e.g. the ISO 4217 currency code EUR relates to Euro) rather than the minor currency (e.g. Euro cents). Furthermore, competent authorities have agreed to use the major currency to identify the unit price when sharing transaction reporting information with one another under Article 25 of MiFID.

[29] Article 27(1)(a) of the MiFID Implementing Regulation.
[30] This reiterates Recommendation °2 of CESR's Level 3 guidelines and recommendations on publication and consolidation of market transparency (Ref.: CESR/07-043).
[31] Annex I, Table 1 of the MiFID Implementing Regulation.

6. CESR believes the discrepancy between the Level 3 recommendations for price notation and unit price may have contributed towards an inconsistent approach with some market participants publishing information related to a transaction in the minor currency whilst others publish information in the major currency. Where a unit price is submitted in the minor currency, e.g. Euro cents, it may appear to be 100 times greater than a unit price submitted in the major currency, e.g. Euros.

7. CESR is of the view that this inconsistent approach is a barrier to consolidation and to promote consolidation it would be preferable for information to be published in a harmonised format. As the ISO 4217 currency codes identify the major currency CESR believes it may be preferable if the unit price were provided in the major currency.

Question 1: Do you agree to use ISO standard formats to identify the instrument, price notation and venue? If not, please specify reasons.

Question 2: Do you agree that the unit price should be provided in the major currency (e.g. Euros) rather than the minor currency (e.g. Euro cents)? If not, please specify reasons.

Exchange of shares determined by factors other than the current market valuation of the share and non addressable liquidity

8. MiFID[32] requires RMs, MTFs and investment firms to publish additional information in relation to some transactions. This includes an indication that the exchange of shares is determined by factors other than the current market valuation of the share. In addition, MiFID[33] requires a transaction related to an individual share in a portfolio trade and a volume weighted average price (VWAP) transaction to be considered as transactions where the exchange of shares is determined by factors other than the current market valuation of the share. However, there is no requirement to identify such transactions in a standard way and, as a result, there is no consistency in the way any publication arrangement identifies such transactions. This has been identified as adversely impacting the quality of post-trade information.

9. Also, market participants have suggested other types of transactions (e.g. ex/cum dividend/bonus/rights/coupon transactions) which should be identified as transactions where the exchange of shares is determined by factors other than the current market valuation of the share.

10. Finally, some market participants have suggested that a transaction where another investment firm could not have been a party to the transaction should be identified. Such transactions are referred to below as 'non addressable liquidity'. For example, where a firm providing the service of portfolio management transfers the beneficial ownership of a share from one fund to another and acts on behalf of both the buying and selling funds and where no other investment firm is involved (referred to below as interfund transfers). Many market participants believe this proposal would enable them to distinguish non addressable liquidity transactions for the purpose of transaction cost analysis and to assist the operation of the best execution obligation. Other types of non addressable liquidity would include 'give up/give in' transactions[34] and OTC hedges of a derivative (although in some cases such a transaction may not be addressable).

11. CESR generally considers that such 'non addressable liquidity' transactions should be identified. However, CESR also recognised that this kind of granularity is currently not

[32] Article 27(1)(b) of the Implementing Regulation.
[33] Article 3 of the MiFID Implementing Regulation.
[34] A 'give-up/give-in' transaction occurs where an investment firm transfers a hedge position acquired on a client's instruction to another investment firm who is selling that client a derivative contract.

available to regulators. If considered beneficial to the overall market efficiency, CESR intends to promote consolidation by proposing that each type of transaction be identified in a harmonised way across regulated markets, multilateral trading facilities and OTC publication arrangements, where applicable, in line with the table below:

Table 10 - Transaction type standards[35]

Type of transaction	Standard identifier	Publication arrangement on which standard would need to be applied
VWAP	V	RM, MTF, OTC
Portfolio transaction[36]	P	RM, MTF, OTC
Ex/cum dividend + other	D	RM, MTF, OTC
Give up / give in	G	OTC
OTC hedge of a derivative	O	OTC
Interfund transfers	I	OTC

Question 3: Do you agree that each of the above types of transactions would need to be identified in a harmonised way in line with table 10? If not, please specify reasons.

Question 4: Are there other types of non addressable liquidity that should be identified? If so, please provide a description and specify reasons for each type of transaction.

Identification of dark trading

12. Some market participants consider it to be necessary for the post-trade transparency information related to a transaction to indicate whether the transaction was subject to pre-trade transparency. CESR proposes that a transaction that is not pre-trade transparent would need to be identified.

13. CESR proposes two options for meeting this obligation. Either the information would need to be made public in real-time in which case a new field is required that would need to contain 'D' where a transaction was not pre-trade transparent or the information could be published by the relevant trading venue on a monthly basis.

Question 5: Would it be useful to have a mechanism to identify transactions which are not pre-trade transparent?

Question 6: If you agree, should this information be made public trade-by-trade in real-time in an additional field or on a monthly aggregated basis? Please specify reasons for your position.

Question 7: What would be the best way to address the situation where a transaction is the result of a non-pre-trade transparent order executed against a pre-trade transparent order?

Unique transaction identifier

[35] This proposal would replace the recommended flag 'D' for 'determined by other factors' in Recommendation °3 of CESR's Level 3 guidelines and recommendations on publication and consolidation of market transparency (Ref.: CESR/07-043).
[36] Article 3 of the MiFID Implementing Regulation.

14. MiFID does not require each transaction published to be assigned a unique transaction identifier however CESR recognises that many publication arrangements use unique transaction identifiers so that cancellations and amendments to published information can be linked to the originally published information.

15. To ensure consistency of approach and to improve the process for correcting and amending published information CESR proposes each transaction would need to be identified uniquely. CESR considers that this obligation could be met by requiring a unique transaction identifier to consist of a unique transaction identifier provided by the party with the publication obligation supplemented with a unique transaction identifier for the transaction provided by the publication arrangement and a code to identify the publication arrangement uniquely.

Question 8: Do you agree each transaction published should be assigned a unique transaction identifier? If so, do you agree a unique transaction identifier should consist of a unique transaction identifier provided by the party with the publication obligation, a unique transaction identifier provided by the publication arrangement and a code to identify the publication arrangement uniquely? If not, please specify reasons.

Cancellations

16. MiFID[37] requires any amendments to previously disclosed information to be made public. However, there is no requirement to make public a cancellation of previously disclosed information. Therefore there is no consistency in the way the market is informed where a transaction is cancelled and there may be instances where the market is not informed at all or where the information is published after a considerable delay. CESR recognises that many publication arrangements republish previously disclosed information with a cancellation identifier where a transaction is cancelled. In the US under FINRA rules where a trade is cancelled the firm with the responsibility to report the trade must report the cancellation within 90 seconds of the time the trade is cancelled.

17. To ensure consistency of approach and to improve the process for correcting published information CESR proposes that when there is a decision to cancel a transaction the information relating to the transaction would need to be republished together with the unique transaction identifier of the previously disclosed information as soon as possible and no later than 90 seconds and, in accordance with the CESR Level 3 Recommendation[38], a new field is required that would need to be populated with 'C'.

Question 9: Do you agree with CESR's proposal? If not please specify reasons.

Amendments

18. MiFID[39] requires that any amendments to previously disclosed information be made public. However there is no requirement that specifies how this obligation should be met and so there is no consistency in the way information related to amendments is made public.

19. In line with the proposal above for cancellations, CESR proposes that when there is a decision to amend information related to a transaction the information relating to the transaction would need to be republished together with the unique transaction identifier of the previously disclosed information as soon as possible and no later than 90 seconds with 'C' for cancellation and the amended version of the information would need to be published together with the unique transaction identifier of the previously disclosed information as soon as possible and no

[37] Article 27(1)(d) of the MiFID Implementing Regulation.
[38] Recommendation °3 of CESR's Level 3 guidelines and recommendations on publication and consolidation of market transparency (Ref.: CESR/07-043).
[39] Article 27(1)(d) of the MiFID Implementing Regulation.

later than 90 seconds and, in accordance with the CESR Level 3 Recommendation[40], a new field is required that must be populated with ‘A’.

Question 10: Do you agree with CESR’s proposal? If not please specify reasons.

Negotiated trades

20. MiFID[41] requires that an indication be provided where a trade was a negotiated trade. However there is no requirement that specifies how this obligation should be met and so there is no consistency in the way this information is made public.

21. CESR proposes that where a transaction is a negotiated trade, in accordance with the CESR Level 3 Recommendation[42], the flag ‘N’ would need to be used.

Question 11: Do you agree with CESR’s proposal? If not please specify reasons.

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[40] Recommendation °3 of CESR’s Level 3 guidelines and recommendations on publication and consolidation of market transparency (Ref.: CESR/07-043).
[41] Article 27(1)(c) of the MiFID Implementing Regulation.
[42] Recommendation °3 of CESR’s Level 3 guidelines and recommendations on publication and consolidation of market transparency (Ref.: CESR/07-043).

<u>ANNEX III –</u> CLARIFICATIONS OF THE POST-TRADE TRANSPARENCY OBLIGATIONS

1. Under MiFID[43] where the transaction is executed outside the rules of a regulated market or MTF one of the following investment firms shall, by agreement between the parties, arrange to make the information public:

   (a) the investment firm that sells the share concerned;
   (b) the investment firm that acts on behalf of or arranges the transaction for the seller;
   (c) the investment firm that acts on behalf of or arranges the transaction for the buyer;
   (d) the investment firm that buys the share concerned

2. In the absence of such an agreement, the information shall be made public by the investment firm determined by proceeding sequentially from point (a) to point (d) until the first point that applies to the case in question.

3. CESR acknowledges however there may be difficulties in applying the requirements to complex trading scenarios and recognises that trades are sometimes reported more than once, leading to a distorted picture of the market. This problem may cause an adverse impact on the overall price formation process and the ability of investment firms to use the information to assist the effective operation of the best execution obligation and to perform transaction cost analysis. Furthermore, the lack of clarity in the post-trade transparency obligations may present difficulties for competent authorities monitoring compliance. To address these concerns CESR makes a number of proposals and clarifications below:

Determination of the investment firm that shall make information public

4. To address difficulties faced by competent authorities monitoring compliance and to address concerns that trades are sometimes reported more than once, CESR proposes the requirement for determining the investment firm that shall make information public is strengthened by requiring <u>only one</u> of the investment firms described in point (a) to (d) to make the information public.

Two matching trades

5. MiFID[44] states that two matching trades entered at the same time and price with a single party interposed shall be considered to be a single transaction for the purpose of the post-trade transparency obligations. Under MiFID[45] the parties shall take all reasonable steps to ensure that the transaction is made public as a single transaction. To address difficulties faced by competent authorities monitoring compliance and to address concerns that trades are sometimes reported more than once, CESR proposes the requirement is strengthened such that the parties to a transaction <u>must</u> ensure that the transaction is made public as a single transaction.

6. To address the lack of clarity in the post-trade transparency requirements, CESR proposes that two matching trades would need to include:

   - where an investment firm acts on its own account and on behalf of a client and simultaneously executes a buy and a sell transaction and where there is no change in the price;

[43] Article 27(4) of the MiFID Implementing Regulation.
[44] Article 27(4) of the MiFID Implementing Regulation.
[45] Article 27(4) of the MiFID Implementing Regulation.

- where an investment firm acts for the account of and on behalf of both the buyer and the seller and where there is no change in the price[46].

Transactions on behalf of a client

7. CESR recognises there is inconsistency in the application of the post-trade transparency requirements where one or more transactions are executed on behalf of one or more clients. Where a transaction is executed under the rules of a regulated market or an MTF that transaction will be made public by the regulated market or MTF on which it was undertaken. Where a transaction is executed outside the rules of a regulated market or an MTF MiFID[47] defines the process for determining the investment firm that shall make the information public. Where the beneficial ownership of the share that is the subject of the transaction is transferred from the investment firm to the client(s) CESR considers that the publication of information related to the transfer(s) would lead to a distorted picture of the market and is unnecessary for price formation purposes unless there is a change in price. Therefore CESR proposes that where a transaction is executed outside the rules of a regulated market or MTF on behalf of one or more clients the investment firm will need to ensure they do not make public information related to the transfer(s) of beneficial ownership of the share from the investment firm to the client(s) unless there is a change in price. To comply with this requirement, the principal or initiating seller (i.e. investment firm B in examples 1 and 2) would have the legal responsibility for publishing the transaction. However, CESR considers that there should also be flexibility for firms to agree on a different arrangement for publication or to have a standing agreement as to who is responsible for reporting all trades between them (i.e. an example of an alternative standing arrangement could be that whenever investment firm A deals with investment firm B, investment firm A will be responsible for publishing the trade report).

Example 1 – Single over the counter transaction on behalf of a client Investment firm A buys 100 shares over the counter on behalf of a client: Client ↔ Investment firm A ↔ Investment firm B Publication: Investment firm B (unless investment firms A and B have a standing agreement about who makes information public) Market sees: Total volume of 100 shares

Example 2 – Multiple transactions on behalf of a client Investment firm A buys 100 shares (80 on a RM or MTF and 20 over the counter): Client ↔ Investment firm A ↔ RM or MTF (80 shares) Client ↔ Investment firm A ↔ Investment firm B (20 shares) Publication: RM or MTF makes information public in relation to 80 shares Investment firm B makes information public in relation to 20 shares (unless investment firms A and B have a standing agreement about who makes information public). Market sees: Information related to 80 shares and information related to 20 shares

[46] Where an investment firm does not act on its own account or for the account and on behalf of a client and instead brings together two investors who execute a transaction between themselves CESR would consider that the investment firm has received and transmitted orders and would not have an obligation to make information public.
[47] Implementing Regulation Article 27(4)

Chain of transactions

8. CESR recognises that where the ownership of a share is transferred from one investor to another via chain of investment firms and there is no change in price and the investment firms are not putting their own capital at risk there may be inconsistency in the application of the post-trade transparency requirements. CESR considers that in this scenario the publication of information related to each transfer would lead to a distorted picture of the market and is unnecessary for price formation purposes. To address this inconsistency, CESR proposes that such a chain of transactions will need to be considered to be a single transaction for the purpose of post-trade transparency. To comply with this requirement the principal or initiating seller (i.e. investment firm A in example 3) would have the legal responsibility for publishing the transaction. If the investment firms have different standing arrangements about the responsibility for making information public, they must also have the capability to identify situations where a trade report is not necessary. Trading participants will need to be explicit as to who is taking responsibility for making the information public.

Example 3 – Chain of investment firms An order for 100 shares passes through a chain of investment firms where there is no change in price. Selling client ↔ Investment firm A ↔ Investment firm B ↔ Investment firm C ↔ Selling client Publication: Investment firm A (unless the investment firms have a standing agreement who shall make information public) Market sees: Information related to 100 shares

Transactions where one party is not an investment firm

9. CESR would like to clarify that where a transaction is executed outside the rules of a regulated market or an MTF and one of the parties is not an investment firm the information shall be made public by the investment firm.

Question 1: Do you agree with CESR's proposals? Are there other scenarios where there are difficulties in applying the post-trade transparency requirements?

ANNEX IV – PROPOSED GUIDANCE FOR APPROVED PUBLICATION ARRANGEMENTS

Security

APAs would need to ensure there is:

- certainty over which firms submit trade information;
- no corruption of data in the input process at the APA; and
- no unauthorised access to trade information at the APA.

APAs would need to ensure there are controls over their facilities and the individuals providing the services to ensure trade information is monitored securely and to prevent the misuse of the information. At a minimum, the following controls would need to be in place at the APA:

- the working environment would need to be secure;
- the computer-based systems would need to incorporate:
    - access controls;
    - procedures for problem management and system changes; and
    - arrangements to monitor system performance, availability and integrity.
- the working environment would need to be free of unauthorised surveillance;
- individuals providing the APA service would need to be under a duty to keep confidential any trade information to which they might have access; and
- if there is a breach of any security measure relating to the provision of a APA service, the clients involved would need to be notified immediately and, if requested, a detailed report of the breach should be provided and any corrective steps taken.

Dissemination

APAs would need to have arrangements in place to disseminate trade information to the market without delay;

Trade information would need to be made public in a way which:

- is accessible by automatic electronic means in a machine-readable way;
- utilises technology that facilitates consolidation of the data and permits commercially viable usage;
- is accompanied by instructions outlining how users can access the data; and
- conforms to a consistent and structured format based on MiFID and industry standards.

Identification of incomplete or potentially erroneous information

APAs would need to have appropriate systems and controls in place to identify on receipt trade reports from investment firms that are incomplete or contain information that is likely to be erroneous. These systems and controls may include various automated price and volume alerts, taking into account:

- the sector and the segment in which the security is traded;
- liquidity levels including historical trading levels;
- appropriate price and volume benchmarks; and
- if needed, other parameters to be set manually according to the characteristics of the security.

Where an APA determines that a trade report it receives from an investment firm is incomplete or contains information that is likely to be erroneous, it would need to ensure it does not publish this information. It would need to alert the investment firm that the trade report is incomplete or contains information that is likely to be erroneous and has not been published.

An APA would need to periodically review its systems and adjust them when necessary.

Correction of trade information

An APA would need to have the ability to amend a trade report itself when a firm cannot do so for technical reasons in exceptional circumstances. The APA would not otherwise be responsible for correcting information contained in trade reports. Where an APA determines a trade report is incomplete or contains information that is likely to be erroneous and therefore does not publish the trade, the investment firm would need to correct the trade report and publish a complete and accurate trade report as soon as the error is detected.

Monitoring

An APA would need to have the capability to monitor its own systems and controls to ensure with reasonable certainty that the trades it monitors have been successfully published.

Operational hours

An APA would need to be capable of monitoring trade reports throughout the normal trade publication hours of the investment firms submitting trade reports to it.

Resources

An APA would need to have appropriate numbers of staff overseeing the APA service who are competent to perform their duties.

An APA would need to notify its clients of the person with overall management responsibility for the APA service and compliance with the APA standards.

Contact arrangements

An APA would need to provide a facility for market participants to query the accuracy of the trade publications it disseminates and would need to have procedures in place for market participants to raise complaints regarding the APAs' services and activities.

Recovery provisions

An APA would need to be able to adequately provide for possible disruptions to its operations by having arrangements to ensure IT systems are not prone to failure and would need to ensure business continuity if a system or systems failed.

An APA would need to regularly review these provisions and ensure they remain sufficient to ensure there is minimum disruption to the continuous operation of an APA service. An APA would need to inform its clients without delay if its operations are disrupted.

Conflicts of interest

APAs would need to have appropriate arrangements for managing conflicts of interest.

Outsourcing

Where an APA arranges for functions to be performed on its behalf by third parties, the APA would need to be satisfied that the person performing the function is fit, able and willing to perform the function.

Regulatory reporting responsibilities

Periodic report

The information that an APA would be expected to provide to the competent authority of each investment firm using the facilities of the APA on a periodic basis would include (but not be limited to) the proportion of information to be made public received by the APA from the investment firm that:

- The APA did not publish because the information was incomplete;
- The APA flagged as being likely to be erroneous;
- Were later cancelled by the investment firm;
- Were later amended by the investment firm; and
- Were not received by the APA within the time required under Article 29(5) of the MiFID Implementing Regulation or the delays allowed under Article 28 of the MiFID Implementing Regulation.

Ad hoc report

Where an APA considers that an investment firm is consistently providing poor quality data, it would in the first instance inform the investment firm of its concerns. If the submission of poor quality data continues, the APA would need to report its concerns to the investment firm's competent authority.