



Equity Market Resilience

IA Position Paper on how to manage exchange outages

About The IA

The Investment Association (The IA) represents UK investment managers, a world-leading industry which helps millions of households save for the future while supporting business and economic growth in the UK and abroad. Our 270 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £10 trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond 46% of this is for overseas clients. The UK asset management industry is the largest in Europe and the second largest globally and supports 122,000 jobs across the UK. Our mission is to make investment better. Better for clients, so they achieve their financial goals. Better for companies, so they get the capital they need to grow and better for the economy, so everyone prospers.

The need for clear best practice in the event of a market outage

There is currently no guidance or standardised communication to market participants in the event of a market outage and yet, Exchange outages can have a severe impact on the market. A recent outage of note, the Euronext outage on 19th October 2020, saw a three-hour outage that effectively ceased trading in the region and caused issues in the closing auction. This incident illustrates the market’s current inability to sustain trading when there is a market outage, instead operating on a “watch and wait basis.”

In addition, and at a time of heightened cyber security risks globally, where the possibility of venue outages could become more apparent, The IA and its members consider it vital that regulators work to establish clear best practice in the event of market outages to ensure resilience is strengthened and disruption is minimised.

To this end, we are extremely supportive of HM Treasury’s proposals for the UK authorities to work with the industry to implement a playbook for market participants and operators to follow in the event of future market outages.

The IA has produced the below position paper which sets out members’ recommendations as to how regulators can assist the industry to address market outages when they occur. This paper also identifies the expectations IA members have in terms of the steps exchanges should take to communicate a market outage and further feedback the industry would expect to be communicated during the immediate aftermath of such an incident.

Current legislative limitations that impeded or impact continuation of trading during a market outage



Certain requirements within MiFIR such as article 4 (1) (a) which states that “ *the reference price waiver (RPW) can be used when systems match orders based on a trading methodology by which the reference price of the financial instrument is derived from the trading venue where that financial instrument was first admitted to trading or the most relevant market in terms of liquidity, where that reference price is widely published and is regarded by market participants as a reliable reference price*” requires reconsideration. As currently structured, this requirement restricts the ability of markets to continue to function if the primary venue goes down as that is deemed the “most relevant open market” and the market loses that reference point.

To overcome this the IA suggests either granting permission to the operator of the primary venue to assemble a consolidated Best Bid Offer (BBO) or utilising the BBO of any sufficient robust/liquid venue.

From past experiences of market outages our members have also observed that market participants operating venues have felt pressured to resume trading within the timeframe mandated in RTS 7 despite not necessarily being ready to do so. Despite this, they go ahead regardless of the fact they may still have system issues which can have further unintended consequences for the market.

In order to alleviate this perceived pressure to ensure trading is resumed within the outlined two-hour timespan and reduce the impact of any unintended repercussions on the market, IA members suggest amending article 15 (2) of RTS 7 which currently states that “*The business continuity arrangements shall ensure that trading can be resumed within or close to two hours of a disruptive incident*” to read “The business continuity arrangements **will aim** to ensure that trading can be resumed within or close to two hours of a disruptive incident provided it is safe to do so.” The business continuity arrangements should be intended as guidance and not an absolute with the intention that trading can be resumed within or close to two hours of a disruptive incident, however there should be **no** obligation to reopen the venue and resume trading until the operator is confident that all issues that contributed to the outage have been resolved. The priority in any outage situation must be to ensure all known issues are rectified before re-opening the venue and resuming trading.

Recommendations for regulators

The IA believes regulators should:

- Ensure a standardised notice is issued during an outage which should set out how trading venues manage these outages and the ensuing disruption to trading.
- Provide clear guidance setting out:
 - A timeframe during which participants should be informed when a market is down and;
 - a timeline of when trading can be expected to resume.
- Provide guidance on the immediate halting of market data during an outage. This would ensure that exchanges put processes in place to completely and clearly halt their market data streams during an outage, and thus mitigate current confusion.
- Seek feedback from venues, index providers and participants on the potential for an alternative mechanism to act as a closing auction in the event of an outage. This



could involve alternative venues stepping in to provide key benchmarks as a backup during primary outages, like those being tested by Nasdaq.

- For intermediaries (broker dealers) to be encouraged to utilise the use of European Best Bid and Offer (EBBO) price feeds to continue trading on other venues in an instance of an outage, this would ensure the execution of inflows and outflows in an orderly manner, particularly for those trades that are time sensitive.

Furthermore, and as widely agreed amongst market stakeholders, the development of a consolidated tape for equities that includes pre-trade data would significantly improve the resilience of equity markets, as market participants would have access to a broader range of market data which would mean less reliance on one single venue. We welcome the announcement as part of the Wholesale Markets Review that the FCA will be working towards the development of a consolidated tape in the UK and encourage regulators to work with market participants to ensure the creation of a tape that is beneficial to and supportive of the market as a whole.

Expectations for Exchanges and Venues

In the event of an outage, the IA would expect the following from exchanges and trading venues:

- Clear, structured communication, including a standardised protocol followed by all exchanges and trading venues if they experience an outage. It is our view that ideally there should be standard messaging on a global basis including universal standard flags disseminated by venues when they suffer an outage.
- Immediate halting of market data. Exchange data should be halted immediately with a clear, standardised message disseminated electronically.
- To clarify within one hour whether trades executed from the moment the problem was detected still stand, if they do not stand all orders should be cancelled.
- Standard reopening procedures. There should be a standard reopening procedure, including a communication in advance of reopening. For example, ***“Exchange X will reopen in 15 minutes with an auction”***.
- In the event that the primary exchange/trading venue is experiencing technical disruptions/difficulties, an industry agreed alternative exchange/venue needs to be identified. The criteria for agreeing this alternative should be determined based on the venues’ ability to trade those instruments effected by the outage and technical capability rather than on ownership or domicile of the exchange/venue.
- The industry back-up for the closing auction should mirror the exact mechanisms of the primary auction provider.

Whilst these improvements can largely be solved by market participants, regulatory enforcement would guarantee their success and ensure market disruption is largely curtailed and the impact on the end investor minimised.