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Briefing Doc - PS24-14

Improving Transparency for

Bond & Derivative Markets



Detailed Briefing Document

PS24-14 Improving Transparency for Bond & Derivative Markets

1. Introduction

This document reviews the key themes and proposals of the FCA's Consultation Paper (CP) 2024/38, focusing on the proposed changes to the UK's bond and derivatives transparency regime under the Markets in Financial Instruments Directive (MiFID II).

2. Key Themes

The overarching aim of CP24/38 is to enhance transparency in bond and derivatives markets, aligning with the UK's post-Brexit regulatory framework. The paper addresses several key areas:

- **Improving the accuracy and utility of trade reporting data:** This includes the introduction of new flags to identify portfolio and package transactions, deletion of redundant flags, and revisions to technical aspects of trade reporting to facilitate better liquidity analysis.
- **Revisions to Large-in-Scale (LIS) thresholds and deferrals:** The paper proposes adjustments to the LIS regime for both bonds and derivatives to achieve a higher level of real-time price and size transparency while considering market liquidity and hedging needs.
- **Evaluating the future of the Systematic Internaliser (SI) regime for bonds and derivatives:** CP24/38 questions the relevance of the SI regime for bonds and derivatives, particularly in light of the removal of the pre-trade transparency obligations and the EU's decision to remove the SI regime for these asset classes.

3. Key Proposals and Facts

3.1 Trade Reporting Enhancements

- **Introduction of a portfolio transaction flag ('PORT'):** This flag aims to identify transactions involving five or more different financial instruments traded simultaneously by the same client as a single lot against a specific reference price. *“Most respondents agreed with our proposal to introduce a portfolio transactions flag ‘PORT’. Regarding the assertion that the price of a bond in a portfolio trade may not reflect the market price for the individual bond, we believe that this is precisely why a ‘PORT’ flag is useful.” (CP24/38, 7.59, 7.61)*
- **Deletion of redundant flags:** Flags such as agency cross ('ACTX'), non-price forming transaction ('NPFT'), illiquid instrument transaction ('ILQD'), and post-trade SSTI transaction ('SIZE') are proposed for deletion due to their lack of relevance or redundancy in the new regime.
- **Clarifications on the definition of the 'notional amount' field:** This clarification aims to ensure consistency in trade reporting across different asset classes, particularly for bonds and derivatives.

3.2 LIS Thresholds and Deferrals

- **Revised grouping of bonds:** The FCA proposes a more granular grouping of bonds based on issuer, issuance size, maturity, currency, and credit rating, with the aim of establishing LIS thresholds that better reflect the actual liquidity of instruments within each group. *“The thresholds therefore do not reflect the actual liquidity of instruments within a group and are either too high or low, with harmful effects on liquidity and transparency.” (CP24/38, 5.2)*
- **New LIS thresholds and deferrals for derivatives:** The paper proposes two models for calibrating LIS thresholds and associated deferrals for interest rate and credit derivatives,

factoring in liquidity metrics, hedging capabilities, and the availability of pre-trade information.

- **Differential treatment for broken-dated swaps:** The FCA proposes allowing transactions in broken-dated swaps above the LIS threshold to benefit from a longer deferral (T+1) compared to benchmark trades (end of day). This acknowledges the potential liquidity challenges associated with these instruments. *“We intend to allow transactions in broken-dated swaps... that are above the large in scale threshold to benefit for a longer deferral until T+1.”* (CP24/38, 5.35)

3.3 The Future of the SI Regime for Bonds and Derivatives

- **Questioning the relevance of the SI regime:** With the removal of pre-trade transparency obligations for Sis in bonds and derivatives, the FCA questions the continued need for firms to identify themselves as Sis for these asset classes. *“In respect of bonds and derivatives, the removal of the pre-trade transparency obligations applicable to Sis raises the question of whether, without that regime, it makes sense to continue to require firms to identify themselves as Sis in bonds and derivatives.”* (CP24/38, 9.5)
- **Seeking stakeholder views on potential alternatives:** The paper poses questions to stakeholders on the potential impact of removing the SI regime and explores alternative approaches to identifying addressable liquidity in post-trade transparency reports.

4. Conclusion

CP24/38 presents a comprehensive set of proposals aimed at enhancing transparency in UK bond and derivatives markets. The proposed changes to trade reporting, LIS thresholds, and the potential removal of the SI regime for bonds and derivatives are significant developments that warrant careful consideration by market

participants. The FCA seeks feedback on these proposals to ensure the implementation of a robust and effective transparency regime that supports market integrity, competition, and investor protection.

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