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DMIST-Derivatives Market Institute for Standards
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FIA Operations Americas Response to DMIST’s *Consultation Paper: Standard Regarding Average Pricing*

FIA Operations Americas Division (“Division”) appreciates the opportunity to comment on the Derivatives Market Institute for Standards *Consultation Paper: Standard Regarding Average Pricing*. The Division membership includes more than 200 representatives from FCMs, exchanges, clearinghouses, industry service providers, and law firms. The primary objective of the Division is to develop and promote uniform practices and procedures for the futures industry.

In order to respond to the Consultation Paper, the Division convened a committee of its board of directors who work with customers on a daily basis to execute and clear average price transactions. This response was reviewed and approved by the Division board.

The Division has been supportive of standardization around average pricing for many years and even conducted a study in 2005 to document how firms handle average pricing and the feasibility of developing an industry standard that could be used globally. The Division fully supports the goal of achieving consistency across clearinghouses, which will go a long way in alleviating client confusion and help to ensure their transactions are fairly and equitably distributed among their clients. The Division, however, recognizes that full adoption of an average pricing standard is subject to regulatory considerations in each jurisdiction.

We appreciate and support the work that DMIST has done on this important topic. Our comments are divided into two sections: responses to the consultation questions, and comments on certain functions and priorities listed in the Functionality table of the Proposed Standard.

CONSULTATION QUESTIONS

1. Are there advantages to performing Average Pricing off-CCP versus on-CCP?

Off-CCP pricing exists today because of 1) lack of average price tools available across CCPs globally, and 2) lack of consistency among the CCP offerings. It can be more efficient for a broker or client to average

price all trades it executes using the same off-CCP average pricing methodology rather than manage the variety of ways in which CCPs approach average pricing.

Also, off-CCP average pricing has the advantage of allowing allocation of trades throughout the day as an order is worked and filled. It should be noted that average pricing at the CCP level could delay the give-up process from an executing broker perspective, since an order must be completed before an average price group can be created. From the clearing broker perspective, however, CCP-level average pricing is generally more efficient and effective.

Using a CCP's average price system has several advantages. First is the ability to more fully automate the average pricing process from back to front, using middleware systems to interact with clearing. On-CCP average pricing can also significantly reduce the number of allocations in the system. This is most notable for large orders with many fill levels that are allocated across multiple FCMs.

The buy-side benefits from the consistency of on-CCP average pricing especially when the order is cleared by multiple clearing brokers. Off-CCP average pricing across multiple clearing brokers will generally lead to small differences in average prices across FCMs and funds. Not only will clients benefit from less complexity in managing average pricing, they also can be confident that using CCP average pricing will help them meet their obligation to achieve fair and equitable allocations.

2. Do you currently use average pricing functionality where offered by CCPs? If not, why not? Would you use on-CCP Average Pricing functionality if there were standards surrounding it?

The Division represents a diverse group of executing and clearing brokers that generally have the ability to and do leverage CCP functionality when offered and would welcome more standardization among CCPs.

The buy-side frequently decides and, in fact, must approve how average pricing is achieved. Some clients may have their own average pricing systems or use a clearing broker's proprietary system because they want to apply the same average pricing methodology to all their transactions. If CCPs adopt a standard approach to average pricing, more buy-side firms are likely to elect to use on-CCP functionality.

As more CCPs offer average pricing and FCMs support it, a higher percentage of allocations will likely be processed after an order is fully completed. While this would not conflict with the 30/30/30 Standard when averages are generated at the order level (given the DMIST definition of a completed order¹), it could have the effect of delaying allocations when averages need to be generated across multiple orders. Overall, the efficiency of on-CCP average pricing, especially adhering to a uniform standard, would outweigh any delays.

3. Is there an optimal number of decimal places that should be used for on-CCP Average Pricing?

¹ A completed order is an order to buy or sell a product in the Exchange-traded market that has resulted in: (1) a complete fill of the full quantity on a working order; (2) a partial fill of the full quantity on a working order where the remaining quantity is cancelled, or (3) a partial fill of the full quantity on a working order where the remaining quantity expired at the close of the trading day for the product.

The Division recommends that the minimum number of decimal places to be used for Average Pricing in Phase 1 be 10 decimal places. The greater the number of decimal places the higher degree of accuracy, which would limit the number of small residual cash journals to account for differences.

4. What impediments exist for Clients, Executing Brokers, Clearing Brokers, Exchange, CCPs and Vendors, respectively to meet the proposed standard?

The Division believes the biggest challenge is getting the CCPs to fully support a standardized approach to average price grouping logic. For example, some CCPs allow TAS and TAM trades to be incorporated into an average price group and others do not. Inconsistencies across CCPs create confusion and challenges for the buy side. This becomes a clearing challenge, causing back and forth between clients, executing brokers, and clearing brokers to resolve and effectively redistribute those allocations by breaking them into their different order or trade type components. A standard would create a greater level of efficiency and support the ability to meet the 30/30/30 standard.

5. What products would you like to be able to group for Average Pricing purposes? Are there regulatory restrictions in any jurisdictions that prevent grouping certain types of transactions?

CCPs should allow all products and product types to be available for product grouping. This would avoid client confusion about what's eligible for average pricing and what is not. The Division recognizes, however, that different jurisdictions may have regulatory restrictions related to product grouping.

While there may be regulatory restrictions, especially relating to EFRP and/or block transactions, these fields and others are also critical to brokerage accrual and settlement between brokers. As such, the Division would recommend that DMIST establish a standard to govern grouping criteria i.e., which fields are considered for grouping and cannot be grouped across.

6. What additional standards would be helpful to support or facilitate this proposed standard?

- The Division recommends that DMIST make it standard practice that the executing broker handles average pricing orders and gives it up to the clearing broker through the CCP API or GUI. We believe this is preferable over the two-step process required when the clearing broker first claims the fills and regroups at the CCP to sub allocate at an average price.
- In addition to the recommended standards, we ask DMIST to consider standardizing the length of time the give-up window is open across CCPs. The Division believes that this contributes to operational resilience during periods of market stress. When some CCPs extended the number of days give-ups could be processed during COVID, it provided significant benefit to industry resilience. Clients and their executing and clearing brokers are incentivized for many reasons to complete give-ups and allocations on Trade Day, but when trades are not completed on T+0, it is extremely beneficial to have an extended period to handle the transaction. It also would mitigate the need to initiate a position transfer which is very manual, especially in the case of an average price transfer, and requires different layers of approvals.

7. Are there regional-specific regulatory requirements relating to Average Pricing that need to be considered?

The Division recommends that DMIST survey global CCPs to determine what regulatory restrictions impact average pricing and may prevent product grouping.

In the U.S., the Commodity Futures Trading Commission, National Futures Association, and exchanges have rules that govern the application and computation of average prices, as well as how to handle cash residuals. These rules also cover system and disclosure requirements. These rules should be considered before publishing the final standard.

8. What trade-specific attributes (i.e., fees, Tag 1031 etc.) should remain available throughout Average Price processing (even if it creates additional records when grouping by a single Average Price)?

It is important to have trade-specific attributes available throughout the average pricing process in two areas:

1. All information that distinguishes the original execution attributes (such as order and execution IDs) should be carried through the lifecycle of the trade, including the average pricing process.
2. Any trade attribute that is leveraged by the CCP, such as Tag 1031, to differentiate fees or any attribute that is leveraged by FCMs to differentiate commissions must persist throughout the trade flow. As referenced in response #5, DMIST should establish a standard related to grouping criteria where attributes need to be retained for commission and fee purposes.

All FIXML tags that relate to those trade-specific attributes should be available on the API for processing.

9. How important is it to have CCPs add functionality to allow Executing and Clearing brokers to prevent Average Pricing?

While the Division supports on-CCP average pricing, brokers should have the flexibility to support both on-CCP and off-CCP average pricing as appropriate to meet client needs. Mechanisms already exist across various CCPs to reject a give-up transaction. If an executing firm allocates APS trades, the claiming firm should have the capability to simply reject the trade and then convey the reason it was rejected to the client and executing broker.

COMMENTS ON FUNCTIONALITY AND PRIORITIES

In addition to the responses provided above, the Division has comments on Section 2 of the Consultation Paper: Proposed Standard.

In general, the Division believes that the Average Pricing Standard should acknowledge that the work needed to comply goes beyond the clearinghouses. While the initial build out resides with the CCPs, first vendors and then executing and clearing brokers must adopt that functionality in their products and platforms. The Standard also should acknowledge that there will be friction through the change process as vendors adapt existing platforms or build new systems to accommodate the functionality.

Table #5. Original orders used for Average Pricing are referenced via audit trail (Original Trade Identifiers, Trade References, etc.)

In addition to the original order detail, the original trade level fill/execution details should be maintained throughout the lifecycle of the trade. The order reference ID is going to be different from the individual execution reference IDs on each fill included in that order. The audit trail should include not only the original order ID but subsequent reference IDs for each fill included in the average pricing group.

Table #8. Cash Residual field or data is not amendable

The CCP should automatically calculate the residual based on the fills provided. Further, the formula to calculate the residual should be consistent across CCPs. The Division agrees that this field should not be editable. When standard average pricing functionality is available across CCPs, brokers should not need to calculate average prices or populate the cash residual field. We believe that cash residual is a key component of average pricing and should be maintained through the clearing process. This will alleviate the need for brokers to edit the field.

Table #15. Offer Average Price alternatives(s) (i.e., Notional Value Average Pricing)

The Division agrees that average pricing alternatives should be encouraged and would be beneficial for clients and brokers. While it is appropriately labeled a Phase 2 initiative, we believe it is important for both CCPs currently offering average pricing and those developing average pricing for the first time to be aware of the desire for alternatives and incorporate them into their development plans. As alternatives emerge, the Average Pricing Working Group should consider whether a standard is appropriate; for example, the Working Group should consider proposing a Standard for Notional Value Average pricing to encourage consistency among CCPs. This would provide a roadmap for CCPs to implement an industry-standard approach to an alternative method.

Table #16. Average Price Cash Residual visible on APIs and CCP GUI

The Division recommends moving this to Phase 1 because it's important to have cash residual visible and available on the API message. This gives clearing firms the ability to reverse engineer the price and book to a further number of decimal places, regardless of what the standard says. The description should include specific reference to the residual details included and available in the FIXML messages.

Table #17. Cash Residual transfers with Average Price give up

As stated in comments on Table #8, cash residuals should persist throughout the average pricing process. The Division recommends assigning this a Phase 1 priority because it is critical to the efficient clearing of average priced trades. Assigning this a Phase 2 priority may suggest that cash residuals could be separate and not maintained through clearing, which would create reconciliation and top-day processing challenges. To avoid confusion with "position transfers," the Division recommends replacing "transfers" with "moves" in the description.

In addition, all Average Price trades must include the decimalized average price, the rounded price and the residual because some firms do not have the ability to book a decimalized trade.

Conclusion

The Division appreciates the opportunity to comment and will be ready to assist with implementation of the final standard.