# Annual Report
2017/18

FCA
Markets Practitioner Panel

# Chair’s foreword

I am pleased to introduce the FCA Markets Practitioner Panel Annual Report for 2017-18. I took over from Robert Mass as Chair of the Panel on 1 July 2017 and would like to pay tribute to the effective way he led the Panel to enable it to support the FCA with expert technical advice and to provide constructive challenge.

The implications of Brexit have continued to dominate our work over the past year and will do so as we approach 29 March 2019, the date of formal exit of the UK from the European Union, and beyond. We remain committed to doing all that we can to advise on how to maintain and promote the attractiveness of the UK's markets. We have sought to ensure our key concerns are priorities for the FCA in its own work and also in its role of advising government on the needs of the financial services sector.

The pace and cost of regulatory change and the demands of Brexit planning have put a heavy burden on the industry. This has been a focus of our constructive challenge to the FCA. We have represented the views of the wholesale market to encourage the FCA to take a proportionate and judgment-based approach.

Our relationship with the FCA Board and Executive Committee continues to be strong and professional. We have welcomed regular engagement with the FCA Chairman, CEO and other Board and ExCo Members. I would like to thank all the FCA staff who have presented openly and thoughtfully to us and particularly to the Panel members for giving their time and sharing their expertise. It is that experience and the open and constructive way in which it is shared that enables the Panel to be efficient and productive and to support the FCA in ensuring that relevant markets work well.

**John Trundle**
Chairman, FCA Markets Practitioner Panel

# 1

# Introduction

The Markets Practitioner Panel is a statutory panel of the FCA. It is one of a number of panels that the FCA is required to establish and maintain under the Financial Services and Markets Act 2000 (as amended), and represents the interests of practitioners who are likely to be affected by the exercise of the FCA's functions relating to financial markets.

The Panel benefits from some of its members belonging to other panels, which broadens our understanding and encourages a closer working relationship across the panels. We have also welcomed FCA Board members to a number of Panel meetings, who have helped us to understand the FCA's strategy and they have been able to hear and respond to our detailed discussions at first hand. We have a constructive working relationship with the FCA Chairman, CEO and other members of the FCA's Executive Committee. A number of ExCo members attend Panel meetings regularly both to contribute and observe; and we have close engagement with senior representatives from the FCA's Markets Policy team who seek to make effective use of the expertise available in the Panel.

The Panel meets formally six times each year, and holds sub-group meetings and conference calls on specific topics as required, as well as other strategy meetings. Following our "Panel Effectiveness" review in February 2017, where we considered how to maximize the positive impact on the FCA and the FCA Board, we have kept the Panel's membership under review. We seek to ensure it continues to reflect different market perspectives and we made a number of new appointments as listed at the end of this report. We have also engaged with other FCA panels in shared areas of interest.

This report outlines the Panel's main areas of focus and activity between 1 April 2017 and 31 March 2018. The FCA's responsibilities are very wide and there are many areas of regulatory policy and practice that affect financial markets. The Panel therefore has to proritise as to what is important for practitioners and where we can make a difference through our interaction with the FCA. We held our annual prioritisation meeting in November 2017 and established five strategic priorities for 2018:

**The UK's exit from the European Union (Brexit)**

**Liquidity**

**Market preparedness for crisis scenarios**

**Regulatory change**

**Cyber, middleware and technological resilience**

# 2

# The UK's exit from the European Union (Brexit)

Brexit has continued to be our principal focus due to the risks and uncertainties it poses for financial markets; it remains a standing agenda item for our meetings.

We were concerned throughout the year about the uncertainty as to whether an appropriate transition period after Brexit would be agreed. This uncertainty has resulted in many firms beginning to implement sub-optimal, costly and potentially irreversible contingency plans, including moving some business activities to EU27 and other locations, to protect themselves against the risk of a "cliff-edge" hard Brexit or an unfavourable outcome as to the future trading relationship for financial services. We urged the FCA to inform the government about the severe risks to market stability, especially if access to markets became restricted, and the potential impact on the financial services sector as a whole. We argued that there was a need for a transitional arrangement to be agreed as early as possible. We have welcomed the FCA's clear public messages of support for free trade and open markets in financial services.

We have encouraged the FCA to engage closely with other relevant UK regulatory stakeholders (e.g. Prudential Regulatory Authority, Bank of England, Her Majesty's Treasury) to ensure a more transparent, consistent, and holistic approach to help tackle the challenges faced. We were pleased with their coordinated announcement that they would take a pragmatic approach in grandfathering permissions for European firms post Brexit, and encouraged the FCA to press its European counterparts to be equally pragmatic.

We have welcomed the UK's and EU's political agreement in March 2018 for a transitional period, but believe significant uncertainty and risks will continue until the final EU withdrawal agreement is agreed and ratified.

# 3

# MiFID II

MiFID continued to present the biggest immediate regulatory challenge to the industry and we have discussed many different aspects during the year as we approached the 3 January 2018 implementation date. These very technical discussions included the question of the definition and treatment of systematic internalisers, the calibration of permitted tick sizes on trading venues, the collection and use of Legal Entity Identifiers particularly in jurisdictions where they are not widely used, and the rules around transaction reporting.

We raised concerns about the divergence in the market's interpretation and implementation of certain aspects of the legislation, as well as different interpretations in different jurisdictions. This was reinforced by the very short period between the finalisation of some detailed rules and the date they became effective. We welcomed the FCA's pragmatic and reasonable approach to its supervision and enforcement for firms that made every reasonable effort to be ready by the implementation date.

We also raised concerns about the potential impact on the market for research. In part, a decline in research was an inevitable consequence of the change in regulation. We highlighted, however, the risk that there may be short term disruption and that the provision of research on SME companies may prove uneconomical in the long term. It is possible a working market for research may develop and work effectively but we encouraged the FCA to monitor this market closely to see whether this is the case.

We were pleased that there was no major disruption to markets on and immediately after the MiFID II implementation date. We encouraged the FCA to continue to monitor its impact and work with its European counterparts to respond to issues as they emerge, and we will continue to highlight areas of concern that arise as the legislation is applied and interpreted.

# 4

# Asset Management Market Study

We have continued to engage extensively with the FCA on this subject and broadly supported its final recommendations, which struck a sensible balance between improving clarity for investors and ensuring transparency of fees on the one hand and minimizing disruption to existing business models. We also drew the FCA's attention to the regulatory costs associated with its recommendations and the need for consistency with MiFID II requirements.

We have highlighted the practical implementation challenges for firms to make a lot of change in parallel. Asset managers need both to improve clarity for investors on the quality and value for money of individual investment products and make important governance changes to the funds. This includes introducing greater independence into fund governance structures within a 12-month period which we thought might be too short a period. The personal responsibilities of trustees are significant which makes fewer suitable candidates willing to accept the role and a very large increase in the demand for independents in a short period could make it difficult to make appropriate appointments. We advised the FCA to extend the deadline in which to appoint independent directors and to publish guidance on their role and expectations, and were pleased to learn that the FCA would take such an approach.

We will continue to engage constructively with the FCA as it continues to develop its thinking and proposals for the asset management sector.

# 5

# Industry codes of conduct

We have supported the development of codes by the industry and the FCA's encouragement of the use of codes as an effective way to shape good conduct rather than relying on direct regulation alone. We cautioned the FCA against formal recognition of codes as this would inevitably turn them into quasi FCA rules, and it would be hard for the FCA not to be held accountable for them, including their detail and their policing. We were pleased that the FCA would take a middle ground approach by enforcing codes through the Senior Manager & Certification Regime rather than through direct regulation. This seems to us to be more proportionate and allows for the codes to be applied through judgement and firms' own internal governance processes.

# 6

# Replacement of LIBOR

The FCA has been pro-active in raising the important issue of LIBOR's long-term sustainability. It has taken steps to ensure the continuity of the benchmark in the immediate future and has sought to galvanise efforts for the market to transition to new and more representative reference rates by the end of 2021. We very much support this forward planning but question whether this transition period was feasible. LIBOR is used globally in many different types and large volumes of contracts worth trillions of dollars. A great deal of change would be needed in many different types of contracts and uses, and there would be a fundamental risk to market and economic stability if there was insufficient liquidity or a loss of continuity in the new reference rate.

We recognize that it is a complex and urgent topic and look forward to continuing our engagement with the FCA on next steps.

# 7

# Cyber, middleware and technological resilience

We have continued to discuss various aspects of cyber, middleware and technological risks and developments with the FCA during the past year. We have strongly supported its "Project Innovate" initiative that is exploring how technology can help firms reduce the administrative burdens and costs of regulations and regulatory reporting.

The interconnectedness between firms makes individual firms and the market as a whole vulnerable to successful cyber-attacks. The threat of successful attacks is high and rising. Some firms, especially smaller ones, may lack the expertise and resources to achieve a high level of cyber resilience. We have encouraged the FCA to promote greater sharing of information and best practices and to engage closely with firms on their contingency planning for security breaches. We were pleased to learn that the FCA is doing so.

We have also expressed our concern about market dependence on unregulated third-party infrastructure middleware providers (including IT services providers). These are increasingly central to the proper functioning of the market but it is hard for individual firms to assess the risks of failure. We have suggested that such firms are becoming of systemic importance and some direct regulation may be appropriate. The FCA's proposed approach of indirect oversight through regulated firms could be ineffective and impractical. At the same time, the Panel was mindful that any proposed regulation should not be such as to reduce the number of providers in the market or increase costs materially.

# 8

# Liquidity

Liquidity in all markets has remained a strategic priority for the Panel. We are pleased that the FCA, working with others such as the Bank of England, has sought to measure and analyse the evolution of liquidity.

Prudential regulatory changes since the global financial crisis have resulted in changes to financial firms' business models and trading strategies. Much less use in now made of their balance sheets to provide liquidity. In addition, significant changes in market structure as a result of MiFID II and other regulations may also affect liquidity.

At the time of this report, primary and secondary market liquidity appears to be relatively stable. Typical trade sizes have reduced but markets still appear to function. Liquidity in markets however is supported by central banks' quantitative easing (QE) policies in many jurisdictions. At some point this QE will be withdrawn. The Panel has discussed the risk that liquidity will be less readily available in the future, especially in stressed market conditions, which could exacerbate volatility. We expressed our concern that industry was less confident about how markets would behave in a period of significant stress. We encouraged the FCA to undertake scenario testing of a range of potential events that could affect market liquidity.

Both market participants and regulators want to see a stable and less levered market with more effective liquidity management. We have encouraged the FCA to continue to monitor liquidity in both equity and debt markets, to assess the effects of regulatory changes such as MiFID II as well as changes in market structure and central bank monetary operations.

# 9

# Primary Markets

The FCA proposed to create an additional premium listing segment that could be more appropriate for sovereign-controlled companies. This is a balancing act between promoting the highest standards of governance and transparency and making high quality issuers readily available to a wide group of investors. We welcomed the FCA's proposal on the basis that sufficiently high standards would be maintained and provided that remedies would be available in the event of any abuse by controlling shareholders. We have submitted, together with the FCA's Listing Authority Advisory Panel, a detailed formal response to the FCA's consultation and may look at any change to the FCA's proposals.

# 10

# FCA Strategic Initiatives

We have also drawn on the Panel's extensive financial services experience and knowledge to advise the FCA on its strategic initiatives (such as the Business Plan, the "Approach to" documents, and work on culture within financial services) and on reputational risk.

We have welcomed this strategic approach and the specific initiatives. We have encouraged the FCA to take a judgement-based and outcome-focused approach. We agree that culture and conduct are closely linked and welcome the emphasis on the former to get results on the latter. We have also encouraged the FCA to ensure that its business planning is sufficiently flexible to accommodate Brexit-related pressures. We have also reiterated our view that the FCA should always consider whether UK regulation is proportionate and competitive compared with other well-regulated jurisdictions. The Panel's view is that the UK and the firms operating in its financial market benefit enormously from being seen to be well-regulated and being overseen by a world-leading regulatory authority. That will be one component of seeking to remain the world's leading financial centre.

# Members of FCA Markets Practitioner Panel
1 April 2017 – 31 March 2018

### John Trundle
Chairman from July 2017
(previously Deputy Chairman)
CEO, Euroclear UK & Ireland

### Marisa Drew
(since August 2017)
CEO, Impact Advisory and Finance Department, Credit Suisse

### Suvro Dutta
Partner, Financial Services, KPMG LLP

### Duncan Ford
Chief Operating Officer,
Marshall Wace LLP

### Dermot McDonogh
(since May 2017)
EMEA COO and CFO,
Goldman Sachs International

### Bernard Mensah
President for EMEA and Co-Head of Global FICC Trading, Bank of America Merrill Lynch

### Abdallah Nauphal
CEO, Insight Investment Management

### James Palmer
Senior Partner, Herbert Smith Freehills

### Nikhil Rathi
CEO, London Stock Exchange plc

### Alan Trotter
CFO, Invesco Perpetual

### Tim Throsby
(since May 2017)
President of Barclays International and CEO of its Corporate and Investment Banking

### Stuart Williams
(since January 2018)
President, ICE Futures Europe,
Intercontinental Exchange Inc.

### Robert Mass
(Chairman until June 2017)
Head of International Compliance and Global Head of Securities Division Compliance,
Goldman Sachs International

### Jim Kandunias
(until November 2017)
Partner and COO, Immersion Capital LLP

### Annemarie Durbin
(until March 2018)
Chair of the FCA's Listing Authority Advisory Panel; and Non-Executive Director of WH Smith plc,
Santander UK plc and Ladbrokes plc.

### Mark Ibbotson
(until March 2018)
Group CEO, G.H. Financials

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