

## **1. Suspending the use of pre-trade transparency waivers for a trading venue for the purposes of the Double Volume Cap under Article 5(3B) UK MiFIR<sup>1</sup>**

### *Background*

1. The European Union's (EU) Markets in Financial Instruments Regulation (MiFIR) includes a provision known as the "Double Volume Cap" or "DVC" as a mechanism for protecting the price formation process in equity financial instruments by limiting the level of "dark" trading on trading venues. Dark trading is where trading takes place without pre-trade transparency i.e. without the details of the terms on which market participants are prepared to trade being publicly advertised. MiFIR permits trading venues to use waivers that, in specified circumstances, allow trading to take place without this pre-trade transparency.
2. Under the DVC, if the proportion of trading taking place under two of the waivers from pre-trade transparency for an individual equity instrument exceeds certain thresholds, then the use of those waivers is suspended for a period of 6 months. The suspension for that equity instrument may either apply across the market as a whole (if trading under the waivers across all trading venues exceeds 8 per cent of total trading across the EU in that equity instrument) or on a specific trading venue (if trading under the waivers on that venue exceeds 4 per cent of total trading across the EU in that equity instrument). In the EU, DVC suspensions take place on a monthly basis after the European Securities and Markets Authority (ESMA) publishes data showing which instruments have exceeded the thresholds.
3. The UK MiFIR gives us a power for the duration of the "transparency transitional period"<sup>2</sup> to make and renew suspensions of waivers under the DVC without undertaking and publishing the calculations of whether trading has exceeded the 4 and 8 per cent thresholds. Under these powers, we may suspend the use of a waiver for period of up to six months and may renew a suspension where we feel that the circumstances which led us to impose the suspension of a waiver continue to exist.

### *The legal framework for our power*

4. We may exercise the power to suspend pre-trade transparency waivers if we consider it necessary to advance our integrity objective under section 1D of the Financial Services and Markets Act 2000 (FSMA). In deciding whether that test has been met we -
  - a. must take into account -
    - i. our consumer protection objective and competition objective under sections 1C and 1E of FSMA;
    - ii. the thresholds applying under Article 5 of MiFIR as it has effect in the EU; and
    - iii. the most recent information published by ESMA under Article 5(4), 5(5) and 5(6) of MiFIR before exit day.
  - b. we may also take into account -
    - i. any relevant information produced under Article 3 of UK MiFIR, or under equivalent pre-trading transparency requirements in other jurisdictions, about

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<sup>1</sup> UK MiFIR is the UK version of Regulation (EU) No. 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012, which is part of UK law by virtue of the European Union (Withdrawal) Act, 2018.

<sup>2</sup> A period of four years from the UK's exit from the EU or shorter if directed by the Treasury.

the use of the waiver in the United Kingdom, or under equivalent waiver arrangements in any other country, in relation to the financial instrument; and

- ii. any relevant information available in relation to trading volumes in the financial instrument concerned, whether in the United Kingdom or in any other country.

### *Policy*

5. We shall consider information that may indicate that suspending the use of a waiver would be necessary to advance our integrity objective. Such information may come from UK trading venues or from market participants and users, from our own analysis or from the analysis of other authorities with whom we co-operate. We will also consider the extent to which such trading is being used to minimise execution costs for end investors. We may seek to assess how dark trading is impacting on measures of market quality such as those we considered in Occasional Paper No.29: Aggregate Market Quality Implications of Dark Trading<sup>3</sup>.
6. In relation to instruments with significant trading on trading venues in the EU as well as in the UK we shall pay close attention to the market-wide suspensions announced by ESMA under the DVC regime as it applies in the EU, in particular where ESMA calculations take account of UK trading data. There is likely to be a strong case for using our power in these circumstances, particularly given that ESMA has confirmed it will include data from the UK, albeit less and less each month, in its calculations until the figures it publishes in April 2020.
7. We will publish our decision to use this power on our website.

## **2. Withdrawing a pre-trade transparency waiver granted for a trading venue in respect of non-equity financial instruments under Article 9(3) UK MiFIR**

### *Background*

8. Under MiFIR, national regulators can grant trading venues the ability to use one or more of a set of pre-trade transparency waivers in respect of trading in bonds, structured finance products, emissions allowances or derivatives. Where a waiver is granted, it allows trading to occur in specified circumstances, without the terms on which market participants are willing to trade being made public in advance of execution. National regulators are also granted the power, on their own initiative or at the request of another national regulator in the EU, to stop a trading venue using a waiver it has been previously granted permission to use. The power to withdraw waivers is to protect the price formation process from possible abuses of the use of waivers.
9. The power for us to withdraw permission to use a pre-trade transparency waiver has been onshored by the [Markets in Financial Instruments \(Amendment\) \(EU Exit\) Regulations 2018](#) in respect of trading in bonds, structured finance products, emissions allowances or derivatives and is a permanent power.

### *The legal framework for our power*

10. We may use the power to remove permission to use a pre-trade transparency waiver where:
  - (i) we observe that the waiver is being used in a way that deviates from its original purpose; or
  - (ii) we consider that the waiver is being used to circumvent the pre-trade transparency requirements for trading in bonds, structured finance products, emissions allowances or derivatives.

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<sup>3</sup> <https://www.fca.org.uk/publications/occasional-papers/no-29-aggregate-market-quality-implications-dark-trading>  
statements-of-policy-mifid-transparency-regime.DOCX

11. Under UK MiFIR the reference to exercising this power at the request of another national regulator has been deleted.

#### *Policy*

12. To be granted a pre-trade transparency waiver, trading venues need to provide us with information on how the waiver will be used. This provides us with a baseline against which to judge how waivers function in practice and whether their use deviates in a significant way from their original purpose. A waiver would, for example, be used in a way that deviates from its original purpose where its functionality is different from that described to us in the application.

13. We would usually assess whether a waiver could be used to circumvent the aims of the pre-trade transparency regime before granting a waiver. The waivers are there to provide an exception to the general requirement for pre-trade transparency. Circumvention therefore would need to involve something more than just significant use of a waiver. There would need to be some sign that the waiver was able to be used in circumstances that were either not envisaged by the trading venue itself, or where the trading venue and/or market participants were taking a very expansive view of what is permitted under the terms of the waiver.

14. We will publish our decision to use this power on our website.

### **3. Suspending the pre-trade transparency obligations for trading venues in respect of non-equity financial instruments referred to in Article 8 under Article 9(4A) of UK MiFIR and suspending the post-trade transparency obligations for trading venues in respect of non-equities referred to in Article 10 under Article 11(2A) of UK MiFIR**

#### *Background*

15. Under MiFIR, national regulators can temporarily suspend pre-trade transparency obligations (requirements to make public the terms on which market participants are willing to trade) and post-trade transparency obligations (requirements to make public the terms on which market participants have concluded transactions) for trading venues in respect of a class of bonds, structured finance products, emission allowances and derivatives where the liquidity in that class of instruments declines by a specified amount. This is to ensure that, in difficult market circumstances, the transparency regime does not unnecessarily impair liquidity.

16. The above powers have been onshored by the [Markets in Financial Instruments \(Amendment\) \(EU Exit\) Regulations 2018](#). We have also been given a power for the duration of the transparency transitional period to allow us to suspend the same pre-trade and post-trade transparency obligations in relation to specific financial instruments or specific classes of financial instruments without being bound to specific thresholds for declines in liquidity.

#### *The legal framework for our powers*

17. We may exercise the power to suspend pre-trade transparency and post-trade transparency obligations for trading venues in respect of bonds, structured finance products, emission allowances and derivatives if we consider it necessary to advance our integrity objective under section 1D of FSMA. In making our decision we:

a. must also take into account –

i. our consumer protection objective and competition objective under sections 1C and 1E of FSMA;

ii. the most recent specified threshold published before exit day on the basis of calculations under Articles 16 of Commission Delegated Regulation (EU) 2017/583 supplementing Regulation (EU) No 600/2014 on markets in financial instruments with regard to regulatory technical standards on transparency requirements for trading venues and investment firms in respect of bonds, structured finance products, emission allowances and derivatives;

b. we may also take into account any other relevant information available in relation to liquidity in the relevant class of financial instrument concerned, whether in the United Kingdom or in any other country.

### *Policy*

18. From the context in which we were granted these powers (i.e. maintaining continuity of the legal framework) and the factors we must and may take into account in using the power, we do not view this power as being intended to be used to curtail the application of pre-trade and post-trade transparency for bonds, structured finance products, emission allowances and derivatives in the ordinary course of events. Our intention is to use it only in circumstances in which there is a significant fall in liquidity, which we interpret as going beyond normal short-term fluctuations in trading activity, and where we assess that the suspending the obligations would have a material prospect of improving market functioning. Any decision made is likely to relate to both pre- and post-trade transparency, reflecting the fact that the quantitative trigger in MiFIR for suspensions is the same for both types of transparency. We will take into account suspensions of transparency obligations by national regulators in the EU under their powers in MiFIR if we think that this might adversely affect the level of trading on trading venues in the UK.
19. We will review any suspensions we introduce on at least a quarterly basis to check whether there remain grounds for pre and post-trade transparency to continue to be suspended.
20. We will publish our decision to use these powers on our website.

## **4. Determining the standard market size of equity instruments for the purposes of the pre-trade transparency regime for Systematic Internalisers under Article 14(6A) of UK MiFIR**

### *Background*

21. Under MiFIR, investment firms acting as market makers when trading outside a trading venue – known as “systematic internalisers” (SIs) - are subject to pre-trade transparency obligations. This is to ensure the integrity of the price formation process and to ensure SIs do not have an unfair advantage over trading venues.
22. SIs are required to make public the prices they are prepared to trade at when trading in equity instruments that have a liquid market in sizes up to a threshold known as Standard Market Size (SMS). There are seven bands or ‘class’ of SMS and equity instruments are allocated to them on the basis of annual calculations by ESMA of the arithmetic average value of orders for those instruments.
23. The above requirements have been onshored by the [Markets in Financial Instruments \(Amendment\) \(EU Exit\) Regulations 2018 with the ESMA calculation requirements transferring to the FCA. These regulations also](#) give us a power for the duration of the transparency transitional period to be able to determine the class of each share, depositary receipt, ETF, certificate and other similar financial instruments (and therefore its SMS) otherwise than on the basis of the arithmetic average value of the orders executed in the market in that instrument.

### *Legal framework for our power*

24. We may exercise this power if we consider that it is necessary to do so to advance our integrity objective under section 1D of FSMA.
25. To determine the class of financial instruments referred to above we:
- a. must take into account –
    - i. our consumer protection objective and competition objective under sections 1C and 1E of FSMA;
    - ii. the most recent classes determined for the financial instruments in question before exit day;
  - b. may also take into account –
    - i. any other relevant information available in relation to the value of the orders executed in relation to the financial instrument concerned, whether in the United Kingdom or in any other country.

### *Policy*

26. If we do not exercise this power during the transparency transitional period then the SMS class determined for an equity instrument before the UK's exit from the EU will apply. In using this power, we expect to take account of any updates to SMS calculations by ESMA for illiquid instruments traded on trading venues in the UK as well as the EU, in particular where those ESMA calculations take account of UK trading data.
27. We will also need to consider using the power to make any adjustments to the SMS class to which an instrument is allocated both on the normal annual cycle provided for in MiFIR, as well as in response to any significant and sustained changes in the trading of an instrument on an intra-year basis. SMS is a means of trying to protect SIs from being exposed to undue risk as a result of making the quotes on which they are prepared to trade publicly available. Therefore, we would change an instrument's SMS class if we thought that changes in the trading of an instrument meant that the existing SMS for that instrument was no longer appropriate because either it exposed liquidity providers to too much risk and needed to be lowered, or liquidity providers could cope with increased transparency because of the strength of liquidity and an increase was merited. The proxy used in MiFIR for the level of undue risk is the average size of orders. We will use data from trading venues and publicly available sources to look at the evolution of order sizes and could also look for signs of shifts in the volume of trading on trading venues as against SIs, for evidence that an instrument should change SMS class.
28. We will publish our decisions using this power on our website.

## **5. Suspending the post-trade transparency obligations for non-equity transactions taking place outside a trading venue referred to in Article 21(1) under Article 21(4A) of UK MiFIR**

### *Background*

29. MiFIR requires that investment firms make public the details of completed transactions in financial instruments that take place outside a trading venue (i.e. 'over-the-counter') where the instrument traded is also traded on a trading venue. The transactions have to be made public through a firm authorised under MiFID and known as an Approved Publication Arrangement (APA).
30. UK MiFIR gives us a power for the duration of the transparency transitional period to suspend post-trade transparency obligations for trading venues in relation to non-equity instruments. During the transparency transitional period, the FCA may also suspend the obligation on

investment firms to make public the volume and price of transactions through an APA, as set out in Article 21(1) of UK MiFIR.

31. The FCA may exercise this power in relation to a specified class of financial instruments if we consider it necessary to do so to advance our integrity objective under section 1D of FSMA.

#### *Legal framework*

32. We may exercise the power to suspend post-trade transparency if we consider it necessary to advance our integrity objective under section 1D of the Financial Services and Markets Act. In making our decision:

- a. we must also take into account –
  - i. our consumer protection objective and competition objective under sections 1C and 1E of FSMA;
  - ii. the most recent specified threshold published before exit day on the basis of calculations under Article 16 of Commission Delegated Regulation (EU) 2017/583 supplementing Regulation (EU) No 600/2014 on markets in financial instruments with regard to regulatory technical standards on transparency requirements for trading venues and investment firms in respect of bonds, structured finance products, emission allowances and derivatives;
  
- b. we may also take into account any other relevant information available in relation to liquidity in the relevant class of financial instrument concerned, whether in the United Kingdom or in any other country.

#### *Policy*

33. We will consider the exercise of this power when we are exercising the power to suspend post-trade transparency obligations for trading venues in Section 3. Suspending the obligations for both trading on trading venues and on an over-the-counter basis will avoid a situation in which the decision on where to trade is based on factors related to the regulatory environment rather than the economics of the specific trade. We will therefore consider data from APAs and other publicly available sources in making this decision.

34. We will publish our decision to use this power on our website.

### **6. Directing that an equity instrument is to be treated as not having a liquid market under Articles 5(1) and 5(1A) of Commission Delegated Regulation 2017/567**

#### *Background*

35. Under MiFIR, firms acting as market makers in equities when trading outside a trading venue – known as ‘systematic internalisers’ (SIs) – are required to make public the quotes they are prepared to trade at when trading in equity instruments that have a liquid market in sizes up to a threshold known as Standard Market Size (SMS). The determination of whether an equity instrument has a liquid market is based, in the main, on calculations by ESMA looking at whether an instrument exceeds thresholds for:

- a. the free float
- b. the average daily number of transactions
- c. the average daily turnover

36. The above determination of liquidity, which is included in Commission Delegated Regulation 2017/567, has been onshored and amended by the [Markets in Financial Instruments \(Amendment\) \(EU Exit\) Regulations 2018](#). [These regulations also](#) say that during the transparency transitional period and until we make an assessment of whether an instrument has a liquid market, the most recent assessment made by ESMA prior to exit day shall apply (there are separate arrangements for instruments admitted to trading for the first time after Exit Day). However, we are given a temporary power to direct that the previous assessment is set aside such that the instrument is deemed no longer to have a liquid market. If we direct that an instrument does not have a liquid market, then SIs trading that instrument will not be required to make public firm quotes in that instrument.
37. We are required by the the onshored Commission Delegated Regulation 2017/267 [to make at least one determination of the liquidity of all equity instruments traded on UK trading venues based on free float, transactions and turnover no later than the date 6 weeks before the end of the transparency transitional period](#).

#### *The legal framework*

38. We may disregard the most recent liquidity assessment made in relation to a relevant instrument before exit day and direct that the instrument concerned is to be treated as not having a liquid market if —
- (i) an assessment would ordinarily be required under the timetable set out in MiFIR but we do not have the data to carry out such an assessment; and
  - (ii) it appears to us that—
    - a. the liquidity of the financial instrument in UK trading venues has reduced since the relevant instrument was last assessed, and
    - b. the extent of the reduction in liquidity is so material that continuing to treat the relevant instrument as having a liquid market would have an adverse effect on price formation in that instrument.

#### *Policy*

39. We do not view this power as being intended to suspend the ordinary operation of the transparency regime for SIs. It is to enable us to suspend those obligations where SIs may be exposed to heightened risk as a result of being required to make firm public quotes in what has become an illiquid financial instrument. We will therefore, based on data from trading venues, APAs and publicly available sources, look for evidence of significant declines in transactions and turnover such that it no longer makes sense to regard an instrument as liquid.
40. We will publish our decision to use this power on our website.