



WORLD FEDERATION OF EXCHANGES

7th June 2007

Ms. Tillie Rijk
IOSCO General Secretariat
Oquendo 12
ES - 28006 Madrid

Via e-mail to t.rijk@iosco.org / original by mail

Re: Public comment on “An Overview of the Work of the IOSCO Technical Committee.”
March 2007

Dear Ms. Rijk,

The World Federation of Exchanges, WFE, welcomes the opportunity to respond to the IOSCO Technical Committee Consultation Report on “*An Overview of the Work of the IOSCO Technical Committee*,” dated March 2007. As the global association for the exchange industry and the operators of the world’s regulated securities and derivatives markets, WFE greatly values its dialogue with IOSCO.

This response is based on comments made by several of the Federation’s members, along with those from the Secretariat. The working group limited itself to topics where exchanges feel themselves best qualified and able to support the work of IOSCO by drawing on their experience as operators of regulated markets. In addition, other comments are offered when a particular expertise may be drawn on within WFE to assist the Technical Committee, or when exchanges have identified other topics on the capital markets that IOSCO may wish to explore. This response was then reviewed and approved by the Federation’s Board of Directors.

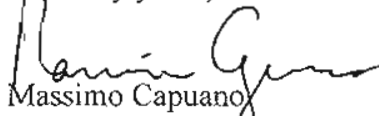
I express my thanks to IOSCO Technical Committee Chairman Michel Prada for having included the WFE Secretariat and several exchange delegates in the public meeting he convened on this subject at IOSCO headquarters last March.

For this public inquiry, the WFE Board of Directors found value not only in being asked to contribute comments, but in actually seeing how IOSCO is laying out its plans and priorities. The Federation’s response can be made public in its entirety, in respect of IOSCO’s own clear method of proceeding.

WFE attaches great importance to the public consultation process that the IOSCO Technical Committee has undertaken, and especially appreciated the extensive citation of its remarks in last June’s policy paper completed by Standing Committee 2. It would request that all major programs continue to be issued in consultation form, in order to enable exchanges and other actors to shape regulatory conclusions that make good business sense for developing robust and fair markets. It would be a useful discipline for IOSCO to accept, as other global standards-setting bodies do.

This request to IOSCO is made along with an offer of cooperation and partnership : IOSCO would want to know that for the Federation to respond to such consultations, it is forming a standing global Regulation Committee, enabling WFE to be reactive and comprehensive in the comments it will offer.

Sincerely yours,

A handwritten signature in black ink, appearing to read 'Massimo Capuano', written over the printed name.

Massimo Capuano
Chairman of the World Federation of Exchanges
President and Chief Executive Officer of Borsa Italiana SpA

The following comments are structured in accordance with IOSCO's own Report.

A. Issuers

Regarding issuers, there are a few areas where WFE may offer support to IOSCO at this time. The first is that within the diversity of the Federation's membership, some exchanges have set up specific market segments where issuers have to comply with higher standards, notably on corporate governance or more broadly on ESG (environment, social, governance) matters. If IOSCO were to choose to explore this, members' expertise and experience to date might prove useful, and would be made available to it.

Also as regards issuers, on the point of their disclosure of financial information, WFE has long held a strongly favourable position on IFRS. Throughout the 1990s, the Federation's precursor institution (FIBV) and several exchange leaders were actively involved in the work of the International Accounting Standards Board. Simply stated, exchanges have an interest in having clear and more explicitly comparable financial information produced for the world's capital markets by the issuers of securities.

At the General Assembly of members in October 2000, the FIBV voted a resolution in support of the development and implementation of what has become IFRS.

The quality of financial information is a critical component of investor protection. At the very outset of IOSCO's own document, this concern is restated. WFE affirms that exchanges and their regulatory authorities have a common base in stressing investor protection, and exchanges can play a particular role here because of their market-neutral position.

As IOSCO returns to this central point, the Federation suggests that it may wish to include in its analyses of investor protection the initiatives taken in the self-regulatory field, as is stated in the IOSCO Report. IOSCO might do so as this relates to issuers, and of course in other business areas.

B. Accountants and auditors

WFE supports IOSCO work in this field. On behalf of WFE, the Secretary General has served for five years as a member of the International Federation of Accountants (IFAC) Consultative Advisory Group on International Audit and Assurance Standards Board (IAASB) issues. Likewise, IOSCO has also been a long-serving member of this Consultative Advisory Group; in this area, WFE and IOSCO have been effective partners.

In October 2006, to mirror the resolution voted six years earlier in support of IFRS, the WFE General Assembly endorsed the IFAC structure of public oversight and the processes its bodies have established for creating high quality global standards for audit work and assurance reviews. In mailing its 2006 annual report, IFAC noted this endorsement of its work by WFE at the top of its list of achievements last year.

In a related vein, WFE would propose that IOSCO consider adding interactive data, or XBRL (Extensible Business Reporting Language), as a topic of investigation. This technology should prove to be an opportunity for promoting more just, efficient and sounder markets – which ties back to the common interest expressed above on investor protection.

XBRL has been an important subject for WFE since it first figured on the 2003 Annual Meeting agenda, and earlier in the case of several of its members. Numerous exchanges have been involved in promoting XBRL in their national jurisdictions, and have developed specific services based on that IT language.

At the invitation of the XBRL Steering Committee, the WFE Secretary General has been serving as the first chairman of the XBRL Board of Advisors. At the March 2007 meeting of that body, it was resolved to invite a representative of IOSCO to join in this effort. It is critical to broaden the involvement of official institutions at the XBRL Board of Advisors level beyond the central banking representation already present; the XBRL International consortium understands that implementation and ongoing robustness of these standards will not work as well without it. The invitation was extended in April 2007 to the IOSCO Secretary General for him to identify the most appropriate person for this work.

As with the common work both institutions provide on global audit standards, IOSCO and WFE should logically be productive partners on XBRL.

C. 1.1 Bond Market Transparency

WFE supports initiatives that reinforce transparency in financial markets. Transparency enhances investor protection, which remains a paramount concern at every turn of the path.

For the corporate and public debt markets, member exchanges would again underscore the value of transparency, exactly as they do for the trading segments they operate for other financial instruments, and for the very same reasons of fairness to participants.

Some WFE members have conducted studies showing that trade reporting requirements have engendered more transparency in the markets they operate, resulting in narrower spreads and increased secondary market trading volumes, and so greater efficiency over all. But others have shown that according to the market segment, efficiency measures would tend to confirm that professional traders have achieved a high level of liquidity – and therefore efficiency – under the pressure of market conditions alone, without being subject to too much regulation on their operations in the form of reporting. Still other exchanges would want to underscore that perhaps a differentiation by client type (individual versus institutional) as well as market segmentation by type of instrument would be worthy of further reflection. Post-trade transparency enabled by central reporting can be seen as a key element to achieving greater fairness, and this element could be extended to making some information public on pre-trade positions as well.

For the IOSCO Technical Committee, if it chooses to go forward with work in this area, WFE would recommend that it above all investigate different existing models of successful markets. It would appear that there are a variety of ways of advancing in the enhancement of these markets, and monitoring of these segments and client types should take this into consideration. For those markets where pre- and post-trade reporting requirements have been established, and judging by trading liquidity these markets work successfully, the Federation would recommend that these existing rules be respected.

C. 1.2 Multi-jurisdictional Information Sharing for Market Oversight

WFE members favour information sharing across borders as a support to the operations of public regulated capital markets. WFE would be willing to cooperate with IOSCO to the extent legally possible for its members, as this is typically an area of shared responsibility between exchanges and their regulators, in any case. The Federation appreciates the emphasis IOSCO puts into this work, as witnessed by the progressive implementation of its Multi-lateral Memorandum of Understanding (MMOU).

Market surveillance is a core mission for exchanges. WFE is a longstanding supporter of the Inter-market Surveillance Group (ISG). As from earlier this year, the Secretariat has stepped up to provide some practical assistance as ISG positions itself as a more global body with a stated interest in a wider membership. In addition, the Futures Industry Association years ago established a multi-lateral MOU of its own to cover information sharing in the derivatives markets; this serves as another example of private-sector response to this business need within the Federation's universe.

Logically, the work of ISG and the FIA in the private sector would have many parallels to the spreading implementation of the IOSCO MMOU, and so may be thought of as a complementary contribution from exchanges to the work of their market supervisors. The Federation would indeed go further, and encourage IOSCO to be sure that its MMOU remains the standard for capital markets in this area. This would enhance the timely sharing of information among exchanges and their supervisory agencies in the multi-jurisdictional sense that IOSCO is indicating. Regulatory agencies are often the channel for passing sensitive market information from one jurisdiction to another.

C. 2.1. Price formation on fragmented markets

WFE reconfirms the statement it made in its comment last June to IOSCO, which remains pertinent and of great importance to exchanges :

“The WFE Secretariat would fully support the IOSCO Technical Committee view that competition between trading venues is positive, but unintended side effects on market integrity, efficiency and investor protection must be carefully monitored. These principles should remain the core features of all market organizational arrangements.”

Fragmentation to the extent already seen – and to the extent that could take place in the coming months - is a relatively new phenomenon. It has been made possible due to technological developments in recent years, as well as changes in regulation. It does result directly from competition, which in its pure sense is a good thing; but fragmentation then does raise specific issues that will need addressing by market operators and their supervisory agencies. Unrestrained competition can have certain undesirable side effects.

For the WFE community, while only a minority of markets have regulation that fosters fragmentation, the issues of market integrity raised are of prime concern for exchanges everywhere.

The effects of fragmentation are utterly different according to the size of markets. The few largest capital markets in the world would likely be better able to adapt to these changing trading conditions by using commercially-based solutions. The smaller capital markets are not likely to have the means to do so.

When fragmentation is the result of regulatory changes encouraged by public authorities, the expected beneficial outcomes of such policy changes should be clarified. To evaluate the results down the road, what success measures for the capital markets did the public authorities have in mind when these changes were implemented? How will they know when the new regulations are working as intended, and how will they measure progress being made towards their goals along the way? In understanding these points, exchanges will be better able to continue to fulfil their responsibilities to the markets in this changing environment.

Are the expected gains from more intense competition greater than the offset of costs arising from fragmentation? Every change in economics has a cost, so what was considered here? If the ultimate aim of competition is more efficient capital markets and so savings for final investors, the WFE would want to be sure that these lower costs for capital formation and secondary market trading are indeed passed on to them. These are the parties whose welfare IOSCO and WFE are charged with safeguarding.

At this time of rapid regulatory change, it behoves all market actors to remain vigilant towards the risk of regulatory arbitrage as an unintended and undesirable result of trading venues not being submitted to the same regulatory constraints as exchanges. There is a need for a level playing field.

Indeed, the notion of fairness of “competition” needs to be underscored. When the WFE Board of Directors met with IOSCO Technical Committee Chairman Prada in January, the point was raised that unequal contributions to support central market infrastructure in these new circumstances does not constitute fair competition in the Federation’s thinking.

The “free-riding issue” will arise if in the post-Regulation NMS and post-MiFID environment, or elsewhere, exchange prices remain the market reference for most purposes, while others trade off them without supporting the central market infrastructure. This may be particularly aggravated by a lack of transparency (pre- and post-trade); e.g. internalization without pre-trade transparency.

To see where the market is in valuing a security, it is likely that there will be a commercial response from the markets themselves that will join together different pools of price discovery. This will be needed in the MiFID context for demonstrating that the new best execution requirements are being met. Today, however, it is hard to see clearly how this will be working after these regulatory changes have taken effect.

One of the key effects of MiFID is the introduction of a new sense of “best execution,” which has been redefined for European Union markets as a broader, more complex goal and obligation of participants. This introduces a different meaning to a globally understood principle of central significance to regulated exchange operations. Because its impact may go well beyond the European Union, IOSCO may wish to evaluate its effects after a pre-established lapse of time.

In sum, WFE would recommend that IOSCO monitor the fragmentation question carefully. IOSCO might want to consider the need to assess the effects of fragmentation over time, taking into account the several factors that combine to set the global cost of a trade transaction. These include the explicit costs, such as exchange fees, brokers fees, clearing and settlement fees; and the implicit costs of market impact, execution time, and opportunity cost.

C. 2.2. ‘Direct’ access to exchanges and other markets

Direct market access (DMA) is a matter of central concern to WFE members.

Historically, the success record of regulated exchanges being able to assure that their participants are good for their orders is solid, and it has been over decades and more. This responsibility on their part must be maintained.

WFE appreciates that changing technology would prompt IOSCO to wish to investigate this area, and can only support such an initiative given the scale and pace of events. Moreover, WFE stands ready to be involved in any such fact-finding research in this complex area, and would suppose that other actor-members of the SRO Consultative Committee would also be involved in drawing up any report. Electronic access may be making this question more acute, and WFE would agree that it is as important to protect the market's integrity as it is the investors themselves.

The Federation would also want to introduce a word of caution here : there is no clear definition accepted by all exchanges as to the meaning of DMA, and it would also say that the term can be something of a misnomer. But what is understood by exchanges is that there is something of a blurring in the distinction made among end-users of central market transaction services. Given this diversity and each exchange's need to have a response appropriate for its local market conditions, the Federation would say that this element of the question should remain a commercial issue for each regulated exchange to handle, but clearly IOSCO needs to understand the controls introduced by exchanges to ensure proper and orderly markets notwithstanding such direct access arrangements.

One other issue that WFE would suggest to IOSCO : securities lending

The WFE is currently studying this wide-spread practice. In particular, the Federation is looking into how securities borrowing is being used in the governance area of public listed entities.

In the Federation's work, reference is made to the document on this topic written by the IOSCO Technical Committee and the Committee on Payment and Settlement Systems in 1999, "*Securities Lending Transactions: Market Development and Implications.*" Also, the WFE is using the International Corporate Governance Network (ICGN) "*Stock Lending Code of Best Practice,*" published in 2005, and has been working with the author of that report.

Given the rapid increase in the scale of this market practice this decade, with revenues generated now far exceeding on-exchange securities transaction revenues themselves, IOSCO might consider an update of its work, or at least keep the question on its radar screen.