



FESE response to the IOSCO consultation on the evolution in the operation, governance and business models of exchanges

Brussels, 2nd July 2024

FESE welcomes the opportunity to respond to the IOSCO consultation on the evolution in the operation, governance, and business models of exchanges. We appreciate the comprehensive nature of the report and the recognition of significant changes affecting exchanges globally. We also would like to underscore the necessity of robust regulatory frameworks to manage cross-border activities effectively, ensuring market stability and investor protection. In most jurisdictions, that is already the case and the operational risks of regulated exchanges are usually well-managed, even alternative markets like those for cryptoassets are treading their path towards the construction of a reliable framework. Taking note of this, as a first principle, we call for the same level of regulatory requirements for execution venues which are not exchanges and currently benefit from a lighter regime.

FESE concurs with IOSCO's assessment of global industry drivers such as demutualization or increasing demand for better data, trading solutions, and connectivity. We share the consultation's observation on market integration, which has driven efficiencies and innovation in Europe. However, while we understand that IOSCO's approach needs to be broad given the diversity of jurisdictions covered, we believe that the European dimension has not been duly covered in the paper. EU exchanges already operate under specific regulatory environments, such as MiFID II/R and DORA and the EU supervisory regime, setting organisational requirements which should be adequately reflected to ensure relevant and effective recommendations. Moreover, in the EU, many operational constraints and risks arise from divergent supervision rather than a lack of regulatory instruments or the exchanges themselves. Since the introduction of MiFID in 2007, efforts have been made to balance the recognition of local specificities with integration. Yet the main challenge remains the lack of harmonization across the 27 jurisdictions. Exchanges and market participants still have to comply with different rules and regulations at the national level (e.g., company law, securities law, or taxation), and, in some instances, they have to cope with numerous different regulators with an array of substantial gold-plating practices and, at times, conflicting regimes. Streamlined supervision practices delivering harmonised and identical outcomes across Member States would be a big step forward and promote a level playing field.

Exchanges in Europe also operate in diverse organisational settings, some on an individual basis, some in a group setting, consolidating multiple trading and settlement solutions. Within FESE, we have witnessed the challenges the European legislative and supervisory framework pose today for the operations within a group as detailed above.

From this perspective, realising the reality of exchanges operating in groups, we believe the IOSCO report should better reflect the diverse nature of how exchanges are organised. The current recommendations are primarily focused on individual, national responsibilities, a focus that in our view does not do justice to the efforts taken in the EU to integrate markets

based on sound and prudent regulatory frameworks. We are not suggesting any organisational situation should be preferred. Yet we are asking IOSCO to accept that exchanges are organised differently and that the good practices should be applied differently depending on the nature of the organisation.

Regarding IOSCO's proposed good practices, FESE wants to raise awareness on the need for principle-based, outcome-focused and non-prescriptive measures, having regard to the different legal and regulatory frameworks that exchanges operate under. Otherwise, exchange groups are likely to face duplicative or inconsistent regulation, inefficiencies in regulatory processes and increased compliance costs without enhancing investor protection.

We do not agree with IOSCO's proposals requiring that "the regulatory function of an exchange be carried out by an independent department/entity, with qualification criteria for the directors of the independent body"; or "an exchange's regulatory functions be performed by a wholly-owned subsidiary with separate management and board, which reports to the board of the parent company of the Exchange Group". Such requirements fail to take into account the varying sizes and business models of exchanges. The independence of regulatory functions from the commercial functions of an exchange can be achieved through internal measures, such as provisions requiring that commercial interests must not adversely affect the performance of the exchange's regulatory functions or general conflicts of interest management obligations. There are also other well-established mechanisms under domestic laws and regulations as well as industry practices for managing conflict of regulatory and commercial interests.

Equally, FESE objects to the proposal in the report that regulators be authorized to impose "limits to the activities that an exchange can perform other than its regulatory role." Exchanges, by their nature as market operators, have to engage in non-regulatory matters to a certain extent. Imposing limits on exchanges' activities that are non-regulatory would mean a significant departure from how for-profit exchanges operate and would require a fundamental re-evaluation of exchanges' role in the financial ecosystem. Moreover, the report ignores that limits could stifle competition or innovation.

While we agree that letterbox entities constitute potential risks for market systems, we do not support all of the elements in the proposed toolkit to address letterbox issues and most of those regarding management bodies are already implemented in the EU. Requiring "identification of a function specifically in charge to monitor the outsourcing and deliver adequate reports to the administrative and control bodies" or requiring that an "exchange shall operate with qualified staff and that key executives and senior members need to have effective decision-making powers and dedicate sufficient amount of time to fulfil their duties" ignores the jurisdictional differences that exist. The decision-making matrix of key executives and senior members should be left to the exchanges. Likewise, requiring "a 'statement of responsibilities' by those persons accepting a Senior Management Function, subject to the approval of the regulator, clearly setting out their role and responsibilities" is not necessary. The appointment of persons to critical senior management functions in exchanges is, in the EU, subject to regulatory approval. Many jurisdictions also impose individual accountability on persons in these functions.

We also believe that exchange regulation on outsourcing practices, whether intragroup or external, should align with the approaches taken in the regulation of other entities like investment firms, distinguishing critical outsourcing from that of ordinary activities. Some regulatory regimes do not even recognise the notion of a group of regulated markets, which needs to be addressed to ensure consistency and clarity. Furthermore, we want to allude that some European exchanges are already comprehensively regulated regarding outsourcing

practices. The recommended tools to identify “extensive” use of outsourcing seems like a rather unpractical approach. Practically, this would lead to difficulties of interpretation. An approach to be preferred for those jurisdictions that are currently lacking regulation on that matter would be to identify functions that cannot be outsourced and a reasonable review in this regard. Lastly, we want to add that the main focus should be on the rights and responsibilities linked to organisational decision-making rather than simply on whether activities are insourced or outsourced.

In closing, FESE wants to highlight that, from a European point of view, most of the identified risks are already being taken care of and the regulators as well as supervisors are sufficiently equipped to face the described risks, if necessary. Regarding the recommended regulatory toolkit, the principle of proportionality should be reiterated, as further regulation should always be in proportion with its goal and only implemented if a regulatory gap is identified. The IOSCO paper identifies risks based on a broad cross-jurisdictional approach. In order to make meaningful changes, the respective national legislators must assess the identified risks in detail and investigate whether they are not already being addressed. For example, one cannot imagine an EU exchange being part of a letter-box company nor EU supervisors being unable to counteract this risk. Furthermore, the question of the effectiveness of supervision should always take precedence over any possible expansion of supervisory powers leading to higher complexities and costs for all parties affected.

Lastly, we would like to correct some inaccuracies in the consultation, such as Boerse Berlin, Boerse Stuttgart Tradegate, Boerse Duesseldorf, Boerse Muenchen, Equiduct, Nordic Growth Market, or BX Swiss being incorrectly identified as part of the Deutsche Boerse Group. The equity trading venue operated by Deutsche Boerse Group is Frankfurter Wertpapierboerse - Frankfurt Stock Exchange. We would like to specify the business lines performed at the Deutsche Boerse group level: trading services and related joint services; further market data services and feeds, and analytics; services for funds; settlement and custody of financial instruments; management of collateral and liquidity; provision of indices, data, software, SaaS and analytical solutions. Boerse Stuttgart Group operates the Boerse Stuttgart Stock Exchange, BX Swiss as well as the Nordic Growth Market.