Regulation of trading in financial instruments - "dark pools" etc.

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The Committee on Economic and Monetary Affairs adopted the report drafted by Kay SWINBURNE (ECR, UK) on regulation of trading in financial instruments – 'dark pools' etc.

In its report, the committee recalls that the G20 set out that no financial institution, no financial product and no territory should remain outside the scope of intelligent regulation and effective supervision and agreed that all standardised OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate.

Despite the provision in the Directive of waivers to allow dark trading on organised markets, the establishment of MTFs and Systematic Internalisers (SIs) and the definition of OTC trades as being irregular and ad hoc, OTC trades not carried out on an SI basis continue to account for a high proportion of equities trading at 38% of all reported trades. This proportion has not declined since the implementation of the Directive on markets in financial instruments (MiFID). The report states that **tighter and more effective enforcement of MiFID rules and waivers should therefore be ensured**.

Market fragmentation in equities trading has had an undesired impact upon liquidity and market efficiency owing to a decrease in transparency based on an increase in dark pools and crossing networks, the effect of an increased number of venues both in the on-exchange and off-exchange space.

MIFID Trading Venues: Members call upon the Commission to **strengthen market infrastructures** across all trading venues and clearing systems to enable them to cope with future risk through **enhanced transparency**, improved resilience and regulatory oversight of all aggregated trades.

The report calls for **thorough enforcement of the provisions in MIFID** in order to ensure that Broker Crossing Networks (BCNs) that are carrying out activities equivalent to a regulated market (RM), multilateral trading facilities (MTF) or SI are **regulated as such**, and, in order to facilitate this enforcement, insists that all BCNs should be required to submit to the competent authorities all necessary information.

Members suggest that, in the interests of equitable treatment, MTFs should be subject to the same level of supervision as, and therefore regulated in a comparable way to, competition between MTFs and that RMs should happen on a level playing field, while noting the important role of MTFs for market entry.

Members call on the Commission to conduct a **review of the existing MiFID pre-trade transparency waivers** and for a uniform application of pre-trade waivers across Member States to limit implementing differences that can lead to uncertainty, regulatory arbitrage and an uneven playing field They suggest that technical standards defined by ESMA could be an appropriate way of achieving this, in keeping with the concept of a single rule book for financial services.

Consolidated Tape: the Commission is called upon to establish a working group to overcome the difficulties preventing the consolidation of market data in Europe and particularly the poor quality of reporting data across all transactions. The report calls upon ESMA to draw up **common reporting standards and formats for the reporting of all post-trade data**, both on organised trading venues and

OTC, to aid in data consolidation. It asks that all reporting venues be required to unbundle post-trade data from pre-trade data so information can be made available to all market participants at a commercially reasonable and comparable cost.

Micro-structural issues: the committee insists that post-'flash crash', all trading platforms must be able to demonstrate to national supervisors that their technology and surveillance systems are able to withstand the kind of barrage of orders experienced on 6 May 2010.

It calls on ESMA to conduct an examination of the **costs and benefits of algorithmic and high-frequency trading** (HFT) on markets and its impact upon other market users. An investigation is called for into whether to regulate firms that pursue HFT strategies in order to ensure that they have robust systems and controls with ongoing regulatory reviews of the algorithms they use.

The report calls upon regulators to **monitor and regulate the provision of sponsored access** and upon the Commission to consider additional measures.

Members request that no unregulated market participant be able to gain direct or unfiltered sponsored access to formal trading venues and that significant market participants trading on their own account be required to register with the regulator and allow their trading activities to be subject to an appropriate level of supervision and scrutiny for stability purposes.

Lastly, the report calls for a **proposal from the Commission** to ensure that all OTC derivative contracts that can be standardised are traded on exchanges or electronic trading platforms, where appropriate, in order to ensure that the price of such contracts is formed in a transparent, fair and efficient manner, free from conflict of interest.