



FCA IMPROVING EQUITY SECONDARY MARKETS: CP22/12

UK Finance response
16 September 2022



Linklaters

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About Linklaters

Linklaters LLP is a leading international law firm, specialising in innovative, complex work for investment banks, asset managers, exchanges, private and public companies and their owners, private equity houses and governments. We offer a full cycle service for our clients, including advice on complex regulatory issues, IPOs, mergers & acquisitions, corporate finance and dispute resolution. We have a market leading financial services practice that is ranked band 1 by the key legal directories (Chambers and Legal 500) and considered to be at the forefront of market and regulatory developments. We aim to build enduring relationships with our clients and to be their lawyers of choice for their most important mandates. Further information is available at www.linklaters.com.

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FCA Improving Equity Secondary Markets: CP22/12 UK Finance response

Date: 16 September 2022

Sent to: **Fabio.Braga@fca.org.uk**
Trading and Wholesale Conduct Policy
FCA

Also submitted via: <https://www.fca.org.uk/publications/consultation-papers/cp22-12-improving-equity-secondary-markets>

Dear Fabio,

Please find enclosed the UK Finance response to CP22/12: Improving Equity Secondary Markets, produced with the advisory support of Linklaters LLP.

We welcome this opportunity to share our views and recommendations for improving the UK's equity secondary markets, following the Wholesale Markets Review.

An effective regulatory regime, which upholds robust and proportionate standards, will be fundamental in ensuring the UK continues to be a market of choice for investors and issuers, both domestic and international.

We are pleased therefore that the FCA is approaching reform with ambition and openness in mind, and we look forward to working with you in the months ahead to support and contribute to this important agenda.

If you have any questions in relation to the information within our submission, please do not hesitate to get in touch.

Kind regards,



Conor Lawlor

Managing Director, Capital Markets
and Wholesale, UK Finance

POST-TRADE TRANSPARENCY

Question 1 - Do you agree with maintaining the exemption for inter-funds transfers in Article 13?

UK Finance members agree with the FCA's proposal to maintain the exemption for inter-fund transfers in Article 13 of UK RTS 1.

Question 2 - Do you agree with the new definition of inter-funds transfers?

UK Finance members agree with the new definition of inter-funds transfers as suggested by the FCA. We also note that there will be some inter-fund transfers that require broker facilitation, as such the definition should also capture this.

Question 3 - Do you agree with amending the exemption from post-trade reporting for give-ups and give-ins?

UK Finance members agree with amending the exemption from post-trade reporting for give-ups and give-ins, as we agree that the 'market leg' of an RFMD (request for market data) would have already been trade reported by the executing broker.

We note that there might be a gap arising from RFMDs which receive principal liquidity as we would not consider there to be an 'execution' at the time members provide indicative pricing to clients. As such, where members do not report the resulting give-up, there may not be price transparency. However, the vast majority of activity that is ultimately given up is likely to be conducted on-venue (and reported) and it would not be proportionate to continue to report give-ups for the small minority of instances where it represents principal liquidity. The benefits of removing the noise give-up activity generates on the tape, would far outweigh the benefit of the principal liquidity being reported.

We would also highlight that hedging derivatives is not the only reason for a give-up. A trade can be given up to a prime broker for the purposes of safekeeping. The proposed definition below suggests that brokers know when a give-up is conducted for hedging versus other types of trades. However, there is no way of knowing this when giving the trade up. In addition, the definition should adequately capture the scenarios which may involve third-country firms.

A "give-up transaction" or "give-in transaction" means a transaction where:

- i) an investment firm passes a client trade to, or receives a client trade from, another investment firm or third country firm for the purpose of post-trade processing; or
- ii) following a request for market data, an investment firm passes a trade to, or receives a trade from, another investment firm or third country firm.

A request for market data refers to a request for illustrative pricing for financial instruments. For the purposes of ii) an investment firm passes a trade following a request for market data in instances where it creates an own account position (which may involve sourcing a proprietary cash equity position) following a request for market data from a third party, which position it subsequently offers to, and is accepted by, another investment firm or third country firm. For the purposes of ii) an investment firm receives a trade from another investment firm or third country firm following that investment firm's or third country firm's receipt of a request for market data, in instances where it is offered and it accepts a position which it holds as a custodian or on its own account as a hedge to a derivative, in each case, for a third party."

Question 4 - Do you think guidance to clarify further the types of give-ups and give-ins that can benefit from the exemption from post-trade transparency is required, and, if so, what issues do you think it should cover?

UK Finance members agree that guidance to clarify further the types of give-ups and give-ins that can benefit from the exemption from post-trade transparency would be useful. However, we stress that any guidance should not amount to an exhaustive or prescriptive list of trades that can benefit from the exemption, instead, examples would be helpful.

Question 5 - Do you agree with introducing an exemption for inter-affiliate trades?

UK Finance members agree with introducing an exemption for inter-affiliate trades. Given that inter-affiliate trades do not contribute to price formation, their exemption would be a welcome change in creating a more efficient and effective UK regime.

Question 6 - Do you agree with our proposed definition of inter-affiliate trades?

UK Finance members agree with the proposed definition of inter-affiliate trades, with the exception of specifying that these trades are carried out as part of a centralised booking for intra-group risk management purposes. This is because intragroup risk management might not always be taken as part of a centralised booking model; a variety of booking models exist. As such, we recommend the definition for inter-affiliate transactions to read as:

“Inter-affiliate transaction’ means a transaction between entities within the same group carried out exclusively as part of centralised booking for intragroup risk management purposes.”

Question 7 - Do you agree with the deletion of point d) from Article 13? If not, please explain why.

We note the FCA’s clear statement in paragraph 3.10 of CP22/12, namely that the FCA considers the exemption in Article 13(d) of RTS 1 (being deleted) to be included in Article 2(5)(d) of RTS 22. However, we query whether the exemption in Article 13(d) of RTS 1 would be fully captured by Article 2(5)(b) of RTS 22, rather than by Article 2(5)(o) of RTS 22, or a combination of Article 2(5)(b) and (o).

In light of this and our comments in response to Question 9 below, we would encourage the FCA to include a statement in the policy statement amending RTS 1 to the effect that the deletion of any specific exemption from RTS 1 was not intended to reduce the scope of RTS 1 exemptions, as any deletion is adequately compensated for by the other changes made by the FCA to RTS 1, including in particular the cross-references to the exemptions in Article 13 of RTS 1, which in turn incorporates the exemptions listed in Article 2(5) of RTS 22.

Question 8 - Do you agree with the proposal to introduce a deferral for all transactions within scope of Article 13 of RTS 1? If not, please explain why.

UK Finance members agree with the proposal to introduce a deferral for all transactions within the scope of Article 13 of RTS 1. We note that this would be a useful change which will help to reduce the level of noise that exists in post-trade data.

Question 9 - Do you agree with our proposals to align the definitions of non-price forming trades in Articles 2, 6 and 13? If not, please explain why.

We agree that the current multitude of exemptions in Articles 2, 6 and 13 of RTS 1 and Article 2(5) of RTS 22 should be aligned where relevant. However, we note that the way the different provisions are currently phrased means that it is not always straightforward to match existing RTS 1 exemptions, which are proposed to be deleted, to the RTS 22 exemptions that will be referenced going forward, and the wording is not always the clearest.

One example of this is the proposed deletion of Articles 13(d), 2(f) and 6(f) on collateral transfers which (as further explained in our response to Question 7 above) could track across to Article 2(5)(b) and (o) of RTS 22, yet the consultation suggests it is only Article 2(5)(b), which requires “a contract exclusively for clearing or settlement purposes”, which would not obviously capture “transfers of financial instruments as collateral in bilateral transactions”.

Another example is the proposed deletion of Articles 2(g) and 6(g) relating to the delivery of shares / financial instruments in the context of the exercise of convertible bonds etc. Although Article 2(5)(h) of RTS 22 contains an exemption for “the exercise of a right embedded in a financial instrument, or the conversion of a convertible bond and the resultant transaction in the underlying financial instrument”; it could be made clearer that the exempt “resultant

transaction” applies to both “the exercise of the right embedded in a financial instrument” and “the conversion of a convertible bond” (the current drafting could suggest it applies only to the latter). This could be achieved by placing a comma after “the conversion of a convertible bond” in Article 2(5)(h) of RTS 22.

In addition, in Article 6(j) of UK RTS 1, the cross-references should refer to “points (a) to (ca)” to ensure that the “equivalent transactions” provision in (j) adequately captures transactions which have been deleted from Article 6 on the basis they are reflected in the RTS 22 list of exemptions, which is to be captured by new Art 6(ca) of UK RTS 1.

In light of the above specific observations and proposed changes, we would encourage the FCA to include a statement in the policy statement amending RTS 1 to the effect that the deletion of any specific exemption from RTS 1 was not intended to reduce the scope of RTS 1 exemptions, as any deletion is adequately compensated for by the other changes made by the FCA to RTS 1, including in particular the cross-references to the exemptions in Art 13 of RTS 1, which in turn incorporates the exemptions listed in Art 2(5) of RTS 22.

Finally, we noticed that the base version of RTS 1 which has been marked up and included at Annex A of the CP does not reflect changes made to EU RTS 1 ahead of the end of the Brexit transition period, most notably changes to Articles 2 and 6 made by **Commission Delegated Regulation 2019/442**. We note that **UK RTS 1 on the FCA Handbook (technical standards) webpage** also has the same issue.

Question 10 - Do you agree with our proposal to amend the definition of benchmark transaction to include transactions that reference to the market closing price? If not, please explain why.

We note that the proposal to amend the definition of benchmark transaction, should only capture within the definition of “benchmark trade” those transactions which are pre-determined to happen at the market closing price (rather than inadvertently capturing transactions which simply “happen to” close at market closing price). The definition of “benchmark trade” in new Art 1(5A) of UK RTS 1 may benefit from clarifying either way, e.g., the word “at” may need to be deleted from sub-paragraph (b), so that it reads on properly from the introductory language.

Question 11 - Do you agree with our proposal to amend the definition of benchmark transaction to include transactions that reference to the market closing price? If not, please explain why.

UK Finance members agree with the proposal to delete SI-related flags “SIZE” and “ILQD”.

Given the operational challenges and complexities firms will be required to navigate, we request that an adequate implementation period of 12 months is given. This would allow for firms to undertake the additional work.

Question 12 - Do you agree with the deletion of the agency cross flag “ACTX”, the duplicate trade flag “DUPL” and the algorithmic trade flag “ALGO”? If not, please explain the value these flags offer, how providing practical examples.

UK Finance members agree with the deletion of the agency cross flag “ACTX”, the duplicate trade flag “DUPL” and the algorithmic trade flag “ALGO”.

Question 13 - Do you agree with the proposal of identifying “benchmark”, “portfolio” and “contingent” trades with one single flag, “TNCP”? If not, please explain why and set out your preferred approach.

UK Finance members would prefer to retain the ability to differentiate between “benchmark”, “portfolio” and “contingent” trades. This is because we believe there is value in being able to distinguish between these trade types, as the granularity provides a helpfully detailed picture of the market. We also note that this is an example where comparability and consistency with the EU is helpful.

Question 14 - Do you agree with our proposal to aggregate the three negotiated transactions flags into one single flag, "NETW"? If not, please explain why.

Yes, we agree with the proposal to aggregate these into a single flag.

Question 15 - Are there any other flags that we should consider removing, amending or adding?

Yes, UK Finance members recommend that a new flag for 'benchmark trades executed at market closing price' is added, following on from our response to question 10. This is in order to ensure that benchmark trades which are executed at market close under the extended definition of "benchmark trade" can be distinguished from other benchmark trades. This level of granularity in turn would helpfully allow for greater transparency and clarity and would also allow market participants to compare EU and UK benchmark trade data (by being able to filter out benchmark trades executed at close from the UK data, as EU benchmark trade data would not include such trades).

Question 16 - Do our proposals to modify the flags for trade reporting impact your systems for transaction reporting? If yes, could you describe how and what problems maintaining the flags for transaction reporting would cause?

UK Finance members note that current RTS 1 indicators will still continue to be used in UK RTS 22, which are in transaction reporting fields 61 (waiver indicator) and 63 (OTC post-trade indicator). It will be challenging to maintain two forms of the flags.

UK members also highlight the linkage between these flags and the removal of the STO and the sequencing of these changes posing operational concerns.

Question 17 - Do you agree with the proposed changes to the reporting fields? If not, please explain why.

UK Finance members agree with the proposed changes to the reporting fields.

Question 18 - Are there other changes that you suggest we should make to the fields of reported transactions?

UK Finance members do not have any suggestions for further changes to the fields of reported transactions at this stage. We would, however, like to work with the FCA, other trade associations, and market infrastructure providers (CCPs, trading venues etc) to identify opportunities to improve the reporting fields and templates. Reporting fields need to remain functional in the face of digital innovation in financial markets. With these in mind, we recommend that the FCA set up a reporting advisory group to identify upcoming challenges and opportunities, with a view to recommending changes to MiFID reporting, as well as EMIR and SFTR, given the overlap in certain fields.

Question 19 - Do you agree with our proposal to create a regime where firms will be able to opt in as designated reporters at an entity level? Please explain your answer.

UK Finance members agree with the proposal to create a regime where firms are able to opt in as designated reporters. This would be a very welcome change that would significantly improve the regime as it exists today.

Specifically, we agree with the FCA proposal to decouple post-trade reporting obligations from SI status and to introduce the concept of designated reporter status.

With regards to the reporting hierarchy, we agree with the FCA proposal that (i) if a designated reporter transacts with a non-designated reporter, the designated reporter reports, (ii) if two designated reporters transact, then the seller reports, and similarly (iii) if two non-designated reporters transact, then the seller reports.

We believe this model would bring clarity to the current post-trade reporting regime through:

- Enabling firms to simply verify the designated reporter status of their counterparty by checking the designated reporter database;
- Aiding clients to identify quickly and clearly who will report on their behalf, thereby mitigating any uncertainty and increasing efficiency; and
- Removing the overly burdensome and complex relationship between post-trade reporting requirements and SI status.

Opting-in at an asset class level

- Whilst we welcome and support the proposals to implement a designated reporter regime that allows for the certainty and simplicity to report at an entity level, there are firms that, when trading instruments in respect of which they are not SIs, choose to only trade with counterparties who are themselves SIs. The SI then provides the relevant post-trade reports. Whilst firms may be SIs in selected asset classes for which they have the relevant post-trade reporting systems in place, creating a new designated reporter regime with opt-in only at an entity level would require those firms to build, for the first time, post-trade reporting systems across all remaining asset classes. For this reason, the option to register as a designated reporter at an asset class level should also be made available. The regime should not disadvantage smaller firms at the expense of larger firms who operate across all asset classes.
- Although we fully support the proposals for the new designated reporter regime, we consider that it could be improved by allowing the relevant election to be at asset class level. We believe that this would not add undue complexity but would strike the right balance between this welcome simplification of post-trade reporting, while not leaving smaller investment firms with a need to re-write their post-trade reporting systems.
- To define the “asset classes” we recommend adopting the 13 top level designations set out in RTS 1 and RTS 2:

a) Equity and Equity like	h) Foreign exchange derivatives
b) Bonds (all bond types except ETCs and ETNs)	i) Securitised derivatives
c) Bonds (ETC and ETN bond types)	j) Commodity derivatives
d) Equity derivatives	k) C10 derivatives
e) Interest rate derivatives	l) Emission allowances
f) Credit derivatives	m) Emission allowance derivatives
g) Structured finance products	
- Under the above proposed approach, some firms will opt in to be designated reporters for all 13 asset classes (i.e., at an entity level) while other firms may select a subset.
- **Ease of use** – We recommend that for ease of use and data recovery, when the database returns the designated reporter status of a firm opted in for all asset classes, it should do so in a form or forms that ensure simplicity of consumption by any firm querying the database.
- **Definition** – As currently drafted, the new definition of “designated reporter” appears to rely on the relevant entity acting as “buyer”. However, as indicated by the FCA in CP22/12 and outlined above, the relevant designated reporter may also be responsible for post-trade reporting trades undertaken as seller in certain circumstances. We recommend amending the “designated reporter” definition in both UK RTS 1 and 2, e.g., by deleting the wording

“where it is the buyer of a financial instrument either on own account or on behalf of clients”, or by referring the “buyer or seller” in this part of the definition.

- UK Finance members also consider that the definition of “designated reporter” in both UK RTS1 and 2 would benefit from a clarification that UK branches of third-country firms can also opt in to being designated reporters for UK post-trade purposes. We note that the designated reporter proposal should not require UK branches of third-country firms to seek an LEI for that branch, instead they should be able to opt-in using their home/parent LEI.

Question 20 - Do you agree that the FCA should maintain the register of designated reporters for firms to determine who reports OTC trades? Please explain your answer.

UK Finance members note that a register of designated reporters is central to an efficient and effective regime. Whilst we do not have a position on who should operate and maintain the designated reporter database, we would like to highlight the merits of the existing industry-led reference data utility (RDU) solution that houses both UK and EU data in a machine-accessible format (rather than presenting information on a website).

When determining who should operate and maintain the designated reporter database, we would ask the FCA to ensure that key objectives are met such as those set out below:

- Clear and easily- accessible data should be available to all market participants;
- Ensuring that the data is machine accessible (for example via an application programming interface (API)) so that both applications can interact, and the data can be consumed by systems on a continuous basis (e.g., by systems operating in different time zones); and
- Careful consideration of operational issues, such as disconnecting from the existing industry-led RDU database and reconnecting to a database (such as for example a database run by the FCA).

We also agree with the suggestion to keep historic records of when a particular firm was (and ceased to be) a designated reporter. It is helpful for market participants to confirm the relevant status of counterparties retrospectively.

Question 21 - Do you agree with the proposed implementation timetable? If not please explain your answer.

UK Finance members recommend an implementation period of 12 months. This is due to the operational challenges firms will need to navigate in order to implement changes to RTS 1, alongside retaining old RTS 1 flags, within RTS 22 transaction reports. Working through the difficulties of the divergence between EU and UK post-trade reporting regimes, will also add an additional layer of operational complexity.

UK Finance members also would recommend that RTS 1 changes be aligned with the timing of the STO removal (so as to not have to reflect changes to RTS 1, e.g., Article 2 exemptions, in systems, only to make another change once the STO ceases to apply altogether).

WAIVERS FROM PRE-TRADE TRANSPARENCY

Question 22 - Do you agree with the proposal to change the definition of the MRMTL to allow trading venues to derive the price from a nonUK venue provided that the price is transparent, robust and offers the best execution result?

UK Finance members support this proposal; however, we note that the drafting of UK RTS 1 Article 4(1A) could be further improved by allowing venues to not just refer to the third-country venue of first admission, but also to the third-country market with the highest turnover for that financial instrument.

Question 23 - Do you agree with the proposal to change the definition of the MRMTL for the purpose of the tick size regime?

Yes, UK Finance members agree with this proposal, however, in line with our comments in response to question 22 above, it must be possible to reference third country venues of first admission, as well as the third country venue with the highest turnover.

Question 24 - Do you agree with the proposal to delegate the decision to set a minimum size threshold for reserve and other orders to trading venues using the OMF waivers? Please explain why.

Yes, UK Finance members agree with the proposal to delegate the decision to set a minimum size threshold for reserve and other orders to trading venues using the OMF waivers.

Question 25 - Do you agree with the proposal to allow trading venues to adopt the minimum tick size of the primary market located overseas when that tick size is smaller than the one determined based on calculations using data from UK venues? Please explain your views.

Yes, we support this proposal as it would aid UK venues when trading overseas shares.

IMPROVING MARKET-WIDE RESILIENCE DURING OUTAGES

Question 26 - Do you agree with the above proposals to be included in the FCA/industry guidance for trading venues? If not, please explain why.

Yes, UK Finance members believe that guidance should be developed to cover how venues should operate during an outage and govern expectations on how trading should resume on a primary venue. We set out below key considerations for the development of such guidance:

- There should be greater clarity, and standardisation where possible, on the content that should be provided in communications during an outage. Both the content within such communications and the frequency of them can be insufficient. In particular, our members have found that the estimates provided by trading venues on when trading can resume can be inaccurate. This can impact the routing of orders by market participants to other venues.
- The guidance should encourage primary venues to take the appropriate amount time to prepare and stabilise their systems before resuming trading, as opposed to restarting before full stability has been assured. In this regard, it would be helpful for the guidance to reemphasise that Article 15(2) of RTS 7, which encourages trading venues to resume services within or close to two hours, is intended to be guidance and not a prescriptive target; the full stability of the market should be prioritised and assured before trading is resumed.
- Where, due to an outage, an index provider cannot make use of closing benchmarks provided by a primary venue, it should be made clear in the guidance that the index provider can where necessary make use of alternative sources of closing benchmarks.

Question 27 – Are there any other areas we need to consider for guidance?

UK Finance members do not have any other areas to suggest in this regard.

Question 28 - Is the current arrangement for an alternative closing price on the primary market appropriate?

No, please refer to our response to question 29.

Question 29 - Is an alternative closing auction needed?

Yes, UK Finance members believe that alternatives to the closing auction are needed. We understand that no venues in the current environment are able to conduct a closing auction across the full suite of London Stock Exchange instruments.

It would be helpful if the set of contingencies available to market participants were extended to include factors in addition to the 'last continuous price' which is currently used but which will not always be available. Examples of other such contingencies could include the opening price, or the last price of the previous day. Expanding the contingencies which are available in these circumstances will provide the market with an appropriate level of certainty.

Given that there is currently no industry consensus on further contingencies that could be used, we encourage the FCA to facilitate further engagement with market participants to identify a comprehensive suite of potentially appropriate information which can be considered in such events.

Question 30 – Do you agree with the above proposals to be included in the FCA/industry guidance for market participants? If not, please explain why.

Yes, we agree with the proposal to be included in the FCA/industry guidance for market participants.

Question 31 - Are there other areas we need to consider for the guidance?

UK Finance members have nothing further to suggest at this stage.

THE UK MARKET FOR RETAIL ORDERS

Question 32 - Are there other areas we need to consider for the guidance?

UK Finance members note the importance of retail investor participation in UK capital markets. At this stage we do not have any areas to put forward for consideration nor views on this question.

Question 33 – Do you have any suggestions for changing the regulatory regime as it applies to the execution of orders by retail clients?

See above.

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