More to be done to strengthen transparency: FESE position paper on the MiFIR review proposal

Brussels, 1st March 2022

FESE welcomes the opportunity to give feedback on the MiFIR review proposal. We share its objectives to increase transparency and liquidity, to strengthen the level playing field between execution venues, and to enhance the competitiveness of capital markets.

In this respect, **FESE very much endorses the removal of the open-access provisions for exchange-traded derivatives, the prohibition of payment for order flow, and the removal of the exception to the exemption from authorisation as investment firm for DEA users**, which together will make markets stronger. However, other aspects deserve further reflection.

EU capital markets face a concerning reality: according to Big xyt data[1], half of trading is happening in the dark. This, in our view, goes against the objectives stated above. The renewed dark trading cap suffers from the same limitations as the current cap and, as such, it falls short of appropriately framing dark flow in the EU, by only including trades below the reference price and negotiated transactions waivers.

- **Hence, FESE suggests capturing all trades without pre-trade transparency (except LIS blocks) under a single cap to limit dark trading.**

The proposal to require SI public quotes to be up to twice the standard market size, whilst it is a step in the right direction, is not sufficient to truly increase transparency because these quotes are only accessible to a few customers, since SI enjoys discretionary access.

- **To address this reality, we believe that limiting SI equity trading only to above large in scale (LIS) via Art. 1(8) would be an efficient way to incentivise lit trading and ensure the quality and robustness of price formation.**

In order to support strong markets that strengthen the price formation process, benefitting companies and investors, **changes to the current market structure are essential. The creation of a consolidated tape (CT) in and of itself will not address these issues.** Whilst the CT proposal makes some wise choices, such as defining a single post-trade CT per asset class covering all venues as well as the exclusion of ETDs from scope, it regrettably opts for the establishment of a real-time CT and leaves the door open to a pre-trade CT, thus raising significant policy risks.

The possibility of a pre-trade CT is deeply concerning. A pre-trade CT would create a false sense of liquidity and would lead to the emergence of an European best bid and offer (EBBO)

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[1] FESE, "Europe Must Foster Transparent Markets to Remain Competitive" (Brussels, 2021)

or de facto reference price, thereby creating an environment that is ripe for arbitrage at the expense of retail investors.

In addition, introducing a real-time CT could deprive exchanges of an important revenue source, seriously affecting exchanges' continued ability to run and maintain a full suite of operations underpinning the Capital Markets Union (CMU) – such as the listing of companies and the nurturing of SME growth markets - and to ensure the proper functioning of markets. This risk is not mitigated by the revenue-sharing model proposed as the scope and conditions of this model are unclear. Any revenue compensation model should be properly defined at Level 1 and should aim to ensure that market contributors are properly compensated for their input to the tape.

In light of these concerns in relation to the risks of a pre-trade tape and the need to adequately compensate exchanges for their contribution to a CT, FESE proposes:

- **Amending Recital 20 and Art. 1(10), 1(15), and 1(16) establishing a 15-minute delayed post-trade CT.**
- **Removing the reference to best bid and offer in the definition of core market data under Art. 1(2), thus altering the definition of core market data to cover only post-trade data.**

A 15-minute delayed CT[2] is the most pragmatic approach to delivering a tape which meets the goals of all investors at the least disruption to the industry. Such a CT would draw on the current requirement to make data available free of charge 15 minutes after publication and, consequently, obviate the complex issue of distribution models, particularly the question as to the scope of revenues that should receive compensation (because there would be no need to redistribute revenue to its contributors). In this way, a delayed CT would provide easy and low-cost access to a consolidated view of the market without any undue impact on small venues. Importantly, this model would also allow for a phased approach towards reducing the delay in the future once the CT has proven its value.

Finally, we propose deleting Art. 1(7) mandating ESMA to translate the Level 3 reasonable commercial basis (RCB) Guidelines to Level 2. FESE does not deem further regulatory technical standards to specify the RCB regime to be warranted at this stage. ESMA has recently issued a report[3] continuing with the 'transparency plus' approach which sets out Guidelines on market data that market data providers are working intensively to implement. These Guidelines having started to apply only as of January 2022, the market should be given time to adjust to this new reality before another set of rules is introduced.

Regarding non-equities, we believe that the proposed changes to the post-trade transparency framework are going in the right direction. A less complex regime, balancing the need for enhanced transparency whilst recognising the specificities of such markets, would help to promote their resilience and competitiveness.

To develop stronger, more transparent, and more competitive European capital markets, FESE encourages EU policymakers to be ambitious and adopt a strategic approach. Casting light on Europe's markets is paramount if we are to foster a CMU which serves all market participants.

[2] Oliver Wyman, "Caught On Tape: a Consolidated Tape for Europe" (2021)

[3] ESMA, "Guidelines on the MiFID II/MiFIR obligations on market data" (2021)