Guiding Principles for Market Transparency Requirements

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INTRODUCTION

Market transparency requirements should support specific policy objectives, consider the fundamental structural differences between markets and among asset classes, and provide meaningful and useful information to market participants while doing no harm to market integrity, liquidity, efficiency and resilience. If designed appropriately, transparency—whether through regulatory reporting to support market surveillance duties or public dissemination—can achieve these objectives. The Global Financial Markets Association (GFMA)[i] supports regulatory reporting requirements that enable regulators to fulfill their regulatory surveillance duties, monitor trading irregularities, detect market abuse, and support market integrity. The design of public market transparency requirements relating to the dissemination of quotes or transaction details on a market-wide-basis, however, requires caution to avoid unintended consequences of diminished market efficiency and end-user choice. End-users access markets for price discovery, risk diversification, and risk management and have varying demands for price and risk transfer immediacy. Mandating greater public transparency should support the functioning and integrity of the market. Requirements need to consider the timing of disclosure, liquidity of the underlying asset, and needs of the end-user. Fundamental structural differences between markets (including participants and their needs) preclude a "one-size-fits-all" approach. Increasingly, more regulators are providing public or regulatory reporting requirements that impact global firms across jurisdictions, drawing attention to a lack of consistency of objectives for rules and the need for shared global transparency principles. Accordingly, GFMA encourages policymakers and regulators to clearly define policy objectives as they design market transparency frameworks in line with the following principles:

GFMA Guiding Principles for Market Transparency

I. **Transparency to regulators should be timely, consistent and appropriate to fulfill regulatory surveillance duties and to support market integrity.**

II. **Public market transparency requirements should support the provision of liquidity for price formation and risk management, while doing no harm to market integrity, liquidity, efficiency and resilience.**

III. **The level of transparency and timing for reporting should be appropriately calibrated based on regulatory intent, market structure, and liquidity profiles of specific assets.**

IV. **An effective transparency framework is based on consultation with all market participants and a cost-benefit analysis.**

V. **The market's ability to implement requirements, including on a cross-border basis, if appropriate, is critical.**

I. Transparency to regulators should be timely, consistent and appropriate to fulfill regulatory surveillance duties and to support market integrity.

Regulators should have access to the information necessary to monitor trading irregularities, detect market abuse, identify market structure changes, enhance market integrity, and facilitate risk surveillance. It is critical, however, that the timeliness of the reporting, and the breadth of elements reported, should be considered in the context of a robust cost-benefit analysis, taking into account the: (i) importance of timing to fulfill market regulator's surveillance duties; (ii) objective to support liquidity for price formation and risk management; and (iii) need to ensure customer privacy[ii].

Global supervisory forums support regulatory efforts to harmonize reporting requirements to mitigate inconsistent or duplicative jurisdictional rules and to reduce operational complexity, while increasing the utility of data gathered for prudential purposes. Such cross-border coordination and consistency in reporting regimes enables regulators to have a holistic view of risks in certain markets that are global in nature. Cross-border regulatory coordination is necessary to: (i) ensure that regulators have the policy tools necessary to address divergences in data privacy and security rules across jurisdictions that introduce conflicts of law; and (ii) help address compliance risks for multinational firms operating in a global environment.

Coordinating regulatory reporting requirements across borders, where appropriate, can also support supervisors' access to information necessary for regulatory surveillance. For example, international regulatory cooperation helps identify systemic risks in the global swaps market, and design regulatory regimes that address legal and operational issues affecting swap trade reporting globally, including data privacy and confidentiality requirements.

II. Public market transparency requirements should support the provision of liquidity for price formation and risk management, while doing no harm to market integrity, liquidity, efficiency and resilience.

Market transparency requirements can be part of an overall framework that ensures fair and effective markets. Regulators and supervisors formulating market transparency rules, however, should carefully examine tradeoffs to ensure that any public dissemination requirements provide market participants with meaningful information, while doing no harm[iii] to market integrity, liquidity, efficiency, and resilience. Ultimately, transparency frameworks should achieve specific policy objectives, be tailored to different market structures and seek to minimize the risk of unintended consequences.

The design of transparency requirements should be flexible and consider different elements: calibration, waivers, deferrals and exemptions. When designed appropriately, market transparency requirements should:

- **Facilitate Price Discovery:** Market participants should have access to information that informs them where the market is trading, at what level they should be able to enter into a transaction and at what size.
- **Encourage Market Participation:** Transparency requirements should not unduly favor one set of participants, or one market segment, to the detriment of others to ensure a level playing field between market participants providing similar functions.
- **Instill Market Confidence:** Market transparency requirements, consistent with regulatory objectives, should support the functioning and integrity of the market by supporting the provision of liquidity for price formation and risk management.
- **Do No Harm:** Market transparency requirements should be calibrated in such a way that market integrity, liquidity, efficiency, and resilience are not adversely affected.

There is a considerable body of research[iv] that details the effects of greater market transparency on market liquidity in certain segments along the continuum of agency to principal-traded markets. Careful consideration of the tradeoff between public transparency and liquidity is necessary to ensure that the outcomes align with both regulatory intent and end-user needs. To foster market liquidity, transparency requirements should support principal-driven markets, especially where markets rely on the provision of liquidity by market-makers for price immediacy and in size.

For liquid instruments, public transparency tends to be inherently high. As such, mandating transparency does not necessarily change prices (e.g. spreads quoted on dealer-to-dealer and dealer-to-client transactions). However, mandating public transparency for instruments that are not actively traded without taking into consideration timing of public dissemination may lead to greater volatility in prices and valuations and smaller trade sizes, influencing issuer and investor behavior. Mandating greater transparency without consideration of timing of public dissemination for less liquid bonds may, for example: (i) cause end-users to reduce trade sizes; (ii) deter investment activity by large investors with concentrated positions (especially in illiquid securities); and (iii) pressure liquidity providers to reduce inventory levels to manage exposures to price volatility. This may, in turn, raise the cost of funding for issuers, and similarly make it more difficult for investors to exit their positions in a timely fashion without incurring unnecessary and potentially significant costs. Empirical studies on the effects of mandated transparency requirements generally bear this out[v].

A theory that is sometimes asserted: *increasing market transparency will attract new market participants and, in turn, increase market liquidity.* This presumes that a temporary decline in liquidity would recover to former levels once investors are able to source liquidity from a broader range of market participants. While increasing market transparency might attract new market participants that invest on a short-term basis (such as firms that do not commit significant overnight capital to meet client demand), it could also reduce participation of large, concentrated, long-term investors. These tradeoffs must be carefully weighed to assess how the evolution of market participant behavior impacts liquidity and financial market resilience over the long-term.

The appropriate level of transparency varies across asset classes, instruments, and market segments. In some circumstances, to preserve appropriate levels of market liquidity, it is imperative to design waivers and deferrals to deliver the highest possible level of transparency while not adversely impacting term investors or quotes made by liquidity providers. In this approach, the calibration of block trade thresholds, for example, would have to ensure that liquidity providers are truly indifferent as to whether—below the set thresholds—their quote or executed trade is made public. It has been recognized in some regulatory regimes that a “one-size-fits-all” approach to pre- and post-trade transparency can impair market liquidity, and for this reason there are liquidity and notional thresholds above which post-trade market transparency is either withheld or delayed. Therefore, it is important to carefully examine tradeoffs in advance to ensure that the design of any public dissemination requirements provides useful information to market participants while doing no harm to market integrity, liquidity, efficiency and resilience.

III. The level of transparency and timing for reporting needs to be appropriately calibrated based on regulatory intent, market structure, and liquidity profile of specific assets.

Market transparency requirements, when properly designed, contribute to the price discovery process, improve data quality, and enable market participants to better assess execution quality.[vi] The challenge is designing the appropriate level of transparency for the specific asset class/product/instrument to achieve regulatory objectives (in Principle II). Policymakers should consider the nuances of distinct asset classes and products before replicating transparency and disclosure requirements from one market segment or jurisdiction to another.

Levels of market transparency vary from:

- **Regulatory reporting:** As stated in Principle I, market transaction or trading data should be provided to regulators or supervisors, as appropriate, to support regulators’ surveillance duties and financial stability duties.

- **Public dissemination:** Publication of quotes or transaction details can facilitate price formation and support risk management, if designed appropriately (Principle II). End-users access markets for price formation, risk diversification, or risk management. Mandating greater transparency without considering timing of public dissemination on the liquidity profile of the relevant asset class may negatively impact market makers' ability to effectively meet end-users' needs.
- **Other regulatory obligations:** Some obligations that are not directly linked to transparency may still interact with provisions related to public dissemination. This can, for instance, be the case for rules leading to the public disclosure of details that are either not targeted by transparency provisions (but can be tallied with transparency information to increase their significance) or are covered by a transparency waiver or deferral. For such obligations, the potential interactions with public dissemination rules should be carefully assessed prior to implementation.

Fundamental structural differences between financial market segments also precludes a "one-size-fits-all" framework for transparency requirements. The needs of end-users drive market makers. The ability of market-makers to facilitate end-users' requests will depend on the size of trades as well as the market structure.[vii] Transparency rules should therefore be carefully designed and tailored to the specific market structure, considering the:

- **Types of market participants** (e.g. wholesale vs. retail investors, and regulated/ supervised vs. unregulated/unsupervised participants), which informs how rules should be designed to add value to end-users and ensure a level playing field;
- **Liquidity profile of the financial instrument** to which transparency requirements would apply (i.e. to avoid reducing the depth of liquidity for trading in less liquid instruments);
- **Necessity of anonymity and confidentiality** provisions to protect market-sensitive information and risk management strategies; and
- **Timing** of disclosure and where reporting delays (e.g. appropriate deferrals and waivers) may be necessary to avoid unintended harm to investors and end-users.

Timeliness of market transparency should support the provision of liquidity and enable risk management by investors and market-makers (that provide liquidity to meet the needs of end-users). Depending on the regulatory objective and market structure, market transparency can be provided on a:

- pre-trade basis, where prices quoted to participants are made public; or
- post-trade basis[1], where executed trades are made public either real-time or with delays, with the possibility of masking the size of large trades.

Further, reporting requirements are most effective when market participants are required to report quotes/transactions to central trade repositories, who then onward report to the regulator subject to masking/delays, as appropriate.

Pre-Trade Transparency

Pre-trade transparency requirements should be pursued with particular caution to avoid hampering market-makers' abilities to meet investors' needs.[viii] Pre-trade transparency can be beneficial for certain market segments but could otherwise be unworkable in others. Authorities considering pre-trade transparency requirements should: (i) ensure that displayed position sizes would not unduly move the market; (ii) presumptively calibrate pre-trade waivers at a smaller size than thresholds for post-trade requirements; (iii) carefully evaluate the performance of new regulatory requirements in one jurisdiction before considering similar requirements in other jurisdictions; and (iv) ensure that any pre-trade disclosure is anonymous.

Post-Trade Transparency

For post-trade transparency, consistent with the "do no harm" objective, the requirement to publicly disseminate the executed price should not adversely impact the quoted and executed price. End-user investors (especially with concentrated positions) are adversely impacted when reporting requirements do not provide sufficient time to risk manage their exposures before revealing the transaction to the marketplace. Post-trade

1 Alternatively, trades can be required to be conducted on trading venues or exchanges, which are in turn mandated to provide transparency.

transparency regimes should provide delays to allow numerous trades to be executed before the transaction details are exposed, particularly for illiquid market segments. Time deferrals and masking should be considered in tandem, rather than in isolation, according to the liquidity profile of the instrument.

Several mechanisms are available to afford this protection when designing reporting regimes, including:

1. Calibrating time deferral before disclosure to address the specific risks needing to be hedged. These waivers should be based on transaction size as well as frequency of trading. Where the price quoted is impacted by public disclosure, that instrument should be classified as "illiquid."

   Displaying quotes or transactions for "average trade size" or "standard market size" poses different risks for investors and market makers across markets. Policymakers and regulators must carefully calibrate the threshold at which "block trades"[2] would be delayed or exempt from reporting requirements to avoid unintended consequences. Reliance on "average trade size" or "standard market size" metrics forces the market to smaller ticket sizes,[ix] since market-makers must reduce the trade sizes quoted to the point at which they are not exposed to undue risk by others knowing their positions. To mitigate these risks, policymakers and regulators should scale waivers across multiple products based on risk, rather than based on "average trade size" or "standard market size" (which only works for fungible, or interchangeable, assets prevalent in agency-based markets with a lot of market participants).

2. Masking the actual/full size of large, less liquid trades. Public disclosure of the size of large, less liquid trades (sometimes referred to as "block trades") significantly increases risks for real-money investors (particularly with concentrated positions), as well as for market makers to facilitate liquidity and hedge positions. To prevent these adverse impacts, policymakers should avoid mandating public disclosure of the actual size of transactions above the "block trade" threshold.

IV. An effective transparency framework is based on consultation with all market participants and a cost-benefit analysis.

Policymakers should conduct a robust cost-benefit analysis on proposed market transparency requirements based on clearly defined policy objectives. The analysis should consider the value added by new transparency requirements to investors and end-users while balancing the overall impact on market integrity, efficiency, liquidity, and resilience. It is critically important that market participants have the opportunity to provide input on the proposed market transparency framework, as well as the cost-benefit study, to better understand potential outcomes.

Market transparency requirements should have a clear benefit, provide meaningful and useful information, and be readily understood by the public. For example, the utility of the specific market information to the buy-side should be carefully considered to avoid prescribing market transparency requirements that do not inform investor behavior. Appropriate levels of market transparency are often achieved without regulatory intervention: Market-led developments are already enhancing the level of pre-trade transparency through current modes of price dissemination by market-makers, such as electronic market-making, dealers providing more regular price runs to clients and bond e-trading platforms, among others. Policymakers should be able to demonstrate that proposed market transparency requirements: (i) foster appropriate risk management strategies; (ii) provide sufficient transparency for investors to make informed investment decisions that they otherwise would not be able to make; (iii) enable economic and market forces to drive market structure changes; (iv) encourage two-way liquidity provision and otherwise do no harm to market integrity, liquidity, efficiency, and resilience.

2 The term "block trades" refers to transactions that meet certain quantity thresholds and are often permitted (or, as in the case of MAT transactions, required) to be executed away from the public market, and disclosed on a delayed and masked basis to avoid adverse market movement.

Further, as transparency rules are implemented, ongoing evaluation of reporting requirements is necessary to assess the overall effectiveness of the regime to promote efficient, liquid, resilient markets by evaluating changes in market structure (including technological developments).

V. The market's ability to implement the requirements (including on a cross-border basis, if appropriate) is critical.

Policymakers and regulators should ensure that market transparency guidelines are workable well in advance of implementation. Divergences in trade reporting requirements, as well as data privacy and security rules, across jurisdictions introduce conflicts of law and compliance risks for multinational firms operating in a global environment. It is vital to provide clarity on technical aspects of the reporting frameworks, such as product scope, timing, reporting party determination logic, reportable fields, technical reporting formats and standards, such that all market participants have clear guidelines prior to implementation of the rule. In addition, we encourage policymakers and regulators to provide adequate time to test the reporting systems before they go-live. Further, where market transparency regimes have a cross-border reach, global coordination and regulatory consistency is desirable and clearly beneficial to multinational firms operating across different markets and jurisdictions.

Cross-border consistency in regulation is also beneficial for policymakers and regulators as it facilitates the aggregation of data across different jurisdictions to obtain a global view of the market to support their surveillance obligations (Principle I). The international community—principally the Group of 20 (G20)—has long-recognized the importance of mechanisms that allow for deference in the context of cross-border rules implementing G20 over-the-counter (OTC) derivative reforms. The G20 Leaders' St Petersburg Declaration of September 2013 stated that:

Regulators should be able to defer to each other when it is justified by the quality of their respective regulatory and enforcement regimes, based on similar outcomes, in a nondiscriminatory way, paying due respect to home country regulatory regimes.[x]

Policymakers and regulators should have the policy tools necessary to mitigate duplicative or inconsistent reporting requirements to multiple regulatory agencies or spread across different pieces of regulation.

Where jurisdictions have transparency regimes that achieve similar regulatory outcomes, deference to local authorities is appropriate. Coordinating regulatory reporting guidelines across borders in advance of finalizing regulations, where appropriate, can help recognize and accommodate different data privacy requirements across jurisdictions—which may be necessary to improve data quality, avoid conflicting requirements, and increase efficiency of data reporting. Ultimately, cross-border coordination and consistency of regimes helps prevent the negative consequences of duplicative or conflicting laws, and instead serves to reduce transaction costs, foster competitive markets and facilitate cross-border trading and investment—especially for end-users.

Cross-border regulatory harmonization is imperative to understand systemic risks in the global swaps market and to solving legal and operational issues affecting swap trade reporting globally, including data privacy and confidentiality requirements. The ongoing work by the Committee on Payments and Market Infrastructures and International Organization of Securities Commissions to harmonize common data elements across regulatory reporting regimes, as well as efforts to streamline supervisory reporting by National Competent Authorities, are very important in this regard.

CONCLUSION

GFMA supports transparency requirements that are appropriately tailored for regulators to enhance market integrity through surveillance. Fundamental differences between markets should be carefully considered to design public market transparency requirements, where appropriate, in a way that: (i) facilitates price discovery; (ii) encourages market participation; (iii) instills market confidence; (iv) supports regulatory surveillance; and (v) does not harm market integrity, resilience, liquidity and efficiency.

Public market transparency requirements, consistent with regulatory objectives, should support the functioning and the integrity of the market by supporting the provision of liquidity for price formation and risk management. In contrast, requirements that do not consider timing of public dissemination, proportionate with risk and trading volumes and frequency, may unintentionally: (i) increase transaction costs for end-users or reduce their access to market intermediaries; (ii) risk deterring the participation of long-term investors, to the detriment of liquidity and financial market resilience over the long-term; (iii) decrease market liquidity by reducing the willingness of market-makers to commit capital to warehouse risk; (iv) expose firms' positions in the market or reveal firms' proprietary data; or (v) result in conflicts of law due to divergent data protection and privacy regimes across jurisdictions. Particular caution is paramount in designing market transparency requirements where market-makers take inventory onto their own balance sheets to serve end-users or where there is a concentrated investor base.

Clearly defining the risk or policy objective enables regulators and policymakers to design market transparency requirements for the benefit of all market participants. Fundamental structural differences between markets precludes a "one-size-fits-all" design. GFMA encourages policymakers and regulators to harmonize regulatory reporting requirements in key jurisdictions to avoid inconsistent or duplicative reporting requirements across jurisdictions. The GFMA Guiding Principles for Market Transparency aim to improve the design of market transparency requirements to ensure that they are calibrated to serve the needs of different market structures and asset classes while providing meaningful information to market participants and regulators. GFMA encourages global policy and standard-setting bodies to consider these principles to further support market integrity provided by liquid, efficient, and resilient markets.

REFERENCES

i The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA. For more information, visit http://www.gfma.org.

ii International Organization of Securities Commissions, "Regulatory Reporting and Public Transparency in the Secondary Corporate Bond Markets," Final Report, April 2018, https://www.iosco.org/library/pubdocs/pdf/IOSCOPD597.pdf, page 26.

iii U.S. Securities and Exchange Commission Chairman Clayton, Fixed Income Market Structure Advisory Committee Meeting, Jan. 11, 2018, https://www.sec.gov/video/webcast-archive-player.shtml?document_id=011118fimsac.

iv See SEC Fixed Income Market Structure Advisory Committee (FIMSAC) briefing materials, including on from the Jan. 11, 2018 meeting: https://www.sec.gov/spotlight/fixed-income-advisory-committee; Report by the Committee on the Global Financial System, "Fixed income market liquidity," January 2016, https://www.bis.org/publ/cgfs55.htm; and Darrell Duffie, "Why Are Big Banks Offering Less Liquidity to Bond Markets?" March 11, 2016, https://www.forbes.com/sites/lbsbusinessstrategyreview/2016/03/11/why-are-big-banks-offering-less-liquidity-to-bond-markets/#58cf68a29de5.

v See Asquith, Covert, Pathak study in the National Bureau of Economic Research, "The Effects of Mandatory Transparency in Financial Market Design: Evidence from the Corporate Bond Market," September 2013, https://economics.mit.edu/files/9018.

vi For instance, the European Commission Expert Group on Corporate Bond Market Liquidity concluded that, "A well calibrated trade transparency regime can provide numerous benefits: (i) improve data quality; (ii) reduce information asymmetries; (iii) enhance price discovery; and (iv) increase market efficiency," page 76, http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetailDoc&id=35768&no=1.

vii See Asquith, Covert, Pathak study in the National Bureau of Economic Research, "The Effects of Mandatory Transparency in Financial Market Design: Evidence from the Corporate Bond Market," September 2013, https://economics.mit.edu/files/9018.

viii Committee on the Global Financial System, "Market-Making and Proprietary Trading: Industry Trends, Drivers and Policy Implications," Nov 2014, https://www.bis.org/publ/cgfs52.htm.

ix See Asquith, Covert, Pathak study that shows the reduction in trade sizes as a result of mandatory transparency even with delayed dissemination of transactions above a certain block threshold, "The Effects of Mandatory Transparency in Financial Market Design: Evidence from the Corporate Bond Market," Sept. 2013, http://www.nber.org/papers/w19417.

x Financial Stability Board Report to the G20 Finance Ministers and Central Bank Governors, "Jurisdictions' ability to defer to each other's OTC derivatives market regulatory regimes," September 2014, http://www.g20.utoronto.ca/2014/11%20Jurisdictions%20ability%20to%20defer%20to%20each%20others%20OTC%20derivatives%20market%20regulator%20regimes.pdf.

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