



NEW ZEALAND'S EXCHANGE
TE PAEHOKO O AOTEAROA

Indications of Interest

Consultation Paper

August 2020



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This Consultation Paper has been issued by NZX to seek comment on the proposals contained in the paper, with a view to ensuring that the proposals will enable NZX to operate its markets on a fair, orderly and transparent basis. The proposals set out in this paper do not reflect NZX’s concluded views of the matters raised. Capitalised terms which are not defined in this Consultation Paper have the same meanings given to them in the NZX Participant Rules and Derivatives Market Rules.

Introduction

In 2017, as part of the amendments that were made to the NZX Participant Rules and Trading Conduct Guidance Note, NZX consulted on domestic practices relating to the use of indications of interest (**IOIs**). In late 2019, NZX Surveillance undertook a market survey of Trading Participants and obtained the views of institutional investors on the use of IOI in the New Zealand market. In addition, NZX has been monitoring international best practice in respect of the use and dissemination of IOIs.

As a result of that analysis, NZX is proposing amendments to section 4.2 of the Trading Conduct Guidance Note (**Guidance Note**) to:

- clarify conduct expectations in respect of advertising IOIs; and
- adopt the European Association for Financial Markets in Europe and the Investment Association (**AFME/IA**) framework for flagging IOIs.

This Consultation Paper provides further detail of the proposed changes which are set out in the draft amended section 4.2 of Guidance Note which is available [here](#).

Consultation Process

NZX is seeking responses to the proposed changes relating to the use and dissemination of IOI as set out in the draft excerpt of the Guidance Note.

We invite interested parties to provide their views on the proposals raised in this paper by emailing a written submission to policy@nzx.com. The closing date for submissions is **28 August 2020**.

NZX may publish the submissions it receives, so please clearly indicate in your submission if you do not wish your submission to be published, or if part of your submission contains confidential information.

If you have any queries in relation to the review, please contact:

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Background

IOIs are non-binding, usually electronic expressions of trading interest that are used to identify potential counterparties to a large transaction. While IOIs may contain information such as the name of the financial product, trade direction (buy or sell), capacity (agency or principal), volume and price indication, they are not an Order and are usually also not a contractual offer. IOIs are often used by Trading Participants to identify Crossing opportunities.

Internationally, regulatory regimes are becoming increasingly prescriptive in respect of the requirements and expectations for the use of IOIs. Regulators and industry groups across North America, Australia (ASIC), Europe (via MiFID II) and Asia, have sought to clarify minimum expectations for IOI, via a combination of regulatory guidance and market consensus.

NZX is therefore proposing amendments to section 4.2 of the Guidance Note to bring greater integrity to the domestic process for utilizing IOIs, in line with global practice. These changes are intended to improve the value of using IOIs for Clients, without being unduly onerous for NZX Participants to implement.

The proposed changes will also assist Clients who are subject to the MIFID II guidelines, by improving the transparency relating to the placement and management of their Orders.

This Consultation Paper provides further explanation of the changes we are proposing to:

- clarify conduct expectations in respect of advertising IOIs; and
- adopt the AFME/IA framework for flagging IOIs.

Description of the Proposed Amendments

Conduct expectations for advertising IOI

We are proposing to clarify the conduct expectations for the use of IOIs, by providing more detail of our expectations for NZX Participants to adopt controls and procedures to:

- manage the risks of an actual or perceived conflict of interest arising from the advertisement of the IOIs;
- address information imbalances that may result in a worse outcome for the Client due to the use of IOIs;
- manage the risk of IOIs being used to front-run a Client Order; and
- prevent non-genuine IOIs being used to gather and exploit information about genuine Trading intentions.

We wish to ensure that NZX Participants have appropriate arrangements in place to manage the risk of a conflicts of interest occurring between their Clients' interests and their own interests when Trading as Principal. We expect that a Participant's conflict management procedures that are designed to prevent conflicts of interest in respect of their Principal Trading activities, and maintain the confidentiality of client information in respect of Client Orders, will apply equally to Client IOIs.

We have expanded the Guidance to note that we believe that the use of non-genuine IOIs to gather and exploit information about genuine Trading intentions would violate existing provisions of misleading and deceptive conduct under Part 2 and/or Part 5 of the Financial Markets Conduct Act 2013 (**FMCA**), NZX Participant Rule 8.1, NZX Derivatives Rule 4.4 and be contrary to Good Broking Practice.

We are also proposing new requirements that electronic IOI dissemination systems are kept up-to-date and secondly, and that a searchable record should be kept of all disseminated IOI in a manner that is easily retrievable.

Flag all IOIs according to the two “flags” system

Current international best practice requires brokers to use flags for IOIs to indicate different types of IOIs, with the European Association for Financial Markets in Europe and the Investment Association (**AFME/IA**) having the most developed implementation of IOI flag framework. In addition most global IOI dissemination systems accommodate the AFME/IA framework.

We are therefore proposing to introduce requirements for NZX Participants to “flag” all disseminated IOIs following the two “flag” system according to the AFME/IA framework.

NZX wishes to align domestic IOI dissemination with global IOI practices following the “Class:Subclass” system. This involves coding individual IOIs by class (these being either Client, Potential or House), followed by a sub-class describing the nature of the order (numbered from 1 to 3). Please refer to heading 4.2 of the Guidance Note for further detail and examples of the use of the two “flags” system.