

MEMO# 24946

February 4, 2011

ICI Letter on European Commission Review of MiFID

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CLOSED-END INVESTMENT COMPANY MEMBERS No. 17-11 RE: ICI LETTER ON EUROPEAN COMMISSION REVIEW OF MIFID

As we previously informed you, the European Commission ("Commission") has issued a public consultation ("Consultation") on the review of the Markets in Financial Instruments Directive ("MiFID"). ICI has filed a letter, a copy of which is attached, on the Consultation. The most significant aspects of the letter are summarized below.

Scope of Proposed Changes to MiFID

The letter discusses several aspects of the scope of the proposed changes to MiFID. In particular, the letter urges the Commission to be cognizant of the potential to create unintended consequences for investors through the implementation of a wide range of changes to MiFID in a short timeframe. The letter also urges the Commission to carefully balance the potential costs and benefits of new regulations. The letter states that issues relating to the derivatives and fixed-income markets are ripe for reform but cautions against using the regulations overseeing the equities markets as the basis for changes in those markets given their differences and complexity. Finally, the letter recommends that the Commission allow sufficient time to closely study the comments received by market participants on the Consultation.

Developments in Market Structures

The Consultation discusses several significant developments in the structure of the European markets and the impact of these developments on trading. Most significantly, the Consultation requests comment on several issues relating to "automated trading" and

“high frequency trading.”

The letter recommends that the Commission define “automated trading” more precisely to ensure that it does not capture trading which is not the focus of the MiFID review. The letter also notes the lack of information about high frequency trading and therefore supports Commission efforts to increase transparency for this segment of the marketplace.

The letter discusses several other aspects of “automated trading.” Most significantly, the letter supports Commission action to clearly define practices that may constitute market abuse to ensure adequate enforcement of illegal activities and urges the Commission to act to address the increasing number of order cancellations. The letter states that the idea that all high frequency traders over a specified minimum quantitative threshold be required to be authorized is worthy of further examination. The letter also provides comments on issues such as co-location, sponsored access and circuit breakers. Specifically, the letter notes that standards by which the Commission could judge co-location services are whether the terms of the services are non-discriminatory and the fees are equitably allocated and reasonable; supports requiring firms that provide sponsored access to have in place robust risk controls and filters to detect errors or attempts to misuse facilities; and supports the implementation by operators of trading venues of proper risk controls and arrangements to mitigate the risk of errors generated by automated trading.

Pre- and Post-Trade Transparency

The Consultation discusses the importance of pre- and post-trade transparency of market information to investors in general, and specifically the quality, reliability and timeliness of market information.

Pre-Trade Transparency

Among other things, the Consultation discusses the increased use of “dark pools” and several related regulatory concerns. The Consultation also discusses the waivers, or exceptions, under MiFID from pre-trade transparency.

The letter strongly supports the flexibility provided by pre-trade transparency waivers and the Commission’s recognition that the reasons for allowing waivers still appear valid. The letter states that any changes to waivers must be carefully crafted to not create difficulties for investors when executing orders and that it is imperative that “dark pools” remain available to funds and that regulations overseeing these venues facilitate their continued use.

Post-Trade Transparency

The Consultation states that market participants have expressed concerns related to the timing of publication of post-trade information and suggests reducing the maximum permitted delays for trade reporting. The letter generally supports reducing delays in trade reporting but urges the Commission to ensure that adequate exceptions to post-trade transparency remain for large orders and to protect the anonymity of investors. The letter does not support the real-time disclosure of the identity of an individual dark pool on trade reports but states that ICI would support such disclosure on a delayed basis, specifically at the end of the trading day, on a stock-by-stock basis.

Equity-Like Instruments

The Consultation discusses pre- and post-trade transparency for “equity-like” instruments.

The Consultation states that the regulatory regime for these instruments would be based on the regime that applies to shares but with appropriate differentiation to take into account specific differences in the nature of the instruments. The letter supports the goal of extending transparency requirements to, for example, ETFs and agrees that taking into account the differences in how ETFs are structured and traded is critical in formulating specific transparency rules.

Data Consolidation and the Need for a European Consolidated Tape

The Consultation states that it is important that market data be brought together in a way that allows for comparison of prices across different venues. The Consultation specifically discusses the benefits of a European consolidated tape to provide comprehensive consolidation of post-trade data.

The letter strongly supports the establishment of a European consolidated tape. The letter states that ICI believes that as the Commission examines the establishment of a consolidated tape, it also should consider issues surrounding the fairness of the systems for market data distribution and the latency for investors receiving market data.

Transaction Reporting

The Consultation discusses several options for addressing concerns regarding the scope of the current MiFID reporting regime and the possible extension of transaction reporting to new financial instruments. The Consultation also discusses the current content of reporting and several issues relating to the channels through which transactions are reported.

The letter supports a more robust transaction reporting regime to enable regulators to monitor the activities of firms, ensure compliance with MiFID, and monitor for market abuses but states that the Commission should ensure the confidential treatment of any data provided to regulators and consider the costs of any new reporting regime.

Access of Third Country Firms to EU Markets

The Consultation requests comment on standards to permit access of third country firms to EU markets. The letter states that ICI does not believe it is necessary to base access to EU markets on a “strict equivalence” standard and recommends that the Commission consider a more flexible regime such as a standard determined by reference to the third country firm’s supervision and regulation in its home state or an equivalence standard based on transparent, proportionate, and objective grounds.

Ban on Specific Activities, Products or Practices

The Consultation discusses several issues relating to the ability of regulators to ban specific activities, products and practices under certain situations. The letter strongly supports providing regulators with the tools to ensure the fair and orderly operation of the financial markets and the protection of investors but questions whether the imposition of a ban is an appropriate or proportionate response and recommends that the Commission consider alternatives that may be more measured.

Regulatory Reform in the Derivatives and Fixed-Income Markets

The letter supports a robust examination of the current market structure for derivatives and fixed-income securities and agrees that the existing transparency regime for these markets can be strengthened to the benefit of investors.

Derivatives Markets Reform

The letter agrees with the goal of having derivatives trade on exchanges or other regulated trading venues but states that providing investors with options and flexibility in executing trades is critical. The letter therefore states that investors are best served by not introducing a requirement mandating where executions must take place. The letter also states that hard position limits are inappropriate for all categories of market participants and opposes imposing position limits on funds that invest in certain types of derivatives.

Review of Fixed-Income Markets

The letter states that more needs to be done to address concerns in the fixed-income markets but urges the Commission to proceed cautiously in recommending any new regulations given the complexity of the issues facing these markets.

Ari Burstein
Senior Counsel - Securities Regulation

[Attachment](#)

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