

**Response to**

**EUROPEAN COMMISSION CALL FOR EVIDENCE on**

**Pre- and post-trade transparency provisions of the MiFID in relation to**  
**transactions in classes of financial instruments other than shares**

The European Commission published a Call for Evidence on pre- and post-trade transparency in relation to transaction in classes of financial instruments other than shares. The document presents the Commission preliminary orientation and seeks feedback from the industry on this, via a number of questions.

Borsa Italiana is thankful for the opportunity to comment the Commission Call for Evidence and is pleased for this occasion to contribute to the discussion.

As a general statement we believe on the importance of transparency on trading in financial markets.

With MiFID and with the expected increasing number of competing trading venues we believe that fairness in price-discovery will be ensured only by an effective pre-trade and post-trade transparency and we believe that the regulatory framework should eliminate the informative gap between the transparency in the trading of financial instruments either on a regulated markets either on MTF and OTC. For this reason we support the necessity to introduce mandatory transparency rules for the class of instruments that are widely traded and listed in regulated market or admitted to trading on MTF.

At the same time we recognise that each market segment requires that rules have to be adapted to its specific instruments and players.

In particular we believe that for non-equity instruments it is important not only the pre- and post-trading transparency but also the availability of a set of information that would ensure a clear knowledge of the product and of the issuer (like availability of issue rules or other information on issuer's financial prospects). Moreover, we do not see any problem in having more than one transparency regime, under the condition that a level playing field between trading venues is ensured.

In addition, we believe on the importance to define more consistent transparency requirements if the trading involves the retail investors. To this end, with regard to retail investors pre-trade and post-trade transparency could be useful for example in order to achieve best execution and to compare prices of similar products. In contrast, we believe that for institutional investors post-trade transparency is more important than pre-trade due to better information available and greater technical knowledge, in order to price the "fair value" of financial instruments.

## Responses to the Commission's Questions

### *Question 1: Do you have any comment on the proposed scope of the Report?*

We agree with the proposed scope and with the proposed adaptation of the transparency regime considering the characteristics of instrument's market, the nature of the instrument and the characteristics of the investors who use that market.

We do not see any problems in having different transparency regime for different instrument classes under the condition that this do not represent an obstacle, as an increase in cost or a decrease in efficiency, for such a market.

### *Question 2: Do you consider this classification scheme to be sufficient for the purposes of the review?*

We believe that the classification proposed is quite extensive but it should be integrated as below:

“ ...

- Other financial instruments
  - **certificates and warrants**
  - **stock derivatives traded on a regulated market and//or MTFs**
  - **index derivatives traded on a regulated market and//or MTFs**
  - ....”

We believe that stock derivatives transactions are linked to transactions on their underlying and that derivatives prices provide information on their underlying prices. For this reason a level of transparency on stock derivatives markets is important to ensure deeper information on stock prices. The same can be said for indices derivatives.

For certificates and warrant, according to Italian experience these instruments are highly traded by retail investors for which a certain level of mandatory transparency would be an important instrument of protection.

### *Question 3: Do you consider there are possible policy rationales for mandatory transparency we have not listed?*

We agree with the rationales listed.

We also think that a distinction between wholesale and retail investors is highly relevant as either they operate in different segments of capital market, either the directive provides for retail investors an higher level of protection and different duties on investment firms. In addition, we believe that transparency would increase retail investors protection detecting or reducing possible mispricing and that it would also reduce other unfair behaviours by intermediaries.

### *Question 4: Do you agree with our proposals for prioritisation of the review?*

We agree on focus on those markets where investor protection concerns are more prominent but we do not understand the *a priori* exclusion of supranationals bonds. At the same time we believe it is necessary a certain level of transparency for ETFs, certificates and warrants (these all are instruments that according to Italian experience are highly traded by retail investors) and for stock and index derivatives traded on a regulated market and/or MTFs (these derivatives provide information on their underlying prices).

***Question 5: To what extent do you consider there to be:***

***a. observable or demonstrable problems with respect to the possible policy rationales for transparency identified above in relation to one or more of the instrument markets under review?***

***b. evidence that mandatory pre- or post-trade transparency would solve any of those problems?***

In relation to problems that mandatory transparency could solve we refer to Italian experience where corporate bonds (mainly issued by banks) are typical retail financial instruments negotiated in alternative trading system (called SSO, mainly bilateral trading systems). Since 1998 national regulation requires for SSOs a minimum level of transparency. Such experience has demonstrated that a certain level of transparency can increase the protection of retail investor with an affordable level of costs.

***Question 6: To what extent could recent and upcoming technological and market developments in relation to the instrument markets under review:***

***a. contribute to a relatively inexpensive extension of mandatory transparency?***

***b. render mandatory transparency unnecessary?***

We believe that technology is an important element to be considered in assessing costs and impact analysis of mandatory transparency. Also according to our experience as a regulated market, we believe that technology development could reduce the costs of market transparency especially the cost to maintain quote for instruments traded. But we do not believe that technological more advanced players would “spontaneously” bring transparency in financial instruments markets regardless to the minimum legal requirements.

We see transparency as a choice of a minimum requirement between market players who should operate under the same rules.

***Question 7: To what extent are non-equity financial instruments different from equities so that lower levels of mandatory transparency in those markets may be justified?***

In our view a different level of mandatory transparency can be defined for different asset classes considering the specificity of each financial instrument and the need of investors protection for these markets.

At the same time we believe that for non-equity instruments it is important not only the pre- and post-trading transparency but also the availability of a set of information that would ensure a clear knowledge of the product and of the issuer (like availability of issue rules or other information on issuer’s financial prospects).

***Question 8: What data sources do you consider relevant to the issues you have raised (if appropriate, cross-refer to your answers below)? Would you or your organisation be prepared to produce any relevant data if necessary?***

Borsa Italiana is ready to provide all data relevant to this inquiry as required.

***Question 9.: Are there academic or institutional papers or ongoing work that should be considered in preparing the Report not included in our bibliography?***

***Question 10.: What conclusions do you draw from the existing academic debate and the ongoing work being conducted by interested parties?***

***Question 11.: In your view, how applicable is the academic or institutional literature concerning transparency in the cash equities markets to the present discussion?***

With reference to the above questions nn. 9, 10 and 11, we refer to FESE Response

*“We first of all draw attention to the IOSCO Paper May 2004 entitled “Transparency of Corporate Bond Markets”, which provides useful analysis on what should be considered in the transparency obligations in the corporate bond/government debt securities markets. In the economic literature, views are divided as to the way transparency impacts liquidity, transaction costs or price formation on the bond markets. Some consider that transparency enhances liquidity (Pagano, Roell and Naik), whereas others believe that transparency affects market efficiency (Madhavan, Bloomfield and O'Hara). As for the institutional papers, we note the recent study commissioned by a number of banking sector associations (May 2006, LIBA et al). This study covers directly two of the five categories of instruments within the scope of the Call for Evidence and reaches a conclusion about the desirability to study further the benefits of post-trade transparency in one specific case and subject to several conditions. Although this study covers only some elements that need to be studied by the Commission in its report over the next year, we find it a useful contribution to the debate.*

*The academic literature is important but not conclusive. For the reasons explained above, we find the latter institutional study to be of some value but not conclusive with respect to the Commission's study of the full range of options to be considered for these markets.”*

***Question 12: What similarities, and what differences, are there between US and EU markets that should be borne in mind when seeking to draw inferences from the TRACE experience in the US?***

With reference to this question we fully refer to FESE Response

*“The two markets are indeed very different in important ways: For example, while the US market benefits from a federal but unified legal system, the EU legal context relevant to securities markets is less advanced in its integration. Similarly, the US market structure shows less heterogeneity than the EU markets in the features referred to in our response 6. Moreover, electronic trading is more widespread in the EU than the US. Another important difference is the different role played by self-regulation in these two marketplaces, with the EU exchanges generally having left behind a big portion of their regulatory responsibilities to the competent authorities, and therefore the market structure offering fewer instances of conflicts of interest among market participants. By contrast, organisations such as NASD have a regulatory role which was intricately linked to the initiation of the TRACE system.*

*Finally, any attempt to draw lessons from the (positive or negative) observations with respect to the TRACE experience should take into account the different regulatory practices in the EU, in particular the structured Better Regulation agenda of the EU institutions, which requires a different process to be followed for any similar project in the EU than would have been the case in the US.”*

***Question 13: To the extent that you have identified problems or believe that others might do so, do you agree that only EU-level action would be appropriate in the present case?***

We agree that only a EU-level action would be appropriate in the present case, first, because of the increasing number of global payers in financial markets and the large number of cross-border trades, and, second, because in any case we support the development of a level playing field across borders.

This matter is very important in Italy because, as indicated above, the majority of Italian banks manage bilateral alternative trading system (SSO) where are mainly traded bonds. According to existing Italian regulation, these SSOs are already required to comply with a certain level of transparency. Whenever there would not be any EU-level action on transparency for instruments other than shares, for Italy there would be a decrease of transparency required for some trading venues and consequently the risk of a lower level of investors protection. To keep the current level of transparency Member State would be required to introduce national transparency requirements, that seems a sub-optimal solution considering possible impact on competition.

***Question 14: If you have identified problems or believe that others might do so, to what extent do you consider those problems would disappear as a natural product of market evolution in the short-to-medium term?***

N/A

***Question 15: In respect of both pre- and post-trade transparency, are the four options the right ones to consider, and in particular should other options be considered?***

***Question 16: Would you, in light of your answers to the other questions, favor any of the four options in relation to pre- and post-trade transparency (or another option you might propose for consideration) in respect of transactions in any of:***

- cash government bonds;*
- cash investment-grade corporate bonds;*
- cash high-yield corporate bonds;*
- asset-backed securities;*
- credit default swaps, interest rate swaps and bond futures; or*
- any other financial instrument you consider relevant?*

We believe that the four options identified by the Commission are exhaustive and as a general principle we consider that a “MiFID like system” both for pre-trade transparency and post-trade transparency is the more desirable because it is flexible and easy to adapt to any financial instrument it will be decided to extend transparency requirements.

Afterward, we believe that for each class of financial instruments it should be evaluated when pre-trade transparency only, post-trade transparency only, or both would be mandatory.

We add that, for “credit default swaps, interest rate swaps and bond futures” and for “stock derivatives traded on a regulated market and/or MTFs” and “index derivatives traded on a

regulated market and/or MTFs” (that we are proposing to include in the list - see above our answer to question n. 2) we believe that mandatory MiFID-like system for post-trade transparency would ensure an adequate level of information (without pre-trade transparency).

### **Conclusions**

As a general point of fact we believe that transparency is of high importance for cash bonds market as well as for other market segments like certificates, warrants and ETF, and stock and indices derivatives. We believe that for such instruments, listed in regulated markets or admitted to trading in regulated markets or MTFs, it would be very important that the same level of transparency is provided when they are traded on an regulated market, on MTF or OTC with an investment firm.

In conclusion, we fully support the extension of transparency provisions to non-equity markets and we propose to consider this extension for any trading venue.

We hope that Commission will find our comments useful and we remain at your disposal for further discussion. With our best regards.

Milan, 25 September 2006