FINANCIAL CONDUCT AUTHORITY

Guidance on the trading venue perimeter

Consultation Paper
CP22/18**

September 2022

How to respond

We are asking for comments on this Consultation Paper (CP) by **25 November 2022**.

You can send them to us using the form on our website at: www.fca.org.uk/publications/consultation-papers/cp22-18-guidance-trading-venue-perimeter

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1 Summary

Why we are consulting

1.1 We are consulting on new guidance on the regulatory perimeter for trading venues. We want to ensure that firms have greater certainty about the permissions they require to carry on their business. Greater clarity about the perimeter helps maintain a level playing field, which supports competition. It also helps protect the integrity of the United Kingdom's (UK) financial system.

1.2 The evolution of the definition of a multilateral system and technological developments have made it more challenging to distinguish certain types of arrangements and systems from trading venues. This has created some uncertainty about the trading venue perimeter.

1.3 We are proposing new guidance in the Perimeter Guidance Manual (PERG) of our Handbook to clarify the definition of a multilateral system, as well as Questions and Answers (Q&As) on the application of the general guidance to specific types of arrangements in financial markets.

1.4 We are also seeking views but are not, at this stage, making proposals on whether regulatory obligations for trading venues can be made more proportionate for smaller firms, while maintaining high standards of market integrity.

1.5 This consultation paper (CP) is part of the Wholesale Markets Review (WMR), the review of the UK wholesale financial markets we have been conducting with HM Treasury. The WMR consultation in July 2021 asked if the trading venue perimeter should be clarified, and whether this was best done through legislation or guidance. In its WMR consultation response in March 2022, HM Treasury recognised that there is a need for greater clarity about the types of firms which need to be authorised as a trading venue and recommended that the Financial Conduct Authority (FCA) consult on guidance in the first instance. This CP addresses that recommendation, building on the responses received to the WMR.

Who this applies to

1.6 This consultation will primarily be of interest to:

- trading venues
- service companies
- investment-based crowdfunding platforms operating in primary and/or secondary markets
- interdealer brokers
- broker-dealers
- portfolio managers
- technology firms offering platforms and systems for trading

- firms providing communications systems or bulletin board services
- appointed representatives providing or using communications systems or bulletin board services, and their principals

1.7 The consultation will also be of interest to:

- trade associations
- law firms
- issuers
- investors

What we want to change

1.8 We are not modifying the perimeter, which would require legislative change. Instead, we are proposing guidance on the different elements of the definition of a multilateral system and Q&As on the application of the general guidance to specific types of arrangements, where our supervisory experience and discussions with firms suggest that further clarity would be beneficial.

1.9 We set out below some key areas that the proposed guidance covers.

- **Investment-based crowdfunding firms operating primary market platforms:** The proposed guidance indicates that a crowdfunding platform in which the business funding interests of an issuer of shares, debentures or alternative debentures are matched with those of investors does not amount to a multilateral system.
- **Bulletin boards:** The proposed guidance clarifies the demarcation between multilateral systems and bulletin boards.
- **Technology providers:** The proposed guidance draws a distinction between general purpose communications systems and multilateral systems.
- **Voice brokers:** The proposed guidance clarifies that arranging or executing client orders over the telephone without operating a trading system or facility does not constitute a multilateral system.
- **Portfolio managers operating internal matching systems:** The proposed guidance sets out the circumstances where the execution of trading interests by a portfolio manager does not constitute a multilateral system.
- **Blocking onto trading venues:** The proposed guidance indicates that where a firm operates a system for the purpose only of blocking trades onto a trading venue consistent with the intentions of the parties to the underlying transactions to trade on a trading venue, these arrangements do not amount to the operation of a multilateral system.

1.10 Where a firm does not operate a multilateral system, it will not require authorisation as a trading venue. However, a firm must consider how its arrangements relate to the permissions in Article 25 of the Financial Services and Markets Act 2000 (Regulated Activities Order) 2001 (RAO). Depending on the activity undertaken and client types, some firms may choose to be authorised as service companies. The current definition of a service company in our Handbook refers to client categorisation terminology used in the UK before the implementation of MiFID in 2007. We are proposing to update the definition of a service company in the Glossary Terms section of our Handbook, so that it also refers to the current client categorisation terminology with respect to client limitation types.

1.11 Before the UK's withdrawal from the European Union (EU), we said that we would continue to have regard to EU non-legislative material, such as Opinions and Q&As, where and if they are relevant. We consider that asking firms to continue to have regard to the European Securities and Markets Authority's (ESMA) Q&As on the trading venue perimeter when we are issuing our own guidance could lead to uncertainty for firms as to how our new guidance and the ESMA Q&As fit together. Therefore, we propose that ESMA's Q&As dealing with the trading venue perimeter – Q&As 7, 10, 11 and 12 in Section 5 of the ESMA Q&As on MiFID II and MiFIR market structures topics – should not form part of our supervisory expectations following the issuance of our final guidance. We will continue to have regard to all other Q&As in the ESMA market structures Q&As, in line with our approach to EU non-legislative materials.

Measuring success

1.12 As we said in our Strategy and the 2022/23 Business Plan, we will use a variety of metrics to assess whether our work is strengthening the UK's position in global wholesale markets. We said that we will monitor how our actions enhance UK markets.

1.13 We will consider our proposed guidance successful if it provides sufficient clarity to firms and allows us to be clear on the trading venue perimeter. We will measure this through feedback from firms (including those already operating trading venues), trade associations and law firms.

1.14 We also wish to continue to promote innovation and competition in the market. This would be assessed by looking at whether innovative firms continue to launch in the UK market and perceptions that our regime is proportionate and promotes new entrants. We will measure this through surveys.

Next steps

1.15 We are seeking views on our proposals by 25 November 2022.

1.16 Based on the responses we receive, we will finalise the draft guidance and publish a policy statement in Q2 2023.

2 The wider context

Legislative context

2.1 The UK regulatory framework that governs the buying, selling and organised trading of financial instruments, and which includes the trading venue perimeter, is spread across legislation and rules in our Handbook. They are derived from EU legislation (the Markets in Financial Instruments Directive – MiFID) that took effect in November 2007 and was subsequently amended in January 2018 (MiFID II). These were amended to address deficiencies arising as a result of the UK's withdrawal from the EU at the end of the transition period.

2.2 Under the general prohibition in section 19 of the Financial Services and Markets Act 2000 (FSMA), a person may not carry on a regulated activity by way of business in the UK, or purport to do so, unless they are either an authorised person or an exempt person. What is considered as a regulated activity is specified in the RAO. The list of regulated activities includes operating a multilateral trading facility (MTF) or an organised trading facility (OTF) and arranging deals in investments. The definition of a multilateral system is included in the UK Markets in Financial Instruments Regulation (UK MiFIR).

2.3 PERG is the section of our Handbook giving guidance about where authorisation is required, or exempt person status is available under FSMA. PERG 2 focuses on the scope of regulated activities under the RAO and PERG 13 provides guidance on the operation of an MTF and an OTF.

2.4 The requirements applicable to MTFs and OTFs are set out in the Market Conduct Sourcebook (MAR) 5 and 5A of our Handbook. MAR 5AA also contains guidance on multilateral systems.

The evolution of the trading venue perimeter

2.5 Over the years, the regulatory framework applicable to secondary markets trading has evolved, largely to reflect technological developments and changes in market structure. It has also changed as a consequence of the G20 commitment to move trading from opaque and fragmented over-the-counter (OTC) markets to transparent exchanges or electronic trading platforms.

2.6 MiFID I provided for two types of trading venues, regulated markets (RMs) and MTFs. These were characterised as multilateral systems which operate in accordance with non-discretionary rules bringing together multiple buying and selling interests in financial instruments in a way that results in a contract under the system's rules.

2.7 In 2018, the revised MiFID framework came into effect in the UK. One of the aims of the MiFID II regime was to bring more trading to regulated trading venues, thereby increasing market transparency, investor protection and access to liquidity.

2.8 MiFID II achieved this objective by introducing a new definition of multilateral system, which is common to all three types of trading venues. The definition is not restricted by whether transactions are executed through the use of discretion or according to automated systems. In addition, it does not require the conclusion of contracts under the system's rules, but that trading interests can interact in the system. This means that firms which operate systems or facilities where organised trading occurs are within the definition of multilateral system, even where the finalisation of the transactions between the counterparties occurs bilaterally outside the operator's systems.

2.9 A new category of trading venue, the OTF, was introduced. An OTF is a multilateral system which is not an RM or an MTF, and in which the operator can use discretion to bring about transactions. Under MiFID I, systems using discretion when matching orders did not fall within the definition of an RM or an MTF. Permitting the use of discretion as a mode of execution extended the trading venue perimeter and supported the delivery of the G20 commitment that all standardised OTC derivatives should be traded on regulated trading venues.

The UK trading venue perimeter

2.10 Regulated trading venues are organised markets where transferable securities and other financial contracts, like derivatives, are bought and sold. They differ from OTC trading, where contracts are traded bilaterally between firms without a market operator sitting in between. They are also distinct from unregulated trading venues which sit outside of our perimeter because the assets they trade, such as spot FX, are not financial instruments.

2.11 Regulated trading venues are subject to organisational requirements that promote fair and orderly trading, as well as obligations relating to market surveillance and transparency. This promotes investor protection and market integrity.

2.12 Article 2(1)(11) of UK MiFIR defines a multilateral system as *"any system or facility in which multiple third-party buying and selling trading interests in financial instruments are able to interact in the system"*.

2.13 This is complemented by a rule in MAR 5AA.1.1R of our Handbook, which requires that *"where a firm operates a multilateral system from an establishment in the UK, it must operate it as an MTF or an OTF"*.

2.14 The combination of the definition of multilateral system under Article 2(1)(11) of UK MiFIR and the rule in MAR 5AA.1.1R aims to ensure that all organised trading in financial instruments is carried out on regulated trading venues.

2.15 There are three types of regulated trading venues under UK MiFIR:

a. an RM is a multilateral system operated or managed by a market operator, which brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments (in the system and in accordance with its non-discretionary rules) in a way that results in a contract, in respect of the financial instruments admitted to trading under its rules or systems.

b. an MTF is a multilateral system, operated by an investment firm or a market operator, which brings together multiple third-party buying and selling interests in financial instruments (in the system and in accordance with non-discretionary rules) in a way which results in a contract.

c. an OTF is a multilateral system which is not an RM or an MTF; and in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in the system in a way that results in a contract.

2.16 A UK RM is a recognised body under FSMA (a UK Recognised Investment Exchange (RIE)). It is an exempt person for the purposes of the general prohibition, meaning it does not require permission under FSMA to carry on regulated activities as part of its business as an investment exchange.

2.17 MTFs and OTFs are trading venues that are alternatives to traditional exchanges. Unlike an RM, an MTF and an OTF can be operated by an investment firm, which requires authorisation under Part 4A of FSMA. Operators of an MTF or an OTF need to demonstrate that they comply with our rules, including those set out in MAR 5 and MAR 5A, both at authorisation and on an ongoing basis.

Activities outside the UK trading venue perimeter

2.18 Firms which do not operate a multilateral system do not require authorisation as a trading venue. However, a firm would still need to consider how its arrangements relate to the permissions in Article 25 of the RAO.

Arranging deals in investments

2.19 The regulated activity of arranging deals in investments is described in Article 25 of the RAO. Article 25 covers two different permissions:

a. arranging (bringing about deals in investments): Making arrangements for another person (whether as principal or agent) to buy, sell, subscribe for or underwrite a particular investment.
b. making arrangements with a view to transactions in investments: Making arrangements with a view to a person who participates in the arrangements buying, selling, subscribing for or underwriting investments.

2.20 As we state in PERG 8.32.2G, *"article 25(1) applies only where the arrangements bring about or would bring about the particular transaction in question. This is because of the exclusion in article 26. In the FCA's view, a person brings about or would bring about a transaction only if his involvement in the chain of events leading to the transaction is of enough importance that without that involvement it would not take place. The second limb (article 25(2)) is potentially much wider as it does not require that the arrangements would bring about particular transactions".*

2.21 Therefore, the regulated activity of "bringing about deals in investments" is aimed at arrangements that have the direct effect of concluding (i.e. bringing about) a particular transaction. Firms arranging transactions for clients without operating a multilateral facility or dealing on behalf of their clients typically rely on this permission as a basis for providing investment services.

2.22 "Making arrangements" with a view to transactions in investments relates to arrangements of an ongoing nature, which aim to facilitate other parties entering into transactions.

2.23 This activity has a broader scope and typically applies in one of two scenarios: where a person provides arrangements of some kind (1) to enable or assist investors to deal with or through a particular firm (such as the arrangements made by introducers), or (2) to facilitate the entering into of transactions directly by the parties (such as service companies, including persons who provide communication facilities for the routing of orders or the negotiation of transactions).

The service company regime

2.24 Making arrangements with a view to transactions in investments is a non-MiFID permission and can fall within the UK service company regime.

2.25 Service companies are firms whose regulated activities are restricted to making arrangements with a view to transactions in investments and agreeing to carry on that regulated activity, and whose permissions are limited to certain client types and other requirements. These firms are authorised by us to carry on investment business only with specified types of clients, as set out in their permissions, which operate as limitations on the firms' investment activities.

2.26 Many of these are technology companies that provide order routing, post-trade processing or other services to market participants, which assist them to deal in investments or arrange (bring about) deals in investments among themselves. A lighter regulatory regime applies to these firms, as set out in our Handbook requirements for service companies.

The harm we are trying to reduce

2.27 When we consulted in CP15/43 on the implementation of MiFID II in 2015, we considered providing clarity on the definition of a multilateral system. There were differences of opinion as to whether the scope of the definition of a multilateral system should be construed more broadly or more narrowly. In addition, respondents stressed the need for a common EU approach.

2.28 Therefore, at that time, we decided to issue limited guidance (PERG 13, Question 24B) and chose to support achieving a common approach through Q&As produced by ESMA.

2.29 Since MiFID II was implemented in 2018, we have continued to develop our understanding of how the trading venue perimeter operates, and of areas of potential uncertainty or where industry may lack clarity. The way in which a multilateral system is defined, coupled with innovation in the market, means it has become more difficult to distinguish clearly between unregulated communication arrangements, authorised firms that arrange deals in investments and trading venues. Following the UK's withdrawal from the EU, we are now in a position to consider approaches which are better tailored to the specificities of the UK market.

2.30 Respondents to the WMR noted that the ambiguity about the definition of a multilateral system has created some uncertainty about the perimeter and resulted in firms taking different approaches to the permissions they require. Most respondents to the WMR agreed that the definition should be clarified through guidance, rather than legislative change, to ensure that the trading venue perimeter remains flexible to accommodate changes in technology and not unduly limit innovation.

2.31 The current lack of clarity about the trading venue perimeter may cause harms to our objectives. Principally, we are concerned that some firms may be providing arrangements which constitute a multilateral system without being authorised and regulated as a trading venue. This, in turn, could undermine the policy objectives of the trading venue regime and be detrimental to investor protection and market integrity. Additionally, the inconsistent application of the regime could potentially create an unlevel playing field and negatively impact competition in the market.

How it links to our objectives

2.32 The proposals set out in this CP support the FCA's strategic objective of ensuring that the relevant markets function well. In addition, they help us achieve our Business Plan commitment of strengthening the UK's position in global wholesale markets. To achieve this, we said that we would take action to deliver a clear, well-understood proportionate regime which upholds high standards and supports innovation.

Consumer protection

2.33 One of our operational objectives is to secure an appropriate degree of protection for consumers. We expect that the proposed guidance will primarily advance our market integrity and competition objectives. It will have an indirect positive impact on investor protection by ensuring that all arrangements which constitute a multilateral system are appropriately regulated in order to secure an appropriate degree of investor protection.

Market integrity

2.34 Our proposed guidance is intended to ensure the consistent application of the trading venue regime. It will also provide greater certainty to some firms about their regulatory status and ensure they can operate in financial markets with confidence. We therefore expect that it will protect and enhance the integrity of the UK financial system.

2.35 For example, trading venues have to report market data, including transparency and transaction reporting data. This increases market transparency and liquidity, aids price formation, and protects against market abuse. Trading venues are also subject to market surveillance requirements and must ensure that their systems are resilient. Compliance with these requirements enhances market integrity and investor protection.

Competition

2.36 We expect that the proposed guidance will help support competition by better ensuring the consistent regulatory treatment of firms. Due to ambiguity around the definition of a multilateral system, some firms may be operating outside the trading venue perimeter, either by relying on incorrect regulatory permissions or by being unauthorised.

2.37 Unauthorised firms, or those subject to less stringent regulatory requirements because of holding incorrect permissions, may be at a competitive advantage compared with their appropriately authorised competitors. This negatively affects competition and could potentially create an unlevel playing field. Over time, it could also undermine confidence and trust in the operation of financial markets.

2.38 By ensuring the consistent application of regulatory requirements to all firms which fall under the definition of a multilateral system, we expect to improve competition in the market.

Wider effects of this consultation

2.39 The proposed guidance could have implications for firms other than trading venues, for example issuers of financial instruments.

Issuers

2.40 The UK Market Abuse Regulation (UK MAR) aims to increase market integrity and investor protection, enhancing the attractiveness of securities markets for capital raising. It contains prohibitions of insider dealing, unlawful disclosure of inside information and market manipulation, and provisions to prevent and detect these.

2.41 UK MAR covers financial instruments admitted to trading or traded on UK or EU trading venues. This means that issuers who have requested or been approved admission of their financial instruments to UK or EU trading venues must make certain notifications to us, including any delay in the disclosure of inside information, the provision of insider lists, and reporting managers' transactions. Our proposed guidance may affect the status of issuers of financial instruments if those instruments are admitted to trading on systems that require authorisation as trading venues.

Consequences of our proposed guidance on technology and innovation

2.42 Our focus is not on the technology being used but on whether a set of arrangements, usually involving digital systems, amount to the operation of a system or facility where multiple counterparties can interact through the broadcasting of buying and selling trading interests. We are looking at the way in which technology is used in terms of bringing buyers and sellers together and how transactions are agreed rather than concentrating on the properties of the technology.

2.43 However, we recognise that clarification of the definition of a multilateral system may have consequences on innovation and the decision of firms to offer new products and services. On the one hand, increased clarity might support innovation and competition where firms have greater confidence about the regulatory status of their business.

On the other hand, some firms (e.g. those currently operating outside the perimeter) might decide to exit the market where the cost of being regulated as a trading venue is deemed disproportionate to the scale and nature of their business.

Equality and diversity considerations

2.44 We have considered the equality and diversity issues that may arise from the proposals in this CP.

2.45 Overall, we do not consider that the proposals materially impact any of the groups with protected characteristics under the Equality Act 2010. However, we will continue to consider the equality and diversity implications of the proposals during the consultation period and will revisit them when making the final guidance.

2.46 We welcome comments on this as part of the consultation.

3 Proposals

Existing guidance on the trading venue perimeter

3.1 The MAR Sourcebook of our Handbook is where current guidance on multilateral systems sits. MAR 5AA.1.2G says:

"In our view, any system that merely receives, pools, aggregates and broadcasts indications of interest, bids and offers or prices should not be considered a multilateral system. This means that a bulletin board should not be considered a multilateral system. The reason is that there is no reaction of one trading interest to another within these types of facilities. However, operating such a facility may amount to performing the activity of making arrangements with a view to transactions in investments."

3.2 This guidance does not adequately clarify all the essential elements of the definition of a multilateral system. It also does not provide detailed insight on the application of the definition of a multilateral system to some of the most common arrangements or systems used in financial markets to support trading. To address this, we propose to provide additional guidance on the key concept of a multilateral system and how this should be applied to specific types of arrangements.

3.3 Under the European Union (Withdrawal) Act 2018, the broad range of non-legislative material (often referred to as Level 3 material) produced by EU institutions was not incorporated into UK law. This Level 3 material includes Guidelines and Recommendations on the application of EU law, Q&As and Opinions.

3.4 In March 2019 we published our approach to EU non-legislative materials, in which we stated that our supervisory expectation in respect of Guidelines and Recommendations remains the same. In relation to other EU-non legislative material, such as Opinions and Q&As, we noted that: "*We will continue to have regard to EU non-legislative material where and if they are relevant, taking account of Brexit and ongoing domestic legislation. Firms, market participants and stakeholders should also continue to do so.*"

3.5 ESMA published Q&As on MiFID II and MiFIR market structures topics (ESMA market structures Q&As) which include Q&As dealing with the trading venue perimeter. The purpose of these Q&As is to promote common supervisory approaches and practices across the EU. Sections 5.1 and 5.2 of those Q&As deal with issues related to trading venues, including the trading venue perimeter.

3.6 In light of our supervisory experience and the responses to the WMR, we are now proposing to publish our own guidance on the trading venue perimeter. It is appropriate therefore to consider whether the ESMA market structures Q&As dealing with the trading venue perimeter, that were published before the UK left the EU on 31 December 2020, should continue to form part of our supervisory expectations.

3.7 We consider that asking firms, market participants and stakeholders to continue to have regard to the ESMA Q&As on the trading venue perimeter when we are issuing our own guidance could lead to uncertainty for firms as to how our new guidance and the ESMA Q&As fit together. Therefore, we propose that ESMA's Q&As dealing with the trading venue perimeter – Q&As 7, 10, 11 and 12 in Section 5 of the ESMA market structures Q&As – should not form part of our supervisory expectations following the issuance of our final guidance. We will continue to have regard to all other Q&As in the ESMA market structures Q&As, in line with our approach to EU non-legislative materials.

> **Q1:** **Do you agree with our approach that following issuance of our final guidance, Q&As 7, 10, 11 and 12 in Section 5 of the ESMA market structures Q&As should not form part of our supervisory expectations?**

New guidance on the definition of a multilateral system

3.8 We propose to issue general guidance in PERG 13 on our interpretation of each of the four elements of the definition of a multilateral system that firms should have regard to when considering whether their activity requires authorisation as a trading venue.

3.9 A multilateral system comprises the following main elements:

- **a.** it has the characteristics of a trading system or facility;
- **b.** it comprises multiple third-party buying and selling trading interests;
- **c.** it allows trading interests to interact in the system; and
- **d.** those trading interests are in financial instruments.

3.10 Please refer to Q24C of the draft Handbook text in Annex B of Appendix 1 to this CP. We provide further detail on our proposed guidance below.

a. Characteristics of a system or facility

3.11 A multilateral system needs to have the characteristics of a trading system or facility. Recital 7 of UK MiFIR clarifies that the term, "system", includes markets composed of a set of rules and a trading platform, as well as those only functioning based on a set of rules. The rules relate to how multiple third-party trading interests in financial instruments can interact in the system (see below). The rules could be reflected in contracts and/or operating procedures set by the operator that the participants or members of the facility comply with.

3.12 Recital 7 also sets out the key functions that an operator of a system should perform – in accordance with the rules or protocols established by the operator itself – for the system to be considered a trading venue: determining the conditions for members or participants to have access to the facility, setting the conditions for the admission of financial instruments to trading, establishing the rules for trading between members and reporting.

3.13 As such, the concept of a system or facility in MiFID II systems is technology neutral for these purposes, as shown by the several types of trading systems referred to in Table 1 of Annex I to MiFID RTS 1 and Annex I to MiFID RTS 2.

3.14 General purpose communications systems, such as chatroom facilities, would not as such amount to trading systems or facilities unless they are part of a facility performing the functions discussed in recital 7 where it is intended to bring about transactions.

3.15 Even if the operator of a general purpose communications system is not operating a multilateral system, a person using that system to operate a trading system or facility will operate a multilateral system if the other elements of the definition of a multilateral system are met.

3.16 We would have regard to whether a system has features specifically designed to enable the interaction of trading interests in financial instruments. We would consider the role of the operator in relation to determining who can access the system and under what conditions (including the fees paid), the monitoring of the performance of the system and of the behaviour of users, the types of financial instruments that can be traded and the reporting of information to members.

3.17 Our assessment of whether there is a system or facility would also take into consideration a wider range of factors. For example, we would consider the target users and the actual use of the system by them, any relevant restrictions on how the system may be used, whether the system is designed to enable trading of any kind, as well as the determinants of the remuneration of the operator, and whether these are linked to the interaction of trading interests in the system.

3.18 Therefore, for example, if a system is designed as a general communications system but it is part of a facility that is operated for the purpose of arranging transactions in financial instruments, we would consider that system a trading venue if the other elements of the definition of a multilateral system are met.

3.19 It is possible that a firm operates more than one piece of technology which, when taken together, have the characteristics of a trading system or facility operated by a person.

b. Multiple third-party buying and selling trading interests

3.20 There need to be multiple third-party buying and selling trading interests in the system for the system to be a multilateral system. Recital 7 UK MiFIR clarifies that the expression "buying and selling trading interests" is to be understood in a broad sense and includes orders, quotes and indications of interest.

3.21 The inclusion of the word "third-party" in this expression makes it clear that the focus of the trading interests in question is those of the users of the system rather than that of the system operator.

3.22 The fact that when any two persons negotiate within the system, they do so between themselves, does not mean that the system is bilateral rather than multilateral. Instead, what matters is whether the system, at the point of entry, is designed to enable one person to interact with others. This is the service a person receives as a user of the system.

c. Interaction within the system

3.23 Multiple third-party trading interests must be able to interact in the system for it to be a multilateral system. A multilateral system involves the bringing together of third-party trading interests (see also recital 7 UK MiFIR).

3.24 Interaction takes the form of an exchange of information relevant to the essential terms of a transaction in financial instruments (being price, quantity or subject matter) and other actions signalling intent to conclude a trade. Accordingly, in our view, a system which enables this information to be inputted and then responded to in the system would allow trading interests to interact in the system.

3.25 Interaction between trading interests can arise in a system because the system:

- matches trading interests within the system; or
- allows users to respond within the system to other users' trading interests, including by communicating in relation to, negotiating or accepting essential terms of a transaction.

3.26 The concept of interaction between trading interests in the system does not require execution and the settlement of a transaction to be entered into within the system as long as it is with a view to the counterparties agreeing the contractual terms of a trade.

d. Financial instruments

3.27 The interaction of multiple third-party buying and selling trading interests in the system must be in financial instruments for the system to be a multilateral system. As such, it does not include, for example, systems to trade foreign exchange spot contracts.

3.28 A financial instrument is an instrument specified in Part 1 of Schedule 2 to the RAO. Further guidance on financial instruments is available in PERG 13.4.

Q2: Do you agree with our interpretation of the definition of a multilateral system?

Q3: Are there any other relevant characteristics to a multilateral system that should be taken into account?

Q&As

3.29 We propose to issue Q&As in PERG 13 on the application of the general guidance to specific types of arrangements covering voice brokers; portfolio managers operating internal matching systems; investment-based crowdfunding firms operating primary market platforms; operators of bulletin boards; and firms operating systems for the purpose of blocking trades onto regulated trading venues.

Voice broking

3.30 Following the implementation of MiFID II, organised trading systems operating voice or voice and electronic hybrid trading systems were required to apply for authorisation as an OTF. There are also other firms that provide voice broking services without being authorised as trading venues. The reason these firms are not authorised as trading venues is because they consider that their arrangements do not amount to a trading system or facility, which is one of the elements of the definition of a multilateral system.

3.31 Arranging trades over the telephone (voice broking) may be part of a multilateral system by being the only method for bringing about transactions. However, generally, voice broking is part of a multilateral system when operating in conjunction with other modes of execution.

3.32 In our view, arranging trades over the telephone is not a sufficient condition for a firm to seek authorisation as a trading venue. When considering whether a voice broking system constitutes a multilateral system, we would look at the characteristics of a trading system or facility and the functions performed by the operator as discussed above.

3.33 We set out our proposed guidance on voice broking in Q24D of the draft Handbook text in Annex B of Appendix 1 to this CP. This should be read in conjunction with the guidance on the 'characteristics of a system or facility' in Q24C.

Q24D. Does voice broking involve the operation of a multilateral system?

Voice broking may but need not comprise the operation of a multilateral system.

Merely arranging or executing client orders over the telephone does not constitute a multilateral system, although it may amount to other investment services such as reception and transmission or execution of orders on behalf of clients.

A trading system or facility could, however, take the form of a voice trading system or a hybrid system (as referred to in Annex I MiFID RTS 2 and Annex I MiFID RTS 1). For example, a firm that operates a platform where trading interests of clients are broadcast to other users and then engages in voice broking to enable negotiation between these parties would operate a trading system or facility, unless Q24F applies. Voice broking may also be part of a multilateral system when operating in conjunction with other modes of execution such as electronic order books.

Q4: Do you agree with our proposed guidance in relation to voice broking?

Internal crossing by portfolio managers

3.34 At the time of the implementation of MiFID II, concerns were raised by investment managers about how the definition of a multilateral system and Article 23(2) of MiFIR on internal crossing systems might affect crossing they carry out between trades

being undertaken on behalf of different mandates. Several respondents to the WMR consultation asked for guidance to be issued on this subject.

3.35 We have therefore sought to set out the circumstances where a portfolio manager does not operate a multilateral system when it executes trading interests relating to funds it manages.

3.36 Please refer to Q24E of the draft Handbook text in Annex B of Appendix 1 to this CP.

> **Q24E. Does a firm that undertakes portfolio management operate a multilateral system by operating an internal matching system to execute trading interests relating to the portfolio of one of its clients against trading interests relating to the portfolio of another of its clients?**
>
> No. A firm engaged in portfolio management, in whatever capacity, must exercise discretion in relation to the financial instruments it manages. We do not consider that a portfolio manager operates a multilateral system when, in the exercise of this discretion, it executes trading interests relating to the portfolio of one of its clients (which may be a fund) against the trading interests relating to the portfolio of another of its clients in an internal matching system. We also do not consider that it is the purpose of COLL 6.9.9R and FUND 1.4.3R to prevent a UCITS management company or an external AIFM that is a full-scope UK AIFM from doing this in these circumstances. This is because in these circumstances the portfolio manager is the only user of the system and hence, there is no interaction of multiple third-party trading interests in the system.

Q5: **Do you agree with our proposed guidance relating to internal crossing by portfolio managers?**

Blocking onto trading venues

3.37 Blocking onto trading venues occurs where an investment firm arranges a transaction between two clients, and that transaction is then executed between the counterparties on a regulated trading venue.

3.38 In our view, where a firm operates a system for the purpose only of blocking trades onto a regulated trading venue, where those instruments are admitted to trading and consistent with the intentions of the parties to the underlying transactions, these arrangements do not amount to the operation of a multilateral system.

3.39 Please refer to Q24F of the draft Handbook text in Annex B of Appendix 1 to this CP.

> **Q24F. Does a firm using a system to block trades on behalf of clients operate a multilateral system?**
>
> No, if a firm operates a system for the purpose only of blocking trades onto a trading venue consistent with the intentions of the parties to the underlying transactions to trade on a trading venue, for example, when arranging a large-in-scale trade in accordance with the rules of the venue, in our view these arrangements do not amount to the operation of a multilateral system in the case of UK MiFIR or otherwise.

Q6: Do you agree with our proposed guidance relating to blocking onto trading venues?

Crowdfunding platforms operating in primary markets

3.40 Investment-based crowdfunding firms provide primary market platforms, which allow firms to raise capital and investors (mainly retail) to take exposure to their businesses by buying shares or debentures. In our view, there is a distinction between the matching of funding interests and the interaction of trading interests referred to in the definition of a multilateral system.

3.41 Therefore, in our view, a crowdfunding platform in which the business funding interests of an issuer of shares, debentures or alternative debentures are matched with those of investors does not amount to a multilateral system.

3.42 Please refer to Q24G of the draft Handbook text in Annex B of Appendix 1 to this CP.

Q24G. Would a crowdfunding platform be regarded as a multilateral system?

We would not regard as a multilateral system a crowdfunding platform in which the business funding interests of an issuer of shares, debentures or alternative debentures as expressed in an offer made by that issuer, on the one hand, are matched with those of investors on the other.

A bulletin board provided to assist investors is not itself a multilateral system where the trading interests would not be able to interact within the system. By contrast, a crowdfunding platform in which multiple third-party buying and selling trading interests of investors in financial instruments are able to interact within a system (for example, in a secondary market) would be a multilateral system.

Q7: Do you agree with our interpretation to regard a crowdfunding platform operating only in primary markets as not involving the operation of a multilateral system?

Bulletin boards

3.43 In 2017, in the run up to the implementation of MiFID II, we held several roundtables with operators of crowdfunding platforms. Those discussions focused on the issue of when a secondary trading facility offered by such firms could be regarded as a bulletin board rather than a multilateral system.

3.44 Since MiFID II was implemented, the issue of bulletin boards and the trading venue perimeter has continued to give rise to questions and supervisory challenges. New crowdfunding firms who were not part of the 2017 discussions have sought authorisation with business plans that have involved the operation of secondary trading facilities. Questions have also been raised about whether existing crowdfunding firms have taken a consistent approach to the functionality of their secondary trading facilities.

3.45 Recital 8 of MiFIR implies that a bulletin board should not be considered a multilateral system. This is because, unlike a trading venue, a bulletin board merely advertises trading interests without enabling the interaction of those interests.

3.46 The proposed guidance clarifies the demarcation between a bulletin board and a multilateral system. Please refer to Q24H-Q24L of the draft Handbook text in Annex B of Appendix 1 to this CP.

Q24H. What is a bulletin board?

There is no definition of a bulletin board. Recital 8 UK MiFIR, however, refers to 'facilities where there is no genuine trade execution or arranging taking place in the system, such as bulletin boards used for advertising buying and selling interests' or 'other entities aggregating or pooling potential buying or selling interests' and implies that such bulletin boards or entities should not be considered a multilateral system.

Q24I. Is a bulletin board a multilateral system?

No, the reason is that, whilst trading interests (including information relevant to essential terms of a transaction in financial instruments (being price, quantity or subject matter)) can be posted on a bulletin board, trading interests are not able to interact in such a system. In light of Q24C (see the section on 'Trading interests are able to interact with each other') above, we would not regard a firm as operating only a bulletin board if:

- it matches trading interests within the system;
- it allows users to respond within the system to other users' trading interests, including by communicating in relation to, negotiating or accepting essential terms of a transaction; or
- users can commit to or enter into contracts for the sale / purchase of the financial instruments (i.e. execute transactions) within the system.

Please see Q24J-L below for further guidance on bulletin boards.

Q24J. Can the operator of a bulletin board as described in Q24H assist users with exchanging contact details?

The operator of a bulletin board could (subject to data protection legislation) provide for the publication on the bulletin board of contact details of users advertising buying and selling interests on that bulletin board, so that users can use these to contact each other bilaterally outside the system.

However, some users may have reservations about the publication of their contact details. In these circumstances one possibility might be for them to agree to sharing contact details on a case-by-case basis. Any such request should be limited to a request to see another user's contact details and not extend to communicating in relation to, negotiating or accepting essential terms of a transaction (being price, quantity or subject matter).

Q24K. Can an operator of a bulletin board as described in Q24H provide template documentation to assist its users with negotiating and executing transactions?

Yes, an operator of a bulletin board can make available template documentation for download by users of a bulletin board. It can also require users to use this template documentation. This will not mean that the bulletin board is a multilateral system, provided that users use the template documentation to negotiate and execute transactions bilaterally outside the system. The operator should not, however, complete the template documentation in relation to the essential terms of these transactions (being price, quantity or subject matter).

Q24L. Can an operator of a bulletin board as described in Q24H provide post-trade services?

Yes, it is possible for the operator of a bulletin board to provide post-trade services, including in relation to settlement. This might include, for example, assisting with the transfer of funds or registering the transfer of financial instruments. The operator could be informed by users of the bulletin board that they have entered into a contract for the sale / purchase of a financial instrument, i.e. executed a transaction, bilaterally outside the system and then provide post-trade services in relation to that transaction to them. Providing these post-trade services will in these circumstances not by itself require the operator to have permission for operating a multilateral trading facility or operating an organised trading facility. The operator should however consider whether the post-trade services provided may include any payment services (see PERG 15.3) or electronic money issuance (see PERG 3A).

Q8: **Do you agree with our interpretation of the characteristics of a bulletin board?**

The definition of a service company

3.47 A service company is a firm that is authorised only to make arrangements with a view to transactions in investments. A service company is authorised by us to carry on investment business only with specified types of clients, as set out in their permissions, which operates as a limitation on the firm's investment activities.

3.48 In the Glossary Terms section of our Handbook a service company is defined as:

"a firm whose only permitted activities are making arrangements with a view to transactions in investments, and agreeing to carry on that regulated activity, and whose Part 4A permission:

a. *incorporates a limitation substantially to the effect that the firm carry on regulated activities only with market counterparties or intermediate customers; and*
b. *includes requirements substantially to the effect that the firm must not:*
   i. *guarantee, or otherwise accept responsibility for, the performance, by a participant in arrangements made by the firm in carrying on regulated activities, of obligations undertaken by that participant in connection with those arrangements; or*
   ii. *approve any financial promotion on behalf of any other person or any specified class of persons; or*
   iii. *in carrying on its regulated activities, provide services otherwise than in accordance with documents (of a kind specified in the requirement) provided by the firm to the FCA.*

3.49 The current definition of a service company refers to client categorisation terminology, which was used in the UK before the implementation of MiFID. In particular, the client limitation types refer to "market counterparties" and "intermediate customers".

3.50 In 2007, MiFID introduced new client categories, which were broadly similar to the then UK customer types. Limitations on firms' permissions relating to the clients they could deal with were affected by the implementation of these MiFID client categories. To smooth the transition, HM Treasury and the Financial Services Authority (FSA) took the approach of mapping UK customer types to the MiFID-based client categories as set out in the table below.

UK customer type applied to activity on a firm's permission	Mapping to MiFID-based client categories
Private customers only	Retail clients
Intermediate customers only	Professional clients
Private and intermediate customers	Retail and professional clients
Intermediate customers and market counterparties	Professional clients and eligible counterparties

3.51 Despite this broader mapping exercise in 2007, the definition of a service company was not updated to reflect the MiFID terminology. Therefore, as part of this consultation, we are proposing to update the relevant section of the Glossary Terms so that the definition of a service company also refers to the current client categorisation terminology with respect to client limitation types. This is intended as a mechanical change and, therefore, should have no adverse impact for firms.

3.52 We are proposing to add to the limitation "professional clients" and "eligible counterparties" client types, whilst also preserving the references to "market counterparties" and "intermediate customers". This will avoid the need for existing authorised firms which are service companies to apply to vary their Part 4A permissions and enable any future applicants to apply for a permission with a limitation comprising the current client types.

3.53 We are proposing to update the client type limitation as follows:

"incorporates a limitation substantially to the effect that the firm carry on regulated activities only with ***one or more*** *of market counterparties, intermediate customers,* ***professional clients or eligible counterparties****"*

3.54 We have set out our proposed amendments to the Glossary definition of a service company in Annex A of the draft Handbook text in Appendix 1 to this CP.

Q9: Do you agree with our approach to updating the Glossary definition of a service company in relation to client limitation types?

4 For discussion - potential areas for future change

Potential future changes to the trading venue regime

4.1 We are not currently proposing to make any changes to the requirements applicable to firms operating an MTF or an OTF. Our view, consistent with the approach outlined in this CP, is that functionally similar arrangements should be subject to a level playing field of regulation. Therefore, firms operating a multilateral system should apply for authorisation as an RM, an MTF or an OTF.

4.2 However, we recognise that the complexity of these regimes may act as a barrier to entry by firms and result in firms structuring their arrangements to operate outside the trading venue perimeter, with detriment to users in terms of quality, choice and innovation. Establishing a more calibrated approach in light of the risks posed by firms – with smaller firms subject to more proportionate regulatory obligations or exempted from certain requirements – could reduce the regulatory burden associated with becoming a trading venue and potentially facilitate more firms to broaden their service offering and apply for authorisation as a trading venue.

4.3 We therefore want to use this opportunity to seek views from firms and other interested stakeholders on specific aspects of the MTF and OTF regimes, which are perceived to create the greatest barriers to entry to the market for smaller firms. We would also welcome views on the extent to which the existing service company regime already addresses this issue.

4.4 We continue to be committed to maintaining the highest standards of regulation. Therefore, any potential future changes to the regime will be guided by reducing costs and burdens for firms, without lowering regulatory standards and market integrity.

Q10: **Which regulatory requirements applicable to MTFs and OTFs are most likely to create barriers to entry to the trading venue market for smaller firms?**

Q11: **Does the existing service company regime already address concerns regarding these barriers to entry?**

Q12: **Based on which criteria should firms be potentially subject to a more scalable set of requirements?**

Annex 1
Questions in this paper

Q1: Do you agree with our approach that following issuance of our final guidance, Q&As 7, 10, 11 and 12 in Section 5 of the ESMA market structures Q&As should not form part of our supervisory expectations?

Q2: Do you agree with our interpretation of the definition of a multilateral system?

Q3: Are there any other relevant characteristics to a multilateral system that should be taken into account?

Q4: Do you agree with our proposed guidance in relation to voice broking?

Q5: Do you agree with our proposed guidance relating to internal crossing by portfolio managers?

Q6: Do you agree with our proposed guidance relating to blocking onto trading venues?

Q7: Do you agree with our interpretation to regard a crowdfunding platform operating only in primary markets as not involving the operation of a multilateral system?

Q8: Do you agree with our interpretation of the characteristics of a bulletin board?

Q9: Do you agree with our approach to updating the Glossary definition of a service company in relation to client limitation types?

Q10: Which regulatory requirements applicable to MTFs and OTFs are most likely to create barriers to entry to the trading venue market for smaller firms?

Q11: Does the existing service company regime already address concerns regarding these barriers to entry?

Q12: Based on which criteria should firms be potentially subject to a more scalable set of requirements?

Annex 2
Cost benefit analysis

1. There is no statutory requirement in the Financial Services and Markets Act 2000 for a cost benefit analysis (CBA) on guidance. In line with our approach to analysing costs and benefits, it is our policy to produce a CBA for general guidance about rules where we identify *"an element of novelty which may be in effect prescriptive or prohibitive such that significant costs may be incurred"*. Our guidance primarily relates to the UK Markets in Financial Instruments Regulation concept of a multilateral system, although this concept is also relevant to rule 5AA.1.1R in our Market Conduct Sourcebook.

2. The guidance focuses on certain issues where our supervisory experience and discussions with firms suggest that there is a need for greater clarity about what types of firms need to be authorised as a trading venue. We consider that it is consistent with our approach to authorisation and supervision and, therefore has the benefit of confirming our position more widely. Further, in some instances, the guidance should provide assurance to firms about the appropriateness of their current permissions whilst having minimal cost implications.

3. Since the guidance is primarily clarificatory, we expect that in most cases firms' interpretation of the definition of a multilateral system should align with it, and so firms should hold the appropriate regulatory permissions. As such, most firms will not suffer significant costs beyond the need to familiarise themselves with the guidance.

4. For some firms, because of the manner in which they have interpreted the law, there may be an element of novelty and/or cost implications associated with compliance with the guidance. These firms may incur higher costs relating to the review of their arrangements and the assessment of the appropriateness of their current regulatory permissions. Based on our supervisory experience, we expect the number of firms affected in this way will be limited.

5. Where the guidance has an impact, the cost implications are highly dependent on the specific circumstances of individual firms and the detailed elements of their current arrangements. The impact will also depend significantly on the strategies those firms choose to pursue. Some firms may decide to adjust their arrangements, for example by winding down or modifying certain functionalities to mitigate the risk of breaching the trading venue perimeter. Others may seek authorisation as a trading venue.

6. We do not think it is reasonably practicable to quantify the associated costs and benefits to firms. This is in part because it would not be proportionate to conduct a detailed supervisory review prior to our finalised guidance coming into effect, and given that some of the firms in the relevant population are currently unauthorised. We have provided monetary values for the impacts where we believe it is reasonably practicable to do so, as well as estimates of outcomes in other dimensions.

7. We have weighed up these dimensions and believe the guidance will deliver net benefits for firms, investors and our resources. We welcome any views or comments on the CBA, including your feedback on any costs or benefits we have not considered.

Benefits

Benefits to firms

a. **Certainty over regulatory status:** Market participants can only compete effectively in financial markets if they have certainty about their regulatory status and the status of their competitors. The guidance will help reduce the risk of holding incorrect permissions for firms and ensure that there is confidence in how the trading venue regime operates.
b. **Consistency of application of regulatory requirements:** The guidance will help ensure that the regulatory framework is clear, well-understood and trusted by all market participants. It should ensure that the regime is applied consistently and that firms are subject to appropriate regulatory requirements and oversight. By doing so, the guidance will enhance market integrity and competition among trading venues.
c. **Reduced legal costs:** We expect the guidance to help reduce the need for firms to seek clarification directly from the FCA, and reduce the likelihood that applications for authorisation are rejected because they do not align with our approach to the trading venue perimeter. In turn, this should reduce legal costs for firms.
d. **Reduction in some compliance costs:** Firms will benefit from efficiency savings relating to compliance because of greater clarity regarding our approach. We expect firms following the guidance to benefit from a reduction in the number of queries from the FCA.

Benefits to investors

a. **Reduced harm and higher investor confidence:** Our guidance is intended to ensure the consistent application of the trading venue regime. It will have an indirect positive impact on investor protection by ensuring that all arrangements which constitute a multilateral system are appropriately regulated in order to secure an appropriate degree of investor protection. This should reduce the likelihood that risks materialise and cause harms to investors and markets, and increase investor confidence in the integrity of these markets.

Benefits to the FCA

a. **More efficient use of resources:** We will be able to refer to our finalised guidance in discussions with firms about applications for authorisation and ongoing supervision, which should allow us to use our resources more efficiently and discharge our functions more effectively.

Costs

Costs to firms

8. Firms will need to familiarise themselves with the guidance.

a. **Familiarisation and gap analysis:**
We have estimated familiarisation costs using our standardised cost model. We expect some firms will need to undertake a review of their arrangements to assess if they constitute a multilateral system and whether they hold the appropriate regulatory permissions.

Since the guidance is primarily clarificatory, we assume minor costs for compliance staff to read the consultation paper (34 pages) and standard costs to read the legal instrument (8 pages). We assume that there are 300 words per page and reading speed is 100 words per minute. This means the consultation would take 2 hours to read, and the legal review would take 1 hour for a small firm, 7 hours for a medium firm, and 18 hours for a large firm. Based on this, approximate per firm costs would be £177 for a small firm, £895 for a medium firm, and £1,848 for a large firm. For the reasons explained above, it is not reasonably practicable to estimate the total number or size of firms affected.

9. If firms identify a gap between our approach to the trading venue perimeter and the regulatory permissions they currently hold, they may decide to wind down certain functionalities to ensure that they remain outside the trading venue perimeter. We expect this may be relevant, for example, for operators of bulletin boards, which may be able to enact certain changes to their platform functionalities to ensure they do not constitute a multilateral system and, hence, cross the trading venue perimeter.

Enacting changes to platform functionalities: Firms wishing to avoid authorisation as a trading venue will need to ensure that their platforms do not enable the interaction of trading interests related to financial instruments. As such, firms may need to withdraw certain functionalities, such as 'buttons' which allow investors to enter contracts within the system.

Where firms make changes to their arrangements because they do not wish to seek authorisation as a trading venue, costs may include IT, legal and project costs, and potential loss of revenue from reducing the services they offer. These will be firm specific, but as a general point, we do not expect the guidance to impact firms' core functions and so expect the costs to be limited.

10. In some circumstances, firms will need to seek different regulatory permissions. We expect, for example, that this may be relevant to some technology firms which operate systems specifically designed to facilitate the interaction of trading interests in financial instruments, although this will ultimately depend on whether other elements of the definition of a multilateral system are also met. Additional costs associated with seeking authorisation as a trading venue include:

a. **Authorisation processing and ongoing fees associated with becoming an MTF or an OTF:** Applications to operate an MTF or an OTF are complex and require assessment from specialist areas across the FCA. The processing fee for a new application for authorisation to become an MTF or an OTF is £50k; and a variation of permission is £25k. Firms will also be subject to periodic (annual) fees, which will

vary according to their annual income. Under our 2022/23 fee structure, operators of MTFs and OTFs with an annual income up to and including £100k pay a minimum fee of £1,222. Firms reporting annual income above £100k pay a variable fee rate of £2.27 for every £1k or part £1k of annual income over £100k. Our rules on fees are set out in the Fees Manual section of the Handbook.

b. **Market data processor (MDP) on-boarding:** Trading venues must report market data to the FCA. The MDP system enables firms to submit market data to us and provides the interface to our Financial Instruments Reference Data System and the Financial Instruments Transparency System. As part of the authorisation process, firms must apply to connect to the MDP system and demonstrate conformance with our technical specification to be on-boarded. The fee for an application for connection to the MDP is charged based on pricing categories, and is in the region of £10-£25k. However, additional costs may be incurred as firms may need to build connections or use a third-party provider.
c. **Systems, resilience and outsourcing:** As part of the authorisation process, we assess whether the firm's systems, resilience and outsourcing are sufficiently robust. To demonstrate this, the firm is required, for example, to provide a penetration test of their systems for resilience purposes. These costs will vary according to the arrangements firms already have in place. Firms will also face ongoing costs of maintaining their arrangements in line with the relevant regulatory requirements.
d. **Surveillance arrangements and procedures:** Trading venues must have effective systems and controls and surveillance arrangements for monitoring market abuse, which we assess as part of the authorisation process. Implementing market surveillance arrangements are likely to lead to additional costs, such as systems and human resources. Firms will also face ongoing costs of maintaining their arrangements in line with the relevant regulatory requirements.
e. **Capital requirements:** An investment firm authorised to operate an MTF; or to operate an OTF with a limitation that prevents it from carrying out matched principal trading or dealing on own account will be subject to a permanent minimum capital requirement of £150k. However, where the investment firm operates an OTF without a limitation that prevents both matched principal trading and dealing on own account, it will be subject to a permanent minimum capital requirement of £750k (see our Prudential sourcebook for MiFID investment firms more details).
f. **Compliance resourcing:** Firms that seek authorisation as trading venues typically require additional compliance resources given the relative complexity of the regime. There will be cost implications – both one-off (i.e. at the point of authorisation) and on an ongoing basis – associated with compliance with the regulatory requirements of the trading venue regime.

Costs to the FCA

a. **Supervisory resources:** There could be an opportunity cost from supervisory resources being used to assess firms' arrangements and/or regulatory permissions in light of our finalised guidance. We expect this to be included in normal supervisory activities. In the longer term, the guidance should result in more efficient use of our supervisory resources, due to the increased clarity of our approach. Overall, we expect any incremental costs to the FCA to be small.

Annex 3
Compatibility statement

Compliance with legal requirements

1. This Annex records the FCA's compliance with a number of legal requirements applicable to the proposals in this consultation, including an explanation of the FCA's reasons for concluding that our proposals in this consultation are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA).

2. Section 1B(1) FSMA requires that the FCA, when discharging its general functions, as far as reasonably possible, to act in a way which is compatible with its strategic objective and advances one or more of its operational objectives, and its general duty under s. 1B(5)(a) FSMA to have regard to the regulatory principles in s. 3B FSMA. The FCA also needs, so far as is compatible with acting in a way that advances the consumer protection objective or the integrity objective, to carry out its general functions in a way that promotes effective competition in the interests of consumers.

3. This Annex also sets out the FCA's view of how the proposed guidance is compatible with the duty on the FCA to discharge its general functions (which include the giving of general guidance) in a way which promotes effective competition in the interests of consumers (s. 1B(4)). This duty applies in so far as promoting competition is compatible with advancing the FCA's consumer protection and/or integrity objectives.

4. In addition, this Annex explains how we have considered the recommendations made by the Treasury under s. 1JA FSMA about aspects of the economic policy of His Majesty's Government to which we should have regard in connection with our general duties.

5. This Annex includes our assessment of the equality and diversity implications of these proposals.

6. Under the Legislative and Regulatory Reform Act 2006 (LRRA) the FCA is subject to requirements to have regard to a number of high-level 'Principles' in the exercise of some of our regulatory functions and to have regard to a 'Regulators' Code' when determining general policies and principles and giving general guidance (but not when exercising other legislative functions like making rules). This Annex sets out how we have complied with requirements under the LRRA.

The FCA's objectives and regulatory principles: Compatibility statement

7. The proposed guidance set out in this consultation is intended to advance the FCA's market integrity and consumer protection objectives. Ensuring that relevant activity is conducted on regulated trading venues will enhance transparency and improve the

quality of information available to market participants. This will help improve efficiency of price formation, enhancing the information available to market participants and so reduce implicit costs of trading. Our proposed guidance should also increase certainty for firms and hence increase trust and contribute to the orderly operation of financial markets.

8. We also expect that the proposed guidance will advance our competition objective by maintaining a level playing field in the market. Ensuring that multilateral systems are subject to the same regulatory requirements and oversight should ensure the fair and consistent regulatory treatment of firms. This should increase participation in UK markets.

9. We consider that proposed guidance is compatible with the FCA's strategic objective of ensuring that the relevant markets function well. Clarifying the trading venue perimeter will provide greater certainty to some firms about their regulatory status and ensure that they can operate in financial markets with more confidence. It is also consistent with ensuring efficient and resilient markets and greater transparency for all participants. For the purposes of the FCA's strategic objective, "relevant markets" are defined by s. 1F FSMA.

10. In preparing the proposed guidance set out in this consultation, the FCA has had regard to the regulatory principles set out in s. 3B FSMA.

The need to use our resources in the most efficient and economic way

11. The proposals set out in this consultation are consistent with an efficient and economic use of our resources. Our supervisory resources will be used effectively as our approach seeks to ensure that firms have greater certainty about the regulatory permissions they require.

The principle that a burden or restriction should be proportionate to the benefits

12. The CBA in Annex 2 sets out the costs and benefits of the proposals in this CP. We believe that the benefits of these proposals outweigh the costs.

The desirability of sustainable growth in the economy of the United Kingdom in the medium or long term

13. We have had regard to this principle including the government's aim of seeing more competition and innovation in all sectors of the UK's financial industry.

The general principle that consumers should take responsibility for their decisions

14. The proposals do not depart from the general principle that consumers take responsibility for their decisions.

The responsibilities of senior management

15. We have had regard to this principle and do not consider that our proposals undermine it.

The principle that we should exercise of our functions as transparently as possible

16. We consider that by consulting on our proposals we are acting in accordance with this principle. We have also spoken to a wide range of firms and other stakeholders in developing our proposed guidance.

17. In formulating these proposals, the FCA has had regard to the importance of taking action intended to minimise the extent to which it is possible for a business carried on (i) by an authorised person or a recognised investment exchange; or (ii) in contravention of the general prohibition, to be used for a purpose connected with financial crime (as required by s. 1B(5)(b) FSMA).

Expected effect on mutual societies

18. The FCA does not expect the proposals in this paper to have a significantly different impact on mutual societies.

Equality and diversity

19. We are required under the Equality Act 2010 in exercising our functions to 'have due regard' to the need to eliminate discrimination, harassment, victimisation and any other conduct prohibited by or under the Act, advance equality of opportunity between persons who share a relevant protected characteristic and those who do not, to and foster good relations between people who share a protected characteristic and those who do not.

20. As part of this, we ensure the equality and diversity implications of any new policy proposals are considered. The outcome of our consideration in relation to these matters in this case is stated in paragraph 2.45 of the Consultation Paper.

Legislative and Regulatory Reform Act 2006 (LRRA)

21. In producing the proposed guidance, we have had due regard to the principles in the LRRA and the provisions in the Regulators' Compliance Code for the parts of the proposals that consist of general policies, principles or giving guidance. We are satisfied that we have had regard to the principles in the LRRA and to the Regulators' Compliance Code to the extent that our proposals consist of guidance and we consider that our proposals are proportionate and consistent with the need for increased clarity.

22. The proposed guidance should help promote transparency and consistency in supervisory decision making, in line with our obligations under Part 2 of the LRRA.

Annex 4
Abbreviations used in this paper

Abbreviation	Description
AIFM	Alternative Investment Fund Manager
CBA	Cost Benefit Analysis
COLL	Collective Investment Schemes Sourcebook
CP	Consultation Paper
ESMA	European Securities and Markets Authority
EU	European Union
FCA	Financial Conduct Authority
FSA	Financial Services Authority
FSMA	Financial Services and Markets Act 2000
FUND	Investment Funds Sourcebook
FX	Foreign Exchange
G20	Group of Twenty
LRRA	Legislative and Regulatory Reform Act 2006
MAR	Market Conduct Sourcebook
MDP	Market Data Processor
MiFID	Markets in Financial Instruments Directive
MiFIR	Markets in Financial Instruments Regulation
MTF	Multilateral Trading Facility
OTC	Over-the-counter
OTF	Organised Trading Facility
PERG	Perimeter Guidance Manual

Abbreviation	Description
Q&A	Questions and Answers
RAO	Financial Services and Markets Act 2000 (Regulated Activities) Order 2001
RIE	Recognised Investment Exchange
RM	Regulated Market
RTS	Regulatory Technical Standards
UCITS	Undertakings for Collective Investments in Transferable Securities
UK	United Kingdom
UK MAR	Onshored Regulation (EU) No 596/2014 on Market Abuse
UK MiFIR	Onshored Regulation (EU) No 600/2014 on Markets in Financial Instruments
WMR	Wholesale Markets Review

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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Appendix 1
Draft Handbook text

PERIMETER GUIDANCE (TRADING VENUES) INSTRUMENT 2022

Powers exercised

A. The Financial Conduct Authority ("the FCA") makes this instrument in the exercise of section 139A (Power of the FCA to give guidance) of the Financial Services and Markets Act 2000 ("the Act").

Commencement

B. This instrument comes into force on [*date*].

Amendments to the Handbook

C. The Glossary of definitions is amended in accordance with Annex A to this instrument.

Amendments to material outside the Handbook

D. The Perimeter Guidance manual (PERG) is amended in accordance with Annex B to this instrument.

Citation

E. This instrument may be cited as the Perimeter Guidance (Trading Venues) Instrument 2022.

By order of the Board
[*date*]

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Amend the following definition as shown:

service company	a *firm* whose only *permitted activities* are *making arrangements with a view to transactions in investments*, and *agreeing to carry on that regulated activity*, and whose *Part 4A permission*: (a) incorporates a *limitation* substantially to the effect that the *firm* carry on *regulated activities* only with one or more of *market counterparties,* ~~or~~ *intermediate customers*, *professional clients* or *eligible counterparties*; and …

Annex B

Amendments to the Perimeter Guidance manual (PERG)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

13 Guidance on the scope of the UK provisions which implemented MiFID

…

13.3 Investment Services and Activities

…

Multilateral system

~~**Q24B. Where can I find more information about what a multilateral system is (article 4.1(19)?**~~

~~There is some *guidance* on multilateral systems in *MAR* 5AA.1.2G.~~

Q24C. What is a multilateral system?

A *multilateral system* is a system or facility in which multiple third-party buying and selling trading interests in *financial instruments* are able to interact in the system (see article 2(1)(11) UK MiFIR).

A *multilateral system*, for these purposes, comprises the following main elements:

- it has the characteristics of a trading system or facility;
- it comprises multiple third-party buying and selling trading interests;
- it allows trading interests to interact in the system; and
- those trading interests are in *financial instruments*.

We provide guidance on each of these elements below.

Characteristics of a system or facility

A *multilateral system* has the characteristics of a trading system or facility. Recital 7 UK MiFIR clarifies that a trading system or facility includes markets composed of a set of rules and a trading platform, as well as those only functioning on the basis of a set of rules. The rules relate to how multiple third-party trading interests in *financial instruments* are able to interact in the system (see below). The rules could be reflected in contracts and/or operating procedures. As such, a system is technology neutral for these purposes, as shown by the different types of trading system referred to in Annex I to *MiFID RTS 1*, and Annex I to *MiFID RTS 2*. For guidance on voice broking, please refer to Q24D below.

General purpose communications systems would not as such amount to trading systems or facilities. This means that the following services in and of themselves would not amount to operating a *multilateral system*:

- acting as an internet services provider;
- providing a telephone network;
- operating a website; or
- providing chatroom facilities.

Even if the operator of the general purpose communication system is not operating a *multilateral system*, a person using that system to operate a trading system or facility will operate a *multilateral system* if the other elements of the definition of a *multilateral system* are met.

If a system has features specifically designed to enable the interaction of trading interests in *financial instruments*, this would indicate that it is a trading system or facility. More generally, we will consider the role of the operator and its monitoring of the performance of the system. Operating the platform requires more than simply providing technology or software. Our assessment of whether there is a trading system or facility will also take into consideration a wider range of factors, including for example:

- its target users and the actual use of a system by its users;
- any relevant restrictions on how the system may be used and their practical effect;
- whether the system is designed to enable trading of any kind amongst users; and
- the determinants of the remuneration of the operator and whether these are linked, directly or indirectly, to the interaction of trading interests in *financial instruments* in the system.

Accordingly, whilst general communications systems, for example, are used for the purposes of trading *financial instruments*, they will not amount to a *multilateral system* unless they were ever operated by a person for these purposes and then subject to these criteria.

It is possible that a firm operates more than one piece of technology which when taken together have the characteristics of a trading system or facility.

There are multiple third-party buying and selling trading interests

There need to be multiple third-party buying and selling trading interests for a system to be a *multilateral system*. Recital 7 UK MiFIR clarifies that the expression 'buying and selling trading interests' is to be understood in a broad sense and includes orders, quotes and indications of interest.

The inclusion of the words 'third-party' in this expression makes it clear that the trading interests in question are not the trading interests of the system operator.

The fact that when any two persons negotiate within the system they do so between themselves does not mean that the system is bilateral rather than multilateral. Instead, what matters is whether the system, at the point of entry, enables one person to interact

potentially with multiple others (other than the operator). This is the service a person receives as a user of the system.

Trading interests are able to interact in the system

Multiple third-party trading interests must also be able to interact in the system for it to be a *multilateral system*. A *multilateral system* involves the bringing together of third-party trading interests (see also recital 7 UK MiFIR).

Interaction takes the form of an exchange of information relevant to essential terms of a transaction in *financial instruments* (being price, quantity or subject matter). Accordingly, in our view, a system which enables this information to be inputted and then responded to in the system would allow trading interests to interact in the system.

Interaction between trading interests can arise in a system because the system:

- matches trading interests within its system; or
- allows users to respond within the system to other users' trading interests, including by communicating in relation to, negotiating or accepting essential terms of a transaction.

Interaction between trading interests in the system does not require a contract to be entered into for the sale/purchase of *financial instruments* (i.e. execution of a transaction to take place) within the system if it is with a view to the parties agreeing the terms of a trade.

As clarified by recital 8 UK MiFIR, any system that merely receives, pools, aggregates and broadcasts trading interests should not be considered a *multilateral system*. This means that a bulletin board should not be considered a trading venue because there is no interaction between trading interests within its system. Similarly, a system which simply notifies the parties of general expressions of interest in relation to *financial instruments* does not amount to an interaction of trading interests in the system. For further guidance on bulletin boards, please refer to Q24H-Q24L below. In addition, neither the service of portfolio compression, which reduces non-market risks in derivative portfolios without changing the market risk, nor post-trade confirmation services, constitute a *multilateral system* by themselves.

Financial instruments

The interaction of multiple third-party buying and selling trading interests in the system must be in *financial instruments* for the system to be a *multilateral system*. A *financial instrument* is an instrument specified in Part 1 of Schedule 2 to the *Regulated Activities Order*. Please refer to *PERG* 13.4 for further guidance on *financial instruments*.

Trading venue perimeter – specific cases

Q24D. Does voice broking involve the operation of a *multilateral system*?

Voice broking may but need not comprise the operation of a *multilateral system*.

Merely arranging or executing client orders over the telephone does not constitute a *multilateral system*, although it may amount to other investment services such as reception and transmission or execution of orders on behalf of clients.

A trading system or facility could, however, take the form of a voice trading system or a hybrid system (as referred to in Annex I *MiFID RTS 2* and Annex I *MiFID RTS 1*). For example, a firm that operates a platform where trading interests of clients are broadcast to other users and then engages in voice broking to enable negotiation between these parties would operate a trading system or facility, unless Q24F applies. Voice broking may also be part of a *multilateral system* when operating in conjunction with other modes of execution such as electronic order books.

Q24E. Does a firm that undertakes *portfolio management* operate a *multilateral system* by operating an internal matching system to execute trading interests relating to the portfolio of one of its *clients* against trading interests relating to the portfolio of another of its *clients*?

No. A firm engaged in *portfolio management*, in whatever capacity, must exercise discretion in relation to the *financial instruments* it manages. We do not consider that a portfolio manager operates a *multilateral system* when, in the exercise of this discretion, it executes trading interests relating to the portfolio of one of its *clients* (which may be a fund) against the trading interests relating to the portfolio of another of its *clients* in an internal matching system. We also do not consider that it is the purpose of *COLL* 6.9.9R and *FUND* 1.4.3R to prevent a *UCITS management company* or an *external AIFM* that is a *full-scope UK AIFM* from doing this in these circumstances. This is because in these circumstances the portfolio manager is the only user of the system and hence, there is no interaction of multiple third-party trading interests in the system.

Q24F. Does a firm using a system to block trades on behalf of clients operate a *multilateral system*?

No, if a firm operates a system for the purpose only of blocking trades onto a trading venue consistent with the intentions of the parties to the underlying transactions to trade on a trading venue, for example, when arranging a large-in-scale trade in accordance with the rules of the venue, in our view these arrangements do not amount to the operation of a *multilateral system* in the case of UK MiFIR or otherwise.

Q24G. Would a crowdfunding platform be regarded as a *multilateral system*?

We would not regard as a *multilateral system* a crowdfunding platform in which the business funding interests of an issuer of *shares, debentures* or *alternative debentures* as expressed in an offer made by that issuer, on the one hand, are matched with those of investors on the other.

A bulletin board provided to assist investors is not itself a *multilateral system* where the trading interests would not be able to interact within the system. By contrast, a crowdfunding platform in which multiple third-party buying and selling trading interests of investors in *financial instruments* are able to interact within a system (for example, in a secondary market) would be a *multilateral system*.

Bulletin boards

Q24H. What is a bulletin board?

There is no definition of a bulletin board. Recital 8 UK MiFIR, however, refers to ‘facilities where there is no genuine trade execution or arranging taking place in the system, such as bulletin boards used for advertising buying and selling interests’ or ‘other entities aggregating or pooling potential buying or selling interests’ and implies that such bulletin boards or entities should not be considered a *multilateral system*.

Q24I. Is a bulletin board a *multilateral system*?

No, the reason is that, whilst trading interests (including information relevant to essential terms of a transaction in *financial instruments* (being price, quantity or subject matter)) can be posted on a bulletin board, trading interests are not able to interact in such a system. In light of Q24C (see the section on ‘Trading interests are able to interact with each other’) above, we would not regard a firm as operating only a bulletin board if:

- it matches trading interests within the system;
- it allows users to respond within the system to other users’ trading interests, including by communicating in relation to, negotiating or accepting essential terms of a transaction; or
- users can commit to or enter into contracts for the sale/purchase of the *financial instruments* (i.e. execute transactions) within the system.

Please see Q24J-L below for further guidance on bulletin boards.

Q24J. Can the operator of a bulletin board as described in Q24H assist users with exchanging contact details?

The operator of a bulletin board could (subject to data protection legislation) provide for the publication on the bulletin board of contact details of users advertising buying and selling interests on that bulletin board, so that users can use these to contact each other bilaterally outside the system.

However, some users may have reservations about the publication of their contact details. In these circumstances, one possibility might be for them to agree to sharing contract details on a case-by-case basis. Any such request should be limited to a request to see another user’s contact details and not extend to communicating in relation to, negotiating or accepting essential terms of a transaction (being price, quantity or subject matter).

Q24K. Can an operator of a bulletin board as described in Q24H provide template documentation to assist its users with negotiating and executing transactions?

Yes, an operator of a bulletin board can make available template documentation for download by users of a bulletin board. It can also require users to use this template documentation. This will not mean that the bulletin board is a *multilateral system*, provided that users use the template documentation to negotiate and execute transactions

bilaterally outside the system. The operator should not, however, complete the template documentation in relation to the essential terms of these transactions (being price, quantity or subject matter).

Q24L. Can an operator of a bulletin board as described in Q24H provide post-trade services?

Yes, it is possible for the operator of a bulletin board to provide post-trade services, including in relation to settlement. This might include, for example, assisting with the transfer of funds or registering the transfer of *financial instruments*. The operator could be informed by users of the bulletin board that they have entered into a contract for the sale/purchase of a *financial instrument*, i.e. executed a transaction, bilaterally outside the system and then provide post-trade services in relation to that transaction to them. Providing these post-trade services will in these circumstances not by itself require the operator to have permission for *operating a multilateral trading facility* or *operating an organised trading facility*. The operator should, however, consider whether the post-trade services provided may include any *payment services* (see *PERG* 15.3) or *electronic money* issuance (see *PERG* 3A).

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