WMBA Response to IOSCO Consultation CR02/11 Regulatory Issues Raised by the Impact of Technological change on Market Integrity and Efficiency

Introduction

The Wholesale Markets Brokers' Association (WMBA) and the London Energy Brokers' Association (LEBA) are the European Industry Associations for the wholesale intermediation of Over-the-Counter (OTC) markets in financial, energy, commodity and emissions markets and their traded derivatives. Our members are Limited Activity firms that act solely as intermediaries in the said wholesale financial markets. As IDBs, the WMBA members' principal client base is made up of global banks and primary dealers. The replies below to the questions in the paper should be seen in the context of WMBA members acting exclusively as intermediaries, and not as own account traders. (Please see www.wmba.org.uk and www.leba.org.uk for information about the associations, its members and products.)

Operating as the hub of the global financial market infrastructure, Interdealer Brokers (IDBs) are MiFID compliant and highly regulated intermediaries by virtue of their regulatory authorisation and from being subject to supervision under CAD as Limited Activity firms. Our members are neutral, independent, and multi-lateral and provide free, fair and open access to their trading venues for all suitably authorised and regulated market participants. IDBs do not take positions in the markets they operate in and their collective service as the gateway to the global financial marketplace creates price discovery and significant liquidity. All transactions, whether executed via voice, hybrid or fully electronic means, are immediately captured at the point of trade, are subject to straight-through-processing, and are made available for transparent and timely transaction reporting to the relevant regulators.

For this reason, the majority of questions in the Consultation Paper are not entirely relevant to WMBA members' activities even though they are to most of their clients. Consequently, WMBA have limited their response to the topics that are relevant to their members and on which they have relevant expertise.

Answers to the Consultation

Q4 To what extent do you believe that the use of trading control mechanisms such as circuit breakers and limit-up/limit-down systems by trading venues should be mandated? If you believe they should be mandated, should venue operators be permitted to design their own controls or should they be harmonised/coordinated across venues (including between interrelated instruments such as a derivative and its underlying)?

WMBA considers that trading control mechanisms are already adequately covered in Europe by Article 26(1) [1] and Article 43 (1) of MiFID2004/39 [2] and that introducing mandatory controls in respect of circuit breakers and limit-up/limit-down systems merely duplicates these requirements.

[1] Article 26(1) Member States shall require that investment firms and market operators operating an MTF establish and maintain effective arrangements and procedures relevant to the MTF for the regular monitoring of compliance by its users with its rules. Investment firms and market operators operating an MTF shall monitor the transactions undertaken by its users under their systems in order to identify breaches of those rules, disorderly trading conditions or conduct that may involve market abuse.

[2] Article 43(1) Member States shall require that Regulated Markets establish and maintain effective arrangements and procedures for the regular monitoring of compliance by its users with its rules Regulated Markets shall monitor the transactions undertaken by its members or participants under their systems in order to identify breaches of those rules, disorderly trading conditions or conduct that may involve market abuse.

However, should IOSCO consider the use of mandatory control mechanisms to be desirable, the systems of circuit breakers and trading halts in Europe needs to be carefully calibrated across exchanges and MTFs and at the appropriate level, such that trading is not halted too often and only where there is a genuine need for the market to pause for breath.

Q6 (i) Do you have suggestions for improvements to regulators' surveillance capabilities with respect to the markets and modern trading techniques? (ii)Who should bear the cost of investing in such capabilities and the cost of operating and supervising the markets in order to ensure fairness among market participants? Please elaborate.

A significant amount of transaction data is already collected by regulators for the markets they monitor. It is also anticipated that additional data will be collected with respect to OTC derivatives transactions under the European Markets Infrastructure Regulation (EMIR), with such data being recorded and warehoused in trade repositories. Regulators' surveillance abilities will likely be significantly enhanced by having access to this broader data set.

That being said, we appreciate that regulators are reviewing their surveillance capabilities in light of the significant changes in market practice and technology over the last few years. A thorough cost/benefit analysis should be central to decisions for significant spending in this area. Regulators providing a clear description of what they regard as the main risks involved with modern trading techniques (and how these should be monitored) will also help firms and trading venues address these risks in their trading systems.

Additional cooperation and harmonisation of approach between regulators would foster an efficient use of resources and surveillance capabilities. Firms and venues would likely benefit from a higher degree of consistency from regulators through adopting more consistent controls and techniques and thereby optimizing their own surveillance capabilities.

Q11 Should charges or fees be imposed on messages, cancellations or high order-to-trade ratios? If so, how should the fees or charges be determined and on what basis?

Whilst the imposition of these additional charges would be beneficial to its members, WMBA believes that the fees or charges imposed by venues on participants should be commercially set at the full discretion of that venue. It strongly disagrees with the concept of imposing firm limit on a ratio of orders to transactions.

Q14 To what extent do you have other comments related to the risks to market integrity and efficiency raised by the issues in this report?

In this section, we have addressed some of the ideas put forward in the "Possible Future Actions" section of the IOSCO paper that begins on page 38.

It is suggested to assess whether HFT or algorithm traders should provide for specific forms of stress testing and internal sign-off processes for new algorithms, similar to IOSCO's Principle 8 for Direct Electronic Access. We do not feel that it would be practical or valuable to define specific stress tests or sign-off processes as every strategy, as well as its testing requirements, is different. However, we believe that the market in general would benefit from higher quality exchange testing environments.

The Report also suggests the introduction of minimum tick size and minimum order book resting time. We are not aware of specific problems with how the market currently functions in these areas and therefore see no need for regulatory intervention.

Conclusions

WMBA hope that IOSCO find our response to this consultation report useful and are available to discuss the contents or provide any further information or clarification that may be required.

Wholesale Markets Brokers' Association/
London Energy Brokers' Association
St Clements House
27-28 Clements Lane
London
EC4N 7AE

Telephone: 020 3207 9740
Email: compliance@wmba.org.uk