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Fair and Effective Markets Review
Bank of England
HM Treasury
Financial Conduct Authority

Re: Fair and Effective Markets Review

Dear Sir or Madam,

Deutsche Bank welcomes the opportunity to comment on the above consultation. We welcome the Review's approach to considering regulatory change that is already in train, its openness to market led as well as legislative solutions, and the fact that FICC markets are global in nature.

On market microstructure, regulators should take into account the interplay between prudential and conduct regulation and in particular its impact on market making activities which are critical to the functioning of FICC markets.

In relation to conflicts of interest, firms should ensure proper monitoring of information barriers, use of electronic communication and conduct periodical assessments of potential conflicts and the preventative action that is being taken.

Once fully implemented, regulatory initiatives on benchmarks should be enough to ensure all benchmarks meet a minimum standard of governance, methodology and transparency, although the focus should remain on the most systemically important benchmarks. Enhanced codes of conduct providing more clarity around information sharing in particular would be welcome. More broadly, market practice standards need to be clearer and in particular, more business specific.

Inadequate governance and incentive arrangements have clearly had a role to play and need to be addressed, although this is an ongoing programme of work for market participants. We think there could be a broader role for the Senior Managers Certification regime as well as the Banking Standards Review Council.

Please do not hesitate to let us know if you have any questions about these points or if there are any issues related to this topic which you would like to discuss further.

Yours sincerely,

Daniel Trinder
Global Head of Regulatory Policy

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Barrier and digital options

Q3: Do trading practices involving barrier or digital options pose risks to the fairness and effectiveness of one or more FICC markets? How hard is it to distinguish between hedging and 'defending' such options in practice? Should further measures be taken to deal with the risks posed by barrier options, whether through market-wide disclosure of significant barrier positions, an extension of regulation or some other route?

At present, it can be difficult to distinguish between hedging and defending barrier options, because the theoretical hedge positions vary strongly near the maturity date, if the spot price of the underlying trades near the strike or barrier level. Further measures should be considered carefully. In particular, market wide disclosure of barrier options would not be desirable, because there would be a risk that with knowledge of the barrier trigger level, some market participants might be incentivised to drive the market towards this price.

All firms should be required to ensure they have clear internal guidance around (i) the appropriate hedging relative to the underlying and guidance around when it is reasonable and proportional to initiate and unwind hedges, (ii) appropriate communication with customers and counterparts, and (iii) who should have access to the information within the firm. However, even the best guidance will necessarily need to leave a significant degree of judgment and discretion to those subject to it.

Market microstructure

Q4: Does the market microstructure of specific FICC markets — including trading structures, transparency, asset heterogeneity or market access — enhance or diminish fairness and effectiveness? Where there are deficiencies, will recent or in-train regulatory or technological changes improve the situation, or are further steps needed? How do these answers vary across jurisdictions, or specific markets within FICC?

In general, we consider FICC markets to be fair and effective. As the Review describes, there has been a trend over time towards greater standardisation and electronification, driven by regulation and natural market evolution. We would make the following observations:

- FX markets are characterised by high levels of electronic execution, are extremely competitive, and the quote driven OTC model delivers benefits to clients

- Corporate bond liquidity remains a challenge and there are questions over the efficacy of the current structure given changes to prudential regulation and its impact on bond market inventory. MiFID 2 transparency and market structure changes could help to improve the situation, but much will depend on the final calibration in the implementing rules which will be produced by ESMA. We also see international consistency with the US as important here, particularly around post trade transparency and volume masking. Market making remains an important aspect of the market structure and should be supported.

- Rates and credit markets are largely characterised by RFQ style trading which we think achieves the right balance between transparency and competition.

Q5: Is greater use of electronic trading venues for a wider range of market participants possible or desirable? Are there barriers preventing a shift to a more transparent market structure?

We are generally supportive of greater use of electronic trading venues and more transparency. However, they should be seen alongside bilateral markets which present some benefits to clients

including: more accurate and better pricing, continuous liquidity provision during times of market stress and knowledge of who the counterparty to the trade is. The principle of client choice should be observed and markets should evolve to meet client demand.

It should be noted that greater transparency does not necessarily lead to more fair and effective markets or better execution quality for clients. If not calibrated in the right manner, increased post trade transparency may reduce market making and limit the trading ability of firms conducting genuine risk transfer, particularly in large sizes and in less liquid products.

Q6: Is standardisation of corporate bond issuance possible or desirable? Should standardisation be contemplated across a broader range of fixed income products? How could that be brought about?

The process around corporate bond issuance is already largely standardised and further standardisation is not considered desirable from the perspective of an issuer or from a market stability standpoint. Standardisation of interest payment dates, maturity dates or coupon structure would remove flexibility from corporate bond issuance, which draws issuers in the first place. Not having diversity in maturities would also create a concentrated volume of redemptions on specific dates, which would cause market volatility. Based on an underlying set of cashflows that a corporate expects within their business, they look to structure bond interest payments to match up. If there is a mismatch, they run the risk of not having the funds in time to satisfy their coupon payment to investors or alternatively can have the cash too early, thereby incurring a cost of carry for days where it sits in short term deposits or money market funds until required. Sometimes flexibility in structure is needed if a company has a specific contract which can require a delayed requirement for funds (thereby needing a delayed settlement on the bond) etc.

We are not aware of a widespread investor interest in further standardisation but are convinced that any move towards it would make corporate bond issuance less attractive to the market.

Q7: Should the new issue process for bonds be made more transparent through the use of auction mechanisms, publication of allocations or some other route?

We believe that the new issue process for bonds is currently sufficiently transparent.

There are a number of factors to be aware of when considering an increase of transparency, including client confidentiality, as investors require confidentiality regarding the allocation they receive and disclosure of allocations would be in breach of this.

From the perspective of a bank who is contracted by corporates to pricing and distribute debt to investors, per our terms of business, we represent the issuer in the first instance. Final allocation is solely decided upon by a corporate after their advisor bank or syndicate of banks on the transaction compiles an orderbook of firm investor interest for them. Based on knowledge of the investor market, banks can share investor behaviour in order to inform the corporates allocation decision more appropriately. After an orderbook is closed the syndicate of banks would analyse it to provide a recommendation of allocations to the corporate to finally make their allocation decision. Approximately 95% of issuances participated in last year was part of a syndicate (more than 1 bank involved), rather than an issuance with a sole lead and therefore the allocation recommendation is typically a group recommendation.

The allocation recommendation is driven by a range of factors including knowing which investors are long term bond holders, the investors who are able to place large orders to start building an orderbook, investors who will support a deal in tougher markets, those who can provide price leadership and feedback early in the process and those willing to sponsor debut issuers and engage

on roadshows. Most of the attributes highlighted here tend to be associated with some of the larger investors in the market, which means that some smaller investors often may not receive their ideal allocation on issuances due to them not having/having less of these traits. Due to the oversubscribed nature of most deals (where the volume of interest in purchasing a bond is far higher than the actual notional being issued), the amount of allocation an investor wants – whether they are a large or smaller investor – tends to get scaled back. Policies and procedures for all major banks in the market are aligned with ICMA Guidelines for the syndicate recommendation on allocation.

Auction mechanisms are already used to a small extent in sovereign bond markets but very little elsewhere due to a lack of investor interest in this form of pricing. Experience from auction priced issuances is that investors find the process more opaque than traditional bond pricing mechanisms and feel less engaged. Having a syndicate and corporate build a book of investors who are less likely to flip bonds provides a sense of comfort for investors on the pricing/final investor base and helps to ensure there is stable to favourable after market performance.

Q8: Are there risks associated with internalisation and last look practices? Are there barriers preventing increased pre and post-trade transparency in foreign exchange markets?

Impact of internalisation on spreads

We agree with the analysis and evidence in paragraph 12, page 25 of the FEMR consultation document that internalisation leads to benefits in terms of narrower bid-offer spreads and allows for the availability of multiple prices from different dealers and platforms.

Tailored liquidity available in the OTC FX spot market also means that clients can be offered more accurate pricing depending on the nature of their flow. As in other industries, such as insurance, the premium will vary depending on the risk and the nature of the client. It avoids the subsidy inherent in an exchange "one-size fits all" central limit orderbook where traders motivated by genuine underlying liquidity demand subsidise opportunistic / predatory traders.

Rate of internalisation over time and in market stress

In general, the rate of internalisation liquidity providers can achieve (and associated spreads they can offer) varies by client and is largely driven by the nature of the client's flow, its execution style, and activity of other participants in the marketplace. Other factors that affect the rate of internalisation include market liquidity & dynamics, risk bearing capacity of the liquidity provider, size and composition of client-base.

Our internalisation rate in electronic spot FX has been relatively constant, with a small downward trend that can be attributed to certain clients moving their execution away from single-dealer platforms to aggregators.

In stressed markets, internalised and on venue volumes have tended to increase, and the closer dealer-client relationship that internalisation provides helps to dampen shocks rather than exacerbate them. In addition, a multiplicity of channels exists for inter-bank trading which can be used when this is necessary. The risks associated with a one directional market are the same regardless of whether the principal model of trading is exchange based or bilateral OTC.

Internalisation and transparency

In contrast to the assumption that the FX market structure reduces transparency, pre-trade transparency is high compared with some markets: (i) at low effort, many competing price streams can be obtained to give the client a very accurate view of where the market is trading and what liquidity is available (ii) the counterparty/liquidity provider is known before the trade, i.e. OTC FX is fully disclosed trading unlike on-exchange trading which is anonymous. In the OTC FX market, there

is a greater incentive for the liquidity provider to maintain fair market prices during times of market stress than there is in the on-exchange market.

Internalisation and Concentration

The Euromoney stats for the last 9 years show that market share of the Top 5 banks in FX spot and derivatives has been relatively stable.

Year	Top 5 Banks – % Market Share
2006	54.55
2007	56.31
2008	58.21
2009	61.5
2010	54.66
2011	45.87
2012	54.98
2013	57.36
2014	60.62

Source: Euromoney

In addition, the buyside have started to compete with banks in terms of liquidity provision in recent years. Their volumes are not accounted for above but are not an insignificant part of the market. The stated figures therefore overestimate the true market share of the top 5 banks.

Internalisation and the existence of external markets are complementary and not substitutes and as stated above, during stressed markets, volumes have increased on both. Overall, the market is relatively dispersed across a range of platforms.

Last look practices

In our view, there should be a requirement for all participants to state clearly and transparently how they approach last look.

Q9: Are there barriers impeding the development of more comprehensive netting and execution facilities for transacting foreign exchange fix orders?

There is no easy solution to the question of greater netting for FX fixing orders. The challenge is the treatment of residual positions left after netting has taken place. It is a significant challenge but DB is supportive of progress towards greater netting for FX fixing orders.

We support initiatives to segregate trading in fix orders from other types of trading to eliminate potential conflicts of interest.

Q10: Are there any material barriers preventing greater transparency in OTC commodity derivatives markets? If so, what could be done to remove them?

Any barriers to transparency that are specific to commodities are structural in the nature of the market itself:

- The market is very fragmented both by underlying (i.e. base metals, precious metals, oil, gas, wheat, sugar etc.) and geographically (i.e. each underlying has multiple producer and consumer countries)

- A high proportion of contracts represent physical shipment and delivery requirements and are therefore bespoke.

These factors tend to mitigate against transparency via standardisation.

Q11: Are there any areas of FICC markets where regulatory measures or internationally co-ordinated regulatory action are necessary to address fundamental structural problems that exist?

International coordination of regulatory measures is an important aspect of fair and effective markets in a global context. Consistent rules on a global basis, or regulators deferring to rules in another jurisdiction are a critical aspect of this.

Conflicts of interest and information flows

Q12: Where do potential conflicts of interest arise in the various FICC markets, and how do they affect the use and potential abuse of confidential information, both within and between firms?

We agree with the conflicts of interests which the Review identifies, although would note that they are not specific to FICC markets. As also identified by the Review, firms have a range of methods they can employ to manage these conflicts.

Q13: How can the vulnerabilities posed by such conflicts be reduced? Are existing internal structures and control procedures sufficient? Where they are not, are further internal management controls required (such as better trading floor design and/or closer monitoring of electronic communications within and between firms) or is more radical action required to remove conflicts altogether?

Management of conflicts of interest are best done through:

- Clearer guidance on, and greater monitoring of the use of electronic communication
- Improved use and monitoring of information barriers and functional / physical separation of business lines
- Incorporating more detailed provisions regarding information flows and contractual standards into market / firm codes of conduct

More radical action such as a specific trading floor design or structural break up of FICC firms is not necessary to reduce conflicts of interest and in some cases could result in detrimental client outcomes. For example, having the derivatives traders sat next to spot FX traders results in better and more informed pricing for clients.

Firms should conduct periodical conflicts of interest assessments which summarise all potential conflicts in relevant business lines, together with their associated mitigating measures. Clear organisational structures/responsibilities and a robust and sustainable control framework are effective provisions to further reduce risks associated with conflicts of interest.

Competition and market discipline

Q14: Is there a relationship between the level of competition in FICC markets globally and the fairness and effectiveness of those markets? What risks are posed by the increase in concentration seen in some FICC markets? In answering this, please have regard to the geographical scope of any relevant markets.

In our experience competition in most if not all FICC markets is generally very strong. For example, a 60% concentration for the top 5 banks in spot FX markets is not unusual compared to other non financial services industries. In many FICC markets only the top 5 or even top 3 banks can operate profitably – one of the reasons for this is increased financial resource requirements particularly for market making activities in FICC markets as well as increasing barriers to entry resulting from higher regulatory standards. Some market participants have ceased offering certain products to clients for this reason.

New regulatory requirements which may further intensify this trend may include:

- MiFID 2 pre and post trade transparency obligations: If insufficiently tailored for less liquid instruments, this could result in reduced market making in those instruments
- Bank structural reforms could further reduce the ability of as well as the incentives for some universal banks to devote capital and financial resources to market making
- Rules relating to capital, liquidity and leverage reduce the ability of banks to hold trading book inventories which are necessary to facilitate market making
- Rules with extra-territorial impact and global rules that are implemented inconsistently across jurisdictions make it harder for institutions operating on a cross border basis

Q15: To the extent that competition is currently ineffective in any of the FICC markets, are there market-led initiatives, technological or structural changes that may remedy this situation?

We have some concerns regarding competition amongst vendors such as technology and data providers. Some practices, such as large subsidies for new technology solutions by incumbent providers may result in some markets effectively being closed to new or startup entrants who would otherwise create competition. This might be an area where there is a risk that monopolistic market structures could evolve in the future.

Q16: Are there any lessons that can be drawn from experiences in other financial markets (or indeed other markets) about the ways that alternative or evolving market structures could impact on competition in FICC markets?

The Review mentions the increased competition in equity markets that resulted from MiFID 1. Whilst there were benefits (exchange fees / cost of execution has reduced), there were also some disadvantages that need to be taken into account when considering potential changes to FICC market structures in order to avoid unintended consequences such as:

- Participants had to adapt to the new environment – e.g. smart order routing and investment in technology which increased search costs
- Inconsistency of post trade data makes it difficult for market participants to obtain a consistent overall view of trading activity in the marketplace

All potential consequences from changes to market structure should therefore be considered carefully. Fragmentation in FICC markets is also fundamentally different to equities, because of the heterogeneous product set, and further fragmentation would therefore not be desirable.

The proliferation of order types that was seen in the equity markets in the US and in the EU post MiFID 2 would also not be particularly welcome.

Q18: In what ways might competition in any of the key FICC markets usefully be addressed by competition authorities (e.g. by assessing the state of competition in relevant markets)?

We welcome the review of competition in wholesale markets that is currently being conducted by the FCA.

Benchmarks

Q21: Do current domestic and international initiatives by industry and regulators to improve the robustness of benchmarks go far enough, or are further measures required?

Regulatory initiatives both in the EU, UK and at global level will, once fully implemented, go far enough to address the robustness of benchmarks. We particularly support the focus that domestic (UK) and global (IOSCO) initiatives have placed on the most systemically important benchmarks, and hope that the final EU regulation will do the same.

Specifically in FX, and consistent with our response to the FSB on FX Benchmarks, we think existing codes of conduct should be enhanced and adherence to be made much clearer. The FSB acknowledged that many banks have already made changes in the areas addressed by the FSB and are working with central banks to develop further execution guidelines and communication standards.

Q22: What steps could be taken to reduce the reliance of asset managers and other investors on benchmarks?

It should be recognised that major benchmarks will remain very important to market participants. We would support the development of alternative benchmarks, with input from market participants, to ensure that they meet their intended purpose and do not disrupt markets. Users of benchmarks could then consider these based on specific intended use and client needs.

Q23: What additional changes could be made to the design, construction and governance of benchmarks?

DB supports initiatives by regulators and central banks to move away from survey-based benchmarks towards transaction-based benchmarks and to improve benchmark controls.

However, it should be recognised that benchmarks will still be important in markets where entirely transaction-based data may not always be available. While efforts should be made to ensure high quality input data, in some cases expert judgment may continue to play a role. Where this is the case, this should be subject to a higher set of controls and the basis for the determination sufficiently documented. As a corollary, it should be recognised that the types of controls required for survey-based benchmarks will differ from those for transaction-based ones, and regulatory requirements should be applied proportionately to the risks in the benchmark's design.

In FX specifically, we support industry led initiatives to deliver greater netting of FX fixing orders, but there is no easy solution to the treatment of residual positions left after netting has taken place. We also supported the development of a volume weighted average price (VWAP) methodology as the most representative of the underlying market. We believe this is the most robust methodology as it is based on actual transactions and would work better across currencies.

Q24: Should there be an industry panel to discuss benchmark use and design with the aim of assisting industry transition?

Yes. If alternatives are developed, this must be in consultation with market participants to ensure they are commercially viable (i.e. have sufficient liquidity and are replicable for hedging purposes). Any transition would need to be carefully managed, market-led and phased over time, given the potential impact on existing contracts that reference benchmarks.

Q25: What further measures are necessary to ensure full compliance with the IOSCO Principles for financial benchmarks by all benchmark providers?

We strongly support further work by regulators and IOSCO to ensure full compliance with the Principles for financial benchmarks. This will be especially important once the EU regulation on benchmarks is implemented, which – while it will ensure compliance within the EU – also imposes obligations on users of non-EU benchmarks which are not equivalent.

Q26: How can the regulatory framework provide protection to market participants for benchmarks administered in other jurisdictions in a proportionate way?

Jurisdictions outside of the EU should provide the necessary legal clarity by implementing the IOSCO Principles for Financial Benchmarks and applying them to the most systemically important and widely used benchmarks. This would support equivalency assessments and provide protection to market participants without restricting the use of benchmarks administered in non EU jurisdictions.

Standards of market practice

Q27: Are existing sources of information regarding standards of market practice across FICC markets globally: (a) already sufficiently clear (or will be once current regulatory reform has concluded); (b) sufficient, but in need of clearer communication or education efforts; or (c) not sufficiently clear, requiring more specific guidance or rules to provide more detail or close genuine gaps?

Standards of market practice should be clearer, and in particular, more business specific. This would provide much needed clarity in a number of 'grey areas' where market participants may be unsure of how they should act in a particular situation. There are specific issues described below which we think warrant further clarification.

Q28: Box 7 on pages 36–37 discusses a number of uncertainties over FICC market practices reported by market participants, including: the need for greater clarity over when a firm is acting in a principal or an agency capacity; reported difficulties distinguishing between legitimate trading activity and inappropriate front-running or market manipulation; and standards for internal and external communication of market activity. To the extent that there are uncertainties among participants in the different FICC markets over how they should apply existing market standards in less clear-cut situations, what are they?

We agree that there is some uncertainty over distinguishing between whether a firm is acting in a principal or an agency capacity and around standards of internal and external communication.

In respect of principal vs agency, venues offering liquidity to clients should be transparent to users on whether finality of the deal sits with that venue, or with a liquidity provider providing quotes on a last look basis, or some mixture of the two. End users of FX liquidity need to be able to make an informed choice and pick the style of liquidity provision that suits them.

In respect of communication standards, we support the Recommendations made by the FSB on FX Benchmarks that existing codes of conduct should be revised to provide clarity around information sharing, in particular where the sharing of information can be done in a lawful and legitimate manner. Changes to codes however need to take into account the nature of the market (e.g. widely traded vs less liquid markets).

Q29: How could any perceived need to reduce uncertainties best be addressed: (a) better education about existing standards; (b) new or more detailed market codes on practices or appropriate controls; or (c) new or more detailed regulatory requirements?

We see an opportunity to conduct a stock taking exercise of the existing patchwork of national and regional standards and rationalise where possible. Generally, there are too many Codes of Practice which in some cases can create complexity, cause uncertainty and hinder compliance, in particular where many may apply in a global business such as FX.

The FEMR Market Practitioners Panel could be used as forum for discussing and taking forward changes to Codes of Conduct from a market participant's perspective.

Alternatively, IOSCO or another global standard setting body could be tasked with producing a simple overarching global set of standards.

Q30: How can the industry, firms and regulators improve the understanding of existing codes and regulations by FICC market participants and their managers?

Firms should ensure that staff are properly trained on Codes of Conduct and that understanding by staff is verified on an ongoing basis. Adherence to Codes of Conduct should form part of performance assessment and determination of variable remuneration.

Q31: Should there be professional qualifications for individuals operating in FICC markets? Are there lessons to learn from other jurisdictions — for example, the Financial Industry Regulatory Authority's General Securities Representative (or 'Series 7') exam?

We think it would be worthwhile exploring this further. Some qualifications covering product knowledge and high level conduct principles could be made mandatory, although many banks already require qualifications to be taken for certain roles.

Q32: What role can market codes of practice play in establishing, or reinforcing existing, standards of acceptable market conduct across international FICC markets?

If designed in the right way, and suitably specific to the business area, Codes of Practice can have a very strong role to play in establishing clear standards for market conduct.

Responsibilities, governance and incentives

Q36: How much of a role did inadequate governance, accountability and incentive arrangements play in the recent FICC market abuses, and to what extent do these remain

potential vulnerabilities in FICC markets globally? In addition to on-going regulatory changes, what further steps can firms take to embed good conduct standards in their internal processes and governance frameworks? And how can the authorities, either internationally or domestically, help to reinforce that process, whether through articulating or incentivising good practice, or through further regulatory steps?

Inadequate governance, accountability and incentive arrangements played a role in the recent financial crisis. Regulators and firms have taken a number of steps to address this, but recent developments in FICC market abuses has highlighted this is an ongoing programme of work which requires continuous improvement.

A focus on risk culture is one way in which good conduct can be embedded within an organisation. Culture cannot be improved through any single initiative or prescribed in regulation, but requires a dedicated focus over a longer period of time and a focus on some key elements against which supervisors can assess progress. A programme designed to improve risk culture might include components such as: communication (tone from the top); training; accountability; and monitoring. Senior cross-divisional and cross-functional sponsorship is also a key aspect.

More generally, steps that firms could also take include conducting reviews of their business practices and issuing guidelines to front office staff on conduct that is deemed acceptable and conduct which is deemed unacceptable. This needs to be clearly communicated and there should be clear reporting lines and board oversight of conduct issues and escalation of possible violations.

An important example is the "Red Flags" process, which explicitly links individuals' adherence to an expected set of risk culture behaviours to their performance assessment and to compensation and promotion decisions. Other disciplinary action may also be taken, depending on the severity or frequency of incidents, up to and including dismissal. These expected risk culture behaviours must be embedded across the organisation in a granular way through numerous workshops at all levels to ensure that there is buy-in to these new expectations.

Some conduct issues may be best addressed through the establishment of industry wide best practice, where variation between firms is detrimental to the fairness and effectiveness of the overall market. Industry should also be encouraged to promote best practice across firms and to drive continuous improvement in conduct and professional standards.

Q37: Do respondents' agree that the thematic areas highlighted in Section 5.5 are key priorities for FICC firms (fine-tuning performance measures; adjustments to remuneration; attitudes towards hiring, promotion and advancement; closer board involvement in governance of FICC activities; and clearer front line responsibilities)? What specific solutions to these challenges have worked well, or could work well? And how best can the authorities help to support these initiatives?

We agree that the thematic areas highlighted are the key priorities for FICC firms.

On remuneration, a substantial amount has been done already for banks, particularly through the Financial Stability Board's (FSB) "Principles and Standards for Sound Compensation Practices" which were implemented in the EU under CRDIII, in 2011. These saw a number of enhancements to improve the alignment of variable remuneration with firms' long-term interests, such as requiring changes to remuneration policies, enhanced transparency and material risk takers having a significant proportion of their variable pay subject to deferrals and clawbacks. We believe that, given the internationally competitive nature of the industry, the UK should ensure consistency across financial firms and alignment with global standards to ensure a level playing field.

We broadly support initiatives such as the UK Senior Managers and Certification Regime and the Remuneration Code, but the focus should remain on people in positions of responsibility and material risk takers only. Firms need to be able to apply these requirements in a proportionate manner.

Q38: To what extent could the Banking Standards Review Council help FICC market participants to raise standards collectively — in particular, are there other steps that could be taken to help complement or extend this initiative in FICC markets for non-banks and internationally?

We are supportive of the Banking Standards Review Council and its role in improving the uptake and value of professional qualifications and training in the banking industry. These could be extended to non bank and international market participants. However, in order for this broad scope to work, the new body's approach will need to take into consideration:

- the regulatory and supervisory requirements that foreign banks must already adhere to in their home country; and

- the variety and different nature of activities that banks and other participants operating in the UK undertake. It is likely in many areas to be necessary to set standards according to different types of activity and customers. Many banks operate across retail and wholesale markets where 'customer' may include sophisticated counterparties, large international corporate clients and retail clients. Standards for dealing with customers will need to reflect that diversity.

From a conduct perspective, the BSRC should be careful not to duplicate what is already contained in existing standards around market practice. Instead, it should focus on defining industry standards for best practice, which can be applied in a flexible and proportionate way depending on the nature and scope of firms' activities.

For example, while there is room for greater improvement and industry-wide awareness of what sound internal processes should look like, a one size approach would not be useful in this context. Internal arrangements will differ between institutions, especially depending on their home country regulatory requirements. While it would be useful to get a sense of how internal problems are dealt with and what the escalation and whistleblowing processes looks like at other firms, new structures should not be imposed. Instead, a new organisation could have a role to play in terms of disseminating information and resources on how to manage and improve internal escalation processes.

Measuring cultural change is extremely difficult, and further, it is unlikely that a single set of metrics will reflect cultural change amongst a diversified group of banks. The limitations of metrics in this area should be acknowledged.

Q39: Are there other regulatory measures the authorities could take to strengthen personal accountability or otherwise improve the way firms manage incentives and governance? In particular, should any or all of the measures in the Senior Managers and Certification regime be extended to non-bank firms active in FICC markets?

We support a level playing field across the industry so - in principle - have no objection to the Senior Managers and Certification regime being extended to non bank firms active in FICC markets. In respect of remuneration, there should also be consistency based on the FSB Principles. However, regulators need to exercise a degree of deference to home state rules for entities which have their parent body based outside of the UK and requirements need to be flexible enough to be applied in a proportionate manner. Finally, as we stated in our response to the SMC consultation, given the

significant changes firms will have to do to undergo to implement this regime, timing should be carefully considered.

Surveillance and penalties

Q40: What role can more effective surveillance and penalties for wrongdoing play in improving the fairness and effectiveness of FICC markets globally? How can firms and the industry as a whole step up their efforts in this area? And are there areas where regulatory supervision, surveillance or enforcement in FICC markets could be further strengthened?

More effective surveillance and penalties can play a role but should not be seen as a panacea for improving fairness and effectiveness of FICC markets. Whilst surveillance can act as a deterrent, it will always only catch activity 'after the event' and so should therefore be seen as part of a package of measures.

However, it is clear that in the past surveillance has been more focused on equity markets, but firms have been steadily increasing their surveillance of FICC markets over the recent past.

Platforms / venues themselves should do much more to surveil their markets more effectively for market abuse and market manipulation. This should include more explicit rule books for example to make clear what behavior is acceptable / unacceptable.

Q41: How can firms increase the effectiveness of their own surveillance efforts across FICC markets globally? What role could the industry play in helping to explore best practices on how to make whistleblowing and other similar regimes more effective? Is there scope to make greater use of large scale market data sets and electronic voice surveillance to help detect cases of abuse in FICC markets? Are there other potentially effective tools?

Surveillance of FICC markets should get easier in the future, particularly with the introduction of public price transparency and post trade reporting under MiFID 2. Whistleblowing has been in existence for some time and it is difficult to suggest what could be done to enhance its effectiveness.

In grey areas where it may be unclear what is deemed as market abuse, guidance from regulators which specifies clearly which activity is prohibited would be helpful. For example, the FCA's Code of Market Conduct was useful in this regard but has historically has a focus on the equity markets. Its expansion to cover examples of market abuse relevant to FICC markets would be welcome.

In our experience, voice surveillance works best as a supplementary evidential tool to assist in identifying malpractice once electronic trade surveillance has generated an initial report.

Q42: Are there processes or structures that can allow firms to punish malpractice by their own staff more effectively (for example, penalties for breaching internal guidelines)?

Malpractice should be taken into account during an individual's performance review, compensation discussions and promotions prospects.

Q43: Could firms active in FICC markets do more to punish malpractice by other firms, for example by shifting business and reporting such behaviour to the authorities?

There are examples of firms in FICC markets reporting malpractice to authorities (see Mark Stevenson case) – this should be encouraged as far as possible.

Q45: Are there ways to improve the data on FICC market trading behaviour available to the FCA, whether through the extension of the regulatory perimeter or otherwise?

The reporting requirements being introduced under MiFID 2 will go a long way towards addressing this.

Q47: Should consideration be given to greater use of early intervention, for example, temporary suspension of permission for a particular trading activity for firms or individuals or increased capital charges?

These are draconian measures and should be used only in extreme cases. The principle of presumption of innocence until proven guilty should be followed.

Q48: Is there a need to widen and or strengthen criminal sanctions for misconduct in FICC markets?

Whilst we support strong sanctions to act as a deterrent against bad behaviour, criminal sanctions have been in existence in the UK for some time, for example for insider dealing under the Criminal Justice Act of 1993, but have not always been actively utilised by prosecuting authorities, or demonstrably led to a decrease in market based offences.