



# FIXED INCOME MARKET REGULATORY UPDATE

January 2018

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*Keeping you informed on recent policy and regulatory developments shaping credit markets in Canada & abroad*

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## Canada

### IIROC Compliance Priorities

On January 18, 2018, the Investment Industry Regulatory Organization of Canada (IIROC) released its list of key Compliance Priorities for the year. The Report helps dealers focus their supervision and risk-management efforts to comply with IIROC regulatory requirements. IIROC Priorities related to fixed income include:

#### *Fair Pricing*

IIROC rules require all dealers ensure that prices for over-the-counter securities are fair and reasonable based on prevailing market conditions. IIROC has found that some dealers do not have reasonable procedures in place to evaluate hard-to-value securities and/or those with stale prices. IIROC will continue to review dealer procedures and testing for fair pricing and encourage review of Dealer Member Rule 3300 and related notices for clarification and guidance.

#### *Supervision of Over-the-counter Debt Trading*

IIROC rules require each dealer that engages in over-the-counter debt trading to have adequate policies and procedures in place and conduct testing to confirm that activity is fair and equitable for their clients and counterparties with whom they transact. IIROC has found that some dealers do not have adequate procedures in place and/or cannot prove that a reasonable level of monitoring and review of OTC debt activity is occurring. IIROC will continue to request and review the controls in place for this activity.

### IIROC's Fixed Income Advisory Committee

On January 30, 2018, the Investment Industry Regulatory Organization of Canada (IIROC) announced it is seeking nominations for their Fixed Income Advisory Committee (the Committee). The Committee's mandate is to review and make recommendations to IIROC staff about proposed IIROC initiatives relating to fixed income trading. In recent years, IIROC has devoted increased attention to fixed-income markets including its launch of a debt surveillance system and a public transparency system for corporate debt. IIROC's announcement may signal additional fixed income initiatives on the horizon. Each dealer may nominate one dealer representative to serve on the committee with nominations due by Wednesday, February 28, 2018.

## Montreal Exchange Proposal to Extend Trading Hours

Bourse de Montréal Inc. (the “Bourse”) has proposed extending its trading hours by opening its market at 2:00 am ET rather than the current 6:00 am ET open to align with the opening of the UK trading day. The Bourse sees the initiative as allowing domestic and international clients to manage their exposure to Canadian markets during non-regular Canadian business hours and cites many other supporting factors for the initiative. The products initially in scope for the extended hours are the Money Market Derivatives, Bond Market Derivatives and Index Derivatives products of the Bourse. On January 30, 2018, the IIAC wrote to the Bourse identifying concerns with their initiative, including its implications on market liquidity and integrity.

## United States

### Inaugural Meeting of SEC Fixed Income Market Structure Advisory Committee

On January 11, 2018, the Securities and Exchange Commission (SEC) convened the first meeting of its Fixed Income Market Structure Advisory Committee (the Committee). The SEC established the Committee to provide a formal mechanism through which the SEC can get advice and recommendations on fixed income market structure issues. The meeting centered on bond market liquidity, with emphasis on credit markets. Some of the key discussion areas included: metrics for measuring liquidity, alternative liquidity providers in the marketplace, the effects of electronic trading, risk considerations for ETF and bond fund investors, and how bond markets respond to periods of stress. Background materials for the meeting, which are available on the SEC website, include studies outlining developments in credit markets. A common theme among several of the studies is the innovation taking hold in bond markets. New technologies, combined with regulatory reforms impacting dealers’ ability to warehouse risk, have resulted in changes to market structure. The way in which market participants measure and obtain liquidity is changing as a result. A webcast of the meeting is also available via the SEC website.

### Republican Senators’ Opposition to FSB Influence

On January 18, 2018, a group of six Republican senators wrote to President Trump expressing concern over the influence the Financial Stability Board (FSB) has been having on U.S. policymaking regarding financial institutions. The senators request that the President clarify that the rules and standards developed by the FSB are advisories only and not binding on the United States or its businesses. The Senators also urge the President to shift the emphasis from global standards imposed on U.S. entities to ensuring that federal regulators consider first and foremost the interest of U.S. entities and consumers. Any move by the U.S. to downplay the role of the FSB could raise uncertainty on the timelines, or degree, to which the U.S. will adopt global reforms. This could impact the commitment other jurisdictions have made to adopt FSB reforms.

## Europe

### European Concerns Regarding Fees Charged by CRAs and Trade Repositories

On January 11, 2018, the European Securities and Markets Authority (ESMA) published a Report on fees charged by Credit Rating Agencies (CRAs) and Trade Repositories (TRs). The Report provides ESMA’s views on the application of the requirements that fees charged by CRAs should be non-discriminatory and cost-based, and TRs provide non-discriminatory access and charge publicly disclosed and cost-related fees. The Report notes several supervisory concerns and finds that

there are areas for significant improvement by both CRAs and TRs in their current fee practices, particularly in the areas of transparency and disclosure. ESMA states it will continue to engage with supervised entities and their clients to ensure effective application of the fee provisions.

## ESMA Updates Transparency Calculations for MiFID II/MiFIR

On January 19, 2018, the European Securities and Markets Authority (ESMA) published an extended version of the MiFID II/MiFIR [transitional transparency calculations](#) (TTC) for equity and bond instruments, adding further instruments to the initial list released in December. The new list was expanded to include bonds traded for the first time on a trading venue between November 1, 2017 and January 2, 2018. Of the approximately 69,000 bonds now captured in the calculations, barely 800 are determined to be sufficiently liquid for the purposes of the pre-and post-trade reporting requirements of MiFID II. This compares to 566 bonds out of 61,761 analyzed by ESMA in December.

## ESMA Publishes Register of Derivatives to be Traded On-Venue under MiFIR

On January 9, 2018, the European Securities and Markets Authority (ESMA) published a public [register](#) of those derivative contracts that are subject to the trading obligation under the Markets in Financial Instruments Regulation (MiFIR). The register provides clarity to market participants on the application of the trading obligation under MiFIR and on:

- the classes of derivatives subject to the trading obligation;
- the trading venues on which those derivatives can be traded; and
- the dates on which the obligation takes effect per category of counterparties.

## 'Cliff Edge Risks' Posed by Brexit

On January 22, 2018, the Association for Financial Markets in Europe (AFME) published a [paper](#) highlighting some of the potential 'cliff edge risks' that Brexit could create for market efficiency and financial stability. These are risks that AFME expects will create market disruption or impede business activities on the day of Brexit if no intervention is undertaken. The paper highlights the following key risks:

1. Cross-border personal data transfers
2. Continuity of contracts
3. Choice of jurisdiction; recognition and enforcement of judgments
4. Access to market infrastructure: recognition of CCPs
5. Recognition of resolution actions

The report notes that while some of these cliff edge risks would be mitigated (in whole or in part) by a longer transition period, risks remain that need to be addressed irrespective of a transition. AFME considers the Withdrawal Agreement the most appropriate mechanism to solve for the risks highlighted in the paper, although the principles of the Withdrawal Agreement may need to be supported by legislation in the UK, EU and EU27 Member States.

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