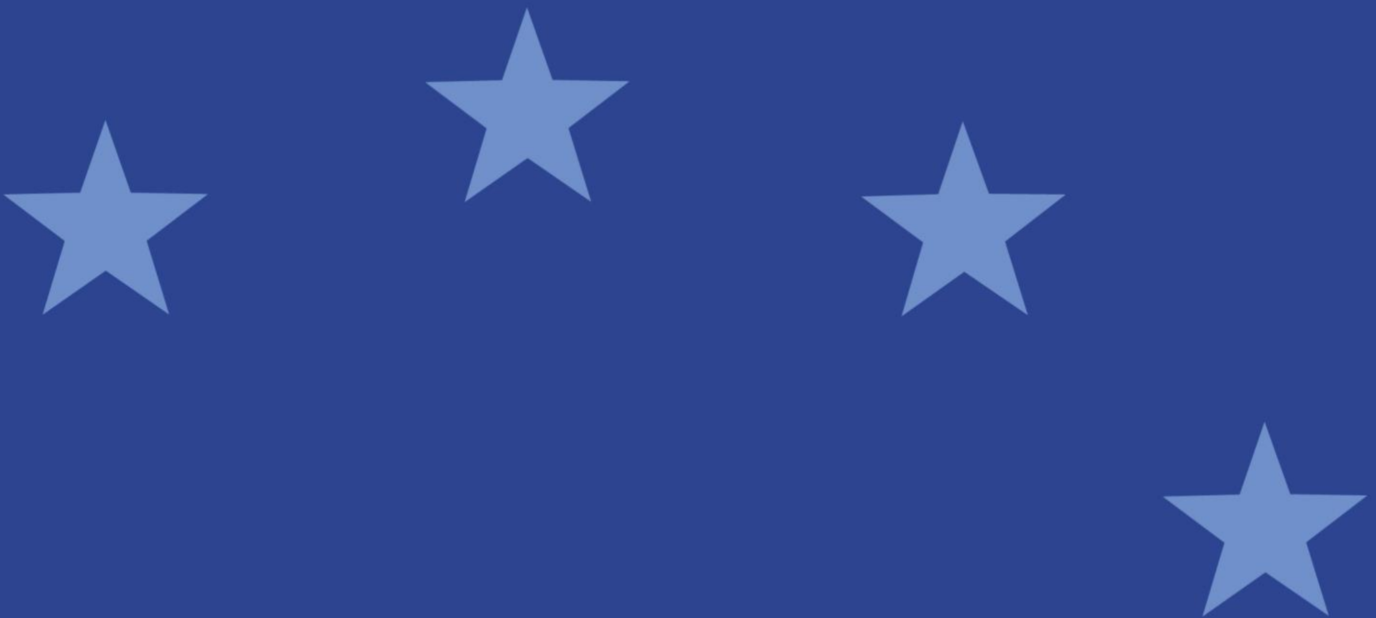
Reply form for the ESMA MiFID II/MiFIR Discussion Paper



22 May 2014

European Securities and
Markets Authority

Date: 22 May 2014

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the ESMA MiFID II/MiFIR Discussion Paper, published on the ESMA website (here).

Instructions

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, please follow the instructions described below:

i. use this form and send your responses in Word format;

ii. do not remove the tags of type <ESMA_QUESTION_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and

iii. if you do not have a response to a question, do not delete it and leave the text "TYPE YOUR TEXT HERE" between the tags.

Responses are most helpful:

- if they respond to the question stated;
- contain a clear rationale, including on any related costs and benefits; and
- describe any alternatives that ESMA should consider

Given the breadth of issues covered, ESMA expects and encourages respondents to specially answer those questions relevant to their business, interest and experience.

To help you navigate this document more easily, bookmarks are available in "Navigation Pane" for Word 2010 and in "Document Map" for Word 2007.

Responses must reach us by **1 August 2014**.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input/Consultations'.

Publication of responses

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Disclaimer'.

1. Overview

2. Investor protection

2.1. Authorisation of investment firms

Q1: Do you agree that the existing work/standards set out in points Error! Reference source not found. **and** Error! Reference source not found. Error! Reference source not found. **provide a valid basis on which to develop implementing measures in respect of the authorisation of investment firms?**

<ESMA_QUESTION_1>
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<ESMA_QUESTION_1>

Q2: What areas of these existing standards do you consider require adjustment, and in what way should they be adjusted?

<ESMA_QUESTION_2>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_2>

Q3: Do you consider that the list of information set out in point Error! Reference source not found. **should be provided to Home State NCAs? If not, what other information should ESMA consider?**

<ESMA_QUESTION_3>
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<ESMA_QUESTION_3>

Q4: Are there any other elements which may help to assess whether the main activities of an applicant investment firm is not in the territory where the application is made?

<ESMA_QUESTION_4>
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<ESMA_QUESTION_4>

Q5: How much would one-off costs incurred during the authorisation process increase, compared to current practices, in order to meet the requirements suggested in this section?

<ESMA_QUESTION_5>
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<ESMA_QUESTION_5>

Q6: Are there any particular items of information suggested above that would take significant time or cost to produce and if so, do you have alternative suggestions that would reduce the time/cost for firms yet provide the same assurance to NCAs?

<ESMA_QUESTION_6>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_6>

2.2. Freedom to provide investment services and activities / Establishment of a branch

Q7: Do you agree that development of technical standards required under Articles 34 and 35 of MiFID II should be based on the existing standards and forms contained in the CESR Protocol on MiFID Notifications (CESR/07-317c)? If not, what are the specific areas in the existing CESR standards requiring review and adjustment?

<ESMA_QUESTION_7>
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<ESMA_QUESTION_7>

2.3. Best execution - publication of data related to the quality of execution by trading venues for each financial instrument traded

Q8: Do you agree data should be provided by all the execution venues as set out in footnote 24? If not, please state why not.

<ESMA_QUESTION_8>
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<ESMA_QUESTION_8>

Q9: If you think that the different types of venues should not publish exactly the same data, please specify how the data should be adapted in each case, and the reasons for each adjustment.

<ESMA_QUESTION_9>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_9>

Q10: Should the data publication obligation apply to every financial instrument traded on the execution venue? Alternatively, should there be a minimum threshold of activity and, if so, how should it be defined (for example, frequency of trades, number of trades, turnover etc.)?

<ESMA_QUESTION_10>
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<ESMA_QUESTION_10>

Q11: How often should all execution data be published by trading venues? Is the minimum requirement specified in MiFID II sufficient, or should this frequency be increased? Is it reasonable or beneficial to require publication on a monthly basis and is it possible to reliably estimate the marginal cost of increased frequency?

<ESMA_QUESTION_11>
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<ESMA_QUESTION_11>

Q12: Please provide an estimate of the cost of the necessary IT development for the production and the publication of such reporting.

<ESMA_QUESTION_12>
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<ESMA_QUESTION_12>

Q13: Do you agree that trading venues should publish the data relating to the quality of execution with regard to a uniform reference period, with a minimum of specific reporting details and in a compatible format of data based on a homogeneous calculation method? If not, please state why.

<ESMA_QUESTION_13>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_13>

Q14: Is the volume of orders received and executed a good indicator for investment firms to compare execution venues? Would the VBBO in a single stock published at the same time also be a good indicator by facilitating the creation of a periodic European price benchmark? Are there other indicators to be considered?

<ESMA_QUESTION_14>
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Q15: The venue execution quality reporting obligation is intended to apply to all MiFID instruments. Is this feasible and what differences in approach will be required for different instrument types?

<ESMA_QUESTION_15>
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<ESMA_QUESTION_15>

Q16: Do you consider that this requirement will generate any additional cost? If yes, could you specify in which areas and provide an estimation of these costs?

<ESMA_QUESTION_16>
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<ESMA_QUESTION_16>

Q17: If available liquidity and execution quality are a function of order size, is it appropriate to split trades into ranges so that they are comparable? How should they be defined (for example, as a percentage of the average trading size of the financial instrument on the execution venue; fixed ranges by volume or value; or in another manner)?

<ESMA_QUESTION_17>
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<ESMA_QUESTION_17>

Q18: Do you agree that a benchmark price is needed to evaluate execution quality? Would a depth-weighted benchmark that relates in size to the executed order be appropriate or, if not, could you provide alternative suggestions together with justification?

<ESMA_QUESTION_18>
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<ESMA_QUESTION_18>

Q19: What kind of cost should be reported (e.g. regulatory levies, taxes, mandatory clearing fees) and how should this data be presented to enable recipients to assess the total consideration of transactions?

<ESMA_QUESTION_19>
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<ESMA_QUESTION_19>

Q20: What would be the most appropriate way to measure the likelihood of execution in order to get useful data? Would it be a good indicator for likelihood of execution to measure the percentage of orders not executed at the end of the applicable trading period (for example the end of each trading day)? Should the modification of an order be taken into consideration?

<ESMA_QUESTION_20>
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<ESMA_QUESTION_20>

Q21: What would be the most appropriate way to measure the speed of execution in order to get useful data?

<ESMA_QUESTION_21>
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<ESMA_QUESTION_21>

Q22: Are there other criteria (qualitative or quantitative) that are particularly relevant (e.g. market structures providing for a guarantee of settlement of the trades vs OTC deals; robustness of the market infrastructure due to the existence of circuit breakers)?

<ESMA_QUESTION_22>
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<ESMA_QUESTION_22>

Q23: Is data on orders cancelled useful and if so, on what time basis should it be computed (e.g. within a single trading day)?

<ESMA_QUESTION_23>
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<ESMA_QUESTION_23>

Q24: Are there any adjustments that need to be made to the above execution quality metrics to accommodate different market microstructures?

<ESMA_QUESTION_24>
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Q25: What additional measures are required to define or capture the above data and relevant additional information (e.g. depth weighted spreads, book depths, or others) How should the data be presented: on an average basis such as daily, weekly or monthly for each financial instrument (or on more than one basis)? Do you think that the metrics captured in the Annex to this chapter are relevant to European markets trading in the full range of MiFID instruments? What alternative could you propose?

<ESMA_QUESTION_25>
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<ESMA_QUESTION_25>

Q26: Please provide an estimate of the costs of production and publication of all of the above data and, the IT developments required? How could these costs be minimised?

<ESMA_QUESTION_26>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_26>

Q27: Would increasing the frequency of venue execution quality data generate additional costs for you? Would these costs arise as a result of an increase of the frequency of the review, or because this review will require additional training for your staff in order to be able to analyse and take into account these data? Please provide an estimate of these costs.

<ESMA_QUESTION_27>
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<ESMA_QUESTION_27>

Q28: Do you agree that investment firms should take the publication of the data envisaged in this Discussion Paper into consideration, in order to determine whether they represent a "material change"?

<ESMA_QUESTION_28>
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<ESMA_QUESTION_28>

2.4. Best execution - publication of data by investment firms

Q29: Do you agree that in order to allow clients to evaluate the quality of a firm's execution, any proposed standards should oblige the firm to give an appropriate picture of the venues and the different ways they execute an order?

<ESMA_QUESTION_29>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_29>

Q30: Do you agree that when systematic internalisers, market makers, OTC negotiation or dealing on own account represent one of the five most important ways for the firm to execute clients' orders, they should be incorporated in the reporting obligations under Article 27(6) of MiFID II?

<ESMA_QUESTION_30>
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<ESMA_QUESTION_30>

Q31: Do you think that the data provided should be different in cases when the firm directly executes the orders to when the firm transmits the orders to a third-party for execution? If yes, please indicate what the differences should be, and explain why.

<ESMA_QUESTION_31>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_31>

Q32: Do you consider that information on both directed and non-directed orders is useful? Should the data be aggregated so that both types of order are shown together or separated? Should there be a similar approach to disclosure of information on market orders versus limit orders? Do you think that another categorisation of client orders could be useful?

<ESMA_QUESTION_32>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_32>

Q33: Do you think that the reporting data should separate retail clients from other types of clients? Do you think that this data should be publicly disclosed or only provided to the NCA (e.g. when requested to assess whether there is unfair discrimination between retail clients and other categories)? Is there a more useful way to categorise clients for these purposes?

<ESMA_QUESTION_33>
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<ESMA_QUESTION_33>

Q34: Do you agree that the investment firms should publish the data relating to their execution of orders with regard to a uniform reference period, with a minimum of specific reporting details and in a compatible format of data based on a homogeneous calculation method? If not, please state why.

<ESMA_QUESTION_34>
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<ESMA_QUESTION_34>

Q35: What would be an acceptable delay for publication to provide the clients with useful data?

<ESMA_QUESTION_35>
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<ESMA_QUESTION_35>

Q36: What format should the report take? Should there be any difference depending on the nature of the execution venues (MTF, OTF, Regulated Market, systematic internalisers, own account) and, if so, could you specify the precise data required for each type?

<ESMA_QUESTION_36>
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<ESMA_QUESTION_36>

Q37: Do you agree that it is proportionate to require investment firms to publish on an annual basis a summary based on their internal execution quality monitoring of their top five execution venues in terms of trading volumes, subject to certain minimum standards?

<ESMA_QUESTION_37>
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<ESMA_QUESTION_37>

Q38: Do you have views on how 'directed orders' covered by client specific instructions should be captured in the information on execution quality? Is it possible to disaggregate reporting for directed orders from those for which there are no specific instructions and, if so, what the most relevant criteria would be for this exercise?

<ESMA_QUESTION_38>
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<ESMA_QUESTION_38>

Q39: Minimum standards to ensure that the summary of the firm's internal execution quality monitoring of their top five execution venues (in terms of trading volumes) is comprehensive and contains sufficient analysis or context to allow it to be understood by market participants shall include the factors set out at paragraph 29. Do you agree with this analysis or are there any other relevant factors that should be considered as minimum standards for reporting?

<ESMA_QUESTION_39>
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<ESMA_QUESTION_39>

Q40: Can you recommend an alternative approach to the provision of information on execution quality obtained by investment firms, which is consistent with Article 27(6) of MiFID II and with ESMA's overall objective to ensure proportionate implementation?

<ESMA_QUESTION_40>
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<ESMA_QUESTION_40>

Q41: Do you agree that ESMA should try to limit the number of definitions of classes of instruments and provide a classification that can be used for the different reports established by MiFID and MiFIR?

<ESMA_QUESTION_41>
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<ESMA_QUESTION_41>

Q42: If this approach is not viable how should these classes be defined? What elements should be taken into consideration for that classification? Please explain the rationale of your classification. Is there a need to delay the publication of the reporting for particular class of financial instruments? If the schedule has to be defined, what timeframe would be the most relevant?

<ESMA_QUESTION_42>
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<ESMA_QUESTION_42>

Q43: Is any additional data required (for instance, on number of trades or total value of orders routed)?

<ESMA_QUESTION_43>
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<ESMA_QUESTION_43>

Q44: What information on conflicts of interest would be appropriate (inducements, capital links, payment for order flow, etc.)?

<ESMA_QUESTION_44>
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<ESMA_QUESTION_44>

3. Transparency

3.1. Pre-trade transparency - Equities

Q45: What in your view would be the minimum content of information that would make an indication of interest actionable? Please provide arguments with your answer.

<ESMA_QUESTION_45>
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<ESMA_QUESTION_45>

Q46: Do you agree with ESMA's opinion that Table 1 of Annex II of Regulation 1287/2006 is still valid for shares traded on regulated markets and MTFs? Please provide reasons for your answer.

<ESMA_QUESTION_46>
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<ESMA_QUESTION_46>

Q47: Do you agree with ESMA's view that Table 1 of Annex II of Regulation 1287/2006 is appropriate for equity-like instruments traded on regulated markets and MTFs? Are there other trading systems ESMA should take into account for these instruments? Please provide reasons for your answer.

<ESMA_QUESTION_47>
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<ESMA_QUESTION_47>

Q48: Do you agree with ESMA's view that ADT remains a valid measure for determining when an order is large in scale compared to normal market size? If not, what other measure would you suggest as a substitute or complement to the ADT? Please provide reasons for your answer.

<ESMA_QUESTION_48>
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<ESMA_QUESTION_48>

Q49: Do you agree that ADT should be used as an indicator also for the MiFIR equity-like products (depositary receipts, ETFs and certificates)? Please provide reasons for your answers.

<ESMA_QUESTION_49>
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<ESMA_QUESTION_49>

Q50: Do you think there is merit in creating a new ADT class of 0 to €100,000 with an adequate new large in scale threshold and a new ADT class of €100,000 to €500,000? At what level should the thresholds be set? Please provide reasons for your answer.

<ESMA_QUESTION_50>
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<ESMA_QUESTION_50>

Q51: Do you think there is merit in creating new ADT classes of €1 to €5m and €5 to €25m? At what level should the thresholds be set? Please provide reasons for your answer.

<ESMA_QUESTION_51>
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<ESMA_QUESTION_51>

Q52: Do you think there is merit in creating a new ADT class for 'super-liquid' shares with an ADT in excess of €100m and a new class of €50m to €100m? At what level should the thresholds be set?

<ESMA_QUESTION_52>
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<ESMA_QUESTION_52>

Q53: What comments do you have in respect of the new large in scale transparency thresholds for shares proposed by ESMA?

<ESMA_QUESTION_53>
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<ESMA_QUESTION_53>

Q54: Do you agree with the ADT ranges selected? Do you agree with the large in scale thresholds set for each ADT class? Which is your preferred option? Would you calibrate the ADT classes and related large in scale thresholds differently? Please provide reasons for your answers, including describing your own role in the market (e.g. market-maker, issuer etc.).

<ESMA_QUESTION_54>
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<ESMA_QUESTION_54>

Q55: Which is your preferred scenario? Would you calibrate the ADT classes differently? Please provide reasons for your answers.

<ESMA_QUESTION_55>
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<ESMA_QUESTION_55>

Q56: Do you agree that the same ADT classes should be used for both pre-trade and post-trade transparency? Please provide reasons for your answers.

<ESMA_QUESTION_56>
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<ESMA_QUESTION_56>

Q57: How would you calibrate the large in scale thresholds for each ADT class for pre- and post-trade transparency? Please provide reasons for your answers.

<ESMA_QUESTION_57>
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<ESMA_QUESTION_57>

Q58: Do you agree with ESMA's view that the large in scale thresholds (i.e. the minimum size of orders qualifying as large in scale and the ADT classes) should be subject to a review no earlier than two years after MiFIR and Level 2 apply in practice?

<ESMA_QUESTION_58>
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<ESMA_QUESTION_58>

Q59: How frequently do you think the calculation per financial instrument should be performed to determine within which large in scale class it falls? Which combination of frequency and period would you recommend?

<ESMA_QUESTION_59>
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<ESMA_QUESTION_59>

Q60: Do you agree with ESMA's opinion that stubs should become transparent once they are a certain percentage below the large in scale thresholds? If yes, at what percentage would you set the transparency threshold for large in scale stubs? Please provide reasons to support your answer.

<ESMA_QUESTION_60>
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<ESMA_QUESTION_60>

Q61: Do you agree with ESMA's view that the most relevant market in terms of liquidity should be the trading venue with the highest turnover in the relevant financial instrument? Do you agree with an annual review of the most relevant market in terms of liquidity? Please give reasons for your answer.

<ESMA_QUESTION_61>
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<ESMA_QUESTION_61>

Q62: Do you agree with ESMA's view on the different ways the member or participant of a trading venue can execute a negotiated trade? Please give reasons for your answer.

<ESMA_QUESTION_62>
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<ESMA_QUESTION_62>

Q63: Do you agree that the proposed list of transactions are subject to conditions other than the current market price and do not contribute to the price formation process? Do you think that there are other transactions which are subject to conditions other than the current market price that should be added to the list? Please provide reasons for your answer.

<ESMA_QUESTION_63>
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<ESMA_QUESTION_63>

Q64: Do you agree that these are the two main groups of order management facilities ESMA should focus on or are there others?

<ESMA_QUESTION_64>
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<ESMA_QUESTION_64>

Q65: Do you agree with ESMA's general assessment on how to design future implementing measures for the order management facility waiver? Please provide reasons for your answer.

<ESMA_QUESTION_65>
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<ESMA_QUESTION_65>

Q66: Are there other factors that need to be taken into consideration for equity-like instruments? Please provide reasons for your answer.

<ESMA_QUESTION_66>
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<ESMA_QUESTION_66>

Q67: Do you agree that the minimum size for a stop order should be set at the minimum tradable quantity of shares in the relevant trading venue? Please provide reasons for your answer.

<ESMA_QUESTION_67>
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<ESMA_QUESTION_67>

Q68: Are there additional factors that need to be taken into consideration for equity-like instruments?

<ESMA_QUESTION_68>
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<ESMA_QUESTION_68>

Q69: Which minimum overall sizes for iceberg orders are currently employed in the markets you use and how are those minimum sizes determined?

<ESMA_QUESTION_69>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_69>

Q70: Which minimum sizes and which methods for determining them should be prescribed via implementing measures? To what level of detail should such an implementing measure go and what should be left to the discretion of the individual market to attain an appropriate level of harmonisation?

<ESMA_QUESTION_70>
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<ESMA_QUESTION_70>

Q71: Which methods for determining the individual peak sizes of iceberg orders are currently employed in European markets?

<ESMA_QUESTION_71>
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<ESMA_QUESTION_71>

Q72: Which methods for determining peaks should be prescribed by implementing measures, for example, should these be purely abstract criteria or a measure expressed in percentages against the overall size of the iceberg order? To what level of details should such an implementing measure go and what should be left to the discretion of the individual market to attain an appropriate level of harmonisation?

<ESMA_QUESTION_72>
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<ESMA_QUESTION_72>

Q73: Are there additional factors that need to be taken into consideration for equity-like instruments?

<ESMA_QUESTION_73>
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<ESMA_QUESTION_73>

3.2. Post-trade transparency - Equities

Q74: Do you agree that the content of the information currently required under existing MiFID is still valid for shares and applicable to equity-like instruments? Please provide reasons for your answer.

<ESMA_QUESTION_74>
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<ESMA_QUESTION_74>

Q75: Do you think that any new field(s) should be considered? If yes, which other information should be disclosed?

<ESMA_QUESTION_75>
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<ESMA_QUESTION_75>

Q76: Do you think that the current post-trade regime should be retained or that the identity of the systematic internaliser is relevant information which should be published? Please provide reasons for your response, distinguishing between liquid shares and illiquid shares.

<ESMA_QUESTION_76>
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<ESMA_QUESTION_76>

Q77: Do you agree with the proposed list of identifiers? Please provide reasons for your answer.

<ESMA_QUESTION_77>
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<ESMA_QUESTION_77>

Q78: Do you think that specific flags for equity-like instruments should be envisaged? Please justify your answer.

<ESMA_QUESTION_78>
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<ESMA_QUESTION_78>

Q79: Do you support the proposal to introduce a flag for trades that benefit from the large in scale deferral? Please provide reasons for your response.

<ESMA_QUESTION_79>
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<ESMA_QUESTION_79>

Q80: What is your view on requiring post-trade reports to identify the market mechanism, the trading mode and the publication mode in addition to the flags for the different types of transactions proposed in the table above? Please provide reasons for your answer.

<ESMA_QUESTION_80>
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<ESMA_QUESTION_80>

Q81: For which transactions captured by Article 20(1) would you consider specifying additional flags as foreseen by Article 20(3)(b) as useful?

<ESMA_QUESTION_81>
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<ESMA_QUESTION_81>

Q82: Do you agree with the definition of "normal trading hours" given above?

<ESMA_QUESTION_82>
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<ESMA_QUESTION_82>

Q83: Do you agree with the proposed shortening of the maximum permissible delay to 1 minute? Do you see any reason to have a different maximum permissible deferral of publication for any equity-like instrument? Please provide reasons for your answer

<ESMA_QUESTION_83>
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<ESMA_QUESTION_83>

Q84: Should the deferred publication regime be subject to the condition that the transaction is between an investment firm dealing on own account and a client of the firm? Please provide reasons for your answer.

<ESMA_QUESTION_84>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_84>

Q85: Which of the two options do you prefer in relation to the deferral periods for large in scale transactions (or do you prefer another option that has not been proposed)? Please provide reasons for your answer

<ESMA_QUESTION_85>
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<ESMA_QUESTION_85>

Q86: Do you see merit in adding more ADT classes and adjusting the large in scale thresholds as proposed? Please provide alternatives if you disagree with ESMA's proposal

<ESMA_QUESTION_86>
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<ESMA_QUESTION_86>

Q87: Do you consider the thresholds proposed as appropriate for SME shares?

<ESMA_QUESTION_87>
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<ESMA_QUESTION_87>

Q88: How frequently should the large in scale table be reviewed? Please provide reasons for your answer

<ESMA_QUESTION_88>
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<ESMA_QUESTION_88>

Q89: Do you have concerns regarding deferred publication occurring at the end of the trading day, during the closing auction period?

<ESMA_QUESTION_89>
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<ESMA_QUESTION_89>

Q90: Do you agree with ESMA's preliminary view of applying the same ADT classes to the pre-trade and post-trade transparency regimes for ETFs? Please provide reasons for your answer.

<ESMA_QUESTION_90>
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<ESMA_QUESTION_90>

3.3. Systematic Internaliser Regime - Equities

Q91: Do you support maintaining the existing definition of quotes reflecting prevailing market conditions? Please provide reasons for your answer.

<ESMA_QUESTION_91>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_91>

Q92: Do you support maintaining the existing table for the calculation of the standard market size? If not, which of the above options do you believe provides the best trade-off between maintaining a sufficient level of transparency and ensuring that obligations for systematic internalisers remain reasonable and proportionate? Please provide reasons for your answer.

<ESMA_QUESTION_92>
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<ESMA_QUESTION_92>

Q93: Do you agree with the proposal to set the standard market size for depositary receipts at the same level as for shares? Please provide reasons for your answer.

<ESMA_QUESTION_93>
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<ESMA_QUESTION_93>

Q94: What are your views regarding how financial instruments should be grouped into classes and/or how the standard market size for each class should be established for certificates and exchange traded funds?

<ESMA_QUESTION_94>
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<ESMA_QUESTION_94>

3.4. Trading obligation for shares (Article 23, MiFIR)

Q95: Do you consider that the determination of what is non-systematic, ad-hoc, irregular and infrequent should be defined within the same parameters applicable for the systematic internaliser definition? In the case of the exemption to the trading obligation for shares, should the frequency concept be more restrictive taking into consideration the other factors, i.e. 'ad-hoc' and 'irregular'?

<ESMA_QUESTION_95>
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<ESMA_QUESTION_95>

Q96: Do you agree with the list of examples of trades that do not contribute to the price discovery process? In case of an exhaustive list_would you add any other type of transaction? Would you exclude any of them? Please, provide reasons for your response.

<ESMA_QUESTION_96>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_96>

Q97: Do you consider it appropriate to include benchmark and/or portfolio trades in the list of those transactions determined by factors other than the current valuation of the share? If not, please provide an explanation with your response.

<ESMA_QUESTION_97>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_97>

3.5. Introduction to the non-equity section and scope of non-equity financial instruments

Q98: Do you agree with the proposed description of structured finance products? If not, please provide arguments and suggestions for an alternative.

<ESMA_QUESTION_98>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_98>

Q99: For the purposes of transparency, should structured finance products be identified in order to distinguish them from other non-equity transferable securities? If so, how should this be done?

<ESMA_QUESTION_99>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_99>

Q100: Do you agree with the proposed explanation for the various types of transferable securities that should be treated as derivatives for pre-trade and post trade transparency? If not, please provide arguments and suggestions for an alternative.

<ESMA_QUESTION_100>

TYPE YOUR TEXT HERE
<ESMA_QUESTION_100>

Q101: Do you agree with ESMA's proposal that for transparency purposes market operators and investment firms operating a trading venue should assume responsibility for determining to which MiFIR category the non-equity financial instruments which they intend to introduce on their trading venue belong and for providing their competent authorities and the market with this information before trading begins?

<ESMA_QUESTION_101>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_101>

Q102: Do you agree with the definitions listed and proposed by ESMA? If not, please provide alternatives.

<ESMA_QUESTION_102>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_102>

3.6. Liquid market definition for non-equity financial instruments

Q103: Do you agree with the proposed approach? If you do not agree please provide reasons for your answers. Could you provide for an alternative approach?

<ESMA_QUESTION_103>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_103>

Q104: Do you agree with the proposed approach? If you do not agree please provide reasons. Could you provide an alternative approach?

<ESMA_QUESTION_104>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_104>

Q105: Do you agree with the proposed approach? If you do not agree please provide reasons. Could you provide an alternative approach?

<ESMA_QUESTION_105>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_105>

Q106: Do you agree with the proposed approach? If you do not agree please provide reasons. Could you provide an alternative approach?

<ESMA_QUESTION_106>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_106>

Q107: Should different thresholds be applied for different (classes of) financial instruments? Please provide proposals and reasons.

<ESMA_QUESTION_107>
TYPE YOUR TEXT HERE

<ESMA_QUESTION_107>

Q108: Do you have any proposals for appropriate spread thresholds? Please provide figures and reasons.

<ESMA_QUESTION_108>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_108>

Q109: How could the data necessary for computing the average spreads be obtained?

<ESMA_QUESTION_109>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_109>

Q110: Do you agree with the proposed approach? If you do not agree please providereasons for your answer. Could you provide an alternative approach?

<ESMA_QUESTION_110>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_110>

Q111: Overall, could you think of an alternative approach on how to assess whether a market is liquid bearing in mind the various elements of the liquid market definition in MiFIR?

<ESMA_QUESTION_111>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_111>

Q112: Which is your preferred scenario or which combination of thresholds would you propose for defining a liquid market for bonds or for a sub-category of bonds (sovereign, corporate, covered, convertible, etc.)? Please provide reasons for your answer.

<ESMA_QUESTION_112>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_112>

Q113: Should the concept of liquid market be applied to financial instruments (IBIA) or to classes of financial instruments (COFIA)? Would be appropriate to apply IBIA for certain asset classes and COFIA to other asset classes? Please provide reasons for your answers

<ESMA_QUESTION_113>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_113>

Q114: Do you have any (alternative) proposals how to take the 'range of market conditions and the life-cycle' of (classes of) financial instruments into account - other than the periodic reviews described in the sections periodic review of the liquidity threshold and periodic assessment of the liquidity of the instrument class, above?

<ESMA_QUESTION_114>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_114>

Q115: Do you have any proposals on how to form homogenous and relevant classes of financial instruments? Which specifics do you consider relevant for that purpose? Please distinguish between bonds, SFPs and (different types of) derivatives and across qualitative criteria (please refer to Annex 3.6.1).

<ESMA_QUESTION_115>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_115>

Q116: Do you think that, in the context of the liquidity thresholds to be calculated under MiFID II, the classification in Annex 3.6.1 is relevant? Which product types or sub-product types would you be inclined to create or merge? Please provide reasons for your answers

<ESMA_QUESTION_116>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_116>

Q117: Do you agree with the proposed approach? If not, please provide rationales and alternatives.

<ESMA_QUESTION_117>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_117>

Q118: Do you agree with the proposed thresholds? If not, please provide rationales and alternatives.

<ESMA_QUESTION_118>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_118>

3.7. Pre-trade transparency requirements for non-equity instruments

Q119: Do you agree with the description of request-for-quote system? If not, how would you describe a request-for-quote system? Please give reasons to support your answer.

<ESMA_QUESTION_119>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_119>

Q120: Do you agree with the inclusion of request-for-stream systems in the definition of request-for-quote system? Please give reasons to support your answer.

<ESMA_QUESTION_120>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_120>

Q121: Do you think that – apart from request-for-stream systems – other functionalities should be included in the definition of request-for-quote system? If yes, please provide a description of this functionality and give reasons to support your answer.

<ESMA_QUESTION_121>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_121>

Q122: Do you agree with the description of voice trading system? If not, how would you describe a voice trading system?

<ESMA_QUESTION_122>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_122>

Q123: Do you agree with the proposed table setting out different types of trading systems for non-equity instruments?

<ESMA_QUESTION_123>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_123>

Q124: Do you think that the information to be made public for each type of trading system provides adequate transparency for each trading system?

<ESMA_QUESTION_124>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_124>

Q125: Besides the trading systems mentioned above, are there additional trading models that need to be considered for pre-trade transparency requirements in the non-equity market space?

<ESMA_QUESTION_125>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_125>

Q126: If you think that additional trading systems should be considered, what information do you think should be made public for each additional type of trading model?

<ESMA_QUESTION_126>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_126>

Q127: Based on your experience, what are the different types of voice trading systems in the market currently? What specific characteristics do these systems have?

<ESMA_QUESTION_127>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_127>

Q128: How do these voice trading systems currently make information public or known to interested parties at the pre-trade stage?

<ESMA_QUESTION_128>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_128>

Q129: Do you agree with ESMA's approach in relation to the content, method and timing of pre-trade information being made available to the wider public?

<ESMA_QUESTION_129>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_129>

Q130: Do you agree with the above mentioned approach with regard to indicative pre-trade bid and offer prices which are close to the price of the trading interests? Please give reasons to support your answer

<ESMA_QUESTION_130>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_130>

Q131: If you do not agree with the approach described above please provide an alternative

<ESMA_QUESTION_131>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_131>

3.8. Post-trade transparency requirements for non-equity instruments

Q132: Do you agree with the proposed content of post-trade public information? If not, please provide arguments and suggestions for an alternative.

<ESMA_QUESTION_132>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_132>

Q133: Do you think that the current post-trade regime for shares on the systematic internaliser's identity should be extended to non-equity instruments or that the systematic internaliser's identity is relevant information which should be published without exception?

<ESMA_QUESTION_133>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_133>

Q134: Is there any other information that would be relevant to the market for the above mentioned asset classes?

<ESMA_QUESTION_134>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_134>

Q135: Do you agree with the proposed table of identifiers for transactions executed on non-equity instruments? Please provide reasons for your answer.

<ESMA_QUESTION_135>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_135>

Q136: Do you support the use of flags to identify trades which have benefitted from the use of deferrals? Should separate flags be used for each type of deferral (e.g. large in scale deferral, size specific to the instrument deferral)? Please provide reasons for your answer.

<ESMA_QUESTION_136>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_136>

Q137: Do you think a flag related to coupon payments (ex/cum) should be introduced? If yes, please describe the cases where such flags would be warranted and which information should be captured.

<ESMA_QUESTION_137>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_137>

Q138: Do you think that give-up/give-in trades (identified with a flag) should be included in post-trade reports or not made public? Please provide reasons for your answers.

<ESMA_QUESTION_138>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_138>

Q139: Do you agree that securities financing transactions should be exempted from the post-trade transparency regime?

<ESMA_QUESTION_139>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_139>

Q140: Do you agree that for the initial application of the new transparency regime the information should be made public within five minutes after the relevant non-equity transaction? Please provide reasons for your answer.

<ESMA_QUESTION_140>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_140>

Q141: Do you agree with the proposed text or would you propose an alternative option? Please provide reasons for your answer.

<ESMA_QUESTION_141>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_141>

Q142: Do you agree that the intra-day deferral periods should range between 60 minutes and 120 minutes?

<ESMA_QUESTION_142>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_142>

Q143: Do you agree that the maximum deferral period, reserved for the largest transactions, should not exceed end of day or, for transactions executed after 15.00, the opening of the following trading day? If not, could you provide alternative proposals? Please provide reasons for your answer.

<ESMA_QUESTION_143>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_143>

Q144: Do you consider there are reasons for applying different deferral periods to different asset classes, e.g. fixing specific deferral periods for sovereign bonds? Please provide arguments to support your answer.

<ESMA_QUESTION_144>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_144>

Q145: Do you support the proposal that the deferral for non-equity instruments which do not have a liquid market should be until the end of day + 1? Please provide reasons for your answer.

<ESMA_QUESTION_145>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_145>

Q146: Do you think that one universal deferral period is appropriate for all non-equity instruments which do not have a liquid market or that the deferrals should be set at a more granular level, depending on asset class and even sub asset class. Please provide reasons for your answer.

<ESMA_QUESTION_146>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_146>

Q147: Do you agree with the proposal that during the deferred period for non-equity instruments which do not have a liquid market, the volume of the transaction should be omitted but all the other details of individual transactions must be published? Please provide reasons for your answer.

<ESMA_QUESTION_147>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_147>

Q148: Do you agree that publication in an aggregated form with respect to sovereign debt should be authorised for an indefinite period only in limited circumstances? Please give reasons for your answers. If you disagree, what alternative approaches would you propose?

<ESMA_QUESTION_148>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_148>

Q149: In your view, which criteria and/or conditions would it be appropriate to specify as indicating there is a need to authorise extended/indefinite deferrals for sovereign debt??

<ESMA_QUESTION_149>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_149>

Q150: In your view, could those transactions determined by other factors than the valuation of the instrument be authorised for deferred publication to the end of day? Please provide reasons for your answer.

<ESMA_QUESTION_150>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_150>

3.9. The transparency regime of non-equity large in scale orders and transactions

Q151: Do you agree with the proposed option? Which option would be more suitable for the calibration of the large in scale requirements within an asset class?

<ESMA_QUESTION_151>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_151>

Q152: Do you consider there are reasons for opting for different options for different asset classes? Please provide arguments.

<ESMA_QUESTION_152>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_152>

Q153: Do you agree that the choice between the two options should be consistent with the approach adopted for the assessment of liquidity? If not, please provide arguments.

<ESMA_QUESTION_153>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_153>

Q154: Do you agree with the proposed approach? If no, which indicator would you consider more appropriate for the determination of large in scale thresholds for orders and transactions?

<ESMA_QUESTION_154>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_154>

Q155: Do you agree that the proxy used for the determining the large in scale thresholds should be the same as the one used to assess the average size of transactions in the context of the definition of liquid markets? Please provide arguments.

<ESMA_QUESTION_155>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_155>

Q156: In your view, which option would be more suitable for the determination of the large in scale thresholds? Please provide arguments.

<ESMA_QUESTION_156>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_156>

Q157: Alternatively which method would you suggest for setting the large in scale thresholds?

<ESMA_QUESTION_157>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_157>

Q158: In your view, should large in scale thresholds for orders differ from the large in scale thresholds for transactions? If yes, which thresholds should be higher: pre-trade or post-trade? Please provide reasons to support your answer.

<ESMA_QUESTION_158>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_158>

Q159: Do you agree that the large in scale thresholds should be computed only on the basis of transactions carried out on trading venues following the implementation of MiFID II? Please, provide reasons for the answer.

<ESMA_QUESTION_159>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_159>

Q160: Do you think that the condition for deferred publication of large in scale transactions currently applying to shares (transaction is between an investment firm that deals on own account and a client of the investment firm) is applicable to non-equity instruments? Please provide reasons for your answer.

<ESMA_QUESTION_160>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_160>

Q161: Do you agree that the large in scale regime should be reviewed no earlier than two years after application of MiFIR in practice?

<ESMA_QUESTION_161>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_161>

3.10. Size specific to the instrument

Q162: Do you agree with the above description of the applicability of the size specific to the instrument? If not please provide reasons for your answer.

<ESMA_QUESTION_162>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_162>

Q163: Do you agree with the proposal that the size specific to the instrument should be set as a percentage of the large in scale size? Please provide reasons for you answer.

<ESMA_QUESTION_163>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_163>

Q164: In your view, what methodologies would be most appropriate for measuring the undue risk in order to set the size specific threshold?

<ESMA_QUESTION_164>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_164>

Q165: Would you suggest any other practical ways in which ESMA could take into account whether, at such sizes, liquidity providers would be able to hedge their risks?

<ESMA_QUESTION_165>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_165>

Q166: Do you agree with ESMA's description of how the size specific to the instrument waiver would interact with the large in scale waiver? Please provide reasons for your answer.

<ESMA_QUESTION_166>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_166>

Q167: Do you agree with ESMA's description of how the size specific to the instrument deferrals would interact with the large in scale deferrals? In particular, do you agree that the deferral periods for the size specific to the instrument and the large in scale should differ and have any specific proposals on how the deferral periods should be calibrated? Please provide reasons for your answer.

<ESMA_QUESTION_167>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_167>

3.11. The Trading Obligation for Derivatives

Q168: Do you agree that there should be consistent categories of derivatives contracts throughout MiFIR/EMIR?

<ESMA_QUESTION_168>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_168>

Q169: Do you agree with this approach to the treatment of third countries?

<ESMA_QUESTION_169>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_169>

Q170: Do you agree with the proposed criteria based anti-avoidance procedure?

<ESMA_QUESTION_170>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_170>

Q171: Do you think it would be reasonable for ESMA to consult venues with regard to which classes of derivatives contracts are traded on venue? Do you think venues would be well placed to undertake this task?

<ESMA_QUESTION_171>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_171>

Q172: The discussion in section 3.6 on the liquid market for non-equity instruments around 'average frequency', 'average size', 'number and type of active market participants' and average size of spreads is also relevant to this chapter and we would welcome respondent's views on any differences in how the trading obligation procedure should approach the following:

<ESMA_QUESTION_172>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_172>

Q173: Do you have a view on how ESMA should approach data gathering about a product's life cycle, and how a dynamic calibration across that life cycle might work? How frequently should ESMA revisit its assumptions? What factors might lead the reduction of the liquidity of a contract currently traded on venue? Are you able to share with ESMA any analysis related to product lifecycles?

<ESMA_QUESTION_173>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_173>

Q174: Do you have any suggestions on how ESMA should consider the anticipated effects of the trading obligation on end users and on future market behaviour?

<ESMA_QUESTION_174>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_174>

Q175: Do you have any other comments on our overall approach?

<ESMA_QUESTION_175>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_175>

3.12. Transparency Requirements for the Members of ESCB

Q176: Do you agree that the above identifies the types of operations that can be undertaken by a member of the ESCB for the purpose of monetary, foreign exchange and financial stability policy and that are within the MiFID scope? Please give reasons to support your answer.

<ESMA_QUESTION_176>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_176>

Q177: What is your view about the types of transactions for which the member of the ESCB would be able to provide prior notification that the transaction is exempt?

<ESMA_QUESTION_177>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_177>

3.13. Article 22, MiFIR: Providing information for the purposes of transparency and other calculations

Q178: Do you have any comments on the content of requests as outlined above?

<ESMA_QUESTION_178>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_178>

Q179: Do you have proposals on how NCAs could collect specific information on the number and type of market participants in a product?

<ESMA_QUESTION_179>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_179>

Q180: Do you consider the frequency of data requests proposed as appropriate?

<ESMA_QUESTION_180>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_180>

Q181: How often should data be requested in respect of newly issued instruments in order to classify them correctly based on their actual liquidity?

<ESMA_QUESTION_181>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_181>

Q182: What is your view of ESMA's initial assessment of the format of data requests and do you have any proposals for making requests cost-efficient and useful for all parties involved?

<ESMA_QUESTION_182>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_182>

Q183: Do you consider a maximum period of two weeks appropriate for responding to data requests?

<ESMA_QUESTION_183>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_183>

Q184: Do you consider a storage time for relevant data of two years appropriate?

<ESMA_QUESTION_184>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_184>

4. Microstructural issues

4.1. Microstructural issues: common elements for Articles 17, 48 and 49 MiFID II

Q185: Is there any element that has not been considered and/or needs to be further clarified in the ESMA Guidelines that should be addressed in the RTS relating to Articles 17, 48 and 49 of MiFID II?

<ESMA_QUESTION_185>

Economic and academic research thus far has provided no direct evidence that algorithmic or high frequency computer-based trading has increased disorderly trading or market abuse. Nevertheless we recognise that automated trading – through its ubiquitous use by all different types of market participants – has changed the market in fundamental ways, not least of which is the speed at which trading occurs. We understand the organisational requirements for investment firms are aimed at improving market performance and reducing the risk of market failure. We believe some policy measures, such as those focused on standardising risk controls and coordinating approaches to monitoring at the gateway to markets (the trading venues) are well worth the effort. We believe other measures, such as identification of algorithms, have less evidence-based support and may not contribute to stated goals, while definitely imposing significant extra costs on both the investment firms needing to comply and the regulators who will have to monitor compliance.

In establishing a framework of organisational requirements for investment firms, the biggest challenge for the market is striking the right balance between managing the complex role computers play in the modern financial field, without unnecessarily introducing more complexity. With respect to organisational requirements, we believe this can be achieved by:

- harmonising approaches where possible, while preserving a proportional approach that respects differences in business models and risk profiles;

- avoiding duplication of requirements at different levels of market participants;

- standardising financial data and making this easily accessible for retention, review and analysis, while preserving confidentiality; and

- making use of industry best practices drawn up by market experts in the best position to draft best-in-class policies.

Since the publication of the 2012 ESMA guidelines on systems and controls in automated trading environment[1] (the "ESMA Guidelines"), certain practices have become more prevalent and standardized, such as "drop-copy" reconciliation, continuous comparison of firm books to exchange and clearing agent rec-

[1] ESMA guidelines on systems and controls in automated trading environment, February 2012, available at: http://www.esma.europa.eu/system/files/esma_2012_122_en.pdf .

ords, and market maker protections. These are discussed in further detail in the specific questions referring to these topics.

Stressing practicality and our industry's 'best-in-class' guidance, the FIA Associations[2] would like to suggest ESMA looks to the practices recommended by FIA ETPA in the 2012 Market Integrity Framework: Best Practices to Preserve Market Integrity[3] document and consider adopting any topics we included in those best practices that were not included in the ESMA Guidelines.

<ESMA_QUESTION_185>

Q186: Do you agree with the definition of 'trading systems' for trading venues?

<ESMA_QUESTION_186>
The FIA Associations believe the definition proposed by ESMA of 'trading system' is very prescriptive, and we question the added value of specifying in detail so many different elements.

ESMA states the purpose of further defining a trading system is to "*narrow down the scope of ESMA's proposals so as to avoid confusion in relation to the elements that would be captured by future technical standards*." ESMA's proposed definition may potentially capture non pertinent elements of a trading system while at the same time, by appearing to be exhaustive, risks omitting one or more critical elements that are or may become (as technology progresses) pertinent to a trading system.

Recital 16 of MiFIR states in order to ensure uniform applicable conditions between trading venues, the same pre-trade and post-trade transparency requirements should apply to the different types of venues. The requirements should be calibrated for different types of trading, including order book and quote-driven systems such as request for quote as well as hybrid and voice broking systems.

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[2] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time-zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

[3] FIA ETPA Market Integrity Framework: Best Practices to Preserve Market Integrity, 2012, available at: http://www.futuresindustry.org/epta/downloads/EPTA-Market-Integrity-Framework_072012.pdf

Table 1 of Annex II of Regulation 1287/2006 includes a description of each type of trading system as follows.

A **continuous order book trading system** is a system that by means of an order book and a trading algorithm operated without human intervention matches sell orders with matching buy orders on the basis of the best available price on a continuous basis.

A **quote driven trading system** is a system where transactions are concluded on the basis of firm quotes that are continuously made available to participants, which requires the market makers to maintain quotes in a size that balances the needs of members and participants to deal in a commercial size and the risk to which the market maker exposes itself.

Instead, the FIA Associations would like to suggest these existing definitions of **continuous order book trading system** and **quote driven trading system** are adequate descriptions leaving room for technology to progress and allowing for a principle-based approach to be applied.

<ESMA_QUESTION_186>

Q187: Do you agree that the requirements under Articles 48 and 49 of MiFID II are only relevant for continuous auction order book systems and quote-driven trading systems and not for the other systems mentioned above?

<ESMA_QUESTION_187>
The FIA Associations agree with ESMA's approach. We do not find the requirements of Articles 48 and 49 suitable or relevant for OTC trading (including Requests-for-Quote systems), periodic auction trading systems (systems that match orders on the basis of a periodic auction and a trading algorithm operated without human intervention) or hybrid systems (systems falling into two or more of the other categories of trading systems where the price determination process is of a different nature than that applicable to continuous order book and quote driven systems).

<ESMA_QUESTION_187>

Q188: Which hybrid systems, if any, should be considered within the scope of Articles 48 and 49, and why?

<ESMA_QUESTION_188>
The FIA Associations cannot currently identify any hybrid systems that should be considered within the scope of Articles 48 and 49 of MiFID II.
<ESMA_QUESTION_188>

Q189: Do you agree with the definition of "trading system" for investment firms?

<ESMA_QUESTION_189>
The FIA Associations believe the definition of 'trading system' for investment firms is not optimal the same reasons set out above with respect to trading venues.

ESMA's proposed definition includes the following text: "those supporting elements without which it would be impossible to implement those techniques" as well as "all internal or external systems where the algorithms are deployed for trading." This text risks being simultaneously vague and over-inclusive. Not all required supporting elements are pertinent to a trading system. It is for example unclear if the proposed definition would include structural hardware elements, cooling systems, and platform monitoring software or data infrastructure elements and what the consequences of regulating such infrastructure would be.

Moreover, we believe strongly that to classify other elements that feed into algorithmic order generation - such as the idea generation process or data analysis stages – as part of a 'trading system' would result a disproportionate duplication of compliance process that are not appropriate to that stage of the algorithmic order generation process. For this reason we do not agree with ESMA's apparent intention to capture within the scope of 'trading system' all elements of the algorithmic order generation process, including 'the algorithmic technologies to interpret signals from the market'.

Therefore, the FIA Associations recommend leaving 'trading system' an open, principle-based concept that has the flexibility to adapt to changing technological circumstances.

<ESMA_QUESTION_189>

Q190: Do you agree with the definition of 'real time' in relation to market monitoring of algorithmic trading activity by investment firms?

<ESMA_QUESTION_190>
The FIA Associations believe it is not necessary to further define 'real time' in relation to market monitoring of algorithmic trading activity by investment firms.

The purpose of further defining 'real time' is to determine the optimally minimised time delay where the purpose of monitoring is the firm's own risk management. We acknowledge that in most cases, particularly with respect to algorithmic trading strategies operated on liquid markets, a five second time period is a realistic time frame for monitoring the entry and execution of orders. However 'real time' as suggested by ESMA is not appropriate in all situations relating to a firm's risk management.

First of all, not all types of risk monitoring may be possible within a five second period. Depending upon the process (for example credit checks), risk monitoring may involve complexities that require longer periods of time to compute or manifest. Not all systems and especially back-end systems permit real time calculations. In some cases monitoring must be grouped by cycle and uploaded. Moreover, some trading venues where algorithmic strategies are used, such as certain power market platforms, do not provide real time trade feeds but feeds on a batch basis instead. For trading on these trading venues it would not be possible to monitor confirmations within a five second period.

Secondly, given the diversity of types of firms engaged in algorithmic trading and differences in the nature, scale and complexity of each firm we do not believe ESMA should prescribe a fixed timeframe for the definition of 'real time.' For some systems, five seconds would be an eternity during which all manner of disruption can occur. In practical terms, 'real time' could range from near-real-time in terms of milliseconds in entirely automated systems to several seconds or even minutes for a human reaction to a trading system operating algorithmic strategies. It strongly depends on context, the feedback or the action that must be generated (whether human or automatic), the interface used for such feedback or action and the sources of information used for that.

As ESMA itself acknowledges, any attempt to define a real time timeframe is bound by the state of technology at the time of adoption of the regulatory technical standards, which means any such definition may become obsolete immediately upon or at any stage after publication.

The FIA Associations therefore advise ESMA to leave 'real time' an open, principle-based concept that has the flexibility to adapt to changing technological circumstances.

<ESMA_QUESTION_190>

Q191: Is the requirement that real time monitoring should take place with a delay of maximum 5 seconds appropriate for the risks inherent to algorithmic trading and from an operational perspective? Should the time frame be longer or shorter? Please state your reasons.

<ESMA_QUESTION_191>
Please see the FIA Associations' comments to Question 190.

<ESMA_QUESTION_191>

Q192: Do you agree with the definition of 't+1' in relation to market monitoring of algorithmic trading activity by investment firms?

<ESMA_QUESTION_192>
The FIA Associations disagree with the definition of 't+1' for the same reasons given in response to Question 190.

ESMA proposes a definition of 't+1' in relation to the monitoring of algorithmic order entry as "all surveillance outputs (alerts) … are available for analysis at the start of the next day (before market opening), i.e. are computed overnight." Given the diversity of types of firms engaged in algorithmic trading and differences in the nature, scale and complexity of each firm, we believe this definition may be overly prescriptive for some operations. Therefore we advise ESMA against prescribing a fixed timeframe for the monitoring of algorithmic trading activity.

We also note that abusive practices are rarely undertaken or identifiable through a single or small group of orders. Such practices are usually statistical and often require a look-back over many trades over a period of time to reveal a manipulative effect.

The FIA Associations therefore recommend a more principle-based approach to post-trade review to detect market manipulation. As FIA EPTA stated in the 2012 Market Integrity Framework: Best Practices to Preserve Market Integrity[4]:

*"[…] investment firms should have procedures in place to ensure that orders and transactions that are investigated and that could constitute market manipulation are reported to the competent authorities *as soon as possible*."* [Emphasis added]

Moreover, the FIA Associations would like to emphasize that abusive practices are rarely undertaken or identifiable through a single or small group of orders. Such practices are usually statistical and often take a look-back over many trades over a period of time to reveal their manipulative effect. A monitoring at t+1 would in itself not provide very valuable information. Valuable information may be derived only after a certain evaluation period. Therefore, from the perspective of market abuse, the FIA Associations strongly recommend that the timing of look-back should correspond with that of the evaluation of the system.

Therefore, we believe a proportional and principle-based approach such as the one we highlighted above is a more appropriate approach. ESMA could provide as part of FAQs further interpretive guidance on specific type of incidents that should be addressed during the next business day. Finally, the FIA Associations believe such an approach will give NCAs the possibility of making a proper assessment of the proportionality and sufficiency with investment firms on an ex-post basis.

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[4] FIA EPTA Market Integrity Framework: Best Practices to Preserve Market Integrity, July 2012, p.8, available at: http://www.futuresindustry.org/epta/downloads/EPTA-Market-Integrity-Framework_072012.pdf

<ESMA_QUESTION_192>

Q193: Do you agree with the parameters to be considered to define situations of 'severe market stress' and 'disorderly trading conditions'?

<ESMA_QUESTION_193>
The FIA Associations agree with the definition of **severe market stress** but disagree with the parameters integrated in the definition of **disorderly trading conditions**.

We believe the parameters to be considered to define disorderly trading conditions should be: significant delays, interruptions or errors in the processing of marketplace transactions.

In our view, disorderly trading conditions are not per se indicated by significant short-term changes in market volume, price or the number of messages. Disorderly trading conditions may not necessarily occur when there are dramatic or severe price or volume shifts.

For example, if a security is negatively impacted by news and dramatically sells off as a result, inherently leading to a dramatic increase in the number and volume of messages, it can and should still be considered 'orderly trading' as long as it does not jeopardise the systems of trading venues and remains controlled and limited by investment firms' appropriate control systems.

In fact, adequate and prudent risk management at investment firms pursuing automated trading necessarily prescribes increased messaging to facilitate stable trading during moments of volatility, in order to prevent mispricing. This 'agility' and flexibility is particularly important in turbulent markets as mispricing has a direct and material impact on other market participants and can contribute to knock-on incidents spreading risk through the market. As set out in our response to Question 167 of the Consultation Paper, for market makers in particular, the ability to update quotes in an agile manner reduces risk for the market as a whole by evening out price movements and facilitating faster recoveries from volatility through small, quick steps as opposed to bigger, slower updates. This ensures tight spreads by allowing market makers to respond quickly to changing markets rather than having to rely on wider spreads for managing risks.

As we state above, what actually contributes to **disorderly trading conditions** are significant delays, interruptions or errors in the processing of marketplace messaging and transactions. While these types of conditions can be related to periods of higher volumes, this is not a necessary condition. Whether due to human error or failure of information and communication systems, situations such as hanging orders (where an order has already been executed but takes extra time to confirm) and order queues due to limited throughput (the number of successful messages sent through the system) caused by technical issues can cause market participants to panic or misprice and systems to slow or lock. This can lead, for example, to multiple entries for the same order, the inadvertent opening of unintended positions or positions for which the investment firm is not appropriately hedged, thus increasing the amount of risk in the system. Such issues can produce substantial losses for market participants and jeopardise market integrity.

Therefore, in addition to redefining the parameters of what constitutes **disorderly trading conditions** as set out above, the FIA Associations believe the focus should be on strengthening the robust capacity of trading venues' systems, particularly under duress, and the stimulation of all market participants to make the appropriate investments in technology processing power, speed and innovation to manage such risks.

<ESMA_QUESTION_193>

Q194: Do you agree with the aboveapproach?

<ESMA_QUESTION_194>
The FIA Associations neither agree nor disagree with ESMA's approach regarding self-assessments to be undertaken by trading venues regarding the nature, scale and complexity of their businesses.

We refer to our comments in response to Question 197 below regarding the frequency of self-assessments generally.

We would like to highlight that paragraph (iii)(g) "*Access provided to different CCPs*" may pose a competition issue as some exchanges mandate the use of certain [affiliated] CCPs, despite users preferring another CCP or CCPs for risk mitigation or commercial reasons. Taking this factor into account when assessing a trading venue's risk profile could increase the risk profile of that trading venue and therefore create an incentive to limit open access to certain CCPs but perhaps not to others. Ideally, also in order to reduce clearing risks or for commercial reasons, more sophisticated market participants would like to assign multiple General Clearing Members (GCM) for different classes of traded products, alongside choosing multiple CCPs for multiple products. Currently, most venues prescribe the use of a certain CCP combined with one GCM for all trades executed by a certain participant.

<ESMA_QUESTION_194>

Q195: Is there any element that should be added to/removed from the periodic self-assessment?

<ESMA_QUESTION_195>
Please see the FIA Associations response to Question 194 above.

<ESMA_QUESTION_195>

Q196: Would the MiFID II organisational requirements for investment firms undertaking algorithmic trading fit all the types of investment firms you are aware of? Please elaborate.

<ESMA_QUESTION_196>
Without addressing the content of the organisational requirements for investment firms undertaking algorithmic trading (discussed in Section 4.2 – Question 199-228), the primary concern of the FIA Associations is that the requirements might fail to capture all of the participants conducting or indirectly facilitating algorithmic trading.

In general the FIA Associations believe regulation should apply equally to market participants based on the substance of their market activity. Investment firms increasingly provide access to their customers through front-end software or API connectivity that allows these clients to access the market and facilitate automated trading. As technology has progressed, there is no difference between the capabilities and potential risks imposed by clients using Direct Electronic Access (DEA) compared to professional algorithmic traders and high frequency traders.

However, to the extent these users may not be subject to the direct requirements of MiFID II, we emphasize that DEA providers have ultimate responsibility for the actions of their underlying clients. Please see the FIA Associations' answer to Question 215 in the section on 'Direct Electronic Access'.

<ESMA_QUESTION_196>

Q197: Do you agree with the approach described above regarding the application of the proportionality principle by investment firms? Please elaborate.

<ESMA_QUESTION_197>

The FIA Associations strongly believe in the application of the proportionality principle to the organisational requirements for investment firms. However, we do not think the approach put forward by ESMA adequately reflects this principle.

First, a proportional application of the organisational requirements should take into account the nature, scale and complexity of different investment firms with different businesses. By definition, this should encompass some flexibility for firms to exercise discretion whether and to what extent each requirement applies to their businesses. While ESMA explicitly states it "*recognises that the risks stemming from algorithmic trading activities (for firms themselves and/or for the fair and orderly functioning of markets) are not homogenous across all firms,*" ESMA has nevertheless removed any discretion for firms when it goes on to state that the extensive list of organisational requirements in the following section "*should constitute a minimum.*" We believe this approach leaves no room for the application of the proportionality principle.

Second, in various places in the Microstructural issues section of the Discussion Paper, ESMA proposes to require investment firms and/or trading venues to engage in semi-annual reviews of various processes and controls. This includes, here, the requirement that investment firms engage "*at least twice yearly*" in a "*detailed and robust self-assessment of their activities*" to identify how to apply the proportionality principle to their own situations. This self-assessment will be difficult for small-to-medium sized firms to implement: it will take them just as much work to go through the process as large firms. We believe this will result in investment firms operating algorithmic trading systems constantly undertaking such periodic reviews. The FIA Associations believe that compulsory formal reviews every six months could even prove counterproductive as the timeframe involved could detract from each review's quality.

Thirdly, some elements such as i(c) the level of automation of trading and other processes or activities of the firm, i(m) the maturity of the firm and level of experience and competency of its personnel and all elements relating to (iii) 'Complexity' are very subjective in nature and therefore difficult to determine. Furthermore, it is difficult to reconcile the many divergent views on the impact of these elements on the overall risk.

Fourth, some provisions will inevitably force trading venues (Article 48(7) of MiFID II) and DEA providers (Article 17(5) of MiFID II) to audit or review their counterparties, i.e. investment firms, in order to be compliant themselves. That would mean investment firms might become subject to audits and inquiries from numerous trading venues and service providers at least twice a year, in addition to their own obligation to be compliant with MiFID II. These overlaps will result in duplication of efforts on the part of market participants to satisfy documentary exercises, without tangible benefits in terms of stability.

Finally, investment firms dealing on own account, such as the members of FIA EPTA, risk their own capital and not that of outside investors when conducting their business. Therefore they have a natural and basic incentive to have the appropriate controls in place because in case of error, they cannot rely on outside help to keep the firm solvent.

The view of the FIA Associations is that the organisation of an investment firm is unlikely to change significantly or lead to a material change every six months; therefore conducting a holistic business review with this frequency would not generate tangible benefits. Moreover, by prescribing a timetable for such reviews, an investment firm who undergoes a material change immediately following the last semi annual review would not be obligated to conduct the next scheduled review for another six months. We do not think this is a desirable approach: material changes should be reported more frequently if and when they arise.

Therefore, the FIA Associations recommend ESMA adopts an approach that simplifies the nature, scale and complexity factors and requires reviews 'annually or more frequently if the circumstances of a materi-

al change give rise'. A more frequent self-assessment should be undertaken only in the event of a material change in the investment firm, as determined by senior management (themselves subject to competent authority oversight) in accordance with the proportionality principle and the nature, scale and complexity of the firm's trading activities.

We suggest '**material change**' in this context would be identified as:

- Nature: a material change in the ownership structure, the regulatory status, or undertaking of trading a substantially new asset class;
- Scale: a greater than 50 percent increase in numbers of employees, capital or number of markets accessed;
- Complexity: a material change in the type of algorithmic approach undertaken, the application of a particular algorithmic approach to a new asset class; the adoption of a totally new asset class.

The FIA Associations believe their suggested approach will also reduce the potential for differences in interpretation of the proportionality principle between regulators and the investment firms they oversee and between regulators of different jurisdictions. Else, we foresee difficulties in standardizing the implementation of the proportionality principal, particularly with regard to the requirement that investment firms be at all times in a position to demonstrate to their NCA how, and on the basis of which considerations, they have applied the proportionality principle in practice (items 49 and 50). Differences in the application of proportionality may lead to different approaches to the elements discussed which will lead to inequalities in implementing this principle within the EU.

To the extent ESMA wishes to preserve its proposed text, we strongly recommend that ESMA clarify that the factors set out are not minimum requirements, but rather only examples of what could be considered in an investment firm's discretionary self-assessment of its nature, scale and complexity. NCAs may always conduct reviews to assess the adequacy of how firms apply the self-assessment criteria.

Notwithstanding anything above, however, the FIA Associations believe any order being sent to the exchange should be subject to a minimum level of requirements with respect to pre-trade risk controls.

<ESMA_QUESTION_197>

Q198: Are there any additional elements that for the purpose of clarity should be added to/removed from the non-exhaustive list contained in the RTS? Please elaborate.

<ESMA_QUESTION_198>
Please see the FIA Associations' answer to Question 197 above.

<ESMA_QUESTION_198>

4.2. Organisational requirements for investment firms (Article 17 MiFID II)

Q199: Do you agree with a restricted deployment of algorithms in a live environment? Please elaborate

<ESMA_QUESTION_199>

The FIA Associations[5] agree with proportionate, risk-based and appropriate testing of algorithms. However, we are opposed to the prescriptive nature of the tests that should be conducted.

Trading technology and its development are the main drivers of the activities of FIA EPTA member firms. As such, we have long been thought leaders in developing best practice recommendations for software development, testing and change management at the investment firm level. We would like to bring to ESMA's attention the FIA PTG/EPTA Software Development and Change Management Recommendations from March 2012[6]. In our recommendations, we offer principles that can be viewed as building blocks all types of market participants may use to tailor their testing and change management process according to their needs. The FIA Associations are currently working on updating and revising these recommendations to include more details in line with all the comments and suggestions included in this response. We strongly emphasize our recommendations are offered as particular guidance based on the professional subset of principal traders, but not suggested as binding.

Investment firms should have a process for testing core software components before they are released to the production environment. A variety of effective testing methodologies exist and each firm should employ a combination of software testing tools that best matches its unique needs. Among the testing methods to consider are: unit testing, functional testing, non-functional testing, acceptance testing, and exchange-based conformance testing.

In contrast to ESMA's approach, the FIA Associations believe that investment firms should have the flexibility – in the context of initial testing, testing within a trading venue testing environment, the controlled roll-out of algorithms, conformance testing and on-going testing – to choose to combine one or more steps into a single step in their process, or to elect to split a particular step into several other sub-steps, depending on their need.

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[5] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time-zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

[6] FIA PTG/EPTA Software Development and Change Management Recommendations, March 2012, available at: http://www.futuresindustry.org/downloads/Software_Change_Management.pdf .

The FIA Associations believe software testing should be appropriate and proportionate to the scope, scale and novelty of an algorithm or a change being made to an existing algorithm. For example, a minor parameter change or careful introduction of a well-functioning algorithm to another market vastly differs from commencing trading on a novel architectural platform. Existing best practices in software development dictate different kinds of changes may warrant different refinements or variants of the process, depending on the nature of the changes and their potential impacts. Therefore:

- A new algorithm or material changes to previous architecture should be extensively tested in a non-live environment, tested in limited-scale production and then enter full-scale in production under close supervision.
- More limited amendments or the roll-out of a well-functioning algorithm on additional exchanges should have a much less stringent, risk-based, regime: testing in limited-scale production and then supervised production will generally suffice.
- For minor amendments, testing in limited-scale production may even be skipped under strictly defined circumstances.

The FIA Associations are concerned that the requirements generally set out by ESMA in Section 4.2 in general, and in particular with respect to 'Testing of trading systems, algorithms, and strategies' are overly prescriptive and burdensome.

First of all, ESMA states in paragraph 11 (p. 214) that "*investment firms should, prior to deploying a trading system or trading algorithm or strategy and prior to deploying updates, make use of clearly delineated development and testing methodologies.*" ESMA seems to suggest that all the methodologies include all the testing methods described in paragraphs 12 and 13, such as performance simulations/back testing, non-live testing within trading venue testing environments. Therefore all software modifications, regardless of their magnitude, should be tested appropriately and proportionately to the modification being made.

It may not be proportionate to apply all of these testing methodologies to minor software updates. It may also not be proportionate to require that every update be flight tested on all venues before deployment. Whereas technical conformance tests must be carried out at each individual trading venue, disorderly market testing (or testing for compatibility with regulatory obligations) is specific to the investment firm's algorithms and does not necessarily need to be repeated at each individual trading venue. Rather, an investment firm might take a risk-based approach and conduct a full range of testing on its primary trading market, followed by more limited tests on the markets on which it trades less.

Secondly, ESMA's suggested approach in this section appears to be rules-based, leaving no room for the application of the proportionality principle. For example, in paragraph 17 on p. 215, ESMA sets out a prescriptive list of limits to be placed on algorithms being rolled out in a controlled fashion that are cumulative ("and") rather than optional ("or"). Likewise, in paragraphs 19 and 20 of the same page, results of conformance tests "*have to be taken into consideration when conducting the risk inventory and the self-assessment*" as well as in the business continuity concept.

In keeping with the proportionality principle, the FIA Associations recommend ESMA replaces the highly detailed, rule-based proposal as currently drafted with core principles for "adequate, proportionate, risk-based and appropriate" testing.

We strongly recommend leaving investment firms discretion to apply appropriate and proportionate testing procedures based on their own determination of the type of change and the materiality thereof. While we trust ESMA acknowledges software modifications can differ in magnitude, we caution against

trying to develop a set of objective criteria to qualify a modification as “material” or “minor.” These are highly subjective terms that are difficult to properly apply and may be misleading to technical and other staff. Instead, those responsible for development, testing, and change management should be allowed to determine the amount and type of testing necessary to confirm that a modification is working as intended since they are best positioned to understand the scope of such a modification as well as any external impacts it may have.

ESMA should require that all development procedures adhere to best practice in order to avoid launches that might contribute to disorderly trading behaviour. For a market-relevant example of such best practice, we refer ESMA to FIA PTG/FIA EPTA’s Software Development and Change Management Recommendations[7]. NCAs may always conduct reviews to assess the adequacy of how firms apply best practice.

<ESMA_QUESTION_199>

Q200: Do you agree with the parameters outlined for initial restriction? Please elaborate.

<ESMA_QUESTION_200>
Please see the FIA Associations comments above in response to Question 199 for our general view.

<ESMA_QUESTION_200>

Q201: Do you agree with the proposed testing scenarios outlined above? Would you propose any alternative or additional testing scenarios? Please elaborate.

<ESMA_QUESTION_201>
The FIA Associations strongly agree with the principles behind the requirement to conduct testing and certification of algorithms. We are however strongly opposed to the prescriptive nature of tests that should be conducted.

Please see our comments above in response to Question 199 for our general view. Investment firms should determine the focus and risks targeted for the purpose of the testing of algorithms. We support exchange based testing mechanisms, but if no standardised testing environments exist then testing cannot be uniform without clear and reasonable standards that incorporate risk-based sensibility.

We also reiterate that a six-month testing interval is too frequent and will cause investment firms to re-test software that hasn’t changed. Annual testing is more than sufficient unless a material change has occurred. Furthermore, software used in the production environment is effectively tested every day, throughout the day, as such software runs under continuous supervision.

<ESMA_QUESTION_201>

Q202: Do you agree with ESMA’s approach regarding the conditions under which investment firms should make use of non-live trading venue testing environments? Please elaborate.

<ESMA_QUESTION_202>
While the FIA Associations fundamentally agree that investment firms should have a process for testing core software components before they are released to the production environment, as software best practices continue to evolve we believe such testing should be appropriate and proportionate. A variety of

[7] FIA PTG/EPTA Software Development and Change Management Recommendations, March 2012, available at: http://www.futuresindustry.org/downloads/Software_Change_Management.pdf .

effective testing methodologies exist, and each firm should employ a suite of software testing tools to suit its unique needs.

The FIA Associations do not support ESMA's position that the testing of algorithms in non-live environments should necessarily be mandatory.

First, testing environments of trading venues are not always able to simulate realistic market conditions and therefore do not reflect what can be expected of the same algorithm operating in a live environment. ESMA acknowledges this limitation on p. 285 of the Discussion Paper, stating "*there may be cases under which the scenarios provided by trading venues might not be sufficient for [testing] purposes*" and that "*members or participants deploying new algorithms are fully responsible for testing them under appropriate scenarios*." For example, BATS Chi-X provides a test environment to participants that is not populated with a model market, and the trading venue believes there would be no practical way of achieving that. To be genuinely useful, non-live testing environments should involve a "model market" that includes simulated aggregate data from all related venues in order to reflect reactions across related products and markets. Obviously this would be a substantial, if not prohibitive, undertaking to develop and implement and in our view would only yield limited benefits.

Second, fees currently charged for use of these non-live testing environments are often prohibitively high and will only increase further if trading venues have to simulate a realistic environment.

The FIA Associations therefore believe requiring mandatory non-live testing, rather than allowing firms to choose the testing methodologies most appropriate to their businesses, may result in algorithms going into the market that have been less rigorously tested than those which have been subject to other techniques, such as non-functional testing, acceptance testing, unit testing, functional testing. ESMA should hold non-live testing out as a goal rather than a requirement, while allowing for study and iterative development. NCAs should in any event be able to assess or discuss adequacy on a firm-by-firm basis.

<ESMA_QUESTION_202>

Q203: Do you consider that ESMA should specify more in detail what should be the minimum functionality or the types of testing that should be carried out in non-live trading venue testing environments, and if so, which?

<ESMA_QUESTION_203>
The FIA Associations do not believe specifying in more detail the minimum functionality of non-live testing will support the objectives of ensuring algorithms operate safely and as intended.

<ESMA_QUESTION_203>

Q204: Do you consider that the requirements around change management are appropriately laid down, especially with regard to testing? Please elaborate.

<ESMA_QUESTION_204>
Subject to our comments above to Question 199, the FIA Associations believe the requirements laid down in Paragraphs 22 and 23 under '*Sign-off and review procedures in relation to change management and testing*' are essential. The core of a robust change management procedure is identifying the desired or required change, developing and testing the change, deploying the change, and verifying the change.

Beyond the elements above, we believe ESMA goes too far in prescribing the elements of change management. Not all algorithms are suitable to performance simulations / back testing, nor do we believe that initiating, running and stopping a large number of algorithms in parallel or conducting high volume tests twice yearly serves the purpose of mitigating the occurrence of disorderly trading conditions. This would

be difficult to realise in practice because, as discussed above, non-live testing environments do not replicate realistic market conditions, and such testing should certainly not take place in a live market.

For a market-relevant example of best practice, we refer to FIA PTG/EPTA's previously cited Software Development and Change Management Recommendations[8].

<ESMA_QUESTION_204>

Q205: Do you agree with the proposed monitoring and review approach? Is a twice yearly review, as a minimum, appropriate?

<ESMA_QUESTION_205>
For the FIA Associations' general view on the proposed monitoring and review approach by ESMA, please see our response to Question 197. We do not believe compulsory semi-annual reviews are a proportionate requirement for the majority of firms. Such reviews take vast amounts of time and resources to undertake. We envision that a semi-annual requirement would require investment firms operating algorithmic trading systems to be constantly undertaking such periodic reviews.

The FIA Associations believe strongly in industry best practice of continuous assessment and testing to ensure algorithmic systems operate under supervised control. Compulsory formal reviews every six months could even prove counterproductive, as the timeframe involved could detract from each review's quality.

We consider a frequency of annual review, or more frequently if circumstances of material change give rise, to be in accordance with the proportionality principle taking into account the nature, scale and complexity of the firm's trading activities.

We have commented on ESMA's detailed proposal paragraph by paragraph below.

Kill Buttons (Paragraph 30)

While kill switches do have merit, the FIA Associations urge ESMA not to encourage their use as a risk control because they have the potential to introduce more risk than they mitigate.

We note there seems to be an overemphasis throughout the Microstructural issues section of the Discussion Paper on firms' ability to use "kill buttons" (or "kill switches") to cancel all outstanding orders at individual trading venues, or originating from individual traders, trading desks, or clients.

In FIA PTG's Recommendations for Risk Controls for Trading Firms[9], we also recommend trading systems should have a manual "kill button" that, when activated, disables the system's ability to trade and cancels all resting orders.

However, the use of kill switches is not a panacea for disruptive algorithms. Both investment firms and DEA providers regard their use as a "nuclear" option. Kill switches are notoriously dangerous to operate in practice because it is difficult for a human operator to distinguish legitimate from non-legitimate systems activity without verifying what is actually happening, particularly in turbulent markets. A hair trigger response of pulling all orders to venues to which a firm is connected can actually create a risk event, rather

[8] FIA PTG/EPTA Software Development and Change Management Recommendations, March 2012, available at: http://www.futuresindustry.org/downloads/Software_Change_Management.pdf .
[9] FIA PTG Recommendations for Risk Controls for Trading Firms, November 2010, available at: http://www.futuresindustry.org/downloads/Trading_Best_Pratices.pdf .

than solving one, as orders pulled may already have been closing out positions to curtail a firm's risk exposure or part of a firm's hedge. When a kill switch is activated, a firm must scramble to reconcile all working orders and find a way to get critical, risk-reducing orders back into the market as soon as possible. Quite often, much more damage is caused than prevented. It is clear kill switches should not be used lightly, and the decision to kill or halt activity should only be made with surgical focus and optimal information about the risks involved.

Instead of overemphasising kill switches, ESMA should allow firms to choose from a variety of mechanisms that may better preserve market stability, such as embedding limits in systems, winding down positions in a controlled manner, and maintaining dialogue between clearing firms and clients. As we set out in FIA PTG's Recommendations for Risk Controls for Trading Firms[10], we recommend investment firms develop their systems with a series of automatic curtailments based on pre-programmed parameters. Trading systems should be built to alert and/or self-curtail, at each level (participant, clearing firm, exchange), prior to the need for human kill switches. The breach or approach of a sanity check, such as the limits discussed on page 224, should alert operators when issues occur. These sanity checks can be based on metrics of orders, levels of loss or profit, or other boundaries related to the type of trading strategy.

Flagging of algorithms (Paragraph 31)

The FIA Associations acknowledge there is a general regulatory impetus behind the concept of flagging algorithms. This requirement was realised for the first time in the German HFT law that entered into force in March 2014. We understand regulators believe the flagging algorithms will facilitate the necessary surveillance, which is perceived to have become more difficult with respect to automated trading and the aggregated data it generates.

Both then and now, the FIA Associations believe creating an identification system based on algorithmic processes is misguided. Computer programs might be made up of numerous algorithms that make decisions or contribute information in a decision tree process that contributes to the ultimate decision to take action in a market. Creating more IDs than necessary for the components of an automated trading system is artificial, leads to an increase in data that trading venues and regulators must analyse during any review of trading activity, and does not in our view provide useful information on the applied strategies.

The FIA Associations note this requirement derives from the requirement of Article 48(10) MiFID II, which imposes on Member States the obligation to require RMs, OTFs and MTFs to have an algorithm flagging system: "*(10) Member States shall require a regulated market to be able to identify, by means of flagging from members or participants, orders generated by algorithmic trading, the different algorithms used for the creation of orders and the relevant persons initiating those orders. That information shall be available to competent authorities upon request.*" Article 48(12) does not contain a specific mandate for ESMA to draft Regulatory Technical Standards for Article 48(10). We note in the analysis on pages 453 to 454 of the Discussion Paper, ESMA states that "*a pragmatic solution should be adopted for identification of algorithms*" over which the investment firm will have responsibility and discretion.

While we appreciate that ESMA has appeared to take a principle-based approach to flagging, the FIA Associations are nevertheless concerned that this leaves the door open to the development of different national algorithm flagging requirements, which would create a compliance burden for any investment firm or market participant using the same algorithm on multiple trading venues. Given the overwhelming

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[10] See footnote 9.

task investment firms had in complying only with the German HFT algorithm flagging requirements, having to go through the same process for several different regimes would be an onerous burden.

We therefore request that ESMA issue respective guidelines and recommendations under Article 16(1) Regulation 1095/2010 ("ESMA Regulation") in due course, taking into account the principles we outline in our response to Question 555 of the Discussion Paper (the "Algo ID") with respect to flagging "unique strategies," rather than "unique code". We briefly discuss this approach below.

In the Discussion Paper analysis preceding Question 555 regarding the "Algo ID" (on page 454 in Paragraph 82), ESMA proposes criteria comprising the process for determining identifiers for algorithms.

The FIA Associations believe some of these are not appropriate and will add complexity, confusion and potential technical difficulties to the order entry process. We believe the following requirements are not feasible from a technical perspective:

(i) the requirement that an exclusive designation must be given to each "unique set of code" constituting an algorithm;

(ii) the same identifier should apply for a specific algorithmic code regardless of the products or markets that the algorithm applies to; and

(iii) an algorithm's designation must be unique over time.

(i) ESMA states investment firms must give "*an exclusive designation to each unique set of code that constitutes an algorithm.*"

Here, the problem lies in the requirement that an ID apply to "*a unique set of code constituting an algorithm.*" From a developer's perspective, providing a new identifier for each element of "*unique code*" would normally result in a constantly changing and variable code string – in other words, a nearly infinite number of IDs.

Software development is an iterative process. In some cases code may have many independent modular elements and may change in material ways even during the trading cycle. Some trading algorithms are made up of a sum of software sub-parts, which are built to receive and relay data from other correlated markets, or perform other separate calculations to handle complex events. These sub-components of code may have been written by separate developers and have a variation of change different to the 'core' code. Some changes may be material to the trading actions of an algorithm, and some may be meaningless. This makes it extremely difficult to identify whether the overarching algorithm is a unique 'whole' or has changed by means of its sub-parts.

For example, while perhaps not common, some trading computational models based on artificial neural networks (ANNs) are capable of machine learning and pattern recognition. As such, the relevant code may automatically adapt and evolve (as with evolving data or with adaptive configurations) while in operation.

Thus, the sheer number of IDs that would be generated in the market following this approach would border on infinite. Such a requirement will create enormous data pollution – for both firms and regulators – without serving an attainable surveillance purpose.

Moreover, while computers can execute calculations at extreme speeds, they cannot store or write data at the same tempo. The algorithm flagging requirements as currently proposed by ESMA will require firms to store exponentially more data, demanding an unforeseeable increase in processing power compared to what they currently need to operate their trading algorithms. It will also add significant latency to trading

and risk management systems. While some observers might not see a problem with slowing markets down, we would like to point out that this effect might limit their economic usefulness.[11]

We do not believe this is the outcome ESMA intends or has foreseen in requiring a new identifier for each element of "*unique code*" resulting in a constantly changing and variable code string.

We acknowledge that the guidelines released by the Exchange Supervisory Authority of the State of Hessen regarding the German algorithm flagging rules try to avoid this outcome by striking a middle path and requiring changed identifiers when the algorithm "*changes in a material way*."[12]

However, we do not recommend ESMA follow the State of Hessen's approach as a blueprint for an implementation for Europe because 'materiality' is a subjective standard that is difficult to maintain without an extensive and inflexible set of guidelines. For example, as discussed earlier, when is a change triggered by a software sub-component a 'material change' to the core code? This would be extremely difficult to determine in a harmonised way. We have been, and remain, concerned that the implementation of the German algorithm flagging rules will prove to be unsustainable, have a dampening effect on the market, and ultimately overwhelm the relevant regulator with data that it will have trouble storing and making sense of.

Instead, the FIA Associations suggest the use of one identifying number that represents a "unique strategy" (not "unique code"), where "unique strategy" is defined as "the software that generates trading actions based on a trading model." Each firm should be required to maintain a log of all elements of the software in use at the time of an order and be able to use the single identification number for the unique strategy to provide a reference of that code.

This approach is in line with ESMA's statement that "*a pragmatic solution should be adopted for the identification of algorithms. The investment firm will have responsibility and discretion over how it identifies its algorithms throughout the lifecycle of the algorithm*."

(ii) ESMA proposes that the same algorithm identifier should apply for a specific algorithm code regardless of the products or markets that the algorithm applies to (82 (iii), page 454).

ESMA hereby explicitly points to the need for a precise definition of the term 'algorithm' and the chain of processes deemed to determine algorithmic trading (see point 1).

However, a volume-weighted average price (VWAP) algorithm used in the cash market might be different from a VWAP algorithm used in the derivatives market.

The FIA Associations therefore recommend following our suggestion to use one identifying number that represents a "unique strategy," which implicitly reflects the differences in a specific strategy per product/market.

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[11] As set out in our response to Question 167 of the Consultation Paper, the ability of market makers to provide agile quote updates reduces risk for the market as a whole by minimising the chance of mispricing, evening out price movements and facilitating faster recoveries from volatility through small, quick steps as opposed to bigger, slower updates. This ensures tight spreads by allowing market makers to respond quickly to changing markets rather than having to rely on wider spreads for managing risks.

[12] Exchange Supervisory Authority of the State of Hessen, Guidelines to the adherence to the requirement of the labelling of trading algorithms, 20 December 2013, page 5, available at: https://wirtschaft.hessen.de/sites/default/files/media/guidelines_to_the_adherence_to_the_requirement_of_the_labelling_of_trading_algorithms_13-12-20.pdf .

(iii) Third, ESMA has proposed that an algorithm's designation must be unique over time (82 (iv), page 453) and not be used again once the usage of an algorithm discontinued.

Even when our recommendation to use one ID per "*unique strategy*" is followed, we still expect a high number of IDs to be active in markets. Therefore, this uniqueness requirement might encounter potential restrictions in terms of technical capabilities of implementations within trading systems.

The FIA Associations believe that such uniqueness principle will still be fulfilled as long as the ID being used to identify the discontinued algorithm will be shelved for a period of time (e.g. three months).

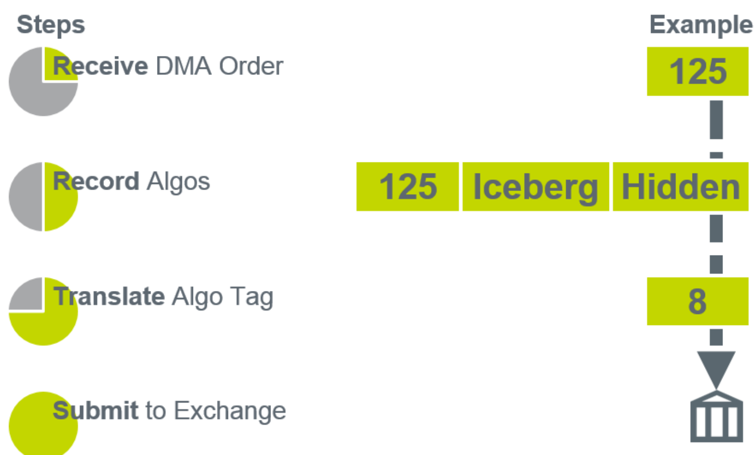
(iv) Finally, above we discuss the methodology for determining an Algo ID, but equally important are the mechanics of how the market uses this ID in end-to-end order flow, including transaction reporting. The FIA Associations are concerned that uniform implementation of algorithm flagging will be impossible without second level detailing of how this should be harmonised across Europe.

The minimum requirements suggested by ESMA in the discussion paper in the context of transaction reporting could be used as a starting point but should be complemented by additional information about how to flag.

The FIA Associations recommend the method below for aggregating Algo ID chains into a single identifier to the market and for purposes of transaction reporting, which has already been adopted in a similar fashion by some market participants in order to comply with German algorithm flagging requirements.

Source - Fidessa, 2014 International Derivatives Expo (IDX)

First, the investment firm generating an order will flag that order with a single identifier designating the unique strategy underlying the order. To the extent an algorithm incorporates more than one strategy, this single identifier at firm level will be an aggregate ID representing multiple strategies, for example, EU-REX, hidden, VWAP. Each firm should maintain a log of all elements of the software in use at the time of an order and be able to use the single identification number for the unique strategy to provide a reference of that code.



Source - Fidessa, 2014 International Derivatives Expo (IDX)

Second, this order, with a unique ID, goes either directly to the trading venue or via a DEA provider. If the order goes first to a DEA provider, the DEA provider aggregates the investment firm's unique ID with an additional element, creating a new, unique designation to flag the order into the market in a single field.

At every step in the order flow process, a participant maintains a table populated with its unique strategy Algo ID and sends this populated table on to next participant in the chain, who then aggregates this label into yet a new ID. This method enables order persistence and the labelling of unique permutations of Algo ID chains, but unlike the German algorithm flagging rules, does not risk generating an infinite number of IDs due to the fact that the initial determinant is at the (useful) level of "unique strategy" rather than "unique code."

With respect to transaction reporting, every investment firm in the order flow process would report its own unique flag.

This solution is relatively easy to implement from a practical perspective, as has been shown by the fact that some market participants have implemented it in a similar fashion already.

The FIA Associations recommend that ESMA issue respective guidelines and recommendations on this topic, taking into account the principles we outline above, under Article 16(1) Regulation 1095/2010 ("ESMA Regulation") in due course.

Drop Copies (Paragraph 32)

Please see the FIA Associations' comments in response to Question 206 below.

Derivatives Exposure Calculation (Paragraph 33)

The FIA Associations agree with this proposal and have no comments.

Real Time Alerts (Paragraph 34)

The FIA Associations agree with the proposal that we discussed further in our response above to Question 190.

Monitoring for Disorderly Trading (Paragraph 35)

The FIA Associations believe the part of this proposal that states monitoring cannot be undertaken in any circumstances by the trader in charge of the algorithm may lead to unforeseen and unwanted effects and should be nuanced.

The 'three lines of defence' has become a standard concept in a modern institution's approach to managing uncertainty and preventing risk. The three lines of defence model distinguishes among three groups (or lines) involved in effective risk management:

- Functions that own and manage risks.
- Functions that oversee risks.
- Functions that provide independent assurance.

The concept of 'three lines of defence' is applied in the context of automated trading as well.

The first line of defence comprises the business' frontline staff: traders. For example, in the context of kill switches, we believe the trader in charge of an algorithm is in the best position of any party to detect signs of disorderly trading and subsequently to decide when it is appropriate to pull orders in a crisis. One of his key responsibilities and expertise is supervising system integrity, market interaction and an algorithm's proper functioning. There should always be adequate managerial and supervisory controls in place to ensure compliance and to highlight control breakdown, inadequate processes, and unexpected events. The head of a trading desk or the head of the trading department should be responsible for using and monitoring these supervisory controls.

Moreover, from an agency perspective, the supervision desk at the DEA provider is considered the Responsible Person for monitoring client flow because the order flow is routed via Operator/Exchange/Trader IDs to the exchange in the DEA provider's name. The supervision desk clearly fulfils a critical monitoring function, while also formally being "the trader in charge of the algorithm."

The second line is created by the oversight function(s) made up of compliance and risk management. These functions set and police policies, define work practices and oversee the business frontlines with regard to risk and compliance.

The third and final line of defence is that of auditors (internal and external).

Necessary Authorisations (Paragraph 36)

The FIA Associations agree with this proposal and have no comments.

Communication Channels (Paragraph 37)

The FIA Associations agree with this proposal and have no comments.

CEBS/EBA Guidelines (Paragraph 38)

The FIA Associations agree with this proposal and have no comments.

Twice Yearly Review (Paragraph 39)

Please see the FIA Associations' comments to Question 197 and above in this answer for our general view on compulsory twice-yearly reviews being a disproportionate requirement for the majority of firms.

However, with respect to scheduled reviews of trading systems and trading algorithms, we would even go further to say – in this specific context only – we do not believe ESMA should prescribe any mandatory reviews on a prescribed time schedule because scheduled reviews may only detract from the quality of daily operations and monitoring. We take this view because trading systems and trading algorithms are used daily, which implies they are constantly being verified by live market operation under close supervision of trained staff. Provided proper procedures are followed with respect to initial testing and change management, ESMA should not impose additional requirements on investment firms in this respect that may push firms toward a 'tick-the-box' compliance approach instead of focusing on the quality of daily operations and monitoring. We believe the concept of scheduled reviews should be reserved for procedures and plans that are not continuously used and verified in practice, such as business continuity and recovery plans.

Review / Evaluation Process Independent from Production (Paragraph 40)

Please see the FIA Associations' comments above in response to paragraph 39.

Validation (Paragraph 41)

Please see the FIA Associations' comments above with respect to paragraph 39.

First, we do not agree with the prescribed time frame for the reasons set out above.

Second, as explained above, we do not agree that trading systems and algorithms themselves need to be subject to additional scheduled reviews beyond the testing to which they are subjected initially and in terms of change management. Procedures, not systems, should be reviewed.

Further, it is unclear to the FIA Associations what is meant by "validation," as this appears to be a subjective concept open to interpretation. We believe this requirement is unnecessary and duplicative of the "*sign-off and review procedures in relation to change management and testing*" proposed on page 216.

We agree that sign-off and review procedures in relation to change management and testing should themselves be subject to review, subject to our comments with respect to frequency of reviews in general (see response to Question 197) and provided this validation can be carried out by designated staff considered appropriate by the investment firm. For example, in most investment firms, the risk control (or compliance) function is not always the function best placed to lead such a "validation process" with respect to individual systems and algorithms. Rather, staff with relevant technical knowledge should lead and sign-off, while risk and/or compliance staff should oversee the integrity of the process.

<ESMA_QUESTION_205>

Q206: To what extent do you agree with the usage of drop copies in the context of monitoring? Which sources of drop copies would be most important?

<ESMA_QUESTION_206>
The FIA Associations strongly agree with the usage of drop copies in the context of monitoring.

Electronic trading systems should have a functionality to accept drop copies from trading venues and clearing firms. Drop copies are copies of orders that allow a firm to compare the trading venue or clearing firm's record of trades and positions with a similar record made by the trading system of an investment firm. This helps to reconcile the systems and assure that all systems are performing as expected and main-

taining accurate and consistent views of trades and positions. In FIA ETPA's Market Integrity Framework: Best Practices to Preserve Market Integrity [13] document, we have already include a requirement regarding reconciliation of trades. Moreover, the drop copy data may also be used by risk managers to view their firm's risk exposure independently of the trading system.

Therefore, the FIA Associations believe drop copies should be available for all trading venues and products whenever technologically practicable. We would strongly favour standardised formats for drop copies, as well as for other forms of reporting, including order messaging and feedback from the trading venues' systems. Trade reports and other information provided by drop copy should be disseminated to the consumer in real time or as near real time as technologically and operationally practicable. When used with kill switch functionality, any trades that may occur while the kill switch takes effect will be reported, and the participant will be confident in its ability to reconcile its positions.

However, we do not believe that making the use of drop copies mandatory for investment firms is an appropriate approach. We would like to emphasise drop copies are currently not always widely available, affordable, consistent in format, of sufficient quality, or delivered timely. The content and method of delivery for drop copy feeds vary. The FIA Associations have released Drop Copy Recommendations[14] for standardisation of drop copies across trading venues. We believe ESMA should either require trading venues to make drop copies available in line with FIA's recommendations or encourage – but not require – investment firms to use these when available.

Finally, drop copy services should not be seen as a profit-generating product for its providers, as good risk management benefits all market participants. Therefore, producers should promote the use of drop copies by providing it to consumers at no charge or for a nominal fee that covers the provider's costs.

<ESMA_QUESTION_206>

Q207: Do you agree with the proposed approach?

<ESMA_QUESTION_207>
The FIA Associations believe ESMA's approach to the security of trading systems and algorithms is too prescriptive, thereby hampering its effectiveness.

ESMA should preserve the flexibility of investment firms to apply those measures that are proportionate and adequate to their businesses, whether or not supplemented by ex-post assessment and discussion by a firm's NCA.

We prefer the principle-based approach promoted in FIA PTG's Recommendations for Risk Controls[15], where it states firms should consider the security of their trading and business networks and be aware of the risk of access to their network infrastructure by unauthorised personnel. We strongly encourage the use of:

- network firewalls
- VPN connections or other security devices to prevent against unauthorised remote access

[13] FIA EPTA Market Integrity Framework: Best Practices to Preserve Market Integrity, July 2012, p.8, available at: http://www.futuresindustry.org/epta/downloads/EPTA-Market-Integrity-Framework_072012.pdf .
[14] FIA, Drop Copy Recommendations, September 2013, available at: http://www.futuresindustry.org/downloads/FIA-Drop_Copy(FINAL).pdf .
[15] FIA PTG Recommendations for Risk Controls for Trading Firms, November 2010, available at: http://www.futuresindustry.org/downloads/Trading_Best_Pratices.pdf .

- authentication through IDs, passwords and/or token-based systems
- detailed logging systems to record user and system activity
- third-party electronic security audits performed at regular intervals
- policies and procedures relating to the removal of physical and electronic access privileges.

Many of the requirements laid out by ESMA with respect to the security of trading systems and algorithms are not appropriate for small-to-medium sized firms in their current shape. The FIA Associations have provided several examples below.

Internationally Established and Recognised IT Standards (Paragraph 45)

ESMA requires investment firms to have an IT environment "*that at least meets internationally established and recognised standards.*" While internationally established and recognised standards may provide reasonable guidance for some aspects of the day-to-day operations of investment firms, generally speaking, they were not developed with the unique technical and operational needs of firms operating algorithmic trading strategies in mind.

Similarly, standards are often quite rigid and may have developed years ago and now represent policies and procedures that have become outdated and obsolete due to the evolving nature of technology and best practices. As a result, we do not believe existing internationally recognised standards are properly suited to address the needs of investment firms in this context. We would rather refer to "internationally established and recognised best practices" such as, for instance, those published by the FIA Associations or other industry bodies.

Recognising the importance of such standards, the FIA Associations have recently initiated a project to further develop a set of standards for market participants. The resulting standards will reflect state of the art best practices, take into account the unique needs of the financial industry's diverse set of participants, and provide enough flexibility to address the evolving marketplace. Developed for the industry, by industry experts, this will provide an effective, cost-efficient solution for firms looking to adopt a recognised standard.

Minimise Risks of Cyber Attacks (Paragraph 47)

ESMA requires investment firms to implement IT security measures that minimise the risk of cyber-attacks in line with Article 2 of Directive 2013/40/EU. This requirement is not proportionate for proprietary trading firms and should be subject to a firm's discretion as to whether to implement. Such systems and networks typically run on dedicated and secured infrastructure and are not open to retail clients or the 'outside world,' meaning the risk of cyber-attack is more limited and thus manageable compared to other entities.

Two Factor Authentication (Paragraph 49)

While ESMA states investment firms should ensure IT access is to be protected by monitoring and authentication "*as appropriate,*" it goes on to state *"(including two factor authentication for critical access rights).*" Due to the formulation, it is unclear whether this is mandatory or only a suggestion, to be applied at the discretion of investment firms.

The FIA Associations believe two-factor authentication is not appropriate or practical in the context of automated trading systems. This is a concept applicable to screen logins for retail banking or brokerage accounts with human operation (and thus may be relevant in certain cases of DEA provision), but not for screenless servers connecting directly to exchanges. We are not aware of any investment firm who has

implemented this for automated trading systems, suggesting even the most sophisticated technology-based trading firms currently active have not found this an advisable mechanism to protect their systems. There is, however, an inherent two-factor authentication in automated trading, where traders log in to systems (whether via the dealing room's secure network or VPN) and the systems subsequently connect to exchanges, all in physically and electronically secure environments (i.e. on a controlled trading floor or in controlled server rooms).

Likewise, we are unclear what it means to "*implement appropriate controls to ensure that the deployed binary codes were actually compiled from the documented source code.*" Notwithstanding, we agree with the principle of source code management and consider this standard best practice, as reflected in FIA PTG/EPTA's Software Development and Change Management Recommendations[16]: "*Firms should maintain a source code repository to manage source code access, persistence and changes. The source code repository may be used to ascertain when software changes were made and the nature of the changes.*"

Penetration / Vulnerability Tests against Cyber Attacks (Paragraph 50)

Please see our comments with respect to Paragraph 47 above. We believe this requirement is reasonable in principle, but must be proportionate, and the manner of performing such tests should not be prescriptive.

Legal / Regulatory / Security Requirements Met by Vendor (Paragraph 51)

The FIA Associations consider the requirement to ensure that legal and regulatory requirements, as well as IT security and continuity requirements, are met by the vendors of hardware and software supporting trading activities to be unrealistic and impractical for many investment firms, particularly small-to-medium and principal trading firms.

First, small-to-medium investment firms do not have the contractual leverage to pass on regulatory obligations in private legal contracts to vendors of hardware and software. At the same time, suppliers of critical infrastructure, software and data services are nearly always in the position to decline acceptance of any terms they do not like as they are often monopolists in their markets and as such are unlikely to accept audit rights or third party reliance.

Second, if regulatory requirements would force all current contracts to be renegotiated, it will take a long period of time and put the requesting party (investment firms) in a disadvantageous negotiating position.

Appropriate Documentation from Procured Software / Hardware (Paragraph 52)

Please see our comments above with respect to Paragraph 51.

Code Escrow (Paragraph 53)

The FIA Associations believe the requirement to enter into a code escrow agreement with software vendors to be impractical and an onerous cost burden.

Code escrow agreements are very occasionally market practice for the larger institutions such as banks and clearing firms. However, such agreements only relate to bankruptcy / insolvency events for business continuity purposes and never to compliance requirements or audit rights.

[16] FIA PTG / EPTA Software Development and Change Management Recommendations, March 2012, available at: http://www.futuresindustry.org/downloads/Software_Change_Management.pdf .

Code escrow agreements cost approximately EUR 20.000, / GBP 15.000, - per product, so they are only entered into for the most business critical issues. Due to their very high costs, it is not a realistic requirement to have code escrow agreements for code generally, even if restricted to business continuity purposes, and even less for small-to-medium investment firms.

Notification of NCAs (Paragraph 55)

The FIA Associations agree in principle with the requirement to inform the home competent authority of breaches in the physical and electronic security measures undertaken, we believe the word "relevant" may lead to confusion and differences in interpretation as to which breaches required notification. We believe this requirement should be subject to an investment firm's judgment as to whether breaches in the physical and electronic security measures are material or minor. Furthermore, we believe that investment firms should in the position, provided it is prompt, to investigate matters themselves first, in order to assess materiality and to facilitate investigation of an incident if warranted.

<ESMA_QUESTION_207>

Q208: Is the proposed list of pre trade controls adequate? Are there any you would add to or remove from the list?

<ESMA_QUESTION_208>
The FIA Associations believe the list of controls proposed by ESMA, if applied proportionally with consideration to the nature, scale and complexity of a firm's business, to be adequate. As discussed before, the FIA Associations have been on the forefront of developing industry best practice recommendations with respect to pre-trade and post-trade risk controls that reduce the risk of market disruptions due to unauthorised access, system failures, and errors. We endeavour continually to refine these best practice recommendations based on evolving technology and recent market experiences in order to contribute to safe and orderly markets.

We emphasise again that all market participants have a responsibility to implement risk controls appropriate to their role. We believe that for risk control requirements to be most effective, they should be principle-based (whether or not subject to ex-post assessment by NCAs) and consideration should be given to the location where they are implemented within the trading lifecycle. Any risk control that is overly prescriptive may fail to take into account the unique characteristics of the diverse market participants, trading strategies, and products that exist today – thus adding, rather than reducing, risk. Furthermore, prescriptive requirements may quickly become obsolete as markets, technology, and trading strategies evolve.

Without prescribing specific risk control implementations, a degree of standardisation across market participants, regardless of their trading strategies, may be achieved by hosting risk controls at the trading venues. ESMA states "*investment firms' controls will be partly duplicative of those of the trading venues*." This is acceptable as long as the controls that are duplicative are not prescribed or enforced 'by proxy' by the trading venues, on top of the investment firms' own obligations. For market stability, it is preferable that sufficiently robust risk controls exist at the trading venues, through which all market orders must pass prior to being accepted for execution. This ensures that a baseline of risk controls is applied within the marketplace regardless of the type of access used or the type of market participant. The specific implementation of these risk controls should not be prescribed by ESMA, since trading venues are the best equipped to understand the performance of their systems, the unique needs of their markets, products and participants, and the nuances associated with introducing new functionality to their systems. Moreover, trading venues can adapt risk controls to new technology and to changes in markets and trading behaviour over time.

An example of a trading venue-hosted pre-trade risk control is the CME-provided Globex Credit Control (GC2). In this implementation, the clearing member imposes an absolute dollar-based limit on a market participant, and all orders submitted contribute to the dollar value of the participant's intraday activity. Any order that would cause a market participant to exceed the limit set by its clearing member is rejected by the trading venue. This check is mandatory for all participants on Globex regardless of whether a customer accesses the market directly or via its clearing member's infrastructure.

Three additional widely adopted trading venue-hosted pre-trade risk controls are Price Collars, Quantity Limits and Cancel-On-Disconnect: (1) A Price Collar is a dynamic price range that defines the range of prices that will be accepted for execution on a specific product by the trading venue at a given time. (2) A Quantity Limit defines the maximum order quantity that will be accepted for execution on a specific product by the trading venue (3) Cancel-On-Disconnect allows direct access participants the additional safeguard of knowing that all working orders are cancelled at the trading venue in the event that the participant loses connection to the trading venue and cannot manage their orders.

The FIA Associations support the application of these provisions to investment firms with regard to all kinds of trading, whether on own account or on behalf of clients (including DEA clients). We believe that appropriate supervision of all market access is an important tool in limiting risk to the financial markets. We do not believe that ESMA should establish different guidelines depending on the type of market access. Because all market access—whether as principal or agent, or whether through direct access to the trading or indirect access via a clearing member's connection—creates risks, the same principles should apply to all types of market access.

Kill Buttons (Paragraph 62 (vii))

With respect to "kill buttons," the FIA Associations reiterate their comments in response to Question 205 above.

Maximum long/short overall strategy position (Paragraph 62 (v))

ESMA should not prescribe the level of aggregation for trade controls "per product and on a per client, group, trader or account basis". The FIA Associations believe it would be more efficient to have a maximum long/short overall position at appropriate levels of aggregation depending on the natural, scale and complexity of an investment firm's business.

Maximum messages limit (Paragraph 62 (ix))

A high number of messages is not necessarily a risk and should not be blocked or throttled unless system integrity is jeopardised: rapid price adjustments, also in market making, are essential to managing risk, to prevent mispricing and to providing ongoing liquidity at a tight spread, particularly under challenging market circumstances. It also facilitates quicker recovery and price discovery.

Market Maker Protections (Paragraph 63)

The FIA Associations do not believe ESMA's current formulation of the requirement of market maker protections ("*Market makers should therefore be able to validate quotes on underlying instruments before executing trades*") adequately describes this concept.

In FIA EPTA's Market Integrity framework: Best practices to preserve Market Integrity[17] document, we state that firms with specific market making obligations should be aware of and, when appropriate, utilise any market maker or sweep protections provided by a trading venue.

Market maker or sweep protections are parameters set by market makers and implemented by the trading venue to provide a degree of risk protection by limiting the market maker's quote execution exposure. This type of protection is provided to market makers because of their special role and the service they provide to the market in the form of liquidity.

When a market maker's defined protection values are met or exceeded within certain time intervals, the protections are triggered and any new messages from such market maker would be rejected and resting quotations cancelled. Such controls cannot function adequately within the systems of the market maker itself and must therefore be provided by the trading venue, who is in a better position than the investment firm to control the rejection of orders when a market makers quotes are swept, threatening orderly trading.

The FIA Associations therefore believe that trading venues should provide a level of protection for market makers.

Automatic Blocks on Orders from a Trader (Paragraph 64)

The FIA Associations believe this requirement is acceptable in principle, as long as there is room for investment firms to implement that requirement taking into account their internal mapping of IDs.

Concluding Remarks

To conclude, a general point with respect to risk controls: throughout the Microstructural section of the Discussion Paper, risk controls and review requirements are cumulatively stacked, from an investment firm's own responsibilities, to those of DEA providers, clearing firms, trading venues and NCAs. We believe ESMA should seek to reduce the incidents of overlapping requirements. Otherwise, we fear that investment firms will face a crushing compliance burden when regulators, DEA providers, clearing firms and trading venues all require the investment firms to demonstrate compliance in different formats and at different moments (in ESMA's current proposals, at least twice a year). This could be a massive claim on investment firms' resources (something that may actually drive small-to-medium and principal trading firms out of the market) without bringing tangible benefits. If possible, we believe investment firms should be able to demonstrate compliance once and use their NCA's confirmation of good standing as a 'central point of approval' for other parties with respect to overlapping requirements. This could eliminate supervision by proxy by nearly every individual EU trading venue, DEA provider and clearing firm.

<ESMA_QUESTION_208>

Q209: To what extent do you consider it appropriate to request having all the pre-trade controls in place? In which cases would it not be appropriate? Please elaborate.

<ESMA_QUESTION_209>

[17] FIA EPTA Market Integrity Framework: Best Practices to Preserve Market Integrity, July 2012, available at: http://www.futuresindustry.org/epta/downloads/EPTA-Market-Integrity-Framework_072012.pdf

Please see our comments in response to Question 208. Trading venues should deploy and enforce the same controls in a consistent manner within the EU in order to maintain a level playing field and simplify development and compliance.

<ESMA_QUESTION_209>

Q210: Do you agree with the record keeping approach outlined above?

<ESMA_QUESTION_210>
The FIA Associations believe ESMA's proposal for record keeping creates a new and very exhaustive "*minimum*" list of items to be tracked and stored by investment firms, adding to the vastly increasing burden of compliance obligations under MiFID II.

ESMA's proposal should facilitate compliance with Article 17(2) of MiFID II, which requires investment firms to "*store in an approved form accurate and time sequenced records of all its placed orders, including cancellations of orders, executed orders and quotations on trading venues.*" ESMA's mandate laid down in Article 17(7)(d) of MiFID II is to develop regulatory technical standards with respect to "*the content and format of the approved form … and the length of time for which such records must be kept.*" ESMA was tasked with providing guidance on the format of such reports so as to create the possibility for standardisation of this data. Standardisation of this data will assist regulators and competent authorities in being able to make sense of such records.

However, we believe ESMA's proposal goes too far. For example, ESMA requires investment firms to keep records of "*a description of the nature of each decision or execution algorithm.*" As discussed in our comments to Question 205 in the context of flagging of algorithms, firms operate numerous algorithms that each make decisions or contribute information in an exponential decision tree process contributing to the ultimate decision to take action in a market. Hundreds of thousands to millions of inputs can be part of "*each decision.*" We urge ESMA to make explicit that storage of order data containing the algorithm flagging IDs addressed in Questions 205 and 555 respectively of the Discussion Paper will satisfy this requirement.

The FIA Associations believe it should be sufficient that investment firms keep records for a minimum of five years of:

- Each order transmitted (order data containing the algorithm flagging IDs),
- Procedures for software development, testing, and change management,
- Descriptions of the risk controls and procedures applicable to trading systems,
- Elaborate descriptions of the workings and inputs used for algorithms in general (rather than what has been processed / 'decided' per order), including the related controls, and
- Business continuity plans.

The FIA Associations fully subscribe to this position and have set the same standard in their Market Integrity Framework: Best Practices to Preserve Market Integrity,[18] which states that "firms should retain for retrieval all orders transmitted, including orders that are executed, modified or cancelled, for a minimum of 5 years."

<ESMA_QUESTION_210>

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[18] FIA EPTA Market Integrity Framework: Best Practices to Preserve Market Integrity, July 2012, available at: http://www.futuresindustry.org/epta/downloads/EPTA-Market-Integrity-Framework_072012.pdf

Q211: In particular, what are your views regarding the storage of the parameters used to calibrate the trading algorithms and the market data messages on which the algorithm's decision is based?

<ESMA_QUESTION_211>
The FIA Associations disagree with both of these suggestions, as they would make compliance nearly impossible for market participants.

Cataloguing "*each modification to any parameter input into trading algorithms*" as suggested in paragraph 71(i) as well as the massive amounts of real time market data feeding an algorithm's decision making (paragraph 71(ii)) would require investment firms to have data processing capacity similar to that required for its actual business operations, solely for record keeping purposes. This approach could hardly qualify as an efficient allocation of resources and would generate no tangible benefits.

To demonstrate the magnitude of this suggestion, one medium-size principal trading firm assessed that raw market data would accumulate to 1.5-2.5 Terabytes[19] per day on an average trading day.

Such raw market data is typically processed before it serves as input for the trading algorithms. Storing such processed data would require another 1.5-7.5 Terabytes to be stored, leading to storing approximately 3-10 Terabytes a day, per data centre used.

As a reference, transferring one day's worth of data would take approximately 35 hours (only raw market data) to 233 hours (raw and processed data) per data centre via a wholesale high-bandwidth line (100 Megabit upload speed) under perfect circumstances (100% dedicated capacity, fault free transfer).

Data stored	Megabyte (x1024x1024)	Megabit (x8)	Seconds to transfer over 100 Megabit/second line	Hours to transfer
1.5 Terabyte	1,572,864	12,582,912	125,829	35
3.0 Terabyte	3,145,728	25,165,824	251,658	70
10 Terabyte	10,485,760	83,886,080	838,861	233

In addition, storing and sending data in a data centre (and making such data available for retrieval) requires further processing for storage in large scale databases, adding to the required transfer and processing time and storage capacity.

Storing market data for 5 years, for all end users, would therefore be of such disproportionate magnitude and expense that no firm operating anything but the most simply, binary automated trading systems will be able to comply.

In addition, investment firms will encounter legal issues in storing and sharing data received from third party vendors, as contractual restrictions typically prohibit or limit storage and disclosure of data to third parties.

These suggestions are not practically feasible and hugely costly. We also believe that storing such data is not necessary given a NCA's ability to centrally and retroactively retrieve the same market data from exchanges or third party vendors. Combining such on-demand data with the records of orders that investment firms are required to store and make available will provide the relevant NCA with all relevant information required for any investigation of any incident.

[19] As indication, 1 Terabyte = 1048576 Megabyte = 8388608 Megabit.

<ESMA_QUESTION_211>

Q212: Do you consider that the requirements regarding the scope, capabilities, and flexibility of the monitoring system are appropriate?

<ESMA_QUESTION_212>
The FIA Associations believe the complexity of an investment firm's monitoring system should be proportional to the type of trading strategies pursued, also taking into account its nature, scale and complexity.

ESMA's proposal is very prescriptive and in places internally contradictory. For example, in Paragraph 78, it states "*the monitoring activity should include, *where appropriate,* the use of automated alerts.*" But in Paragraph 82, it states "*Firms *must* implement automated alert systems.*" [Emphasis added.] We believe ESMA's proposal as currently drafted will force many investment firms to invest in third party software that is very expensive and time consuming to customise and implement. Moreover, again it seems to leave little to no room for the application of the proportionality principle as advocated by ESMA.

Therefore, the FIA Associations recommend a more principle-based approach to post-trade review to detect market manipulation as set out in FIA EPTA's Market Integrity Framework: Best Practices to Preserve Market Integrity[20]:

> *Unless algorithms are specifically designed to prevent market abuse, firms *may* want to implement automated alert systems to flag behaviour likely to trigger suspicion of market manipulation. Such alert systems *should* be in place for all orders transmitted, including orders that are executed, modified or cancelled. Market data is not necessarily required to flag suspicious trading activity. For this reason, firms *should* store all orders transmitted, but *may* decide not to retain market data. Further, investment firms *should* have procedures in place to ensure that orders and transactions that are investigated and that could constitute market manipulation are reported to the competent authorities as soon as possible. [Emphasis added]*

We believe the recommendation above is most appropriate to a proportional, principle-based approach. If ESMA nevertheless prefers its current wording, it should clarify the requirements are not a "minimum" list but are fully subject to the proportionality principle. NCAs may always review an investment firm's approach to assess adequacy.

<ESMA_QUESTION_212>

Q213: Trade reconciliation – should a more prescriptive deadline be set for reconciling trade and account information?

<ESMA_QUESTION_213>
The FIA Associations do not believe a more prescriptive deadline should be set for reconciling trade and account information. Please refer to our comments on reconciliation in response to Question 206 above. It is important to note that investment firms do not always have control over data timeliness or quality, and the cost attached to receiving reconciliation reports is also an issue.

<ESMA_QUESTION_213>

[20] FIA EPTA Market Integrity Framework: Best Practices to Preserve Market Integrity, July 2012, p.8, available at: http://www.futuresindustry.org/epta/downloads/EPTA-Market-Integrity-Framework_072012.pdf .

Q214: Periodic reviews – would a minimum requirement of undertaking reviews on a half-yearly basis seem reasonable for investment firms engaged in algorithmic trading activity, and if not, what would be an appropriate minimum interval for undertaking such reviews? Should a more prescriptive rule be set as to when more frequent reviews need be taken?

<ESMA_QUESTION_214>
The FIA Associations believe that reviews should be done annually or more frequently if circumstances give rise. In conducting a holistic business review, our view is that organisations will not likely change significantly every six months. More frequent reviews should be undertaken only in the event of a material change in the nature, scale, and complexity of the investment firm. We have further defined 'material change' in our response to Question 197 as follows:

- Nature: a material change in the ownership structure, the regulatory status, or undertaking of trading a substantially new asset class;
- Scale: a greater than 50 percent increase in numbers of employees, capital or number of markets accessed;
- Complexity: a material change in the type of algorithmic approach undertaken, the application of a particular algorithmic approach to a new asset class; the adoption of a totally new asset class.

Please refer to our comments in response to Question 197 above for a more detailed argumentation.

<ESMA_QUESTION_214>

Q215: Are there any elements that have not been considered and / or need to be further clarified here?

<ESMA_QUESTION_215>
The FIA Associations strongly emphasise that due diligence by an investment firm is an important factor in the provision of direct electronic access (DEA) to its clients. Moreover, it is in the interest of all parties active on financial markets to ensure that both the client and the DEA provider have suitable controls in place to avoid any form of disruption to fair and orderly trading.

Before providing DEA through Direct Market Access (DMA) or Sponsored Access (SA), the DEA provider should understand the structure and governance of the client, as well as its investment objectives. This will allow the DEA provider to set appropriately calibrated pre-trade controls – as outlined in the ESMA Guidelines on systems and controls in automated trading report[21] (Guideline 8.2(b)) - to minimise the possibility of any trading issues affecting the market. Such controls should also be applied appropriately to the individual users or systems that enter orders at the client.

If the DEA provider is also the clearing broker for the client, it can also use post-trade controls regarding the credit utilisation of the client across their various trading activities. We discuss credit controls further in our response to Question 219.

The DEA provider should actively monitor all controls to ensure that any breaches are proactively addressed with the client. Similarly, any incidents that may occur due to system outages should be proactively managed with the client to ensure that any risk on behalf of the client or DEA provider is mitigated.

[21] ESMA guidelines on systems and controls in automated trading environment, February 2012, available at: http://www.esma.europa.eu/system/files/esma_2012_122_en.pdf .

The FIA Associations strongly recommend that due diligence regarding algorithms used by the client - whether developed in-house or purchased from a third-party – should be managed on a principles basis.

Due to the proprietary nature and commercial sensitivity of trading algorithms (the intellectual property of the algorithm remains with the firm that developed it), it is inappropriate to ask the DEA provider to analyse or review the source code or development processes behind the algorithm. More specifically: it is important to recognise that there is a potential conflict of interest between DEA users and DEA providers who often develop their own algorithms, including those to provide Direct Strategy Access (broker provided/hosted/supported algorithms that clients access via FIX or a GUI, "DSA"). Furthermore, DEA providers may be direct competitors of their clients in trading securities. It would therefore be conflicting to ask the DEA users to share their algorithms with a competitor, being potentially the DEA provider.

It is also natural for the algorithms to change on a frequent basis due to improvements or upgrades, some of which may be immaterial to the function of the algorithm. Rather than require DEA providers to analyse DEA user algorithms prior to their deployment, the focus should be on requiring sufficient risk controls at the DEA user level paired with the obligation for DEA providers to have adequate controls and assessments themselves.

The FIA Associations recommend that there should be an assurance provided by the client that all appropriate quality controls have been employed in the development, testing and deployment of the algorithm that the client is using, and that the client has all appropriate controls around who is using the algorithm, their experience in using electronic trading tools, how the algorithm has been deployed, and how it is monitored whilst in use (similar to the provisions set out in the prior topic for non-DEA users). Such an assurance should be provided by the client to the DEA provider as part of the agreement to provide DEA and reviewed on a regular basis to maintain access.

In our response to Question 216 we include an example of a questionnaire that the DEA provider can submit to the client that can provide the basis of the client's assurance that all appropriate controls are in place.

<ESMA_QUESTION_215>

Q216: What is your opinion of the elements that the DEA provider should take into account when performing the due diligence assessment? In your opinion, should any elements be added or removed? If so, which?

<ESMA_QUESTION_216>
The FIA Associations broadly support the periodic risk-based assessment of DEA client systems and controls as suggested by ESMA in Paragraph 96, with some exceptions highlighted below.

DEA providers currently conduct thorough due diligence on prospective DEA users in accordance with the type of client, the scope and size of their activities and the services being provided. These due diligence efforts include a thorough review of governance structure, training programs, security policies, operational set up, procedures for responding to errors, competency of staff, regulatory status and licenses, algorithm testing policies, and the creditworthiness of the client. This is in addition to meeting Know-Your-Customer (KYC) and Anti-Money Laundering (AML) requirements where applicable.

We would like to emphasise, however, that whilst the DEA provider must understand the nature of the client activity, given the number of clients and different styles of trading that are now employed to access EU and global markets, it is impractical to expect the DEA provider to provide training to client staff. Moreover, the DEA provider is not, and should not be, positioned to assess the commercially sensitive and

proprietary intellectual property of the client (or third-party provider) regarding algorithms that the client will use to trade on a trading platform.

With regard to the elements in Paragraph 92, we would like to clarify the following.

Analysis of all algorithms the investment firm has received from the DEA user in order to deploy them for the execution of orders (Paragraph 92(iii))

As we have stated in our response to Question 215, the FIA Associations believe the analysis of the algorithms of its clients should be limited to a review of their conformance testing and change management policies and procedures and assurance that all necessary controls are in place and work properly. This is in addition to the controls that the DEA provider has in place between the client and the trading venue.

Training and competency of individuals entering orders (Paragraph 92(iv))

As we have stated in our response to Question 215, the FIA Associations would like to clarify that the DEA provider does not provide training to its clients, instead it conducts a review of the practices and procedures of its client, including the level of experience of its employees and their competency regarding the use of electronic trading tools such as algorithmic execution.

In order to address issues raised in Paragraph 92, we suggest the use of a questionnaire that addresses due diligence requirements on behalf of the DEA provider regarding prospective DEA client controls. The following is an example of such a questionnaire, although individual DEA providers should use a format suitable to their specific requirements:

Sample DEA Provider Questionnaire

Below are sample questions DEA providers typically include in their due diligence process. The sample questions are provided for illustration purposes only and may not be appropriate for all investment firms. The FIA Associations believe that prescribing elements that the DEA provider must consider during a due diligence assessment is inappropriate and unnecessary. Rather, we suggest that the industry take the lead in agreeing best practices consistent with the FIA Market Access Risk Management Recommendations.[22] This gives the industry the flexibility it needs to change due diligence processes as the industry evolves. Prescriptive rules may not be applicable or appropriate in future market conditions.

1. Proficiency and Competency
1.1 Have you put in place any control to ensure that, within your legal entity, the System is used only by the individual who is allowed to access the System?

[22] FIA, Market Access Risk Management Recommendations, April, 2010, available at: http://www.futuresindustry.org/downloads/Market_Access-6.pdf. .

1.2 What requirements/criteria need to be satisfied by individuals in order for them to be approved as User(s) of the System? • What is their DMA Trading Experience - with other brokers on the same products? • What is their DMA Trading Experience - with other brokers on different products? • Will there be supervision by individuals who are experienced in using the System? • Education? please elaborate: • Qualification(s)? please elaborate: • Training(s)? please elaborate: • Internal Assessment(s)? please elaborate:
1.3 How do you ensure that the Users continue to be proficient and competent in their use of the System on an on-going basis? • Supervision by individuals who are experienced in using the System? • Training(s)? please elaborate: • Internal Assessment(s)? please elaborate: • Other? Please elaborate
2. Compliance with Applicable Regulatory Requirements
2.1 How do you satisfy that you and the Users understand and have the ability to comply with all applicable regulatory requirements when using or accessing any System for DMA trading (answer all applicable prompts): • Advice by external counsel or professional advisers? • Guidance from local service provider? please provide details: • Qualification(s)? please elaborate: • Training(s)? please provide details:
2.2 Please provide your trading experience in each of the Markets. For each market include products traded, trading experience and indicate whether you have DMA experience in that particular market. Example: Market; product; years of experience; trading method (phone, DMA, algorithmic)
3. Arrangements to Monitor the Orders Entered Through the DMA Services

You are required to have in place adequate arrangements to monitor the orders entered through the DMA services. 3.1 Please elaborate on the arrangements you have in place to monitor the orders entered through the System in addition to the checks brokers may implement for you in the System (e.g. description of your risk control infrastructure): • Order validation (fat fingers) checks (e.g. notional / ADV / price limits) • Market impact checks • Risk Limit checks • Daily limits checks • Internal crossing These may include checks executed to evaluate the maximum positions client can take at any time within the day.
3.2 Are you going to carry out all trading manually, or use your own algorithms to generate orders for trading?
4. Algorithm Trading
4.1 Do you have experience in using any algorithmic trading system?
4.2 If yes, please state years of experience.
4.3 Do you develop your own algorithmic trading systems?
4.4 If yes, please provide an outline of your controls around software development, testing, deployment and monitoring.
4.5 Do you use algorithmic trading systems provided by a 3rd party vendor?
4.6 If yes, please provide an outline of the controls that the vendor maintains around software development, testing, deployment and monitoring, and how this fits within your own controls regarding the usage of algorithmic trading.
5. Sub-delegation of DMA Services
5.1 Do you intend to allow any person who is not within your legal entity (including your clients and affiliates) to have DMA access through the System?

<ESMA_QUESTION_216>

Q217: Do you agree that for assessing the adequacy of the systems and controls of a prospective DEA user, the DEA provider should use the systems and controls requirements applied by trading venues for members as a benchmark?

<ESMA_QUESTION_217>
The FIA Associations disagree with ESMA's contemplated approach that the DEA provider should use the systems and controls requirements applied by trading venues as a benchmark, since these controls vary greatly across venues.

Although we do not recommend benchmarking to individual venues, the FIA Associations also does not recommend a “one -size-fits-all” approach which does not cater to different types of financial instruments. We do, however, believe that the 2012 ESMA guidelines on systems and controls in automated trading environment[23] provide suitable flexibility.

We are concerned that the benchmarking exercise would detract investment firms from an efficient and appropriate risk management.

First, the central objective of an investment firm’s controls should be to ensure compliance with an orderly market, the rules of the market and overarching regulatory compliance objectives. So long as these objectives are met, we do not see how “benchmarking” to individual standards would enhance market protection in a meaningful way.

Second, firms can better manage risk and perform due diligence across multiple markets. A requirement for venue-specific calibration would add unnecessary complexity and increase the cost of providing access to the trading venue.

Therefore, the FIA Associations suggest instead that the ESMA Guidelines on systems and controls in an automated trading environment[24] should be used to apply appropriate controls, in reference with the FOA response[25] published in September 2012 and the FIA Market Access Risk Management Recommendations[26] published in April 2010. These documents outline a comprehensive series of controls that the DEA provider can implement on a consistent basis across multiple trading platforms.

Where clients use Sponsored Access (SA), the DEA provider uses the controls provided by the trading venue to provide risk management. It is important to note that the majority of clients are routed through the DEA provider’s own order routing infrastructure, in which case the DEA provider generally uses a standard set of pre-trade risk controls on a cost-effective and efficient basis across multiple trading venues.

<ESMA_QUESTION_217>

Q218: Do you agree that a long term prior relationship (in other areas of service than DEA) between the investment firm and a client facilitates the due diligence process for providing DEA and, thus, additional precautions and diligence are needed when allowing a new client (to whom the investment firm has never provided any other services previously) to use DEA? If yes, to what extent does a long term relationship between the investment firm and a client facilitate the due diligence process of the DEA provider? Please elaborate.

<ESMA_QUESTION_218>
While new clients will go through an entire vetting process covering KYC, operational risk, credit worthiness, and ownership before they can start trading, the FIA Associations agree with ESMA’s analysis that an investment firm has a higher degree of confidence in a client with which it has a longstanding relationship.

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[23] ESMA guidelines on systems and controls in automated trading environment, February 2012, Guideline 8 b), p. 22, available at: http://www.esma.europa.eu/system/files/esma_2012_122_en.pdf .
[24] ESMA guidelines on systems and controls in automated trading environment, February 2012, p. 22, available at: http://www.esma.europa.eu/system/files/esma_2012_122_en.pdf .
[25] FOA, Guidance on Systems and Controls for Electronic Trading Environments, September 2012, available at: http://www.foa.co.uk/admin/tiny_mce/jscripts/tiny_mce/plugins/filemanager/files/Regulation/Position_Papers/FOA_Guidance_on_Systems_and_Controls_for_Electronic_Trading_Environments_-_Final_-_19092012.pdf .
[26] FIA, Market Access Risk Management Recommendations, April 2010, available at: http://www.futuresindustry.org/downloads/Market_Access-6.pdf.

However, we also feel that this should not detract it from performing the necessary due diligence with respect to ensuring that the client has suitable controls in place regarding how it uses DEA. While the length of the relationship may, in some cases, enable the client to maintain or increase its intraday limit/positions, these clients are given the same level of due diligence and risk controls as any other client, as highlighted in Paragraph 96. Moreover, we would like to emphasise that the length of service provides no guarantee against operational, human or technical error leading to losses.

To conclude, the FIA Associations believe all DEA clients should provide assurance as discussed in our responses to Question 215 and Question 216 – either during on-boarding or during renewal – that appropriate controls are in place, regardless of how long the DEA provider has known the client.

<ESMA_QUESTION_218>

Q219: Do you agree with the above approach? Please elaborate.

<ESMA_QUESTION_219>
Paragraphs 98-108, which have broad industry support, are substantially in line with the ESMA guidelines on systems and controls in automated trading environment[27], as we have discussed in our response to Question 217. However, we would like to emphasise the difference between pre-trade risk controls and credit controls. Although both are critically important to the integrity of the marketplace, they have distinct functions. To this point, it is important to note how markets have evolved over the last decade to provide clients and proprietary traders with the following choices:

- The choice in ***where*** to execute a trade depending on financial instrument availability.
- The choice in ***how*** to execute a trade - for example on the floor (where still available), over the phone with a broker's desk, electronically through a single dealer platform, electronically via a third party vendor system, or directly to the exchange.
- The choice through ***who*** to execute and/or clear a trade through depending on the competitive services that a broker provides as well as the need to minimise counterparty risk.
- The choice in ***when*** to allocate trades (if applicable) to a beneficial owner, either at-trade or post-trade depending on the complexity of the execution.

Risk controls are used to manage trading activity; for example, pre-trade risk controls are used to manage what is acceptable in terms of order size, number of orders, and other controls discussed within this response.

Credit controls, by contrast, are a key feature of how an investment firm that acts as a clearer manages its exposure to its customers through the different types of market activity in which they participate. Due to the choices that clients have regarding how and with whom to execute, client activity is constantly monitored at near-trade and post-trade levels to avoid the possibility of a client being unable to meet its margin requirements. Such monitoring is both quantitative and qualitative. We believe that it is not possible to completely automate pre-trade credit limits without a major change to existing market structure.

The FIA Associations believe it is localised pre-trade risk controls -- not credit-controls -- that should be used to prevent market disruption due to a malfunctioning algorithmic trading system. Such localised controls can use various approaches and act on a very granular level to detect unusual activity and to prevent excessive trading, and can be implemented within existing ESMA guidelines on systems and

[27] ESMA guidelines on systems and controls in automated trading environment, February 2012, Guideline 8 b), p. 22, available at: http://www.esma.europa.eu/system/files/esma_2012_122_en.pdf .

controls. The FIA Associations also recommend that ESMA work with trading venues to provide pre-trade controls that are consistent with the ESMA guidelines and industry papers such as the FIA Market Access Risk Management Recommendations[28] to better support Sponsored Access (SA) where it is appropriate, including the standardised use of FIX drop copies as way of providing as much real-time information to the DEA provider (and clearing firm, if different) as possible.

Paragraph 104 goes further to state that pre-trade limits should work hand in hand with post-trade. As we have mentioned, there is often a delay in when trades are received by the clearing firm due to the give-up process, with the situation frequently occurring where trades can be given in late in the day, putting an entirely different perspective on risk. For smaller clients this is generally handled by not permitting give-ins, and actively monitoring risk on an intraday basis. But for larger clients a T+1 model often applies. In the event that credit controls for a client dictate that trading should be disabled, this can be achieved by removing trading privileges through pre-trade controls – though this must be handled in a manner that ensures that the risk of the client is adequately managed, especially since many clients have multiple DEA providers and clearing relationships.

We strongly suggest that ESMA avoid prescribing how a DEA provider should handle overall client credit controls, as well as trying to enforce an automatic link between pre-trade risk controls and credit controls that have to occur outside of real-time. In Paragraph 99 we would support the intra-day monitoring of the size of order flow from a client. However, the introduction of pre-trade client and intra-day credit controls maintained by the clearing broker across all methods of direct electronic access – for example through a centralised credit hub - would require a major restructuring of how clients access the markets.

Paragraph 105(iii) suggests that DEA providers should ensure that their clients have adequate training on order entry procedures. While we support all efforts to minimise any disruption to fair and orderly trading on a trading venue, providing training to clients with different trading systems and trading objectives is neither practical nor cost efficient. Instead, the FIA Associations suggest that the client should provide assurance that their traders are conversant in all rules and regulations of the trading platforms that they are accessing electronically. The DEA provider should assist the client in understanding the requirements of each trading platform, and regularly review that the assurance made by the client is current and covers all employees that are permissioned to place orders through DEA. The DEA provider also minimises the chance of accidental disruption through the imposition of pre-trade controls between the client and the trading platform.

As previously noted, clients increasingly use algorithms to place orders. Such algorithms can be developed by the client, a third-party vendor or supplied to the client by the DEA provider. As we have already stated in our responses to Question 215 and Question 216, since these algorithms are the intellectual property of the developer, they cannot be readily analysed by another party such as the investment firm without compromising that intellectual property, nor is it practical or cost efficient for the investment firm to allocate resources to analyse code even if it were supplied by the client or vendor. Instead, the FIA Associations recommend that as part of the due diligence process the client provides assurance that all appropriate quality controls have been employed in the development, testing and deployment of any trading algorithm, and that the trading algorithm is compliant with any specific requirements of the trading platform. Please see our response for Question 216 regarding a sample questionnaire that the DEA provider can provide to the client to form the basis for this assurance.

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[28] FIA, Market Access Risk Management Recommendations, April 2010, available at: http://www.futuresindustry.org/downloads/Market_Access-6.pdf .

<ESMA_QUESTION_219>

Q220: Do you agree with the above approach, specifically with regard to the granular identification of DEA user order flow as separate from the firm's other order flow? Please elaborate.

<ESMA_QUESTION_220>
The FIA Associations support the appropriate level of granularity required to identify individual traders placing orders using DEA. However, it is important to note that for data security reasons the individual identification should be that of an anonymised ID allocated by the DEA provider. To facilitate this requirement, trading venues should support a new additional field for individual identity tags, separate to the existing Exchange/Trader ID fields (which are generally used to identify the person that owns/supervises the ID, i.e. the 'responsible person' as opposed to that of the person entering the order). If there is a group/desk of users, then there should always be a primary person that is responsible for that desk/group. A flag identifying an algorithm can also be tied to the person responsible for the overall supervision of that algorithm.

Such granularity allows for the appropriate pre-trade controls to be placed at the DEA provider, and allows for identification of the responsible person either placing the trade or behind the system that places the trade. This ensures that individual traders at the client are clearly identified separately from traders at the investment firm providing DEA.

As discussed in our response to Question 215, we are cognisant that algorithms are the intellectual property of the client or their software provider, and it should not be the responsibility of the DEA provider to understand the deployment of algorithms by their clients for different trading strategies given the potential conflict of interest. We do, however, understand the responsibility of the DEA provider to ensure that such algorithms do not cause disruption to fair and orderly trading. To that end, we stress that clients should provide an assurance regarding the use of algorithms that must be regularly updated for continued DEA. We also emphasize that individual traders and trading systems that use algorithms should be clearly identified so that any questions regarding activity can be immediately addressed to the appropriate person responsible for the activity.

The identification of the individual trader or trading system that uses an algorithm to trade on a trading platform is consistent with the principle that the client has the responsibility to identify who has control of an algorithm. We feel that the NCA should place the onus on the trading platform to regulate how information is sent to the venue, how that information is recorded at the venue, and to ensure that the DEA provider is compliant with the principle.

A robust kill switch—or trading termination—methodology as suggested in Paragraph 115 that can be applied at the clearing firm level should have the ability to be invoked at the most granular resolution possible and should include manual and automated methods for triggering the kill switch. As set out in our response to Question 205, however, the invocation of a kill switch is a final measure only to be taken when other risk control processes have not been successful. As such, policies and procedures should be in place for contacting the market participant to discuss a means of intervention prior to a manual kill switch being invoked - for example at risk limit thresholds set at 25%, 50%, 75%, etc. of the absolute limit - and should also limit the scenario where the kill switch is invoked unilaterally. The procedures should also be written to clearly authorise the clearing firm staff to terminate market access for a customer when action is required immediately to protect market integrity or the financial integrity of the parties involved, even in the event that contact cannot be made with the customer or a supervisor at the clearing firm. Please also refer to our response to Question 205.

<ESMA_QUESTION_220>

Q221: Are there any criteria other than those listed above against which clearing firms should be assessing their potential clients?

<ESMA_QUESTION_221>
The FIA Associations view the criteria in light of the concern expressed in the analysis portion of this section: "*A careful balance therefore must be struck between managing the risks assumed from the clearing firm's clients and not dis-incentivising the clearing firms from providing the clearing service to prospective clients.*" We appreciate ESMA's acknowledgement of the unintended consequences of over-regulation in this area.

Clearing firms already assess their clients on the basis of several criteria (especially as many clearing firms are banks, or part of or subsidiaries of larger banks and thus supervised and regulated as such). They already have client acceptance policies, procedures, and governance structures in place covering the criteria mentioned in 123 and the review process in 124/126.

The FIA Associations, however, disagree with ESMA's approach regarding some of the criteria listed in this section.

Analysis of trading patterns/strategy (Paragraph 123(iii))

The FIA Associations believe this requirement is unnecessarily onerous. A clearing firm in general analyses a prospective client's existing positions and forms a high level opinion about trading strategies. However, they will not, and should not, be in a position to analyse a client's trading pattern or strategy at a more detailed level.

Non-discriminatory, transparent and objective criteria (Paragraph 125)

The FIA Associations welcome ESMA's approach of requiring clearing firms to use non-discriminatory, transparent and objective criteria.

However, we feel that Paragraph 125 applies these principles to a field where exhaustive prescriptive rules would do more harm than good and create a moral hazard. It is critical that clearing firms--as risk takers--retain a high level of discretion as to which client they accept in order to be able to ensure sound risk management within the clearing firm. The acceptance procedures within a clearing firm are based on decisions regarding multiple factors such as client type, assets under management, activities, jurisdiction, legal structure, regulatory status, geographic location, global activity, credit standing, and portfolio—amongst others--that vary significantly across potential clients. There will be always be potential clients ticking all boxes of objective criteria that a clearing firm will not accept based on its own principles regarding sound risk management. Such a decision will always involve a qualitative analysis that can go beyond any attempt at standardisation, and will require a degree of confidentiality regarding that decision. Removing the ability to exercise discretion for the sake of utmost transparency could impact the way that a clearing firm manages its exposure across its client base, and may add to the risk of clearing firm failure if they are forced to accept clients.

The FIA Associations believe that criteria laid down in Paragraphs 129, 132 and 133 are superfluous as these repeat and duplicate EMIR requirements. We are assuming that 'conditions' alluded to in Paragraph 132 refer to conditions to benefit from discounts and rebates as described in EMIR article 38(1).

<ESMA_QUESTION_221>

Q222: Should clearing firms disclose their criteria (some or all of them) in order to help potential clients to assess their ability to become clients of clearing firms (either publicly or on request from prospective clients)?

<ESMA_QUESTION_222>
The FIA Associations believe that clearing firms should not be forced to publicly disclose some or all of their criteria for the following reasons.

First, the FIA Associations believe it is important that clearing firms retain the level of discretion necessary to decide with whom they do business while ensuring sound risk management, as indicated in our answer to Question 221. Any client acceptance procedure/process within a clearing firm would become meaningless if a clearing firm could be forced to accept a potential client. The reality is that clearing services offered depend on type, size, activities, jurisdiction, legal structure, regulatory status, geographic location, credit standing, portfolio and needs of a (potential) client. Therefore they may vary significantly, especially for globally active clients, and are in most cases tailored to the specific needs of the client. It would be very difficult to articulate all the interconnections between these criteria making up the decision process.

Second, the commercial reality is that prospective clients normally assess several clearing firms before selecting a specific firm. The chances that a client is unfairly treated due to a lack of clear criteria are minimal due to the competitive nature of the market.

Finally, clearing firms already have to comply with disclosure requirements under EMIR. Article 37(3) of EMIR states that "*Clearing members shall, upon request, inform the CCP about the criteria and arrangements they adopt to allow their clients to access the services of the CCP.*" The FIA Associations believe this level of disclosure per CCP and to a CCP should suffice.

<ESMA_QUESTION_222>

Q223: How often should clearing firms review their clients' ongoing performance against these criteria?

<ESMA_QUESTION_223>
A clearing firm has its own client acceptance and review procedures tailored to the services it offers and the clients it serves. As stated in our answer to Question 221, client types vary significantly and thus the FIA Associations believe it should be at the discretion of the clearing firm based on its client acceptance and review processes. Continuous monitoring should highlight any issues of concern and prompt earlier review.

<ESMA_QUESTION_223>

Q224: Should clearing firms have any arrangement(s) other than position limits and margins to limit their risk exposure to clients (counterparty, liquidity, operational and any other risks)? For example, should clearing firms stress-test clients' positions that could pose material risk to the clearing firms, test their own ability to meet initial margin and variation margin requirements, test their own ability to liquidate their clients' positions in an orderly manner and estimate the cost of the liquidation, test their own credit lines?

<ESMA_QUESTION_224>
Clearing firms currently already perform overnight stress tests on client portfolios and monitor the overnight / intraday risk exposure to client activities. That risk exposure is an estimate of the cost of liquidation of clients' positions. Clearing firms already have client default procedures are in place. For clearing firms that are banks, stress testing of liquidity and credit lines are in place already. CCPs also separately stress test all positions of their clearing members and as well as test default procedures.

Therefore the FIA Associations believe sufficient safeguards are already in place. Additional onerous testing programs will be extremely costly without generating additional tangible benefits.

<ESMA_QUESTION_224>

Q225: How regularly should clearing firms monitor their clients' compliance with such limits and margin requirements (e.g. intra-day, overnight) and any other tests, as applicable?

<ESMA_QUESTION_225>
Clearing firms already have detailed risk policies and procedures in place for monitoring client positions that are tailored to the client and market as well as applicable regulations. Overly prescriptive regulations in this area could be counterproductive in a rapidly changing environment. It depends on the kind of limit whether real-time monitoring is necessary or not (please see also the discussion on pre-trade and credit limits in the reply to Questions 219 and 226).

<ESMA_QUESTION_225>

Q226: Should clearing firms have a real-time view on their clients' positions?

<ESMA_QUESTION_226>
Clearing firms currently already have post-trade intra-day risk systems that monitor client positions in real-time where required depending on client type, activity, and markets cleared, or once a day depending on the choices that a client has made with regard to where, how, through whom to execute, and when to allocate a trade (see Question 219).

The intra-day monitoring systems mentioned take into account start-of-day positions as well as intra-day activity, calculating position value and risk exposure figures as well as other relevant risk parameters. Again, which parameters are actually relevant depend on client types, activities, products and markets cleared and the choices that a client has made.

<ESMA_QUESTION_226>

Q227: How should clearing firms manage their risks in relation to orders from managers on behalf of multiple clients for execution as a block and post-trade allocation to individual accounts for clearing?

<ESMA_QUESTION_227>
When executing brokers and clients execute block trades, the risk remains on their books until the allocations are completed. As allocations are made, the risk transfers to the clients' clearing firm. Risk management should reflect the risks/responsibilities that the clearing firm actually has at a particular point in the lifecycle of an order/trade. Agreements between the executing and clearing brokers spell out the responsibilities of both parties.

<ESMA_QUESTION_227>

Q228: Which type(s) of automated systems would enable clearing members to monitor their risks (including clients' compliance with limits)? Which criteria should apply to any such automated systems (e.g. should they enable clearing firms to screen clients' orders for compliance with the relevant limits etc.)?

<ESMA_QUESTION_228>
All market participants involved with trading and clearing have a responsibility to implement risk controls appropriate to their role. Effective risk controls that are implemented and enforced by an entity within the

marketplace are a critical component of ensuring the financial integrity of a clearing firm as well as the integrity of the entire marketplace, including the CCP.

The FIA Associations believe that to maximise the effectiveness of a suite of risk controls, its requirements should be principle-based and consideration should be given to the location where they are implemented within the trading lifecycle. Any risk control that is overly prescriptive may fail to take into account the unique characteristics of the diverse market participants, trading venues, trading strategies, and products that exist today thus adding rather than reducing risk. Further, prescriptive requirements may quickly become obsolete as markets, technology, and trading strategies evolve.

Where the clearing firm is also the DEA provider, pre-trade and post-trade risk controls can be combined to provide a holistic view of the client's activity and can be monitored on a real-time basis. Where the clearing firm is not the DEA provider, the clearing firm relies on post-trade risk controls that should be updated as soon as trades are received by the clearing firm. It is important that trades are allocated to the clearing firm as soon as possible so that the clearing firm has an accurate view of the risk of the client as it is transferred from one firm to another. The responsibilities around this risk transfer are the same as we have discussed in our response to Question 227.

<ESMA_QUESTION_228>

4.3. Organisational requirements for trading venues (Article 48 MiFID II)

Q229: Do you agree with requiring trading venues to perform due diligence on all types of entities willing to become members/participants of a trading venue which permits algorithmic trading through its systems?

<ESMA_QUESTION_229>
The FIA Associations[29] believe that orderly markets provide stability and create efficiencies. For this reason, market participants and trading venues should be appropriately regulated. The requirements here

[29] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time-zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

should ensure that trading venues perform the appropriate due diligence on all entities applying to become members/participants, regardless of the type of activity in which the member is involved.

However, in performing that due diligence, venues should not seek or be required to duplicate the work done by national competent authorities (NCAs) where participants are regulated investment firms. For the latter, the approach should be adapted accordingly.

Furthermore, whilst there are a range of controls that trading venues can apply on a market-wide basis, trading venues' rules and contractual relationships apply directly only to members. Trading venues do not have direct contractual relationships with non-member participants, and are therefore only able to influence such participants indirectly via their relationships with members.

Realistically, trading venues are only able to perform due diligence on members (potential and existing). Due diligence of non-member organisations (including clients of members) must be undertaken by the relevant NCA and the relevant member that has the client relationship. As described above, trading venues do not have direct contractual relationships with non-member organisations.

Finally, the Level 1 text does not require the implementation of trader ID by venues. Given that flagging of algorithms was included in Level 1, it follows that trader and client IDs would also have been included if this was the intention of the Council, Parliament and the Commission. Accordingly, the FIA Associations do not believe ESMA should seek to impose additional obligations at Level 2. We believe trader IDs in practice are of limited value in maintaining orderly markets and create practical problems for investment firms that engage in automated trading or where traders share infrastructure. Instead, trading venues should work with member firms to maintain a list of those who are able to authorise trade cancellations and who can account for activity on the venue if questioned. This may not be the trader. See further the discussion of trader IDs and responsible persons in Question 257. Alternatively, trading venues can send a list of trader and client IDs to its members so that the member can verify and confirm.

<ESMA_QUESTION_229>

Q230: Do you agree with the list of minimum requirements that in all cases trading venues should assess prior to granting and while maintaining membership? Should the requirements for entities not authorised as credit institutions or not registered as investment firms be more stringent than for those who are qualified as such?

<ESMA_QUESTION_230>
The FIA Associations believe trading venues should perform the appropriate due diligence on all entities applying to become members/participants. It seems natural that the breadth of information required would likely be greater for a firm that is not regulated as an investment firm at the time of the application by the relevant NCA.

Although we agree that trading venues should perform due-diligence on investment firms to ensure the integrity of their systems, we feel the ESMA list of elements to be analysed should not include a review of a trading firm's staff selection policy. Assessments can be made of the experience of staff in certain key positions within the trading firm, but staff selection policy is and should only be the concern of the investment firm.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

We agree that the testing of trading systems and controls of an investment firm around such things as order entry, order cancellation, disaster recovery etc. should occur. However, we disagree that testing of an investment firm's specific algorithmic activity should take place. Algorithms and specific strategy around these are central to an investment firm's intellectual property and will be kept highly confidential by them as a result.

The criteria surrounding staff selection policy and training, business continuity, disaster recovery procedures and a firm's outsourcing policy are all areas covered during the authorisation and continuing supervision of regulated firms by their NCA, so it would seem onerous and unnecessary to mandate these tests with each and every trading venue on which a regulated firm may be a participant.
<ESMA_QUESTION_230>

Q231: If you agree that non-investment firms and non-credit institutions should be subject to more stringent requirements to become member or participants, which type of additional information should they provide to trading venues?

<ESMA_QUESTION_231>
There is a great value and correspondingly there should be a high bar for entry to the European markets and trading venues. All entities wishing to access these markets as a member/participant should meet similar entry requirements.

However, given that MiFID II is prescribing that firms accessing trading venues should be appropriately regulated, there is little value in requiring that the requirements for becoming a member are similar, but not duplicative, of that authorisation process. As stated in our answer to the previous Question 230, 5 (ii), (iii) and (viii) of the proposed list should not be applied to investment firms and credit institutions but may be applied to unregulated or third country regulated firms.

<ESMA_QUESTION_231>

Q232: Do you agree with the list of parameters to be monitored in real time by trading venues? Would you add/delete/redefine any of them? In particular, are there any trading models permitting algorithmic trading through their systems for which that list would be inadequate? Please elaborate.

<ESMA_QUESTION_232>
The FIA Associations believe most of the criteria are already included in many trading venues' system capacity and monitoring practices. Criteria that are not used for performance and capacity monitoring and provide no value in monitoring include:

11. (ii) – number of trades executed per second.

This is dependent on market activity. We believe system performance is adequately captured under (i), (iii) and (v).

11. (vi) matching engine progress.

Any problems in the matching engine would be highlighted by (v) and the imposition of additional monitoring within the matching engine itself would add unnecessary latency.

13. (i) a potential introduction of such a criterion does not help the trading venue in any way to monitor performance and capacity of their system.

It is unclear how a meaningful conclusion would be derived from calculating the median lifetime of orders modified or cancelled that would be useful to the trading venue or any other party. The

FIA Associations oppose Option 2 for the definition of HFT; therefore, we do not believe venues need to calculate median lifetime of orders.

<ESMA_QUESTION_232>

Q233: Regarding the periodic review of the systems, is there any element that has not been considered and/or needs to be further clarified in the ESMA Guidelines that should be included?

<ESMA_QUESTION_233>
The FIA Associations believe that trading venues are in a better position to respond to this question, but consider the guidelines here to be quite comprehensive. We believe trading venues consider comprehensive penetration testing at least bi-annually to be desirable.

<ESMA_QUESTION_233>

Q234: Do you agree with the above approach?

<ESMA_QUESTION_234>
The FIA Associations believe that trading venues are in a better position to respond to this question, but agree that trading venues ought to have appropriate tools to measure and monitor capacity on an ongoing basis.

<ESMA_QUESTION_234>

Q235: Do you think ESMA should determine minimum standards in terms of latency or is it preferable to consider as a benchmark of performance the principle "no order lost, no transaction lost"?

<ESMA_QUESTION_235>
The FIA Associations believe ESMA should not determine minimum standards of latency, but instead focus on the principle of "no order lost, no transaction lost," in line with our response to Question 193.

<ESMA_QUESTION_235>

Q236: Do you agree with requiring trading venues to be able to accommodate at least twice the historical peak of messages?

<ESMA_QUESTION_236>
The FIA Associations believe that trading systems and processing capacity should be sufficiently robust. While we have no reason to believe that twice peak capacity would be insufficient, trading venues are in a better position to respond to this question.

<ESMA_QUESTION_236>

Q237: Do you agree with the list of abilities that trading venues should have to ensure the resilience of the market?

<ESMA_QUESTION_237>
The FIA Associations fully agree that trading venues should have the abilities in place to ensure the resilience of the market. In general we agree with the list of abilities for trading venues as listed in Paragraphs 31 – 33. However, we want to emphasise trading venues should at all times use these far-reaching powers very sparsely and only in very exceptional circumstance when the integrity of the trading venue's *systems* is threatened.

For example, as indicated in our response to Question 205, kill switches do have merits. However, we urge ESMA not to encourage their use as a risk control. Moreover the establishment of kill switches has potential legal ramifications dependent upon who has ultimate control and who actually has a membership agreement in place with the trading venue.

Therefore, in keeping with the proportionality principle, the FIA Associations believe ESMA should allow participants to choose from a variety of mechanisms that may better preserve market stability, such as limits embedded in systems, controlled winding down of positions and dialogue between clearing firms and clients. As we set out in FIA's Market Access Risk Management Recommendations from 2010[30], we recommend investment firms develop their systems with a series of automatic curtailments based on pre-programmed parameters.

<ESMA_QUESTION_237>

Q238: Do you agree with the publication of the general framework by the trading venues? Where would it be necessary to have more/less granularity?

<ESMA_QUESTION_238>
The FIA Associations believe that the framework should be transparent (see our response to Question 241 for further comment). Throttling arrangements, for example, would likely be member-specific and driven by order flow profiles, and as such should not be published, as this may provide unfair information to the market on a particular member's trading profile.

<ESMA_QUESTION_238>

Q239: Which in your opinion is the degree of discretion that trading venues should have when deciding to cancel, vary or correct orders and transactions?

<ESMA_QUESTION_239>
The FIA Associations believe that the goal of any error trade policy is to promote a marketplace where all trades stand as executed. Promoting such a goal is the only effective way to ensure that no incentive exists for changing outcomes of orders sent into the market after the fact. It also helps to promote the effective use of risk controls before orders are sent to the trading venue. Having clear, deterministic error trade policies is a good first step towards realising that goal.

Clear error trade policies serve to protect all market participants including counterparties to error trades. If error trade policies are unclear or subject to subjective analysis, it is possible that in attempting to reduce the risk of the party responsible and liable for the error trade, the trading venue may introduce risk to the counterparty who may have acted in accordance with just and equitable principles of trade. Therefore, trading venues should have pre-determined, public and unambiguous error trade policies that are not subject to discretion.

We feel that it is the responsibility of the trading venue to implement an appropriate error trade policy for their markets, and encourage consistency in practices for the same types of financial instruments. This includes the time required to report an error, which should be appropriate to allow continued price discovery after the error trade decision and allow the counterparties to the error to mitigate their risk as quickly as possible. Trading venues should also have publicly announced pre-determined "no-bust" or "non-reviewable range" criteria as part of any error trade policy.

[30] FIA, Market Access Risk Management Recommendations, April 2010, available at: http://www.futuresindustry.org/downloads/Market_Access-6.pdf.

Trading venues should have some discretion to cancel, vary or correct orders and transactions in accordance with their published policy or framework but, as set out above, these powers should be used sparsely and only in exceptional circumstances. It is vital to both investment firms and trading venues that trading venues are able to make decisions and provide clear information to the market as soon as possible to promote trade certainty.

<ESMA_QUESTION_239>

Q240: Do you agree with the above principles for halting or constraining trading?

<ESMA_QUESTION_240>
While halting trading is one way to address volatility, investment firms may have other controls including pre-trade controls that prevent the submission of orders that could jeopardise market integrity. It is important to note in this context that volatility is not necessarily bad and in fact inherent to financial markets. That said, the general principles included under subparagraphs 34 (i) to (vii) appear sensible with the exception of 34 (iv), which we consider unnecessary. If venues have an obligation to maintain effective controls, then it follows that they will have to devote appropriate levels of resources to support them.

It would be beneficial, however, to clarify in point 34 (ii) that the trading venues should take into account the specific market model and not the member's trading model. It seems that the term trading is chosen unintentionally, since the relevant criterion that can only be taken into consideration is the trading venues' market model. The trading venue cannot know the member's trading model.

<ESMA_QUESTION_240>

Q241: Do you agree that trading venues should make the operating mode of their trading halts public?

<ESMA_QUESTION_241>
The FIA Associations generally agree that trading venues should make information regarding trading halts publicly available. However, we would not recommend publishing sensitive parameters, which, if disclosed, might disrupt a fair and orderly market.

We therefore propose that ESMA qualify its proposal in point 34(vi) by clarifying that trading venues' disclosures relating to the basis for halting or constraining trading are permitted to exclude details of specific parameters.

<ESMA_QUESTION_241>

Q242: Should trading venues also make the actual thresholds in place public? In your view, would this publication offer market participants the necessary predictability and certainty, or would it entail risks? Please elaborate.

<ESMA_QUESTION_242>
A trading venue should not publish thresholds in the event this would impair market integrity, revoke anonymous trading or otherwise impair orderly trading.

<ESMA_QUESTION_242>

Q243: Do you agree with the proposal above?

<ESMA_QUESTION_243>
As discussed more elaborately in our response to Section 4.2 (Question 199 onward), the FIA Associations agree that standardised conformance testing by users (investment firms) for all trading systems accessing

a trading venue, whether via ISV or a member's own application, should include the connectivity tests mentioned as a minimum before access to the trading venue systems is granted. We also agree that the basic ability of an investment firm to enter, modify and delete orders on the trading platform should be tested.

Beyond these standard tests, however, the FIA Associations believe it should be left to the trading venue to impose further conformance testing for new applications according to its particular business model and type of trading activity.

For example, we envision difficulty in requiring further conformance testing - beyond for the introduction of a new trading application - based on whether a release is a minor release or not, given the subjectivity and ambiguity this introduces.

While recognising the limitations of simulation environments as discussed previously in our response to Question 199, we would rather see a focus on trading venues providing a continuous, robust simulation environment that mirrors the current production environment, and concurrently any proposed upgraded future environment that the trading venue may introduce. Such an environment would give members/participants the ability to carry out the appropriate due diligence on any changes, of whatever scale, at any and all times.

<ESMA_QUESTION_243>

Q244: Should trading venues have the ability to impose the process, content and timing of conformance tests? If yes, should they charge for this service separately?

<ESMA_QUESTION_244>
As stated above, the trading venue already has the right to impose further conformance testing for new applications according to its particular business model and type of trading activity in addition to the standard, mandated, conformance testing noted by ESMA. The FIA Associations believe that alternatives to conformance testing should be allowed and trading firms and trading venues be given flexibility in how they test their systems as technology changes and new testing methods may provide a better alternative. In any case, any conformance testing or access to simulation environments should not be a chargeable service. Charging a member/participant for test or simulation platforms provides a disincentive to the member/participant to be thorough in their testing. Thorough testing of all trading applications accessing those markets should be encouraged.

<ESMA_QUESTION_244>

Q245: Should alternative means of conformance testing be permitted?

<ESMA_QUESTION_245>
The minimum standard conformance testing envisioned by ESMA and tested by the relevant trading venue seem appropriate; however, as stated in our response to Question 244, alternatives to prescribed conformance testing should be allowed as new testing methods may be more effective.

<ESMA_QUESTION_245>

Q246: Could alternative means of testing substitute testing scenarios provided by trading venues to avoid disorderly trading conditions? Do you consider that a certificate from an external IT audit would be also sufficient for these purposes?

<ESMA_QUESTION_246>

The FIA Associations agree with proportionate, risk-based and appropriate testing of algorithms, but are opposed to the prescriptive discussion of tests that should be conducted.

We are very concerned that the requirements generally set out by different trading venues are overly burdensome. Applying the proportionality principle, therefore, would endorse the core principles for “adequate, proportionate, risk-based and appropriate” testing. We strongly recommend leaving it to the investment firms’ discretion to apply appropriate and proportionate testing procedures based on their own determination of the type of change and whether it is material versus minor.

The FIA Associations also question whether the basis for this question is correct. We believe the concept of ‘disorderly trading conditions’ is ill defined and too vague to provide meaningful guidance for system testing (see further our response to Question 193). There are many market conditions that may be considered “disorderly” by some and not by others.

Similarly, it is possible that there are novel, never before considered, disorderly trading conditions that may arise in the future. Rather than attempting to enumerate all possible disorderly market conditions, we believe it is better to test a trading system’s ability to function properly, as well as its ability to be resilient to unexpected market conditions. Taking this approach, in conjunction with requiring members to monitor their compliance with their obligations, is the optimal approach to preventing disorderly trading conditions.

Acknowledging that, we believe that alternative means of testing can substitute for trading venue-provided testing scenarios. Further, we believe that alternative testing scenarios designed and conducted by members/participants are a substantially superior method of testing than using trading venue-provided scenarios. Due to the wide spectrum of possible trading systems and trading strategies employed by market participants, it is impossible for any trading venue to properly construct a meaningful set of testing scenarios that will address the unique aspects of each trading system. Those responsible for designing and implementing the trading system being tested are also the people best suited to design and conduct the necessary tests. They have the best understanding of what must be tested and what constitutes normal and abnormal behaviour for the system being tested. We strongly recommend leaving it to an investment firms’ discretion to apply appropriate and proportionate testing procedures based on their own determination.

We do not believe that a certificate from an external IT audit would be sufficient or advisable for these purposes. Development and testing is conducted in a very advanced and highly specialised way by individual investment firms. External auditors, apart from being costly, are not always best placed to verify or certify trading systems. Instead, as stated above, those responsible for designing, implementing, testing and documenting the system in question are the best suited to attest to the system’s ability to avoid disorderly trading conditions.

<ESMA_QUESTION_246>

Q247: What are the minimum capabilities that testing environments should meet to avoid disorderly trading conditions?

<ESMA_QUESTION_247>
As we stated in Q246, we believe it is better to approach the testing of trading systems holistically, rather than focusing on attempting to enumerate all possible disorderly trading conditions.

For any type of testing it is important that the testing environment being used provides those performing the tests with the flexibility to simulate any market condition or use case deemed to be relevant to the system’s scope of functionality and intended use. Additionally, the testing environment should have the

ability to repeat tests as often as necessary as well as provide data to those performing the tests so they may analyse the results of the tests.

<ESMA_QUESTION_247>

Q248: Do you agree with the proposed approach?

<ESMA_QUESTION_248>
As set out in our responses to Question 208, the FIA Associations strongly support trading venue-hosted pre-trade risk controls. Three additional widely adopted trading venue-hosted pre-trade risk controls are Price Collars, Quantity Limits and Cancel-On-Disconnect: (1) A Price Collar is a dynamic price range that defines the range of prices that will be accepted for execution on a specific product by the trading venue at a given time. (2) A Quantity Limit defines the maximum order quantity that will be accepted for execution on a specific product by the trading venue (3) Cancel-On-Disconnect allows direct access participants the additional safeguard of knowing that all working orders are cancelled at the trading venue in the event that the participant loses connection to the trading venue and cannot manage their orders.

Robust controls at trading venues ensure that a baseline of risk controls are applied within the market-place regardless of the type of access used or the type of market participant. The specific implementation of these risk controls should not be prescribed by ESMA, since trading venues are the best equipped to understand the performance of their systems, the unique needs of their markets, products and participants, and the nuances associated with introducing new functionality to their systems. Moreover, trading venues can adapt risk controls to new technology and to changes in markets and trading behaviour over time.

The FIA Associations believe the controls listed above, in conjunction with the controls at the user level discussed in the context of organisational requirements on investment firms, are mostly consistent with those used today. However, we have reservations regarding points 48(viii) (market impact assessment) and 48(iv) (number of orders).

In respect of item 48(viii) (market impact assessment): to be able to determine the market impact, it would be necessary for the front-end entry system to know the entire order book at any time to be able to forecast an order-book impact (including synthetic matching) according to the matching rules. This complex approach would burst all latency limits, effectively hampering or severely delaying all ordinary-course trading, while it is nearly impossible to assess whether market impact is “irregular” or not. No front end known to us currently has the possibility/capacity to assess “regularity”.

In respect of item 48(iv) (number of orders): as we have stated elsewhere, we do not necessarily associate increased messaging at a higher speeds with disorderly markets. In fact, increased messaging often facilitates orderly trading and proper risk management among market participants, provided it does not jeopardise the integrity of the trading venue’s systems. As set out in our response to Question 282, the number of orders differs per investment firm, and for example, will be absolutely higher for those employing market making strategies. Rather than focus on number of orders per se, we believe trading venues should rather address significant delays, interruptions or errors in processing messaging and marketplace transactions.

<ESMA_QUESTION_248>

Q249: In particular, should trading venues require any other pre-trade controls?

<ESMA_QUESTION_249>

The FIA Associations are in favour of efficient and proper aggregated pre-trade risk controls offered by trading venues, such as the ones proposed in Paragraph 48. Furthermore, examples of adequate pre-trade controls are exchange price limits in order to maintain a level playing field and and limits on aggregated trade value per day. With regard to the latter, if the average traded value per day for member ABC is €100m, this member could have set its limit at €300m or €500m. Having done so, it would at least prevent this member from trading billions and ending up with a position worth billions.

<ESMA_QUESTION_249>

Q250: Do you agree that for the purposes of Article 48(5) the relevant market in terms of liquidity should be determined according to the approach described above? If, not, please state your reasons.

<ESMA_QUESTION_250>
ESMA proposes that the criteria for liquidity halts should take into account trading on the original place of listing and the venue where the instrument trades most (by value). The FIA Associations believe this approach is too narrow given the competitive environment mandated by MiFID II, where liquidity should be assessed on a pan-European basis.

We suggest instead that the NCA consider <u>all</u> venues with a material level of liquidity in determining whether it is appropriate to halt trading on other venues on which an instrument is traded. We do not express an opinion one way or another as to what threshold constitutes a 'material level of liquidity,' as we believe this is best determined by the relevant NCA, but we nevertheless suggest that the percentage of trading considered relevant not be so low as to cause unwanted noise; a level of 10% could be appropriate.

<ESMA_QUESTION_250>

Q251: Are there any other markets that should be considered material in terms of liquidity for a particular instrument? Please elaborate.

<ESMA_QUESTION_251>
The FIA Associations believe all markets relevant to the price formation process of an instrument should be considered, with the relevant NCA making such determination, but could include regulated markets, MTF's, OTF's and OTC markets.

<ESMA_QUESTION_251>

Q252: Which of the above mentioned approaches is the most adequate to fulfil the goals of Article 48? Please elaborate

<ESMA_QUESTION_252>
The FIA Associations believe clearing and trading firms prefer a framework approach (Option A). This should ideally be consistent across trading venues. It is unclear, however, how this would work for DEA providers that allow their clients to provide DEA access to their own customers (i.e. electronic carry broker/white label).

On this basis, trading venues would put in place frameworks for their members (ideally consistent), which should be part of the rules of each trading venue. This framework will then be used by members of trading venues to apply to their clients.

<ESMA_QUESTION_252>

Q253: Do you envisage any other approach to this matter?

<ESMA_QUESTION_253>
The FIA Associations believe that trading venues are in a better position to respond to this question.

<ESMA_QUESTION_253>

Q254: Do you agree with the list of elements that should be published by trading venues to permit the provision of DEA to its members or participants?

<ESMA_QUESTION_254>
The FIA Associations believe that trading venues are in a better position to respond to this question, but we do believe that a list of elements should be published.

<ESMA_QUESTION_254>

Q255: Do you agree with the list of systems and effective controls that at least DEA providers should have in place?

<ESMA_QUESTION_255>
The FIA Associations believe different risk controls are appropriate at different points in the trade lifecycle, and risk controls should not be unnecessarily duplicated at the client, DEA provider and trading venue levels. It is not the role of the trading venue to assess and monitor the underlying client. The trading venue is responsible for its members, and the DEA provider is responsible for its clients.

<ESMA_QUESTION_255>

Q256: Do you consider it is necessary to clarify anything in relation to the description of the responsibility regime?

<ESMA_QUESTION_256>
The FIA Associations believe that trading venues are in a better position to respond to this question.

<ESMA_QUESTION_256>

Q257: Do you consider necessary for trading venues to have any other additional power with respect of the provision of DEA?

<ESMA_QUESTION_257>
The FIA Associations believe trading venues will need to provide a way to identify the person that submits an order on an order-by-order basis. In doing so, they will be able to make a distinction between two important individuals associated with a trading operation: the end user and the responsible person for the trading operation in question.

When an order is submitted to an exchange it is done through a physical and/or logical connection. Depending on the trading venue, this connection may be called an operator, exchange, or trader ID (“Connection ID”).[31] Regardless of the term used, the Connection ID is typically associated with the person respon-

[31] Note, as we have set out in our response to Question 229, the Level 1 text does not require the implementation of trader ID by trading venues. Given that flagging of algorithms was included in Level 1, it follows that trader and client IDs would also have been included if this was the intention of the Council, Parliament and the Commission. Accordingly, the FIA Associations do not believe ESMA should seek to impose additional obligations at Level 2. As discussed above, we believe trader IDs, or as we here describe them, Connection IDs, in practice are of limited value in maintaining orderly markets and create practical problems for investment firms that engage in automated trading or where traders share infrastructure. Instead, we believe trading venues should work with member firms to maintain a list of those who are able to authorise trade cancellations and who can account for activity on the venue if questioned. This may not be the trader.

sible for the trading activity done via that connection. In many cases this person is not the same as the end user.

At an agency brokerage, for example, the responsible person will be one of the supervisors of the operation that manages client orders. In these cases, it is common that multiple end users and multiple trading systems, both manual and automated, will share the same Connection ID.

Similarly, in proprietary trading operations, multiple traders may submit orders for the firm's proprietary trading account on the same Connection ID while being overseen by a shared supervisor.

Connection IDs are operationally burdensome to obtain and administer. They require substantial amounts of paperwork to be completed with the trading venue. Additionally, they need to be manually configured on trading systems prior to making a connection to the trading venue. As such, they are generally kept separate from the easier to administer end user IDs that are assigned to individuals to login into trading systems and submit orders. It is these end user IDs (e.g. "Tag 50" on Globex) that are then sent to trading venues, on an order-by-order basis, where it is required for end user IDs to be sent.

Finally, it is also important to take into account trading operations where members/participants acting in an agency capacity provide access to third parties that then, in turn, may act as DEA providers. This is a common practice due to costs and operational requirements associated with obtaining membership and supporting electronic trade execution services.

In this case, the DEA provider would not be a member/participant of the trading venue and would be re-distributing a white-label platform to its own clients. The member/participant who is the wholesale provider manages risk at the omnibus account level and only faces the DEA provider. In such a scenario, the member providing the wholesale service cannot know the end users of the DEA provider for client confidentiality reasons—all client data of the DEA provider must remain anonymous to the wholesale provider. This may be accomplished via end user IDs that are passed through to the trading venue on an order-by-order basis, provided that the end user ID does not contain any personal identifiable information (such as a national ID / passport / tax number, etc.).

<ESMA_QUESTION_257>

4.4. Market making strategies, market making agreements and market making schemes

Q258: Do you agree with the previous assessment? If not, please elaborate.

<ESMA_QUESTION_258>

Introduction

Before we comment on the obligations to be imposed on investment firms with respect to market making, the FIA Associations[32] feel it is important to explain the business model of a market maker.

[32] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

Liquidity

We all take for granted that investors can buy or sell financial instruments on modern financial markets at a moment's notice. This is because modern financial markets are more liquid and accessible than ever before in history. Liquidity, while rarely defined precisely, generally quantifies how difficult it is to engage in a trade to acquire or sell a financial instrument. Strong indicators of the presence of liquidity are the narrow bid-ask spreads and high volumes present in a limit order book. The presence of liquidity makes it less costly for investors to trade.

It is fair to say that the liquidity available on European financial markets has improved in the last years. This is, for example, reflected in the fact that bid-ask spreads on UK equities have narrowed significantly between 2004 and 2011 from around 0.023 to 0.003 percentage points.[33] Academics point to the presence of algorithmic trading and high frequency trading ("HFT") as factors having narrowed bid-ask spreads – in particular algorithmic traders that engage in liquidity provision strategies. Therefore, through the presence of algorithmic and high frequency trading, it has become cheaper for all investors to trade in Europe.

The role of market makers

Market makers contribute to the provision of liquidity by being readily available to take the other side of trades contemplated by investors. Market maker do so by continuously updating quotes or sending passive orders in the market. Without market makers, investors would not be able to buy and sell stocks whenever they wanted, at the price they want, on the exchange they use every day. This would greatly affect the internal risk management of these investors, as well as increase the costs of these investors.

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of the FIA PTG and FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

[33] "The race to zero" Speech given by Andrew G Haldane, Executive Director, Financial Stability and member of the interim Financial Policy Committee, Bank of England, 8 July 2011, available at: http://www.bankofengland.co.uk/publications/Documents/speeches/2011/speech509.pdf

A crucial part of the market maker role is the ability to monitor and keep prices consistent across trading venues. Market makers face two types of problems in fulfilling this role.[34]

The first problem is an inventory-management problem – how much stock to hold and at what price to buy and sell. Market makers put capital at risk and earn a bid-ask spread for bearing the risk that their inventory loses value and to cover the cost of holding inventory, both long and short.

The second problem is an information-management problem. By making prices, a market maker opens himself up to the risk of losing to informed traders who know more about asset values – an adverse selection risk. Again, the market maker earns a bid-ask spread to protect against this informational risk. Market makers can cushion against all these risks through widening the bid-ask spread as a financial buffer.

Despite the problems market makers face in providing liquidity, bid-ask spreads have narrowed in recent times. This has been possible due to technology and increased speed of algorithmic trading that has been matched by the development of equally improved, highly responsive and effective risk management systems and IT controls. As a result, market makers are able to process information more efficiently and update quotes more quickly.

However, both improved algorithms and risks management systems require market makers to invest huge amounts in technology and infrastructure. Moreover, these investments do not guarantee profitability on every trade continuously. In other words, there is real risk involved in market making, and risk can create losses as well as profits. This is why market makers are generally incentivised to provide the services they do through various means such as reduced trading fees, payment for services, and/or exemption from specific tax and regulatory requirements that would otherwise prove to be a barrier to providing such services (e.g. UK stamp duty, short sale regulation, etc.)

Trading venues supporting liquidity

Trading venues who want to encourage market makers to provide liquidity through narrower quotes within maximum bid-ask spread parameters have chosen to reward bona fide market makers with appropriate incentives and have agreed to temporary waivers of performance obligations in the form of widening of spreads or market exits in times of distress to enable market makers to pause, assess and engage in prudent risk management.

Trading venues fulfil an essential function in financing the 'real economy' as they are a place where excess savings meet capital needs to fund investments in the form of equity or debt instruments issued by companies in the **primary market** (financial market for issuance of new financial instruments). This particular role of trading venues is only possible if sufficient liquidity is present in the **secondary market** where previously issued financial instruments are traded. If investors anticipate small volumes of liquidity in the secondary market, implying that exiting any investment will be costly, they will ask a much higher remuneration on the financial instruments they hold, in the form of higher interest rates on corporate bonds or lower earnings multiples for initial public offerings or secondary share offerings. Less liquidity in the secondary market will thus translate in much higher costs for the 'real economy'.

To avoid this situation, trading venues have taken necessary measures to ensure that liquidity is available by providing the necessary incentives to market makers and making market making obligation conducive to prudent risk management procedures.

[34] Idem.

The European Commission has clearly identified the development of European capital markets as one of its policy priorities to ensure that the 'real economy' is less reliant on bank funding and more on capital markets funding in this period of bank deleveraging.[35] This development of capital markets can only be ensured if sufficient liquidity is present in the secondary markets. Therefore, it is of paramount importance that market makers are not unduly constrained in their role and obligations of providing liquidity.

MiFID II and ESMA Policy Orientation

The combination of (1) of improved algorithms, (2) improved state-of-the-art risk management systems, (3) incentives by trading venues and (4) temporary waivers of market making obligations in exceptional circumstances make it possible for market makers today to contribute to the most efficient markets in history while managing risks effectively and preserving market stability. Therefore, we urge ESMA to be cautious when developing rules applicable to market makers to strike an appropriate balance between regulation and liquidity.

The FIA Associations understand the intended purpose of the market making obligations in Articles 48 and 17 of MiFID II is to reduce the impact of potentially systemic volatility peaks in instruments where algorithmic traders are present as indicated in Recital 62 of MiFID II.

While the FIA Associations understand this risk is highlighted in Recital 62 of MiFID II, based on our experiences as market practitioners, we strongly believe algorithmic trading actually contributes to the dampening of volatility. Numerous academic studies have shown no direct evidence or causality link between increased volatility and the presence of algorithmic trading in the market.[36] Other market participants agree with our view[37] that HFT played a positive role between 2007 and 2009 (at the peak of volatility in the market), evidenced by the fact that bid-offer spreads narrowed by 21 per cent. By posting two-sided quotes, algorithmic and HFT provide important liquidity to the market. Higher liquidity generally

[35] European Commission, Communication to the European Parliament and the Council on Long-Term Financing of the European Economy, March 2014, available at: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52014DC0168 .
[36] See, e.g. Credit Suisse's note July 2014 concluding that record-low volatility in large cap stocks may be due to the presence of HFT: https://edge.credit-suisse.com/Edge/public/bulletin/ServeFile.aspx?FileID=25759&m=459736517;
See also the UK Government Office for Science, The Future of Computer Trading in Financial Markets, Working Paper 2011, Foresight, available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/289058/11-1276-the-future-of-computer-trading-in-financial-markets.pdf.
One empirical study based on price data for 15 futures contracts listed on CME Group, Eurex, IntercontinentialExchange, and NYSE Liffe, found that that algorithmic and high-frequency trading did not affect volatility of prices, and volatility in the futures markets has neither increased nor decreased over the last decade once the effects of macro-economic shocks are removed. Bollen, Whaley study, *Futures Market Volatility: What Has Changed?*, Owen Graduate School of Management, Vanderbilt University, August 2013, available at: http://www.futuresindustry.org/downloads/Volatility_Study_8-27-2013.pdf.
A 2010 study on high frequency trading and its impact on market quality found that HFT activity either had no impact on volatility or tended to decrease it. Brogaard, *High Frequency Trading and Its Impact on Market Quality*, Northwestern University Kellogg School of Management, July 16, 2010, available at: http://www.fsa.gov.uk/static/FsaWeb/Shared/Documents/pubs/consumer-research/jonathan-brogaard-hft.pdf.
Other studies have shown a clear correlation between the presence of algorithmic and high frequency trading and dampened volatility or smoother stock price movements. See e.g., JPX Working Paper, Hasaka, *Analysis of High-Frequency Trading at Tokyo Stock Exchange*, March 2014, available at: http://www.jpx.co.jp/news-releases/ncd3se00000016r9-att/Summary_JPX_wp_en_No.4.pdf and proprietary Eurex Exchange market data analyses on high-frequency trading, 2013, available at: http://www.eurexchange.com/blob/exchange-en/455384/526632/1/data/Automated-Trader_HFT.pdf
[37] Financial Times, Monitor HFT predators, not algorithms, Arjun Singh-Muchelle, June 2014, available at: http://www.ft.com/intl/cms/s/0/2032285a-eb19-11e3-9c8b-00144feabdc0.html#axzz37XoS24zb
The author is a senior adviser at the Investment Management Association (IMA), a trade association whose members manage over £5.8tn of assets.

translates to lower volatility, as potential shocks get evened out through the available liquidity absorbing sales of financial instruments by investors, thus controlling any price drops.

The FIA Associations therefore urge ESMA to consider that algorithmic traders have invested heavily in effective risk management systems and agile trading systems that allow them to amend quotes rapidly and continue providing liquidity in a prudent manner while keeping spreads tight. This has proven to be a mitigating factor against the risks of disorderly trading and promoted quicker recovery after major market disruptions.

While the FIA Associations support enhanced market making obligations, we have consistently opposed a legislatively mandated continuous quoting obligation for the reasons stated above. We remain very concerned that the imposition of minimum obligations on market makers, if not carefully calibrated to take into account the very real downsides of engaging in this type of business model, will conflict with MiFID II's goal that investment firms engage in prudent risk management. Moreover, it may incentivise existing liquidity providers to reconsider their role and potentially shift to more opportunistic behaviour free from obligation.

This would be a serious blow to market quality. A reduction in the number of firms willing to operate market making strategies would have several negative effects on the overall market. First, this would translate into reduced liquidity, making it more difficult for investors to trade. Second, the reduced liquidity would mean fewer buffers on the market to absorb price shocks and would translate into higher volatility, increasing uncertainty for long-term investors. Third, less liquidity will make trading more expensive as it undermines the price discovery mechanism and leads to wider spreads. Finally, a further reduction in the number of market makers would have particularly adverse consequences in an era where banks are retreating from market making and deleveraging. Liquidity provision from independent firms utilising algorithmic and HFT techniques is set to become more important than ever as more economies around the world are set to rely increasingly on capital markets financing. We believe ESMA should do everything in its power to stimulate that investment firms engaging in market making continue to do so.

Subject to the above comments on ESMA's assessment of Articles 48 and 17 of MiFID II, the FIA Associations agree that the requirements of Articles 17 and 48 of MiFID II are correlated and should be addressed jointly. See further our comments to Question 280 below.

<ESMA_QUESTION_258>

Q259: Do you agree with the preliminary assessments above? What practical consequences would it have if firms would also be captured by Article 17(4) MiFID II when posting only one-way quotes, but doing so in different trading venues on different sides of the order book (i.e. posting buy quotes in venue A and sell quotes in venue B for the same instrument)?

<ESMA_QUESTION_259>
If Article 17(4) of MiFID II were to capture firms posting buy quotes in venue A and sell quotes in venue B in the same security, it would capture firms engaging in the most basic kind of equities arbitrage, which is not – and never has been – considered market making. Moreover, as a practical matter, it would be impossible to capture such cross-venue activity in a market making agreement with a single trading venue as required under Article 17(3)(b) of MiIFD II.

The FIA Associations would like to emphasise that strategies pursued today using algorithmic or high frequency technologies are not new. They are simply familiar trading strategies that have been updated for an automated environment. For example, electronic trading firms make markets using the same business model as traditional market makers, but with lower costs, more advanced and efficient risk management

and tighter bid-ask spreads due to automation. In fact, automated market makers have largely replaced human market makers due to the four factors we highlighted in our introduction: (1) improved algorithms, (2) improved state-of-the-art risk management systems, (3) incentives by trading venues and (4) temporary waivers of market making obligations in exceptional circumstances.

Other strategies conduct cross-market arbitrage, aimed at equalising prices of the same share trading on multiple markets (for example British Petroleum trading in both New York and London). In the past, human traders would carry out this type of arbitrage, but the same trading strategy can now be implemented faster and at lower cost with computers. The consequences of capturing this kind of arbitrage under the market making requirements would result in imposing obligations on pure equities arbitrage firms whose business model is not market making.

<ESMA_QUESTION_259>

Q260: For how long should the performance of a certain strategy be monitored to determine whether it meets the requirements of Article 17(4) of MiFID II?

<ESMA_QUESTION_260>
The FIA Associations believe the concept of an 'observation period' to monitor the performance of a certain strategy to detect whether it meets the requirements of Article 17(4) of MiFID II is new and not necessary.

An observation period would set an arbitrary threshold (whether 30 days, 3 months, 6 months, 1 year), enabling participants if so desired to game the timeframe so as to avoid being characterised as a market maker. This could thwart the goal of imposing more stringent obligations on market makers, as well as contradicting the principle of a level playing field.

Instead of using an observation period, the FIA Associations believe that determining whether an investment firm is operating a market making strategy should follow the parameters of market making agreements as set by the relevant trading venue, particularly the obligations regarding (1) maximum spread, (2) minimum size or amount, (3) minimum percentage quoting presence during applicable trading hours, and (4) appropriate incentives. An investment firm whose strategy and behaviour falls within these parameters would be pursuing a market making strategy within the meaning of Article 17(4) of MiFID II.

Moreover, investment firms are required to document the purpose and function of their algorithms prior to deployment as part of the organisational requirements. Therefore, they will know upfront whether a strategy is intended to provide liquidity or not and would be able to know in advance whether it would meet the definition of a market making strategy. Investment firms are therefore in a position as of day one to self-assess whether they will be required to enter in to a 'Market Making Agreement' pursuant to Article 17(3) of MiFID II.

To summarise, an observation period is not needed because:

1. Persons intend to be market makers;
2. Persons intending to be market maker design and test their algorithms accordingly;
3. Strategies that meet the requirements of Market Making Agreements offered by a trading venue are "market making strategies"; and,
4. No assessment of strategies is otherwise required, as it will be obvious which member/participant engages in algorithmic trading to pursue a market making strategy.

Finally, we read the Article 17(3)(b) obligation as incumbent on the member/participant of the trading venue. This article and ESMA's analysis are silent on questions of disputes between a member/participant

of a trading venue and a market operator/investment firm with respect to this determination, but we expect that the trading venues' rules should apply in such circumstances.

<ESMA_QUESTION_260>

Q261: What percentage of the observation period should a strategy meet with regard to the requirements of Article 17(4) of MiFID II so as to consider that it should be captured by the obligation to enter into a market making agreement?

<ESMA_QUESTION_261>
For the reasons stated in our response to Question 260, the FIA Associations do not believe an observation period is necessary.

<ESMA_QUESTION_261>

Q262: Do you agree with the above assessment?

<ESMA_QUESTION_262>
The FIA Associations have consistently promulgated the view that regulation should apply equally to market participants regardless of their means of market access. We note that ESMA's proposed approach has the effect of creating an uneven playing field, as investment firms accessing the market indirectly, for example, through a DEA arrangement, will:

(1) be able to operate a market making strategy without the same obligations as a member firm operating an identical strategy on the same venue; and, conversely,
(2) be denied access to Market Making Schemes operated by trading venues.

We do, however, understand the rationale behind this – indirect participants do not have legal standing to enter into direct agreements with trading venues – and therefore follow ESMA's assessment that indirect participants are excluded from being considered firms pursuing a market making strategy within the meaning of Article 17(4). We would also note that the alternative, to treat indirect participants as a firm pursuing a market making strategy, would necessitate a DEA provider entering into a Market Making Agreement on behalf of underlying clients, but this is also prevented by the inherent limitations imposed by the definition of "market maker" in the Level 1 text, in particular, the reference to "own account [dealing]."

Nevertheless, the FIA Associations believe it is important to maintain commercial choice on the part of market participants. We have made the point elsewhere in our response (see our response to Question 280) that we believe a Market Making Agreement should be underpinned by a Market Making Scheme.

On the basis that any investment firm wishing to participate in a Market Making Scheme (through a Market Making Agreement) will be required to become a member firm of the relevant trading venue, we urge ESMA to ensure that implementation of MiFID II is accompanied by a strong mandate to ensure fair and non-discriminatory member access to all EU regulated markets, including via remote membership, which is not the case today.

<ESMA_QUESTION_262>

Q263: Do you agree with this interpretation?

<ESMA_QUESTION_263>

On the interpretation of “posting firm quotes,” the FIA Associations agree a quote is firm as long as it is executable, provided this excludes “indicative” quotes. For the sake of clarity we would highlight that "quote" is a generic term and should be taken to include all passive order types - please see our response to Question 268.

<ESMA_QUESTION_263>

Q264: Do you agree with the above assessment? If not, please elaborate.

<ESMA_QUESTION_264>
The FIA Associations agree with ESMA’s view that the definition of a market making strategy should only contain strategies where an investment firm operates a firm, simultaneous two-way quote in a single instrument (at least one) on a single trading venue.

<ESMA_QUESTION_264>

Q265: Do you agree with the above interpretation?

<ESMA_QUESTION_265>
The FIA Associations do not believe specifying “*simultaneous*” in a blunt time frame that will quickly become obsolete as technology progresses is appropriate or prudent. We suggest there is no need for a definition of “*simultaneous*” in the draft regulatory technical standards; rather this can be left to be construed and could be amplified in ESMA guidance if needed.

<ESMA_QUESTION_265>

Q266: Do you agree with the above proposal?

<ESMA_QUESTION_266>
As we have previously stated, the FIA Associations believe the criteria of what obligates a firm to enter into a Market Making Agreement should be consistent with the obligations under the Market Making Agreements. In this context, ‘comparable size’ should therefore mean in “at least minimum size,” as set by the relevant trading venue.

<ESMA_QUESTION_266>

Q267: Do you agree with the above proposal?

<ESMA_QUESTION_267>
As we have previously stated, the FIA Associations believe the definition of what obligates a firm to enter into a Market Making Agreement should be consistent with the obligations under the Market Making Agreements. In this context, ‘competitive prices’ should therefore mean “prices within the maximum spread,” as set by the relevant trading venue.

<ESMA_QUESTION_267>

Q268: Do you agree with the approach described (non-exhaustive list of quoting parameters)?

<ESMA_QUESTION_268>
The FIA Associations strongly agree with ESMA’s proposal to set principles applying to market making rather than ‘hard-coded’ conditions.

We agree that ESMA should set a framework for quoting parameters that leave ample room for trading venues to design the most adequate Market Making Agreements according to the instruments traded, market or market segment characteristics and business model. As we have stated above, we believe these parameters should reflect the content of current market practice: the main obligations arising from participation in such schemes are (1) minimum size, (2) maximum spread, (3) percentage of presence in the market during applicable continuous trading periods, and (4) appropriate incentives.

To be clear, we believe no Market Making Agreement should be offered without appropriate incentives, and no prospective market maker should be obliged to enter into a Market Making Agreement without appropriate incentives, to adequately compensate it for the costs and risks incurred in providing continuous liquidity to the market as described elsewhere in this response. We believe this position is justified under the requirements of Article 48(9).

We would also recommend that ESMA take care in the drafting of regulatory technical standards to ensure these are consistent with the different order-types supported on different trading venues. The term "quoting parameters" should not be interpreted as referencing a specific type of order type, but rather it should represent any executable passive order-type permitted by individual trading venues.

<ESMA_QUESTION_268>

Q269: What should be the parameters to assess whether the market making schemes under Article 48 of MiFID II have effectively contributed to more orderly markets?

<ESMA_QUESTION_269>
The FIA Associations have no particular view on the most appropriate means to measure the orderliness of a market, though we believe it could be assessed by its quality which is generally taken to be comprised of (1) the presence of liquidity, (2) price efficiency and (3) transaction costs.

ESMA can assess the presence of liquidity (which generally quantifies how difficult it is to engage in a trade) by looking at the bid-ask spread and the volume present in a limit order book. In assessing the recovery of liquidity after market volatility, ESMA could follow the methodology of Eurex Exchange's 2013 data-driven market analysis of the behaviour of high frequency trading firms in times of extreme market volatility[38]. ESMA should examine data to uncover (1) whether strategies flagged as market making continued to be an important source of liquidity throughout incidents of market distress, (2) whether they continued to supply a relatively stable percent of orders available at the best bid and offer, (3) whether aggregate participation was not skewed to one side or the other and (4) whether the share of passive executions after the incident remained stable in comparison to the period before the incident. Other liquidity measures include daily traded volume and turnover.

<ESMA_QUESTION_269>

Q270: Do you agree with the list of requirements set out above? Is there any requirement that should be added / removed and if so why?

<ESMA_QUESTION_270>
The FIA Associations do not agree with the approach suggested by ESMA and the list of requirements set out on page 266. First, we do not see any legal basis in the Level 1 text to impose different, "minimum" set of organisational requirements on market makers versus investment firms carrying out algorithmic trad-

[38] The EUREX market analysis is available at: http://www.eurexchange.com/blob/exchange-en/455384/526632/1/data/Automated-Trader_HFT.pdf .

ing activities generally. Second, we cannot identify any tangible benefits that would be derived from doing so, as existing rules on organisational requirements for investment firms are subject to a proportionality principle and are therefore already designed to be adaptable to different business models.

A particular example of the over-reach of the list of requirements on page 266 is the requirement with respect to remuneration policies (Paragraph 34 (vii)). This requires investment firms to establish remuneration schemes for staff dedicated to the market activity which do not (a) incentivise disproportionate risk taking, (b) impede compliance with the obligation of the firm to act in the best interest of clients, and (c) encourage non-compliance with the market making scheme. This requirement is duplicative of existing regulation, as any investment firm under MiFID II will also automatically be in scope for CRD IV purposes, such that remuneration rules will already apply. Moreover, these provisions remain subject to proportionate application: institutions must comply with the remuneration requirements "*in a way and to the extent that is appropriate to their size, internal organisation and the nature, the scope and the complexity of their activities*."[39]

We are concerned that if ESMA introduces new, separate and/or additional organisational requirements applying only to a subset of investment firms engaged in liquidity provision, ESMA creates the possibility for interpretive slippage between two sets of requirements, as well as an uneven playing field for participants, where existing rules already adequately address the same goals.

<ESMA_QUESTION_270>

Q271: Please provide views, with reasons, on what would be an adequate presence of market making strategies during trading hours?

<ESMA_QUESTION_271>
As we have previously stated, the FIA Associations believe the criteria for what obligates a firm to enter into a Market Making Agreement should be consistent with the obligations under the Market Making Agreements. The average presence time under a market making strategy should sync with the minimum percentage presence required in a Market Making Agreement during applicable trading hours. Trading venues will be best placed to assess the appropriate presence of market making strategies, which could be on a per symbol or per segment basis and will vary among asset classes.

By defining the minimum presence as being "as per the requirements laid down in the Market Making Agreement," this allows venues to make this assessment and enables them to align the presence requirement with the incentive(s) they are willing to offer market makers, the liquidity of the instrument(s) on their specific order-book, and the overall liquidity of the instrument itself. In accordance with correct market practice, this varies per product, segment and per venue, though in general for liquid shares, 80% of applicable trading hours during the continuous trading period is an accepted standard.

Please note, however, 80% should not be taken as a blanket metric to be applied to other instruments. Each class of derivatives, for example, has its own characteristics that may make such a standard impractical. For example, a number of products trade across multiple time zones, with trading hours in many cases totalling up to 20 hours per day. For such products, the 80% requirement should apply to a specified core trading session rather than the full trading hours (hence, we have referred to "applicable trading hours during the continuous trading period").

<ESMA_QUESTION_271>

[39] See Article 88(2) of the CRD IV.

Q272: Do you consider that the average presence time under a market making strategy should be the same as the presence time required under a market making agreement ?

<ESMA_QUESTION_272>
Yes. As we have previously stated, the FIA Associations believe the criteria for what obligates a firm to enter into a Market Making Agreement should be consistent with the obligations under the Market Making Agreements. The average presence time under a market making strategy should be the minimum percentage presence required in a Market Making Agreement during applicable trading hours.

<ESMA_QUESTION_272>

Q273: Should the presence of market making strategies during trading hours be the same across instruments and trading models? If you think it should not, please indicate how this requirement should be specified by different products or market models?

<ESMA_QUESTION_273>
The FIA Associations disagree with the policy orientation suggested by ESMA.

As we have stated before, the average presence time under a market making strategy should sync with the minimum percentage presence required in a Market Making Agreement during trading hours. In market practice, this varies per product, per venue, though in general for liquid shares, 80% is an accepted standard. However, 80% should not be taken as a blanket metric to be applied to other instruments. Each class of derivatives, for example, has its own characteristics that may make such a standard impractical. For example, a number of products trade across multiple time zones, with trading hours in many cases totalling up to 20 hours per day. For such products, the 80% requirement should apply to a specified core trading session rather than the full trading hours (hence, we have referred to "applicable trading hours during the continuous trading period").

We discourage ESMA from setting out prescriptive guidelines; rather ESMA should allow the trading venues to determine presence requirements depending on the nature of the venue, the instrument traded, the market segment, the presence of liquidity and market circumstances.

<ESMA_QUESTION_273>

Q274: Article 48(3) of MiFID II states that the market making agreement should reflect "where applicable any other obligation arising from participation in the scheme". What in your opinion are the additional areas that that agreement should cover?

<ESMA_QUESTION_274>
The FIA Associations believe this should be left to the discretion of the trading venues. In accordance with correct market practice, the main elements comprising participation in market making schemes are (1) the minimum size of quotes to be send to the market, (2) the maximum spread within which the quotes can be placed, (3) the percentage of trading hours during which presence in the market is required, and (4) appropriate incentives.

<ESMA_QUESTION_274>

Q275: Do you disagree with any of the events that would qualify as 'exceptional circumstances'? Please elaborate.

<ESMA_QUESTION_275>
Article 17(7)(c) of MiFID II mandates ESMA to draft regulatory technical standards to determine "*the situations constituting exceptional circumstances referred to in paragraph 3, including circumstances of extreme volatility, political and macroeconomic issues, system and operational matters, and circum-*

stances which contradict the investment firm's ability to maintain prudent risk management practices as laid down in paragraph 1."

ESMA's proposal is to limit these exceptional circumstances to two categories: (i) technological issues including problems with a data feed or other system that is essential in order to be able to carry out a market making strategy; and (ii) internal risk management issues, which would encompass problems in relation to capital or clearing. (Note: we find the qualifying clause "*which would encompass problems in relation to capital or clearing*" to be a limited clause, whereas language such as "including but not limited to" would have implied room for other interpretations of risk management issues.)

The FIA Associations understand ESMA's desire to limit the circumstances under which investment firms operating market making strategies can cease providing liquidity in an attempt to secure stability of liquidity in times when the market needs it most.

However, we believe ESMA proposes an unduly narrow interpretation of its mandate per Article 17(7)(c) of MiFID II and, if implemented as proposed, would thwart MiFID II's objectives of achieving liquidity resilience.

While ESMA acknowledges investment firms engaged in market making are exposed to significant risks, ESMA goes on to state that incidents involving new information giving rise to unexpected price movements should not – in contrast to the clear mandate provided in the MiFID II text quoted above –be grounds for market makers to pause. ESMA states: "*market makers should be the most responsive participants, and their market making quotes should be based on all information events*."

As we have stated earlier (Question 258), market makers face two types of problem: inventory-management and information management. We identified four factors that enable market makers to mitigate the risks arising from these problems: (1) technology, (2) risk management, (3) incentives, (4) temporary contractual excuse from performance during circumstances of distress. We acknowledge that ESMA's proposed approach supports technology and prudent internal risk management.

By excluding volatility and information events, however, the risks of quoting will be exacerbated because, under MiFID II's new minimum obligations imposed on investment firms operating market making strategies, firms will not be at liberty to widen spreads sufficiently to buffer their risk (even taking into consideration an 80% quoting obligation) or to temporarily pause trading in order to assess shifted risk conditions and adjust the parameters before resuming safe and prudent trading. We are deeply concerned this may result in many liquidity providers substantially reducing their activity, or simply withdrawing from the market, precisely when market risks begin to rise and the end-user's need for liquidity is the greatest.

Thus, the FIA Associations believe ESMA should set non-exhaustive parameters for "exceptional circumstances"/equivalent exclusions, mirroring the Level 1 text.

An alternative commercial approach to stimulate investment firms to remain in the market during times of extreme market volatility would be to offer performance-based incentives for the continued provision of liquidity through such times. This would be a positive reinforcement of the behaviour ESMA wishes to stimulate, rather than hamstringing participants from being able to engage in proper risk management.

<ESMA_QUESTION_275>

Q276: Are there any additional 'exceptional circumstances' (e.g. reporting events or new fundamental information becoming available) that should be considered by ESMA? Please elaborate.

<ESMA_QUESTION_276>
As stated above, the FIA Associations believe ESMA should set non-exhaustive parameters for "exceptional circumstances"/equivalent exclusions, mirroring the Level 1 text ("*including circumstances of extreme volatility, political and macroeconomic issues, system and operational matters, and circumstances which contradict the investment firm's ability to maintain prudent risk management practices*").

The current market practice is that every trading venue implements its own standards to excuse market makers from performance. Common additional "exceptional circumstance"/equivalent exclusions included in Market Making Agreements by trading venues include:

- Cases of a trading halt, specific auctions, the closure of an underlying market, or the suspension or removal from trading of an underlying product.

These circumstances should extend to derivative contracts that reference the financial instrument halted, suspended or removed, even if the derivative contract itself is not subject to automatic suspension or removal from trading. We believe this to be in line with Article 52 and the analysis of Paragraphs 13-18 of Section 6.2 of the Discussion Paper.

- Cases of a "fast market" or other equivalent decision by a market operator/investment firm operating a trading venue regarding extreme volatility.

This is consistent with the mandate under Article 17(7)(c) ("*including circumstances of extreme volatility*").

- Cases where a trading venue has reported any of (a) significant infringements of rules, (b) disorderly trading conditions, or (c) system disruptions to its NCA per Article 31(2) or 54(2).

<ESMA_QUESTION_276>

Q277: What type of events might be considered under the definition of political and macroeconomic issues?

<ESMA_QUESTION_277>
Under the definition of political and macro-economic issues, the FIA Associations believe ESMA should set non-exhaustive parameters that include any event that an investment firm's risk management would reasonably deem relevant cause to suspend market making. Such assessment may be tested for reasonableness and prudence after the fact by the relevant NCA, but should not and cannot be exhaustively prescribed.

Rather than provide an exhaustive list, we would only point to examples of political and macro-economic events over the past years that have heavily impacted markets, such as the collapse of Lehman Brothers in 2008, the Eurozone debt crisis beginning in 2009, the Flash Crash in 2010, the Fukushima nuclear disaster in 2011, the plunge of global markets in 2012 on poor US jobless figures, and since then the Arab Spring, Iraq, Egypt, Syria, ISIS, the Ukraine crisis and the devaluation of the Argentinian peso in 2014.

At the core of any attempt to capture all possible risks, as we have seen in the last decade, is that the unpredictable occurs from time to time. Therefore we encourage ESMA to take a principle-based approach that enables investment firms to engage in prudent risk management.

We believe the burden of justifying "exceptional circumstance"/equivalent exclusion should rest on the investment firm, subject to ex post facto review by regulators, that its performance of market making obligations was adversely affected by the exceptional circumstances, that such circumstances were beyond

its control, and that there were no proportionally reasonable steps to be taken to avoid the event and/or its consequences.

<ESMA_QUESTION_277>

Q278: What is an appropriate timeframe for determining whether exceptional circumstances no longer apply?

<ESMA_QUESTION_278>
The FIA Associations do not believe it appropriate for ESMA to define an appropriate duration or timeframe for "exceptional circumstance"/equivalent exclusion. Together the market operator/ investment firm operating a trading venue and the investment firm relying on the "exceptional circumstance"/equivalent exclusion should determine when that "exceptional circumstance"/equivalent exclusion is no longer applicable.

<ESMA_QUESTION_278>

Q279: What would be an appropriate procedure to restart normal trading activities (e.g. auction periods, notifications, timeframe)?

<ESMA_QUESTION_279>
The FIA Associations believe the trading venues are best placed to determine the appropriate procedure for restarting trading depending on the circumstances but suggest these should include:

- clear and unambiguous communication of the issue at hand;

- realistic timeframes for estimated resolution;

- regular updates to the market regarding suspension of market activities until all participants (not just a subset) have been able to recommence order entry;

- a period of up to 15 minutes of re-order entry and then a re-opening auction.

<ESMA_QUESTION_279>

Q280: Do you agree with this approach? If not, please elaborate.

<ESMA_QUESTION_280>
The FIA Associations take a different view from ESMA's proposal on the optimal interaction between Market Making Agreements and Market Making Schemes.

The FIA Associations understand that Article 17(3) and (4) of MiFID II requires an investment firm to enter into a Market Making Agreement whenever it is pursuing a market making strategy in any financial instrument. Pursuant to Article 48(2)(a) of MiFID II a trading venue has the mirror obligation to have in place a written agreement with any investment firm pursuing a market making strategy. Article 48(2)(b) of MiFID II requires a trading venue (where appropriate) to have in place Market Making Schemes to ensure that a sufficient number of investment firms participate in such scheme and provide liquidity, irrespective of whether they are bound by Article 17(3) of MiFID II.

First, therefore, the FIA Associations would challenge ESMA's analysis in Paragraph 43 sub-paragraph (i), the second sentence of which limits the application of Articles 17 and 48 to a sub-set of financial instruments. We do not see a basis in either article and related recitals to limit their application to all financial instruments -- save for the second sentence of Article 48(9), which applies only to "individual shares or a suitable basket of shares" – but we do not consider this as requiring such limitation.

Second, the FIA Associations strongly disagree with ESMA's implicit contention that market maker liquidity is somehow lesser than other liquidity. Liquidity coming from market makers may not be "natural," but so long as market makers have quoting obligations, the resulting liquidity is "real" and therefore sought after by trading venues and investors at large as it improves market quality. Furthermore, liquidity – a measure of market quality - attracts liquidity. The presence of market makers improves the quality of the market because they contribute to price formation transparency, market efficiency and competition. This increased liquidity and quality will in turn provide an incentive to other market participants to trade on that market. These market participants will increase liquidity through their trading. Therefore, we believe that capping market making liquidity would have a negative effect on the market as well as be anti-competitive.

Third, the FIA Associations see no basis in Article 48 for the draft regulatory technical standards to mandate a "ceiling" on market maker liquidity or market share. We understand it is ESMA's view that if too much volume comes from market makers or if their market share is too high, then there's something wrong with the incentive scheme offered by the trading venue. It may, for example, be over-incentivising the liquidity resulting from market makers, which may give a misleading impression of liquidity in the market.

However, new platforms need to be able to rely on incentivised liquidity from market makers as they start up – without this, no nascent regulated market or multi-lateral trading facility would be able to get off the ground. We believe constraining new trading venues' ability to incentivise liquidity in all financial instruments would seriously undermine key objectives of the MiFID II and MiFIR legislation.

Moreover, we see practical impediments to deciding how much liquidity is sufficient for any given financial instrument. Liquidity as a measure may change quickly and significantly, and any assessment of liquidity is always backward looking.

Fourth, the FIA Associations are concerned ESMA's approach would create a mismatch in scope between market making agreements (all financial instruments) and market making schemes (only financial instruments with insufficient liquidity) and potentially create a two-tier structure: a 'regulatory floor' agreement setting out the obligations of the market maker and separate commercial incentive schemes mirroring existing market practice. The potential scope mismatch highlighted above may lead to the situation that a market maker is only subject to obligations without benefits, for example, when it concerns a financial instrument where there are sufficient market makers. Such a structure would ran counter to the basic principle that the obligations a market maker assumes should be proportional and commensurate to the benefits he enjoys.

Fifth, with regard to the requirement that trading venues be able to prevent access and/or delete orders or transactions that have occurred, the FIA Associations emphasise that this must be in accordance with established, publicly available rulebooks and policies, so that trading venues cannot exercise any arbitrary discretion over access, orders or transactions that could threaten a fair and level playing field or trade certainty.

Finally, the FIA Associations believe the proposal to require trading venues to publicly disclose an investment firm's non-compliance with a Market Making Scheme would be disproportionate and unusual. Public disclosure of breaches of a trading venue's rules is made only in cases of very serious breaches, such as the default of member. We believe it appropriate only for a trading venue to disclose the terms and conditions of a Market Making Scheme and the identity of investment firms participating in the scheme.

The FIA Associations suggested approach

As the FIA Associations have stated before, we support the principle of enhanced market making obligations, provided firms committing to such obligations are facilitated in doing so through due regard for the four factors essential for these additional obligations: (1) technology, (2) risk management, (3) incentives, and (4) temporary contractual excuse from performance during circumstances of distress.

We strongly suggest that ESMA develops rules that are sufficiently flexible to be applied to a variety of different markets and are based on several core principles which should underpin any relation between trading venues and market makers, as follows:

First, all trading venues should offer market making agreements to investment firms pursuing a market making strategy within the meaning of Article 17(4) of MiFID II.

Second, each and every Market Making Agreement should be underpinned by a Market Making Scheme. We believe sub-paragraphs (iii) and (iv) of ESMA's analysis support the FIA Associations' interpretation that Market Making Agreements are necessary components of a Market Making Scheme, and that an investment firm cannot participate in a Market Making Scheme without a formal agreement with the market operator/investment firm operating a trading venue.

By ensuring Market Making Agreements and Market Making Schemes are aligned, ESMA would preserve commercial choice on the part of market participants. Investment firms captured under by Article 17(3) of MiFID II would have a choice either to participate in Market Making Schemes or exit the activity. Investment firms not captured would also have a choice to elect into the Market Making Scheme in return for committing to obligations consistent with Article 17(3) of MiFID II.

Third, obligations imposed on a market maker should be proportionate to the benefits received and should take into account the liquidity provided to the market.

Fourth, each trading venue should have the flexibility to be able to determine the commercial terms of any Market Making Scheme. Rather than imposing a ceiling on market maker liquidity, we would propose that the market operator/investment firm operating a trading venue retain the ability to dial-down Market Making Scheme incentives where there is sufficient liquidity. This is already common practice: trading venues already fine-tune incentives for market makers based on the liquidity of the instrument(s) to ensure there is no "over-supply," as there is no commercial rationale for paying incentives to market makers where sufficient liquidity already exists. A good and current example of this is ICE/Liffe, which has just announced reduced incentives in short term interest rate products – where liquidity is at its greatest – and increased incentives in less liquid, longer-dated interest rate contracts to encourage more liquidity provision there.

Finally, we suggest ESMA include a condition in the regulatory technical standards that trading venues should provide a reasonable time period in which investment firms may remedy a remediable breach of a Market Making Agreement. It should be clear that a market maker would only be in breach of a regulatory obligation if its breach was not capable of remedy or if after a reasonable period of time it had failed to remedy such breach.

The FIA Associations believe there is no risk that these schemes will over-incentivise market participants provided the trading venues are given sufficient flexibility to adapt Market Making Schemes on a fair and non-discriminatory basis and in accordance with trading venue and Market Making Scheme rules. Furthermore, any concerns about an "over-supply" of liquidity can be simply addressed by trading venues rewarding liquidity providers for executions rather than for merely posting quotes.

<ESMA_QUESTION_280>

Q281: Would further clarification be necessary regarding what is "fair and non-discriminatory"? In particular, are there any cases of discriminatory access that should be specifically addressed?

<ESMA_QUESTION_281>
The FIA Associations are of the view that Article 17(3)(b)-(c) and Article 48(2)-(3) support the following interpretation:

- Market Making Agreements and Market Making Schemes are distinct but inextricably linked arrangements.
- Any investment firm engaging in algorithmic trading to pursue a market making strategy must – and must be allowed to – enter into a Market Making Agreement with the market operator/investment firm operating a trading venue.
- From the drafting of Article 48(2)(b) of MiFID II we believe a better construction is that a market operator/investment firm operating a trading venue must have multiple Market Making Schemes to ensure a sufficient number investment firms enter into Market Making Agreements.

Further, we believe that ESMA's analysis at paragraph 43 suggests:

- Market Making Schemes must be or must include a binding agreement between the investment firm participating in a Market Making Scheme and the trading venue offering the Market Making Scheme;
- In order to participate in a Market Making Scheme, a firm is required to enter into a Market Making Agreement. Investment firms not captured would also have a choice to elect into the Market Making Scheme in return for committing to obligations consistent with Article 17(3) of MiFID II.

The FIA Associations strongly support this linkage between Market Making Agreements and Market Making Schemes. We believe that Market Making Agreement obligations without appropriate incentives are essentially unfair and counter to the requirement of "fair and non-discriminatory" schemes.

<ESMA_QUESTION_281>

Q282: Would it be acceptable setting out any type of technological or informational advantages for participants in market making schemes for liquid instruments? If yes, please elaborate.

<ESMA_QUESTION_282>
We only believe that market makers should be exempt from order to trade ratios. No other technological or informational advantages are appropriate.
<ESMA_QUESTION_282>

Q283: In which cases should a market operator be entitled to close the number of firms taking part in a market making scheme?

<ESMA_QUESTION_283>
Please see our comments in Question 280.
<ESMA_QUESTION_283>

Q284: Do you agree that the market making requirements in Articles 17 and 48 of MiFID II are mostly relevant for liquid instruments? If not, please elaborate how you would apply the requirements in Articles 17 and 48 of MiFID II on market making schemes/agreements/strategies to illiquid instruments.

<ESMA_QUESTION_284>

The FIA Associations see no clear basis in the Level 1 text for ESMA's analysis and proposal to limit "*market making requirements*" to liquid instruments. We consider any such limitation as illogical and impractical. Using ESMA's own analysis at Paragraph 43, it would be difficult to justify requiring a trading venue to incentivise additional market maker liquidity in a financial instrument that already meets the conditions of Article 2(1)(17) MiFIR.

As we have stated above, we believe there is no risk that Market Making Schemes will over-incentivise market participants provided the trading venues are given sufficient flexibility to adapt Market Making Schemes on a fair and non-discriminatory basis and in accordance with trading venue and Market Making Scheme rules. Furthermore, any concerns about an "over-supply" of liquidity can be simply addressed by trading venues rewarding liquidity providers for executions rather than for merely posting quotes.

The FIA Associations see no basis in Recital 62 or Article 48 to limit the Market Making Scheme requirement to liquid financial instruments. We also question whether the last sentence of Paragraph 47 follows from the primary legislation. We note that Article 48(2)(b) mandates that a trading venue have in place Market Making Scheme to ensure a sufficient number of investment firms entering into Market Making Agreements "*with the result of providing liquidity to the market on a regular and predictable basis*". There is no reference to coverage against disorderly trading conditions in either Article 48(2) or Article 17(3). In any event, it is not clear that additional liquidity alone would be sufficient to address disorderly trading conditions, which topic we have addressed elsewhere in this response and which ESMA's own analysis (see Discussion Paper, Section 4.1, Paragraph 28, page 205) also suggests is much broader than reduced liquidity or increased volatility.

<ESMA_QUESTION_284>

Q285: Would you support any other assessment of liquidity different to the one under Article 2(1)(17) of MiFIR? Please elaborate.

<ESMA_QUESTION_285>
No, except that the FIA Associations believe the distinction between liquid and illiquid financial instruments for the purposes of Articles 17 and 48 is irrelevant.

<ESMA_QUESTION_285>

Q286: What should be deemed as a sufficient number of investment firms participating in a market making agreement?

<ESMA_QUESTION_286>
As we have stated above, the FIA Associations see no basis for a "ceiling" on market maker liquidity, and therefore we believe ESMA should not set any limits on the number of investment firms able to participate in a Market Making Agreement/Scheme. We believe it should be open to all investment firms to choose to elect into a Market Making Agreement/Scheme in return for committing to obligations consistent with Article 17(3) of MiFID II.

Please see our additional comments in Question 280. The FIA Associations further emphasise the responsibility of the trading venue to act in a fair and non-discriminatory manner.

<ESMA_QUESTION_286>

Q287: What would be an appropriate market share for those firms participating in a market making agreement?

<ESMA_QUESTION_287>

As we have stated above, the FIA Associations see no basis for a "ceiling" on market maker liquidity, and therefore we believe ESMA should not set any limit on the appropriate market share for those firms participating in a Market Making Agreement/Scheme (please see our comments in Question 280).

<ESMA_QUESTION_287>

Q288: Do you agree that market making schemes are not required when trading in the market via a market making agreement exceeds this market share?

<ESMA_QUESTION_288>
The FIA Associations strongly disagree. As we have stated above, the FIA Associations see no basis for a "ceiling" on market maker liquidity, and therefore we believe ESMA should not set any limit on the appropriate market share for those firms participating in a Market Making Agreement/Scheme (please see our comments in Question 280).

<ESMA_QUESTION_288>

Q289: In which cases should a market operator be entitled to close the number of firms taking part in a market making scheme?

<ESMA_QUESTION_289>
The FIA Associations strongly believe there is no circumstance in which a market operator/investment firm operating a trading venue should be entitled to close the number of firms taking part in a Market Making Scheme. As we have stated above, it is paramount to fairness and a level playing field that any investment firm engaging in algorithmic trading to pursue a market making strategy must – and must be allowed to – enter into a Market Making Agreement with the market operator/investment firm operating a trading venue and have a choice to elect into a Market Making Scheme in return for committing to obligations consistent with Article 17(3) of MiFID II. Any concerns about an "over-supply" of liquidity can be simply addressed by trading venues rewarding liquidity providers for executions rather than for merely posting quotes.

Allowing market operators to close the number of firms taking part in Market Making Schemes facilitates vertical silo monopolies whereby issuers sometimes prevent independent market makers from competing to provide liquidity. This is contrary to key objectives under MiFID II concerning fairness, competition, transparency, and a level playing field, as well as being negative for market quality.

Please see our additional comments to Question 280.

<ESMA_QUESTION_289>

4.5. Order-to-transaction ratio (Article 48 of MiFID II)

Q290: Do you agree with the types of messages to be taken into account by any OTR?

<ESMA_QUESTION_290>
The FIA Associations[40] agree with ESMA's approach that "*all messages related to an order (submission, price and volume modifications and deletions*" should be taken into account under any order to transaction ratio ("OTR") regime. However, ESMA should clarify only messages an investment firm can actively control will be included in any calculation.

The purpose of introducing an OTR as required by Article 48(6) MiFID II is to ensure orderly trading conditions on trading venues by controlling the number of orders members may send to the matching engine of a trading venue in order to ensure the capacity of the latter is not exceeded. Because the objective is to restrict the behaviour of members, any OTR calculation should only include messages the member can actively control. Therefore, acknowledgment and confirmation messages relating to an order and sent by the trading venue to the member should be excluded.

Furthermore, the FIA Associations believe special attention should be given to the position of market makers having continuous quoting obligations as required under Article 17(3) MiFID II or under any legally binding Market Making Agreement or Market Making Scheme they have entered into with a trading venue. While market makers actively monitor and control the number of messages they send to the market, in certain circumstances they may be prohibited from reducing the number of messages to comply with the mandatory OTR regime because doing so would be contrary to their continuous quoting obligations. Therefore, bearing in mind the possibility of conflicting obligations, we strongly emphasise the need to provide an exemption for market makers from the application of the mandatory OTR regime as ESMA

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[40] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

has suggested (Paragraph 20 (ii), page 278). For additional arguments on the need for an exemption in the mandatory OTR regime for market makers, we refer you to the answers to Question 304.

<ESMA_QUESTION_290>

Q291: What is your view in taking into account the value and/or volume of orders in the OTRs calculations? Please provide:

<ESMA_QUESTION_291>
As the purpose of introducing an OTR is managing the utilisation of system capacity, the FIA Associations believe an OTR calculation should take into account the metric most likely to affect the utilisation of system capacity of a trading venue.

The FIA Associations believe that volume should be taken into account, which is in line with current market practice. Trading venues currently operating OTRs (for example EUREX[41] or XETRA[42]) or messaging efficiency systems (Chicago Mercantile Exchange[43]) include the volume of orders as parameter in its calculation. From a purely functional perspective, the number of trades that result from an order is outside a member's control. For example, in case of partial execution, an order will be split into several trades; this may affect the resulting OTR. Taking volume into account serves to correct distortions in the calculation of the OTR caused by partial execution. Additionally, from a business perspective a large order has more influence on the market than a small order and should therefore be given a higher weighting. A larger order will also have more impact on the messaging capacity of the system of a trading venue.

The FIA Associations do not believe the value of orders should be taken into account because value has no causal link with the number of orders sent to the matching engine. Furthermore, including the value may potentially render the calculation of any OTR more complicated, unpredictable and subject to constant changes as the "value" of an order will be subject to price fluctuations as a result of changes in the market price. Finally, none of the above mentioned OTR systems currently in place at trading venues take into account the value of orders in the calculation of the OTR, suggesting existing market practice has deemed this unnecessary.

The FIA Associations understand that ESMA is bound by the mandate given to it in Article 48(12)(b) MiFID II. However, that provision only mentions value as one possible metric besides others that may be relevant for calculating the OTR. The FIA Associations believe that the Level 1 text does not compel ESMA to include value as a metric for calculating the OTR.

<ESMA_QUESTION_291>

Q292: Should any other additional elements be taken into account to calibrate OTRs? If yes, please provide an explanation of why these variables are important.

<ESMA_QUESTION_292>
The FIA Associations are not aware of any other factor apart from the number and the volume of orders and the number of transactions that would be a relevant metric for the calculation of an OTR, except the

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[41] EUREX Circular January 2014, p. 5, available at: http://www.eurexchange.com/blob/exchange-en/642134/647520/5/data/concept_otr_12.pdf .
[42] XETRA, OTR calculation method, available at: http://xetra.com/xetra/dispatch/en/klistcontent/navigation/xetra/300_trading_clearing/100_trading_platforms/100_xetra/400_trading_parameter/100_order_to_trade_ratio?horizontal=page1_order_to_trade_ratio .
[43] CME Globex Messaging Efficiency Program, July 2014, available at: http://www.cmegroup.com/globex/files/revisedmep.pdf

consideration given to market makers given their necessarily high OTRs due to continuous quoting obligations.

<ESMA_QUESTION_292>

Q293: Do you agree with the proposed scope of the OTR regime under MiFID II (liquid cash instruments traded on electronic trading systems)?

<ESMA_QUESTION_293>
The FIA Associations agree with the scope of the OTR regime suggested by ESMA. MiFID II would only require a mandatory OTR regime for:

1. Cash instruments (excluding derivatives),
2. Traded on electronic venue, and
3. Which meet the requirement of a liquid instrument for which a liquid market exists within the meaning of Article 2(1)(17) MiFIR.

However, the FIA Associations strongly emphasise the need to determine the OTR at product level instead of instrument level to ensure a higher level of granularity, taking into account the specific characteristics of each product or group of products. This would enable tailored OTRs for each instrument and product taking into account factors such as different trading volume, volatility or frequency of quote-updates as a result of changes in the price of the underlying instrument. The Chicago Mercantile Exchange (CME) and EUREX already use this approach in their respective systems.

<ESMA_QUESTION_293>

Q294: Do you consider that financial instruments which reference a cash instrument(s) as underlying could be excluded from the scope of the OTR regime?

<ESMA_QUESTION_294>
The FIA Associations agree with ESMA's suggested approach of keeping instruments with an underlying reference cash instrument out of the scope of the mandatory OTR regime, as this is unnecessary for the reason ESMA states: "*any change in the OTR of the underlying … would affect the OTR of its derivatives.*"

In this respect, we believe many ETFs more closely resemble derivatives than equities in that prices fluctuate along with the prices of the underlying assets. Multiple underlying assets amplify this effect; therefore OTR regimes should apply a correction by exempting derivatives and ETFs.

<ESMA_QUESTION_294>

Q295: Would you make any distinction between instruments which have a single instrument as underlying and those that have as underlying a basket of instruments? Please elaborate.

<ESMA_QUESTION_295>
As indicated in our answer to Question 293, the FIA Associations believe a distinction should be made between different types of instruments but also between different products within the same range of instruments.

A higher level of granularity in determining the OTR for each instrument and product should be a guiding principle. This would enable tailored OTRs for each instrument and product with consideration for factors such as different trading volume, volatility or frequency of quote-updates as a result of changes in the price

of the underlying instrument. We would like to see any OTR regime closely follow existing market practice, such as the regimes currently operated EUREX and CME.

<ESMA_QUESTION_295>

Q296: Do you agree with considering within the scope of a future OTR regime only trading venues which have been operational for a sufficient period in the market?

<ESMA_QUESTION_296>
The FIA Associations agree with ESMA's suggested approach of only including in the scope of the mandatory OTR regime trading venues that are sufficiently established in the market. We also strongly believe the exemption should extend to new products launched by an existing trading venue.

In both these situations, venues and products need to have sufficient time to develop without facing limitations resulting from a mandatory OTR. The FIA Associations do not believe ESMA should be overly concerned about the potential for regulatory arbitrage, as there already exist differences between venues with OTR regimes in place and those without, and this does not materially impact the market.

However, the FIA Associations do not believe that a given period of time is an appropriate metric to make the assessment as to whether a venue or product is sufficiently established. Since the aim of this approach is to temporarily shield new trading venues (and, in our view, products) from the forces of competition, a more relevant metric would be to assess whether the trading venue (or product) has a particular market share (for example 20%), measured in transaction volumes.

Likewise, as the FIA Associations have stated elsewhere, we believe ESMA should maintain current practice in granting an exemption to market makers from any mandatory OTR regime. This will also help to reduce competitive pressure on new trading venues. New trading venues should be able to appoint market makers to attract liquidity without concern that the volume of orders they generate count toward OTRs.

<ESMA_QUESTION_296>

Q297: If yes, what would be the sufficient period for these purposes?

<ESMA_QUESTION_297>
As indicated in our answer to Question 297, the FIA Associations do not believe that a particular period of time would be an appropriate metric to assess whether a trading venue is exempt from the mandatory OTR regime. We believe that the size of the market share is the most relevant metric to make that assessment.

<ESMA_QUESTION_297>

Q298: What is your view regarding an activity floor under which the OTR regime would not apply and where could this floor be established?

<ESMA_QUESTION_298>
The FIA Associations believe ESMA should allow trading venues to apply a floor under which the OTR regime does not apply. Where trading venues currently operate OTRs (EUREX, XETRA and CME), they have in included this concept in their respective regimes because some participants have so little impact on system capacity that, without a floor, the trading venue would allocate unnecessary resources in monitoring.

However, the FIA Associations believe trading venues should establish this floor rather than ESMA, as the trading venues are the best positioned to make an appropriate assessment.

<ESMA_QUESTION_298>

Q299: Do you agree with the proposal above as regards the method of determining the OTR threshold?

<ESMA_QUESTION_299>
The FIA Associations do not believe ESMA's proposal is the most appropriate method for determining the OTR. We strongly believe that the determination of the OTR should be left to trading venues.

The purpose of introducing the OTR is to ensure orderly trading conditions on trading venues by controlling the number of orders members may send to the matching engine, thereby ensuring system capacity is not exceeded. The trading venue is best positioned to assess what level of messaging its systems can handle.

We believe establishing a multiplier (x) based on the average OTR observed on a trading venue for a group of instruments is a "one-size-fits-all" approach that does not sufficiently take into account differences between instruments and individual products in terms of trading volume, volatility or frequency of quote-updates.

Therefore, the FIA Associations believe ESMA should develop an alternative approach where it formulates key principles to which a mandatory OTR must adhere, but leaves it to trading venues to determine the OTR per instrument and per product based on what their systems can safely accommodate.

<ESMA_QUESTION_299>

Q300: In particular, do you consider the approach to base the OTR regime on the 'average observed OTR of a venue' appropriate in all circumstances? If not, please elaborate.

<ESMA_QUESTION_300>
The FIA Associations do not believe this proposed approach to be optimal for the following reasons.

First, the purpose of introducing an OTR is to ensure orderly trading conditions on trading venues by controlling the number of orders members may send to the matching engine of a trading venue in order to ensure the capacity of the latter is not exceeded. Past observations of the average OTR on a trading venue may provide little information on the utilisation of the current and future messaging capacity of a trading venue.

Second, the average observed OTR of a trading venue in the past period may be quite different from and lower than the maximum OTR that can be handled by that trading venue's system capacity. This may unduly limit the abilities of trading venues to make maximum use of existing capacity.

Third, if a trading venue must apply a mandatory OTR that is based solely on past observations, it is inherently limited in its ability to expand its messaging capacity and grow to meet the demands of members and participants. Therefore, an OTR based on past observations may artificially reduce competition between trading venues. Any new messaging capacity a trading venue adds to its system may not be fully used if that would lead to an OTR higher than what is authorised.

Therefore, we believe ESMA should develop an alternative approach whereby it formulates key principles to which a mandatory OTR must adhere but leaves it to trading venues to determine the OTR per instrument and per product according to what their systems can safely accommodate.

<ESMA_QUESTION_300>

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Q301: Do you believe the multiplier x should be capped at the highest member's OTR observed in the preceding period?

<ESMA_QUESTION_301>
The FIA Associations do not believe that a multiplier (x) should be determined or capped.

As we indicated above, the purpose of introducing an OTR is to ensure orderly trading conditions on trading venues by controlling the number of orders members may send to the matching engine of a trading venue in order to ensure the capacity of the latter is not exceeded.

The highest member's OTR observed in the preceding period will give an indication of what an acceptable OTR may be for that particular member, on the basis of that member's systems, but may not provide sufficient information to determine what an acceptable OTR level should be for the systems of the trading venue as a whole.

<ESMA_QUESTION_301>

Q302: In particular, what would be in your opinion an adequate multiplier x? Does this multiplier have to be adapted according to the (group of) instrument(s) traded? If yes, please specify in your response the financial instruments/market segments you refer to.

<ESMA_QUESTION_302>
The FIA Associations do not believe that a multiplier (x) is an appropriate tool to determine the OTR regime for a particular trading venue. We believe trading venues are the best positioned to make an appropriate assessment, but in any event, we believe it is essential that any OTR regime have sufficient flexibility to allow for the development of distinctive and potentially different OTRs at the level of each product, if necessary, to take into account different trading volumes, volatility or frequency of quote-updates.

<ESMA_QUESTION_302>

Q303: What is your view with respect to the time intervals/frequency for the assessment and review of the OTR threshold (annually, twice a year, other)?

<ESMA_QUESTION_303>
The FIA Associations agree that ESMA should establish a minimum frequency on which trading venues are required to review OTR thresholds. We acknowledge in Germany this review currently takes place every 12 months under the German HFT law, but our members would ideally see a more frequent review schedule every six months. The FIA Associations believe twice a year assessment strikes a good balance between the need for the OTR regime to reflect up-to-date market developments versus the resources a trading venue has to commit to making this review. Finally, we believe trading venues should not be prevented from reviewing the adequacy of the OTR on a more frequent basis if it deems it necessary.

<ESMA_QUESTION_303>

Q304: What are your views in this regard? Please explain.

<ESMA_QUESTION_304>
The FIA Associations strongly believe that market makers should be completely exempt from any OTR regime. Therefore, we support the option (ii) of maintaining the current practice in granting an exemption for market makers and other liquidity providers.

A market maker provides a service to the market in the form of additional liquidity by continuously sending orders into the market to update prices and provide two-sided quotes. A market maker cannot control

how many of these orders will be matched by other members of the trading venue and will result in actual transactions. Therefore, a market maker can control only the level of messaging but not the OTR that level of messaging will generate.

Applying a mandatory OTR regime to market makers may lead to a situation where complying with a continuous quoting obligation may lead to a violation of the OTR (or vice versa). This would create potentially conflicting obligations for market makers, which we do not believe was the intent of the legislator.

We also believe the obligation to provide liquidity to markets should prevail over the obligation to comply with a mandatory OTR regime, as long as this does not put undue stress on the systems of a trading venue.

Additionally, as indicated in our response to Question 296, providing an exemption for market makers from a mandatory OTR regime may significantly reduce competitive pressure on new trading venues or existing trading venues launching new products.

Therefore, the FIA Associations strongly encourage ESMA to include in the mandatory OTR regime an exemption for market makers subject to continuous quoting obligations under Article 17(3) of MiFID II.

<ESMA_QUESTION_304>

4.6. Co-location (Article 48(8) of MiFID II)

Q305: What factors should ESMA be considering in ensuring that co-location services are provided in a ‘transparent’, ‘fair’ and ‘non-discriminatory’ manner?

<ESMA_QUESTION_305>
The FIA Associations[44] believe ESMA should consider the following factors to ensure transparent, fair and non-discriminatory co-location services offered by trading venues.

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[44] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

Non-discriminatory pricing

In order to ensure co-location services are transparent, fair and non-discriminatory, trading venues must publish or make available on demand their commercial policies, including the list of prices as well as the objective conditions for accessing the co-location services. In evaluating reasonableness, trading venues should offer services (a) with rates that are not so prohibitive that only a small percentage of members who might benefit could afford them, and (b) that are priced comparably to similar services offered elsewhere in the market and do not unreasonably benefit from a trading venue's unilateral control over its own data, facilities or other infrastructure.

The concept of equidistant cabling connections

Trading venues should optimally offer equidistant cabling connections to eliminate latency advantages of any participant over another. This is the fairest means by which co-location services should be offered. At a minimum, trading venues should disclose the latency numbers of various co-location services so that market participants have the information required to make their own informed assessment and decision of whether or not to make use of these services.

Transparency of data centre agreements

Trading venues should make available clear documentation about their products and services with all relevant information including pricing. Under no circumstances should trading venues be allowed to inform only certain market participants of the existence of certain services. The fees charged to market participants must be uniform between market participants using the same services and should not discriminate against different classes of market participants – they should offer their services to all qualified participants on identical and transparent terms.

Since the volumes on the various equity and futures markets are nearly all electronically traded, the connectivity to trading venue matching engines is a critical element of the market structure. Therefore, the FIA Associations believe it is essential for ESMA and NCAs to oversee co-location services to ensure the following:

- Trading venues have robust testing and certification procedures to ensure the functionality and risk management controls of the connecting market participant meet the pre-determined testing criteria.
- Trading venues ensure a level playing field among all those who connect to the trading venue matching engine. They oversee all connections and latency measurements to ensure the integrity of the market.
- Trading venues oversee the physical environment to ensure the market is operating in a secure, protected and controlled manner.
- Trading venues allow any market participant who meets the technological requirements of directly connecting to the matching engine to subscribe to the co-location services. The pricing for the co-location services are the same for all market participants, regardless of volumes, and are based on physical space and electrical usage.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

Finally, the FIA Associations would like to emphasise that eliminating co-location at trading venues would not eliminate co-location as a practice. Rather, it would push the practice out from under oversight by trading venues and regulators and into the potentially less regulated arena of private landowners around and near trading venues servers.

<ESMA_QUESTION_305>

4.7. Fee structures (Article 48 (9) of MiFID II)

Q306: Do you agree with the approach described above?

<ESMA_QUESTION_306>
The FIA Associations[45] agree with the approach contemplated by ESMA. We believe regulation should only intervene in commercial arrangements between parties if these arrangements generate certain risks that may affect the market in its entirety. Therefore, we agree that regulation should only intervene in the fee structures used by trading venues if those structures incentivise trading behaviour leading to disorderly market conditions, or if the fee structure is not sufficiently transparent for market participants to make an information decision regarding their trading behaviour.

<ESMA_QUESTION_306>

Q307: Can you identify any practice that would need regulatory action in terms of transparency or predictability of trading fees?

<ESMA_QUESTION_307>
The FIA Associations cannot identify any current practice that would require regulatory action.

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[45] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

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<ESMA_QUESTION_307>

Q308: Can you identify any specific difficulties in obtaining adequate information in relation to fees and rebates that would need regulatory action?

<ESMA_QUESTION_308>
The FIA Associations believe it is essential for trading venues to have an obligation to be transparent about information relating to fees and rebates. We agree with ESMA that trading venues should publish all execution fees, ancillary fees and any rebates available on their website in an easy to find place or in one comprehensive document that is made available promptly on demand.

However, we would like to emphasise that transparency obligations should not be limited solely to fees and rebates but also to other services or advantages conferred to market participants. We support a marketplace that promotes transparency to all market participants in all aspects of operations, including but not limited to:

- Transparency into the process by which working orders (displayed and not displayed) are handled on all trading venues, including regulated markets ("RMs"), multi-lateral trading facilities ("MTFs"), and systematic internalisers ("SIs"),
- Transparency into all trades on all trading venues, including RMs, MTFs, and SIs,
- Transparency into the process by which orders are matched for execution by the trading venue, including the matching algorithm used by the trading venue and any priorities one order may have over another within the matching algorithm,
- Transparency into the fees associated with all executions of all trades on a trading venue,
- Transparency into the services provided by the trading venue to its participants, including pre- and post-trade risk controls, market data feeds, trade execution, co-location, and network connectivity,
- Transparency into the order types available to market participants on a trading venue, including details on how each order type interacts with the market, and
- Transparency into the trading venue's trade "bust/adjust" policy, including when it may be invoked, and the potential actions the trading venue may take.

<ESMA_QUESTION_308>

Q309: Can you identify cases of discriminatory access that would need regulatory action?

<ESMA_QUESTION_309>
The FIA Associations are only aware of incidents in the foreign exchange ("FX") markets.

In FX, trading venues sometimes charge lower fees to investment firms associated to bank and credit institutions compared to independent investment firms.

Likewise, in some instances rules are not published or made centrally available, such that many participants are unaware that most FX markets have a "last look" function, whereby a liquidity provider has the opportunity to reject a trade within a given time interval (i.e. even after giving a price quote that has been hit, the liquidity provider can choose not to deal, which removes trade certainty for the investor). Last look functionality is almost never specified in the rules and conditions applicable to trading on the relevant trading venue.

<ESMA_QUESTION_309>

Q310: Are there other incentives and disincentives that should be considered?

<ESMA_QUESTION_310>
The FIA Associations acknowledge there is discussion around the 'maker-taker' model as well as the topic of payment for order flow (PFOF). We do not take a view either in favour of or against these models because our members have diverging opinions, but we set out some general points below.

The maker-taker model is relatively simple: the resting (passive) order receives a rebate in exchange for making liquidity available, while the order that crosses the spread (aggressive) pays a fee as it takes liquidity. The rebate is offered to the passive order to encourage displayed liquidity. The difference between the fee and the rebate is revenue kept by the exchange.

In the case of PFOF, certain brokers sell order flow to investment firms who are able to execute the orders at the best level possible. These orders are often executed outside the market in dark pools.

The maker-taker model and PFOF are linked, some argue, because if the maker-taker model is prohibited while PFOF is allowed, then liquidity will migrate automatically from lit markets to non-lit markets, thereby decreasing transparency.

We note that it appears from ESMA's proposal that maker-taker models do not fall under the permissible scope for rebates (which ESMA believes "*should only be allowed as far as they are linked to the provision of a specific service*," such as market making). Moreover, the FCA recently expressed its view that PFOF should not be permissible.[46]

Maker-taker model

Various schools of thought exist in the market and industry concerning the maker-taker model. Whether investment firms are in favour or against maker-taker very much depends on the business model.

The proponents of the maker-taker model argue that this model has the following advantages:

1. It creates an incentive for a market maker to provide liquidity to the market as the rebates it receives offset some of the costs he incurs for providing this liquidity.
2. This additional source of revenue enables a market maker to quote tighter spreads.
3. It encourages a market maker to provide real liquidity as it will only receive the rebate when orders are filled.
4. The taker fee is normally sufficiently high to deter non market makers using high frequency trading technology from taking the liquidity while the taker fee is sufficiently low not to deter long-term investors from trading on the markets.
5. It encourages competition amongst trading venues. The maker-taker offers an alternative to current rebate systems used by trading venues based on volumes, which favours incumbents compared to new entrants.

The critics of the maker-taker model, on the other hand, argue that maker-taker has the following disadvantages:

1. It creates an artificial and opaque transfer of profits and costs amongst market participants. The maker quotes an artificially low spread knowing he will gain profits from rebates while the taker –

46 Financial Conduct Authority, Guidance on the practice of 'Payment for Order Flow', May 2012, available at: http://www.fca.org.uk/static/pubs/guidance/fg12-13.pdf
Financial Conduct Authority, Best execution and payment for order flow thematic review report, July 2014, available at: http://www.fca.org.uk/news/tr14-13-best-execution-and-payment-for-order-flow

often a broker – will pass the additional fees on the end customer. Ultimately it is doubtful whether the end customer fully benefits from the lower spread quoted.

2. It can lead to artificially low spreads that do not reflect the true costs and risks associated with market making. Specific rebates for designated market makers, on the other hand, accurately price the additional risk market makers are taking.
3. It exploits and reinforces market fragmentation by allowing trading venues to attract liquidity. Normally, competition between trading venues must improve the service to the end customer. In the case of the maker-taker model, competition between trading venues may redistribute costs and benefits between market participants, so that end customers may be worse off. This may ultimately lead to liquidity migrating to non-lit markets.
4. It becomes very difficult to estimate the true total costs of execution for the takers. Smart order routers need to be more complex and complicated, which requires a lot of resources. The resulting fragmentation and artificial pricing does not create more transparent markets, but actually incentivises the flight of market participants to less complex non-lit platforms.

Payment-for-order-flow

As mentioned earlier, linked to the maker-taker model is the question of PFOF.

Proponents of PFOF argue it has the following advantages:

1. The additional revenue stream of PFOF (whereby an investment firm pays a broker for flow) creates the possibility for small-to-medium size investment firms to do business they might otherwise never see due to commercial incentives for brokers to send client flow to the execution desks of large institutions with which the broker already has other channels of revenue.
2. In essence, PFOF is a factor that levels the playing field for small-to-medium size investment firms competing to provide liquidity and execute client order flow.

Critics of PFOF argue that it has several major flaws:

1. It creates a clear conflict of interest for brokers between routing the order in the most profitable way and ensuring best execution of the orders of clients. As noted above, the FCA has recently made this position explicit.
2. It creates a barrier to entry for new market makers, as market makers cannot compete to fill the orders. In practice only very large market makers can afford to buy the order flow from brokers who will often sell the entire order flow so that only large market makers can fill the orders. For example, if a broker sells his flow of orders to a market maker exclusively, this market maker will execute the order at a price no worse than the price for that instrument on the trading venue. The broker will have guaranteed best execution to his client while the market maker will have guaranteed exclusivity on that order flow, thereby increasing his profitability. This means that market maker could then cross-subsidise his other market making strategies by offering tighter spreads than his competitors on other financial instruments to reduce competition on those other markets.
3. The impact for the overall market is negative as this leads to more orders being filled on non-lit markets, thereby affecting the overall price formation. This may ultimately create a feedback loop effect leading to more trades done on non-lit markets due to the decreased price formation on lit ones.

The FIA Associations' Position

As stated above, the FIA Associations do not take a view either in favour of or against the maker-taker model or PFOF because our members have diverging opinions on the matter.

<ESMA_QUESTION_310>

Q311: Do any of the parameters referred to above contribute to increasing the probability of trading behaviour that may lead to disorderly and unfair trading conditions?

<ESMA_QUESTION_311>
Subject to our comments on the need for fair, transparent and non-discriminatory pricing of exchange services, the FIA Associations take a sanguine view on fee arrangements.

As a general matter, the FIA Associations do not believe the structural parameters of fee schedules are significant inducements one way or another to trading behaviour that might lead to an increased probability of disorderly trading conditions. In most cases, trading venues establish fee structures in reasonable dialogue with their commercial audiences, such that fee structures should reflect a rational approach to charging for services based on market participants' actual and bona fide use of such services. To the extent any market participant may be incentivised to engage in non bona fide trading behaviour in order to secure better pricing (e.g. by intentionally trading specific volume or value in order to trigger bucket or tranche pricing as further discussed below), this should be investigated on the merits and dealt with, if applicable, under relevant anti-market abuse provisions.

In our view, certain regulatory requirements or prohibitions, such as an overly restrictive view on the "exceptional circumstances"/equivalent exclusions under which a market maker may cease continuous quoting (see Section 4.4, Questions 275-279), are more likely to cause disorderly trading conditions than the parameters of fee schedules.

<ESMA_QUESTION_311>

Q312: When designing a fee structure, is there any structure that would foster a trading behaviour leading to disorderly trading conditions? Please elaborate.

<ESMA_QUESTION_312>
Please see the FIA Associations' comments to Question 310 above.

<ESMA_QUESTION_312>

Q313: Do you agree that any fee structure where, upon reaching a certain threshold of trading by a trader, a discount is applied on all his trades (including those already done) as opposed to just the marginal trade executed subsequent to reaching the threshold should be banned?

<ESMA_QUESTION_313>
As a general matter, the FIA Associations do not believe the structural parameters of fee schedules are significant inducements one way or another to trading behaviour that might lead to increasing the probability of disorderly trading conditions. We believe trading venues should have the discretion to establish fee structures in reasonable dialogue with their commercial audiences based on the needs of specific instruments and markets. We feel current fee structures generally reflect a rational approach to charging for services based on market participants' actual and bona fide use of such services.

However, while the FIA Associations do not believe so-called "cliff edge" pricing should be banned, not all of our members like this type of pricing for the following reasons.

First, the critics of cliff edge pricing believe it rewards trading volume quantity over quality. They prefer, in line with ESMA's view, to see rebates granted to market makers having quoting obligations, as this clearly enhances market quality.

Second, there is also some concern that cliff edge pricing incentivises excessive messaging in order to achieve the required volume to benefit from the rebate. This could create improper incentives, which are difficult to reconcile with the obligation for trading venues to have prudent management of the messaging capacity as required by Article 48(6) MiFID II.

Finally, critics say this type of fee reduces competition among trading venues (as incumbents can lock in liquidity to limit competition) and among investment firms (larger firms more easily access this type of rebate, which lowers their marginal cost of trading compared to smaller firms that do not trade the volume required).

However, on balance we believe this type of fee structure is not such a material barrier to competition that market forces cannot adequately cope with it, and we reiterate that we believe trading venues should be permitted the discretion to establish fee structures in reasonable dialogue with their commercial audience.

<ESMA_QUESTION_313>

Q314: Can you identify any potential risks from charging differently the submission of orders to the successive trading phases?

<ESMA_QUESTION_314>
The FIA Associations are not aware of any particular risks associated with charging differently the submission of orders to the successive trading phases.

<ESMA_QUESTION_314>

Q315: Are there any other types of fee structures, including execution fees, ancillary fees and any rebates, that may distort competition by providing certain market participants with more favourable trading conditions than their competitors or pose a risk to orderly trading and that should be considered here?

<ESMA_QUESTION_315>
The FIA Associations are not aware of any particular issues in practice.

<ESMA_QUESTION_315>

Q316: Are there any discount structures which might lead to a situation where the trading cost is borne disproportionately by certain trading participants?

<ESMA_QUESTION_316>
The FIA Associations do not have a view on this topic.

<ESMA_QUESTION_316>

Q317: For trading venues charging different trading fees for participation in different trading phases (i.e. different fees for opening and closing auctions versus continuous trading period), might this lead to disorderly trading and if so, under which circumstances would such conditions occur?

<ESMA_QUESTION_317>
The FIA Associations do not believe this type of trading fee would lead to disorderly trading. Therefore, we do not think this is an area where regulatory action should be undertaken.

<ESMA_QUESTION_317>

Q318: Should conformance testing be charged?

<ESMA_QUESTION_318>
The FIA Associations believe trading venues should not charge for technical conformance testing, which is a mandatory step to confirm a system's functionality while interacting with a trading venue. This process is often guided by a script of tests provided by the trading venue and is performed in a trading venue-provided test environment to simulate the production trading environment.

<ESMA_QUESTION_318>

Q319: Should testing of algorithms in relation to the creation or contribution of disorderly markets be charged?

<ESMA_QUESTION_319>
As the FIA Associations have stated in our responses to testing questions in Section 4.2 on Organisational Requirements for Investment Firms and Trading Venues, we believe this type of testing should not be made compulsory but should rather be proposed as one option in a range of several options available to investment firms for meeting their obligation to have adequate and appropriate testing of their algorithms.

The FIA Associations agree with ESMA that investment firms should make use of trading venues' non-live testing environments. However, as stated in our response to Question 199, currently many trading venues' non-live testing environments do not adequately reflect realistic market circumstances or have capacity adequate to the needs of investment firms. Furthermore, making use of these non-live environments is often prohibitively expensive, creating improper incentives for trading venues in the event this kind of testing becomes mandatory.

The FIA Associations encourage trading venues to develop more robust test environments that more closely simulate trading in the production environment. However, the FIA Associations believe fees for the testing of algorithms should not be a profit generating product for trading venues, as the testing is done to comply with regulatory obligations. The total costs for investment firms of complying with regulatory requirements should remain reasonable. Therefore any fees charged by trading venues for testing should be nominal and only cover the costs of providing the testing services.

<ESMA_QUESTION_319>

Q320: Do you envisage any scenario where charging for conformance testing and/or testing in relation to disorderly trading conditions might discourage firms from investing sufficiently in testing their algorithms?

<ESMA_QUESTION_320>
Here, ESMA has highlighted an area of major concern to the FIA Associations. If the costs for complying with the mandatory testing obligations are unreasonable or disproportionate, it will absolutely discourage some market participants from investing sufficiently in testing their algorithms, and this would be negative for the market as a whole. Therefore, the total costs for investment firms of complying with regulatory requirements should remain reasonable.

<ESMA_QUESTION_320>

Q321: Do you agree with the approach described above?

<ESMA_QUESTION_321>

As set out in our response to Question 280, the FIA Associations take a different view on the optimal interaction between Market Making Agreements and Market Making Schemes.

The FIA Associations understand that Article 17(3) and (4) of MiFID II requires an investment firm to enter into a Market Making Agreement whenever it is pursuing a market making strategy in any financial instrument. Pursuant to Article 48(2)(a) of MiFID II a trading venue has the mirror obligation to have in place a written agreement with any investment firm pursuing a market making strategy. Article 48(2)(b) of MiFID II requires a trading venue (where appropriate) to have in place Market Making Schemes to ensure that a sufficient number of investment firms participate in such scheme and provide liquidity, irrespective of whether they are bound by Article 17(3) of MiFID II.

First, therefore, the FIA Associations would challenge ESMA's analysis in Paragraph 43 sub-Paragraph (i), the second sentence of which limits the application of Articles 17 and 48 to a sub-set of financial instruments. We do not see a basis in either article and related recitals to limit their application to all financial instruments -- save for the second sentence of Article 48(9), which applies only to "*individual shares or a suitable basket of shares*" – but we do not consider this as requiring such limitation.

Second, the FIA Associations strongly disagree with ESMA's implicit contention that market maker liquidity is somehow lesser than other liquidity. Liquidity coming from market makers may not be "natural," but so long as market makers have quoting obligations, the resulting liquidity is "real." Furthermore, liquidity – a measure of market quality - attracts liquidity. The presence of market makers improves the quality of the market because they contribute to price formation transparency, market efficiency and competition. This increased liquidity and quality will in turn provide an incentive to other market participants to trade on that market. These market participants will increase liquidity through their trading. Therefore, we believe that capping market making liquidity would have a negative effect on the market as well as being anti-competitive.

Third, the FIA Associations see no basis in Article 48 for the draft regulatory technical standards to mandate a "ceiling" on market maker liquidity. We understand it is ESMA's view that if too much volume comes from market makers, then there's something wrong with the incentive scheme offered by the trading venue. It may, for example, be over-incentivising the liquidity resulting from market makers, which may give a misleading impression of liquidity in the market.

However, new platforms need to be able to rely on incentivised liquidity from market makers as they start up – without this, no nascent regulated market or MTF would be able to get off the ground. We believe constraining new trading venues' ability to incentivise liquidity in all financial instruments would seriously undermine key objectives of the MiFID II and MiFIR legislation.

Moreover, we see practical impediments to deciding how much liquidity is sufficient for any given financial instrument. Liquidity as a measure may change quickly and significantly, and any assessment of liquidity is always backward looking.

Fourth, the FIA Associations are concerned ESMA's approach would create a mismatch in scope between market making agreements (all financial instruments) and market making schemes (only financial instruments with insufficient liquidity) and potentially create a two-tier structure: a 'regulatory floor' agreement setting out the obligations of the market maker and separate commercial incentive schemes mirroring existing market practice. The potential scope mismatch highlighted above may lead to the situation that a market maker is only subject to obligations without benefits, for example, when it concerns a financial instrument where there are sufficient market makers. Such a structure would ran counter to the basic principle that the obligations a market maker assumes should be proportional and commensurate to the benefits enjoyed.

Fifth, with regard to the requirement that trading venues be able to prevent access and/or delete orders or transactions that have occurred, the FIA Associations emphasise that this must be in accordance with established, publicly available rulebooks and policies, so that trading venues cannot exercise any arbitrary discretion over access, orders or transactions that could threaten a fair and level playing field or trade certainty.

Finally, the FIA Associations believe the proposal to require trading venues to publicly disclose an investment firm's non-compliance with a Market Making Scheme would be disproportionate and unusual. Public disclosure of breaches of a trading venue's rules is made only in cases of very serious breaches such as the default of member. We believe it appropriate only for a trading venue to disclose the terms and conditions of a Market Making Scheme and the identity of investment firms participating in the scheme.

The FIA Associations' suggested approach

As the FIA Associations have stated before, we support the principle of enhanced market making obligations, provided firms committing to such obligations are facilitated in doing so through due regard for the four factors essential for these additional obligations: (1) technology, (2) risk management, (3) incentives, and (4) temporary contractual excuse from performance during circumstances of distress.

We strongly suggest that ESMA develops rules that are sufficiently flexible to be applied to a variety of different markets and are based on several core principles which should underpin any relation between trading venues and market makers, as follows:

First, all trading venues should offer Market Making Agreements to investment firms pursuing a market making strategy within the meaning of Article 17(4) of MiFID II.

Second, each and every Market Making Agreement should be underpinned by a Market Making Scheme. We believe sub-paragraphs (iii) and (iv) of ESMA's analysis support the FIA Associations' interpretation that Market Making Agreements are necessary components of a Market Making Scheme, and that an investment firm cannot participate in a Market Making Scheme without a formal agreement with the market operator/investment firm operating a trading venue.

By ensuring Market Making Agreements and Market Making Schemes are aligned, ESMA would preserve commercial choice on the part of market participants. Investment firms captured under by Article 17(3) of MiFID II would have a choice either to participate in Market Making Schemes or exit the activity. Investment firms not captured would also have a choice to elect into the Market Making Scheme in return for committing to obligations consistent with Article 17(3) of MiFID II.

Third, obligations imposed on a market maker should be proportionate to the benefits received and should take into account the liquidity provided to the market.

Finally, each trading venues should have the flexibility to be able to determine the commercial terms of any Market Making Scheme. Rather than imposing a ceiling on market maker liquidity, we would propose that the market operator/investment firm operating a trading venue retain the ability to dial-down Market Making Scheme incentives where there is sufficient liquidity. This is already common practice: trading venues already fine-tune incentives for market makers based on the liquidity of the instrument(s) to ensure there is no "over-supply," as there is no commercial rationale for paying incentives to market makers where sufficient liquidity already exists. A good and current example of this is ICE/Liffe, which has announced reduced incentives in short term interest rate products– where liquidity is at its greatest – and increased incentives in less liquid, longer-dated interest rate contracts to encourage more liquidity provision there.

The FIA Associations believe there is no risk that these schemes will over-incentivise market participants provided the trading venues are given sufficient flexibility to adapt Market Making Schemes on a fair and non-discriminatory basis and in accordance with trading venue and Market Making Scheme rules. Furthermore, any concerns about an “over-supply” of liquidity can be simply addressed by trading venues rewarding liquidity providers for executions rather than for merely posting quotes.

ESMA has set out four principles in its specific proposal that should apply to the fee structures applicable to Market Making Schemes. The FIA Associations have outlined our view on these principles:

Scope: liquid instruments (Article 2(1)(7) of MiFIR) without sufficient market making agreements (Paragraph 30.i)

As the FIA Associations have stated above, we believe all trading venues have to offer Market Making Agreements to investment firms operating market making strategies. To prevent a two-tier structure, each Market Making Agreement must be underpinned by a Market Making Scheme. We believe trading venues should be able to determine what those Market Making Schemes look like from a commercial perspective.

As set out in our response to Question 284, the FIA Associations see no clear basis in the Level 1 text for ESMA’s proposal to limit Market Making Schemes/incentives to liquid instruments. We consider any such limitation as illogical and impractical. It would be difficult to justify requiring a trading venue to incentivise additional market maker liquidity in a financial instrument that already meets the conditions of Article 2(1)(17) MiFIR.

As we have stated elsewhere in this response, we believe there is no risk that Market Making Schemes will over-incentivise market participants provided the trading venues are given sufficient flexibility to adapt Market Making Schemes on a fair and non-discriminatory basis and in accordance with trading venue and Market Making Scheme rules. Furthermore, any concerns about an “over-supply” of liquidity can be simply addressed by trading venues rewarding liquidity providers for executions rather than for merely posting quotes.

Effective measures to monitor performance (Paragraph 30.ii)

We agree with ESMA that trading venues should have in place effective systems in place to monitor the liquidity that is provided and compliance by market makers with their quoting obligations. This is already current market practice. Therefore, we do not consider additional regulatory action is needed here.

Trading venues should have a system of penalties in place (Paragraph 30.iii)

The FIA Associations fundamentally disagree with the proposal concerning penalties. While we recognise the activity of market making is changing from a purely commercial model, as it currently is, to a regulatory model under MiFID II, the economics do not fundamentally change: market makers are willing to bear the risk of providing liquidity to the market in exchange for the trading venues offering appropriate incentives for this activity. Failure by a market maker to meet obligations will result in not receiving these incentives.

With respect to such a failure constituting a regulatory breach, we have suggested in our response to Question 280 that ESMA include a condition in the regulatory technical standards that trading venues should provide a reasonable time period in which investment firms may remedy a remediable breach of a Market Making Agreement. It should be clear that a market maker would only be in breach of a regulatory obligation if its breach was not capable of remedy or if after a reasonable period of time it had failed to

remedy such breach. This is consistent with ESMA's sentiment that consequences should only trigger when a failure is on a "systematic basis" (page 286).

Following on this point, we cannot stress strongly enough that imposing a fine or economic penalty for a market maker's failure to meet obligations, on top of the missed incentives (in effect a double penalty), will have a profoundly negative impact on the business case of providing liquidity. This may cause existing investment firms operating market making strategies to reconsider or even to give up such strategies.

When a market maker fails to receive incentives, trades are per se less profitable and sometimes even loss making. Thus, there is already sufficient economic incentive for market makers to perform according to their obligations. Penalising them further with additional fines, especially in a regulatory context where investment firms obligated under Market Making Agreements have significantly less discretion as to when to cease quoting, will make the same trades almost without doubt loss-making, at which point no rational business person would choose to continue this activity. A penalty system will also deter new entrants from seeking a role as a market maker, as they may have difficulties meeting liquidity provision obligations when starting up. While missing revenue is already quite challenging, facing additional fines may put them off entirely, thereby significantly reducing competition among market makers. Therefore, imposing fines and penalties on market makers who do not comply with their liquidity obligations will very likely achieve a result that is contrary to ESMA's ultimate objective of stabilising the liquidity provided to the market by deterring potential new market makers and potentially reducing the number of existing market makers.

Trading venues should keep records of penalties (Paragraph 30.iv)

See our comments above with respect to a system of penalties.

<ESMA_QUESTION_321>

Q322: How could the principles described above be further clarified?

<ESMA_QUESTION_322>
Please see the FIA Associations' comments in response to Question 321 above. An essential principle of any Market Making Scheme should be that the obligations imposed on a market maker are proportionate to the benefits conferred. The rebates and incentives given to a market maker must therefore take into account and be proportionate to the (1) risks assumed, (2) the quality of the liquidity provided to the market and (3) the size and nature of the obligations imposed.

<ESMA_QUESTION_322>

Q323: Do you agree that and OTR must be complemented with a penalty fee?

<ESMA_QUESTION_323>
The FIA Associations agree that a penalty fee could complement any mandatory OTR regime for in-scope instruments (see Question 293, page 276 of the Discussion Paper). This is consistent with current market practice, where many trading venues already have policies addressing message rates that have evolved over the past several years into effective mechanisms for controlling excessive messaging.

Typically, these policies are two-tiered in order to address two different aspects of message rate limits. The first level of limits is usually calculated and enforced on a daily or monthly basis as a means to deter market participants from consistently sending orders that are unlikely to be matched for execution. Although specific implementations of such a policy differ among trading venues, repeated violations of the policy typically leads to an additional fee, which acts as a deterrent to similar behaviour in the future as well as to

recoup the costs incurred by the trading venue to maintain systems capable of handling high levels of messaging.

The second level of limits is usually calculated and enforced on a real-time basis to prevent market participants from sending a large number of orders in a short enough period of time as to potentially harm the integrity of the trading venue. This limit is usually implemented as a short-term hard limit that prevents an offending market participant from sending additional orders for some amount of time.

It is difficult to standardise these types of policies across trading venues for the diversity of trading systems and products. Any regulation in this area should acknowledge the differences in markets and give trading venues the flexibility to configure their messaging policies, keeping in mind the unique characteristics of their products and the way they are traded. Requiring a messaging policy but allowing trading venue-by-trading venue and product-by-product flexibility will ensure the sound functioning of a liquid marketplace while meeting the objectives of ESMA.

Additional fees or penalties should in any case not be imposed on any investment firm (not limited to market makers) when the breach of the OTR is the result of an exceptional circumstance within the meaning of Article 17(3) MiFID II. Under no circumstances do we believe a breach of an OTR should be sanctioned through the imposition of a trading ban or trading limitation on a market participant, as this could create additional and unnecessary risk.

Finally, we reiterate our statement that market makers with continuous quoting obligations under Article 17(3) MiFID II should be exempted from the scope of the mandatory OTR regime as we indicated in our answer to Question 304. A market maker cannot control or anticipate how many of its orders will be matched by other members of the trading venue and will result in actual transactions. A market maker can control its level of messaging but not the OTR this level of messaging will generate.

<ESMA_QUESTION_323>

Q324: In terms of the approach to determine the penalty fee for breaching the OTR, which approach would you prefer? If neither of them are satisfactory for you, please elaborate what alternative you would envisage.

<ESMA_QUESTION_324>
The FIA Associations strongly prefer Option A for the reasons stated in our answer to Question 323 above.

The purpose of introducing an OTR as required by Article 48(6) MiFID II is to ensure orderly trading conditions on trading venues by controlling the number of orders members may send to the matching engine of a trading venue in order to ensure the capacity of the latter is not exceeded. In this case, a homogenous methodology applicable to all trading venues may in fact create conditions for disorderly trading conditions, as each platform and its products can vary greatly.

Moreover, trading venues that have made investments in order to have more robust system with larger messaging capacity should be able to apply different OTRs depending on the capacity of their systems.

<ESMA_QUESTION_324>

Q325: Do you agree that the observation period should be the same as the billing period?

<ESMA_QUESTION_325>
The FIA Associations agree with this approach.

<ESMA_QUESTION_325>

Q326: Would you apply economic penalties only when the OTR is systematically breached? If yes, how would you define "systematic breaches of the OTR"?

<ESMA_QUESTION_326>
The FIA Associations generally agree and would defer to the trading venues as to how to define "systematic breaches."
<ESMA_QUESTION_326>

Q327: Do you consider that market makers should have a less stringent approach in terms of penalties for breaching the OTR?

<ESMA_QUESTION_327>
The FIA Associations agree with this approach. As stated above, we believe that market makers subject to a continuous quoting obligation for a proportion of a trading venue's trading hours that have entered into a binding written agreement as required under Article 17(3) of MiFID II should be exempt from any OTR regime. We agree with ESMA that any future OTR regime should preserve the market practice of permitting market makers to submit orders beyond the pre-established limit without surcharge.

<ESMA_QUESTION_327>

Q328: Please indicate which fee structure could incentivise abusive trading behaviour.

<ESMA_QUESTION_328>
We are not aware of any fee structure currently used by trading venues that have triggered participants to engage in abusive trading behaviour.

As a general matter, the FIA Associations do not believe the parameters of fee structures are significant inducements one way or another to market abuse. To the extent any market participant may be incentivised to engage in non bona fide trading behaviour in order to secure better pricing, this should be investigated on the merits and dealt with, if applicable, under relevant anti-market abuse regulation.

<ESMA_QUESTION_328>

Q329: In your opinion, are there any current fee structures providing these types of incentives? Please elaborate.

<ESMA_QUESTION_329>
The FIA Associations are not aware of any fee structure currently used by trading venue that has triggered participants to engage in abusive trading behaviour.

<ESMA_QUESTION_329>

4.8. Tick sizes (Article 48(6) and Article 49 of MiFID II)

Q330: Do you agree with the general approach ESMA has suggested?

<ESMA_QUESTION_330>

The FIA Associations[47] agree with the general approach ESMA has suggested for regulating tick sizes but would like to emphasise important additional points.

We acknowledge it is clearly the intent of MiFID II that regulators control the setting of tick sizes rather than individual trading venue operators. We are very concerned about the danger of making wholesale changes to tick sizes that will impact Europe's capital market structure without first having engaged in a data-driven pilot study or other rigorous market analysis. The regulation of tick sizes is a high impact market intervention. Non-optimal tick sizes will directly damage the price discovery process, reduce liquidity, and hamper companies' ability to raise capital for growth.

A too fine tick size leads to thin liquidity at the top of the book, which deters those looking to trade larger volumes and may push such participants away from lit venues. Some trading venues do not like very granular tick sizes, among other reasons because it can lead to (unnecessarily) high messaging rates. This could be a technological burden on an exchange, depending on the exchange's capacity and tolerance, and potentially also increase overhead costs of trading for participants. A race to the bottom in terms of tick sizes obviously serves no one.

However, the FIA Associations believe that overly constrained tick sizes present even more problems. Too coarse tick sizes will lead volume currently quoted at tight spreads to consolidate at new, wider spreads. This could mean investors will be worse off because liquidity takers, or traders who sweep the book, will end up paying more for the same liquidity they currently get at lower prices. Retail investors will be hardest hit, as they will subsidise other market participants by paying higher prices than they should due to wider tick sizes.[48]

Another potential consequence of volume consolidating at touch points of a wider spread due to an increase in absolute tick sizes is that queue priority will become more important because the time between

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[47] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

[48] The SEC's tick size pilot programs in the U.S. provide an exemption for retail investors to mitigate this impact, which MiFID II does not.

posting and executing an order will increase. This will actually emphasise the importance of speed in trading. This effect could possibly be mitigated through an execution model based on pro rata allocation against all eligible orders in the book, as you find in many U.S. derivatives markets, rather than a price-time priority model. However, pro rata allocation can be susceptible to other problems, such as potentially creating an incentive for participants to post artificially large orders in order to increase the likelihood of execution.

In either case, whether too granular or too wide, the wrong tick size regime may push trading off a trading venue. This would be bad for both market participants and trading venue operators, as well as being contrary to MiFID II's explicit goal of ensuring more trading occurs on lit and transparent markets.

We believe the markets have evolved to reflect generally correct tick sizes for their respective market characteristics and products traded, recognising that different trading venues have taken different approaches. This is because they have not had an external force restricting their ability to reflect the needs of market participants, which may differ per venue. If the current system has to change, ESMA must be sure to implement a flexible tick size regime that is capable of adapting to changing market circumstances. ESMA should leverage the expertise of those best positioned to analyse and understand the unique characteristics of a trading venue and its participants — in this case the trading venue operators can provide that expertise.

Therefore, considering the intent of MiFID II, the FIA Associations believe the factors proposed to be taken into account provide a good starting point, but that other facts must also be considered such as (1) the volatility profile of an instrument, (2) the volume per trade of an instrument and (3) the different impacts a large or small order may have on the stability of the order book. We believe that the trading venues should be left material discretion in tailoring actual tick sizes within the parameters of a principle-based regime set by ESMA (which we believe is possible with a slightly adjusted version of Option 2 that we will explain in more detail in our response to Question 346).

Finally, due to the high impact tick sizes can have on the activity of market participants, we believe no tick size regime should be implemented without first conducting a data-driven analysis of the impact of any proposed change. We support the approach being taken in the U.S. by the SEC in conducting pilot programs studying the effects of tick size changes prior to implementing new rules.

<ESMA_QUESTION_330>

Q331: Do you agree with adopting the average number of daily trades as an indicator for liquidity to satisfy the liquidity requirement of Article 49 of MiFID II? Are there any other methods/liquidity proxies that allow comparable granularity and that should be considered?

<ESMA_QUESTION_331>
The FIA Associations do not support Option 1 and do not agree with using the average number of daily trades as an acceptable and accurate indicator of liquidity because the average number of trades is not an independent variable from the tick size itself. Generally, a small tick-size will be associated with a high number of smaller sized trades. A larger tick-size will be associated with a smaller number of larger sized trades. Different fee structures also lead to different trade (transaction) counts. Additionally, when determining an instrument's liquidity, the relevance of a single trade greatly depends on the number of shares executed within that trade. These factors are amplified when analysing instruments that are composed of other instruments, such as ETFs.

Instead, ESMA could look to a value-based metric as an indicator of liquidity, such as average daily turnover. Total volume available as firm orders in the order book may be an additional proxy for liquidity;

however, when considering this indicator special attention must be given to iceberg orders and other factors that may distort the true available volume in the order book.

<ESMA_QUESTION_331>

Q332: In your view, what granularity should be used to determine the liquidity profile of financial instruments? As a result, what would be a proper number of liquidity bands?

<ESMA_QUESTION_332>
The FIA Associations do not support Option 1 and do not believe any level of granularity would be sufficient to determine accurately the liquidity profile of an instrument if the metric being observed is the average daily number of transactions.

As we stated in our answer to Question 331, we believe that the average daily number of transactions is a misleading indicator of liquidity because it fails to take into account several important factors that impact an instrument's liquidity, such as fee structures and the average number of shares executed within each transaction.

Determining the proper number of liquidity bands for a tick size regime is difficult without fully understanding the other components of the proposed regime. Nonetheless, we are confident that neither a very small number of bands (e.g. 1-4) nor a very large number of bands (e.g. 50+) are correct. The optimal number of bands will likely fall in the range of 5-20 and, at some level, need to be determined arbitrarily until enough data exists to make a more data-driven decision.

<ESMA_QUESTION_332>

Q333: What is your view on defining the trade-off between constraining the spread without increasing viscosity too much on the basis of a floor-ceiling mechanism?

<ESMA_QUESTION_333>
While the FIA Associations do not support Option 1, the general concept of viscosity trade-off is correct; however, we believe including a ceiling mechanism may negatively restrict the natural price discovery process on some markets. We acknowledge the LSE, for example, already operates with a ceiling mechanism in its tick size regime, apparently without detriment. We would not, however, like to see this mechanism mandatorily imposed on all markets, as we do not believe it is necessary, and having only a floor mechanism (such as in Option 2) allows for more natural price discovery.

<ESMA_QUESTION_333>

Q334: What do you think of the proposed spread to tick ratio range?

<ESMA_QUESTION_334>
While the FIA Associations do not support Option 1, in response to this specific question we received a wide range of responses from our members, which we believe reflects the difficulty in defining a standardised tick size regime for all stocks and supports our view that different markets' varying approaches are justified.

As explained in our response to Question 333, we believe a ceiling mechanism is not necessary for all markets, as it may negatively restrict the natural price discovery process. The appropriate spread to tick ratio depends on the dynamics of each individual market. Defining the spread to tick ratio for a broad set of markets based on a narrow set of criteria may inadvertently harm an instrument's natural price discovery process. For instance, although the price and liquidity range of two products may be the same, they

may have different volatility profiles. This difference may necessitate a different spread to tick size regime, otherwise the natural price discovery process may be restricted.

We understand it is ESMA's intention to determine this ratio at the level of regulation across the EU, but we believe this may introduce unintended restrictions on price discovery. Therefore, we believe it is preferable to allow the primary markets (i.e. where an instrument is primarily listed) to set the appropriate spread to tick ratio within principle-based guidelines, as they have the institutional knowledge to do so optimally. This would preserve ESMA's intention to have harmonised tick sizes across Europe, while respecting the individual characteristics of European markets. Our proposal is described further below (see our response to Question 346).

<ESMA_QUESTION_334>

Q335: In your view, for the tick size regime to be efficient and appropriate, should it rely on the spread to tick ratio range, the evolution of liquidity bands, a combination of the two or none of the above?

<ESMA_QUESTION_335>
For the reasons stated previously, the FIA Associations believe Option 1 has several fundamental flaws. For the tick size regime to be efficient, appropriate and preserve the greatest amount of flexibility for different markets, we should implement a slightly modified version of the tick size regime proposed in Option 2. We will outline this modification along with our reasons for support of Option 2 in our response to subsequent questions.

<ESMA_QUESTION_335>

Q336: What is your view regarding the common tick size table proposed under Option 1? Do you consider it easy to read, implement and monitor? Does the proposed two dimensional tick size table (based on both the liquidity profile and price) allow applying a tick size to a homogeneous class of stocks given its clear-cut price and liquidity classes?

<ESMA_QUESTION_336>
For the reasons stated previously, the FIA Associations do not support Option 1. While the common tick size table proposed under this option may have the advantage that it is easy to understand and implement (provided it is not subject to frequent changes), unfortunately, those advantages are outweighed by our belief that there is no such thing as a homogenous class of stocks, and any attempt to classify them as such will overlook important, and unique, defining characteristics. In addition, we do not believe this table works for ETFs.

<ESMA_QUESTION_336>

Q337: What is your view regarding the determination of the liquidity and price classes?

<ESMA_QUESTION_337>
For the reasons stated previously, the FIA Associations do not support Option 1. As we stated in our response to Question 331, we believe the average daily number of transactions is a misleading indicator of liquidity because it doesn't take into account several important factors that impact a product's liquidity, such as fee structures and the average number of shares executed within each transaction. In addition, the average number of trades is not an independent variable from the tick size itself, and it does not work for ETFs as outlined above.

<ESMA_QUESTION_337>

Q338: Considering that market microstructure may evolve, would you favour a regime that allows further calibration of the tick size on the basis of the observed market microstructure?

<ESMA_QUESTION_338>
The FIA Associations strongly favour a regime that allows for further calibration. There will certainly be a wide variation in the correct tick size from instrument to instrument, and it will be difficult if not impossible to calibrate perfectly any proposed tick size from first principles. While we do not support Option 1, we agree that any tick size regime will need to be able to take into account new data and adapt to changing market circumstances. We believe this is possible with a slightly modified version of the tick size regime proposed in Option 2, which is outlined further below.

<ESMA_QUESTION_338>

Q339: In your view, does the tick size regime proposed under Option 1 offer sufficient predictability and certainty to market participants in a context where markets are constantly evolving (notably given its calibration and monitoring mechanisms)?

<ESMA_QUESTION_339>
For the most part, the FIA Associations agree the regime offers sufficient predictability and certainty to market participants. We do have some concerns.

While the LSE, for example, has the ability to implement intraday tick size changes based on hard-coded dynamic parameters, we are aware not all markets find intraday tick size changes operationally feasible. We believe requiring all trading venues to be able to implement such intraday changes could introduce undue complexity and risk to the marketplace. For the same reason, we do not believe all trading venues should be forced to implement very granular tick sizes if they do not have the technological capacity to manage potentially higher messaging rates that may be a result, even if more granular tick sizes would facilitate tighter spreads.

However, even if this concern were to be addressed, the FIA Associations would still be of the opinion that a slightly modified version of Option 2 would better serve the market.

<ESMA_QUESTION_339>

Q340: The common tick size table proposed under Option 1 provides for re-calibration while constantly maintaining a control sample. In your view, what frequency would be appropriate for the revision of the figures (e.g., yearly)?

<ESMA_QUESTION_340>
For the reasons stated previously, the FIA Associations do not support Option 1. However, generally speaking we believe revision of tick size tables should take place no more frequently than every six months (unless market circumstances require a more often revision), and optimally annually at the end of the calendar year.

<ESMA_QUESTION_340>

Q341: In your view, what is the impact of Option 1 on the activity of market participants, including trading venue operators? To what extent, would it require adjustments?

<ESMA_QUESTION_341>
As the FIA Associations have stated above in response to Question 330, because of the material impact tick sizes can have on the activity of market participants, we believe no tick size regime should be implemented without first conducting a data-driven analysis of the impact of any proposed change.

Without having the data and resources available to perform this rigorous analysis, our estimate is that the tick size regime presented in Option 1 will change the current tick size of many stocks outside of the UK and Italy by increasing the absolute tick size. As we strongly believe current tick sizes have in general evolved to be correct and meet the needs of market participants, we believe the fact that Option 1 will necessarily change these demonstrates it is flawed. Moreover, as we have stated in response to Question 330, we believe overly constrained tick sizes make trading more expensive for investors, both retail and institutional, by forcing them to pay more (in the form of spread) for the same liquidity they get now at improved prices, as well as emphasising the importance of speed in trading (in the form of queue formation and priority).

We do not believe adjustments to Option 1 would produce an acceptable outcome. Therefore, we will provide more detailed responses with respect to Option 2, below.

<ESMA_QUESTION_341>

Q342: Do you agree that some equity-like instruments require an equivalent regulation of tick sizes as equities so as to ensure the orderly functioning of markets and to avoid the migration of trading across instrument types based on tick size? If not, please outline why this would not be the case.

<ESMA_QUESTION_342>
While the FIA Associations do not support Option 1, we generally agree that equivalent regulation is useful for equity-like instruments such as ETFs. We believe the general concept should be the same as for shares, but may be calibrated differently (especially due to the fact that liquidity of the ETF highly depends on the liquidity of the underlying), if deemed necessary by, for instance, the trading venue operators. We do not recommend implementing two different solutions/methodologies, (e.g. Option 1 for shares and Option 2 for ETFs), as it would become too complex.

<ESMA_QUESTION_342>

Q343: Are there any other similar equity-like instruments that should be added / removed from the scope of tick size regulation? Please outline the reasons why such instruments should be added / removed?

<ESMA_QUESTION_343>
No.

<ESMA_QUESTION_343>

Q344: Do you agree that depositary receipts require the same tick size regime as equities'?

<ESMA_QUESTION_344>
The FIA Associations believe tick size regimes should initially be limited to shares and ETFs with the possible addition of related products, including depositary receipts at some point in the future.

<ESMA_QUESTION_344>

Q345: If you think that for certain equity-like instruments (e.g. ETFs) the spread-based tick size regime[49] would be more appropriate, please specify your reasons and provide a detailed description of the methodology and technical specifications of this alternative concept.

<ESMA_QUESTION_345>
As we have stated above, the FIA Associations do not believe in using the number of trades as a proxy for liquidity, either for shares or equity-like instruments. We believe that Option 2 with some adjustments would be a workable solution for ETFs (see below for details).

<ESMA_QUESTION_345>

Q346: If you generally (also for liquid and illiquid shares as well as other equity-like financial instruments) prefer a spread-based tick size regime[50] vis-à-vis the regime as proposed under Option 1 and tested by ESMA, please specify the reasons and provide the following information:

<ESMA_QUESTION_346>
The FIA Associations generally prefer a spread-based tick size regime such as the one proposed in Option 2 (with a few adjustments). We believe that one solution/methodology applicable to both shares and other equity-like instruments (including ETFs) makes sense, with some calibrations being necessary.

i. Technical specifications

We propose a modified version of Option 2 and point out two points to be considered:

(1) **Recalibration of the tick size table itself**: We believe that the table suggested in Option 2 for liquid shares is not granular enough and should therefore be recalibrated. We suggest adjusting it as reflected in the following table:

	Stock Prices		Tick sizes							
Band	Lower Limit	Upper Limit	SAF_0	SAF_1	SAF_2	SAF_3	SAF_4	SAF_5	SAF_x	SAF_{19}
1	-	0.4999	0.0001							
2	0.5	0.9995	0.0002	0.0001						
3	1	1.999	0.0005	0.0002	0.0001					
4	2	4.998	0.001	0.0005	0.0002	0.0001				
5	5	9.995	0.002	0.001	0.0005	0.0002	0.0001			
6	10	19.99	0.005	0.002	0.001	0.0005	0.0002	0.0001		
7	20	49.98	0.01	0.005	0.002	0.001	0.0005	0.0002	[...]	
8	50	99.95	0.02	0.01	0.005	0.002	0.001	0.0005	[...]	
9	100	199.9	0.05	0.02	0.01	0.005	0.002	0.001	[...]	
10	200	499.8	0.1	0.05	0.02	0.01	0.005	0.002	[...]	
11	500	999.5	0.2	0.1	0.05	0.02	0.01	0.005	[...]	
12	1,000.00	1,999.00	0.5	0.2	0.1	0.05	0.02	0.01	[...]	
13	2,000.00	4,998.00	1	0.5	0.2	0.1	0.05	0.02	[...]	
14	5,000.00	9,995.00	2	1	0.5	0.2	0.1	0.05	[...]	
15	10,000.00	19,990.00	5	2	1	0.5	0.2	0.1	[...]	
16	20,000.00	39,980.00	10	5	2	1	0.5	0.2	[...]	
17	40,000.00	49,960.00	20	10	5	2	1	0.5	[...]	
18	50,000.00	79,950.00	50	20	10	5	2	1	[...]	
19	80,000.00	99,920.00	100	50	20	10	5	2	[...]	
20	100,000.00	-	200	100	50	20	10	5	[...]	0.0001

[49] Please see the description of Option 2 regarding tick sizes below.
[50] Please see the description of Option 2 regarding tick sizes below.

	Stock Prices		Tick sizes							
Band	Lower Limit	Upper Limit	SAF_0	SAF_1	SAF_2	SAF_3	SAF_4	SAF_5	SAF_x	SAF_{19}
1	-	0.4999	0.0002							
2	0.5	0.9995	0.0005	0.0002						
3	1	1.999	0.001	0.0005	0.0002					
4	2	4.998	0.002	0.001	0.0005	0.0002				
5	5	9.995	0.005	0.002	0.001	0.0005	0.0002			
6	10	19.99	0.01	0.005	0.002	0.001	0.0005	0.0002		
7	20	49.98	0.02	0.01	0.005	0.002	0.001	0.0005	[...]	
8	50	99.95	0.05	0.02	0.01	0.005	0.002	0.001	[...]	
9	100	199.9	0.1	0.05	0.02	0.01	0.005	0.002	[...]	
10	200	499.8	0.2	0.1	0.05	0.02	0.01	0.005	[...]	
11	500	999.5	0.5	0.2	0.1	0.05	0.02	0.01	[...]	
12	1,000.00	1,999.00	1	0.5	0.2	0.1	0.05	0.02	[...]	
13	2,000.00	4,998.00	2	1	0.5	0.2	0.1	0.05	[...]	
14	5,000.00	9,995.00	5	2	1	0.5	0.2	0.1	[...]	
15	10,000.00	19,990.00	10	5	2	1	0.5	0.2	[...]	
16	20,000.00	39,980.00	20	10	5	2	1	0.5	[...]	
17	40,000.00	49,960.00	50	20	10	5	2	1	[...]	
18	50,000.00	79,950.00	100	50	20	10	5	2	[...]	
19	80,000.00	99,920.00	200	100	50	20	10	5	[...]	
20	100,000.00	-	500	200	100	50	20	10	[...]	0.0002

This table becomes more symmetric compared to the original table. For less liquid shares the table will be a modified version of this table, whereby each tick size band is assigned a tick size that is one step larger in comparison to the corresponding tick size table for the liquid instrument.

We believe that, for the sake of simplicity, all ETFs should be assigned to the liquid tables for shares because the differentiation between liquid and less liquid ETFs as proposed by ESMA in the Consultation Paper (Section 3.1, p. 174) does not accurately reflect their true level of liquidity. If ESMA wants to differentiate between liquid and less liquid ETFs, we suggest applying *de minimis* numbers for the average daily number of transactions and the average daily turnover, thus effectively classifying all ETFs as instruments with a liquid market.

However, we note that this section currently refers to the 'old' definition of "liquid" under MiFID, which is based on number of trades per day. We have previously expressed our view that we do not believe number of trades per day is a good proxy for liquidity, and that average daily turnover would be better. As the definition of "liquid" is currently being considered by ESMA in the MiFID II Consultation Paper, this definition is subject to change. Therefore, once again we strongly urge ESMA to submit any proposals to change tick sizes to a thorough market impact analysis when all parameters are clear, prior to being implemented.

(2) **Adjustment of the spread to tick ratio**: We believe the proposed spread to tick ratio of 2 might work for some markets, but not for all. As we have stated above in our response to Question 330, different trading venues may have justifiable reasons to approach tick sizes differently depending on the unique characteristics of their markets and market participants, and we believe the trading venues are best positioned to undertake this analysis.

Therefore, with respect to shares, the FIA Associations suggest that the primary market (i.e. where the share has been primarily listed), should be allowed to choose if they prefer to be on a low or high spread to tick ratio.

With respect to ETFs, the FIA Associations suggest the choice should be left to the venue with the highest turnover in a respective ETF because ETFs are normally cross-listed simultaneously on multiple venues, such that the concept of one primary market as a single listing venue does not exist. The advantage of turnover as criterion is that it is simple to calculate, transparent and accounts for the level of trading activity on each European venue. However, we would like to point out that it is important that calculation of turnover needs to be accurately defined, i.e. exclusively be based on order book transactions in order to have a meaningful and relevant basis underlying the tick size decision.

With respect to the low vs. high spread to tick ratio, without a data-driven study to support any analysis, we do not have a clear view on the appropriate outcome. Nevertheless, discussions internal to the FIA Associations jelled around a low spread to tick ratio range of 2 to 4 and a high spread to tick ratio range of 4 to 8. The right number within each of these ranges should be determined on the basis of further study. Without committing to any particular number, but only by way of example, we could envision primary market operators having a binary choice between a spread to tick ratio of 3, on the low end, or 6, on the higher end. Such an approach would allow flexibility for markets but at the same time tick sizes would be harmonised across Europe as every single instrument has only one tick size.

In the absence of a data-driven study before tick size changes get implemented, the FIA Associations strongly request ESMA to review any changes after two years, to examine how they have impacted the market and make adjustments as necessary.

<ESMA_QUESTION_346>

Q347: Given the different tick sizes currently in operation, please explain what your preferred type of tick size regulation would be, giving reasons why this is the case.

<ESMA_QUESTION_347>

As stated above, the FIA Associations believe that existing tick sizes are generally correct. Based on our preliminary analysis, implementing the Option 1 methodology would change the tick size of many stocks, which we believe may damage price discovery and reduce liquidity traded in the open. If existing tick sizes must change, ESMA should propose a regime capable of adapting to changing market circumstances.

We do not believe this is the case with Option 1 but it could be possible with an adjusted version of Option 2 (see our response to Question 346).

<ESMA_QUESTION_347>

Q348: Do you see a need to develop a tick size regime for any non-equity financial instrument? If yes, please elaborate, indicating in particular which approach you would follow to determine that regime.

<ESMA_QUESTION_348>

The FIA Associations do not see any need to develop a tick size regime for non-equity instruments, as those markets work differently. We are convinced that trading venues can best determine what the tick size for those instruments should be, if any.

<ESMA_QUESTION_348>

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Q349: Do you agree with assessing the liquidity of a share for the purposes of the tick size regime, using the rule described above? If not, please elaborate what criteria you would apply to distinguish between liquid and illiquid instruments.

<ESMA_QUESTION_349>
The FIA Associations agree there should be different tick sizes for liquid and illiquid stocks.

However, we note that as the definition of "liquid" is currently being considered by ESMA in the MiFID II Consultation Paper (Section 3.1, page 174), it may be subject to change. Therefore, once again we strongly urge ESMA to submit any proposals to change tick sizes to a thorough market impact analysis when all parameters are clear, prior to being implemented.

Moreover, we believe the proposed differentiation between liquid and less liquid ETFs in the Consultation Paper (Section 3.1, page 174) does not accurately reflect their true level of liquidity. Instead, we suggest having only one table for ETFs. We believe that for the sake of simplicity, all ETFs should be assigned to the liquid table for shares. If ESMA wishes to differentiate between liquid and less liquid ETFs, we suggest applying *de minimis* numbers for the average daily number of transactions and the average daily turnover, thus effectively classifying all ETFs as instruments with a liquid market.

<ESMA_QUESTION_349>

Q350: Do you agree with the tick sizes proposed under Option 2? In particular, should a different tick size be used for the largest band, taking into account the size of the tick relative to the price? Please elaborate.

<ESMA_QUESTION_350>
The FIA Associations believe Option 2 is not optimal in its current state. However, the FIA Associations do believe on balance that more granular tick sizes present fewer problems for market quality than tick sizes that are too coarse (please see our response to Questions 330 and 346).

<ESMA_QUESTION_350>

Q351: Should the tick size be calibrated in a more granular manner to that proposed above, namely by shifting a band which results in a large step-wise change?

<ESMA_QUESTION_351>
Yes. Please see our response to Question 346 for more details on our suggested approach.
<ESMA_QUESTION_351>

Q352: Do you agree with the above treatment for a newly admitted instrument? Would this affect the subsequent trading in a negative way?

<ESMA_QUESTION_352>
The FIA Associations do not agree that a newly admitted instrument should be treated by definition as an illiquid instrument during the initial calibration period, as this may unnecessarily constrain trading. As stated by IOSCO in David Wright's keynote speech at the FESE Convention 2014, the revival of the European IPO market is vital to the recovery of the EU economy. We strongly agree with this claim and believe active trading in new listings should be stimulated through accurate tick sizes.

Instead, we suggest that new listings be assigned to the equivalent table its peers have been assigned to, i.e. either the table for liquid shares or the table for illiquid shares. As explained above, we believe ETFs should be assigned to the liquid table.

With regard to reassessment, to avoid artificially constrained trading and to stimulate growth in the IPO market, we would prefer to see more flexibility for new listings to be reassigned on a monthly basis during the first six months after listing. The first weeks of trading in some newly admitted instruments are likely to be more active than for the rest of their lifetime, as often trading interest surrounding an initial public offering exceeds trading interest thereafter. In order to minimize market disruptions, however, changes should only be made at the start of a month on the condition an instrument has been trading for at least a full calendar month. For example a stock that floats on 1st of November will be assigned to a potential new table or SAF by 1st of December, while a stock that floats mid-December, will first be assigned to a potential new table or SAF by 1st of February.

<ESMA_QUESTION_352>

Q353: Do you agree that a period of six weeks is appropriate for the purpose of initial calibration for all instruments admitted to the pan-European tick size regime under Option 2? If not, what would be the appropriate period for the initial calibration?

<ESMA_QUESTION_353>
Please see our response to Question 352.

<ESMA_QUESTION_353>

Q354: Do you agree with the proposal of factoring the bid-ask spread into tick size regime through SAF? If not, what would you consider as the appropriate method?

<ESMA_QUESTION_354>
The FIA Associations agree.

<ESMA_QUESTION_354>

Q355: Do you agree with the proposal to take an average bid-ask spread of less than two ticks as being too narrow? If not, what level of spread to ticks would you consider to be too narrow?

<ESMA_QUESTION_355>
The FIA Associations do not necessarily agree. As we have set out in our response to Question 346, we suggest that for shares, primary markets (for ETFs the venue with the highest turnover) should be allowed to choose whether they prefer to be on a low spread to tick ratio or a higher spread to tick ratio. This would allow flexibility for markets within parameters harmonised across Europe, as every single instrument would have only one tick size.

Without a data-driven study to support any analysis, we do not have a clear view, but our internal discussions jelled around a low spread to tick ratio range between 2 to 4 and a high spread to tick ratio range between 4 to 8. Further study should determine the optimal numbers. Without committing to any particular outcome, but only by way of example, we could envision primary market operators having a binary choice between a spread to tick ratio of 3, on the low end, or 6, on the higher end. Such an approach would allow flexibility for markets while allowing for a certain level of harmonisation across Europe, as every single instrument would have only one tick size.

For example, if a stock of a hypothetical company ABC is primarily listed on a regulated market 'Alpha' while at the same time being traded on a multi-lateral trading facility ("MTF") 'Beta', the regulated market Alpha may choose a high spread to tick ratio (being 5) which will also determine the tick size of stock ABC that MTF Beta has to apply as well.

<ESMA_QUESTION_355>

Q356: Under the current proposal, it is not considered necessary to set an upper ceiling to the bid-ask spread, as the preliminary view under Option 2 is that under normal conditions the risk of the spread widening indefinitely is limited (and in any event a regulator may amend SAF manually if required). Do you agree with this view? If not, how would you propose to set an upper ceiling applicable across markets in the EU?

<ESMA_QUESTION_356>
As explained in our response to Question 333, the FIA Associations believe a ceiling mechanism may negatively restrict the natural price discovery process. We generally agree that it is less problematic to have a too granular tick size than a too wide tick size to the extent that it does not adversely create a proliferation of orders and negatively impact desired OTRs. We believe that a floor mechanism (see our responses to Questions 346 and 355) appropriately balances those concerns versus the risks associated with artificially constraining price discovery, especially in light of the added mechanism that an NCA may manually change the SAF if it is deemed necessary. The exact conditions under which an NCA may intervene still need to be specified to ensure that manual intervention will not be misused.

<ESMA_QUESTION_356>

Q357: Do you have any concerns of a possible disruption which may materialise in implementing a review cycle as envisioned above?

<ESMA_QUESTION_357>
As stated in our response to Question 353, the FIA Associations do not believe there is a need for an initial calibration period, as this might lead to market disruptions. An annual review of the SAF, preferably at the end of a calendar year, seems feasible.

To minimise disruption, tick tables and instrument classifications should be available in a standardised machine-readable format, for example in the MiFID database. This should be considered the leading source rather than the current ad hoc system of emails, pdfs, spreadsheets etc., which varies by trading venue.

<ESMA_QUESTION_357>

Q358: Do you agree that illiquid instruments, excluding illiquid cash equities, should be excluded from the scope of a pan-European tick size regime under Option 2 until such time that definitions for these instruments become available? If not, please explain why. If there are any equity-like instruments per Article 49(3) of MiFID II that you feel should be included in the pan-European tick size regime at the same time as for cash equities, please list these instruments together with a brief reason for doing so.

<ESMA_QUESTION_358>
The FIA Associations believe that for shares and ETFs, a differentiation between liquid and illiquid shares makes sense, and we generally agree with ESMA's proposal under Section 3.1 of the Consultation Paper, subject to our comments in that section regarding this definition being subject to change as a result of the consultation and further study being required. Moreover, as stated above, we do not agree with the definition of what constitutes a liquid market for an ETF (please see our response to Question 349) and believe these would better be assigned to one common table, i.e. the liquid table for shares.

<ESMA_QUESTION_358>

Q359: Do you agree that financial instruments, other than those listed in Article 49(3) of MiFID II should be excluded from the scope of the pan-European tick size regime under Option 2 at least for the time being? If not, please explain why and which specific instruments do you consider necessary to be included in the regime.

<ESMA_QUESTION_359>
The FIA Associations believe that only shares and ETFs should be assigned to the regime. Before those regimes have been implemented and proven to work, other instruments such as DRs should not be considered.

<ESMA_QUESTION_359>

Q360: What views do you have on whether tick sizes should be revised on a dynamic or periodic basis? What role do you perceive for an automated mechanism for doing this versus review by the NCA responsible for the instrument in question? If you prefer periodic review, how frequently should reviews be undertaken (e.g. quarterly, annually)?

<ESMA_QUESTION_360>
The FIA Associations agree with ESMA's proposal to maintain the price as a dynamic factor with which to determine appropriate tick sizes during the normal course of trading and only periodically (i.e. on an annual basis) review liquidity and the average spread to appropriately adjust the tick size via the SAF for use in the subsequent period.

<ESMA_QUESTION_360>

5. Data publication and access

5.1. General authorisation and organisational requirements for data reporting services (Article 61(4), MiFID II)

Q361: Do you agree that the guidance produced by CESR in 2010 is broadly appropriate for all three types of DRS providers?

<ESMA_QUESTION_361>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_361>

Q362: Do you agree that there should also be a requirement for notification of significant system changes?

<ESMA_QUESTION_362>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_362>

Q363: Are there any other general elements that should be considered in the NCAs' assessment of whether to authorise a DRS provider?

<ESMA_QUESTION_363>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_363>

5.2. Additional requirements for particular types of Data Reporting Services Providers

Q364: Do you agree with the identified differences regarding the regulatory treatment of ARMs.

<ESMA_QUESTION_364>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_364>

Q365: What other significant differences will there have to be in the standards for APAs, CTPs and ARMs?

<ESMA_QUESTION_365>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_365>

5.3. Technical arrangements promoting an efficient and consistent dissemination of information – Machine readability Article 64(6), MiFID II

Q366: Do you agree with the proposal to define machine-readability in this way? If not, what would you prefer?

<ESMA_QUESTION_366>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_366>

5.4. Consolidated tape providers

Q367: Should the tapes be offered to users on an instrument-by-instrument basis, or as a single comprehensive tape, or at some intermediate level of disaggregation? Do you think that transparency information should be available without the need for value-added products to be purchased alongside?

<ESMA_QUESTION_367>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_367>

Q368: Are there other factors or considerations regarding data publication by the CTP that are not covered in the standards for data publication by APAs and trading venues and that should be taken into account by ESMA?

<ESMA_QUESTION_368>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_368>

Q369: Do you agree that CTPs should be able to provide the services listed above? Are there any others that you think should be specified?

<ESMA_QUESTION_369>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_369>

5.5. Data disaggregation

Q370: Do you agree that venues should not be required to disaggregate by individual instrument?

<ESMA_QUESTION_370>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_370>

Q371: Do you agree that venues should be obliged to disaggregate their pre-trade and post-trade data by asset class?

<ESMA_QUESTION_371>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_371>

Q372: Do you believe the list of asset classes proposed in the previous paragraph is appropriate for this purpose? If not, what would you propose?

<ESMA_QUESTION_372>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_372>

Q373: Do you agree that venues should be under an obligation to disaggregate according to the listed criteria unless they can demonstrate that there is insufficient customer interest?

<ESMA_QUESTION_373>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_373>

Q374: Are there any other criteria according to which it would be useful for venues to disaggregate their data, and if so do you think there should be a mandatory or comply-or-explain requirement for them to do so?

<ESMA_QUESTION_374>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_374>

Q375: What impact do you think greater disaggregation will have in practice for overall costs faced by customers?

<ESMA_QUESTION_375>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_375>

5.6. Identification of the investment firm responsible for making public the volume and price transparency of a transaction (Articles 20(3) (c) and 21(5)(c), MiFIR)

Q376: Please describe your views about how to improve the current trade reporting system under Article 27(4) of MiFID Implementing Regulation.

<ESMA_QUESTION_376>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_376>

5.7. Access to CCPs and trading venues (Articles 35-36, MiFIR)

Q377: Do you agree that exceeding the planned capacity of the CCP is grounds to deny access?

<ESMA_QUESTION_377>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_377>

Q378: How would a CCP assess that the anticipated volume of transactions would exceed its capacity planning?

<ESMA_QUESTION_378>
TYPE YOUR TEXT HERE

<ESMA_QUESTION_378>

Q379: Are there other risks related to the anticipated volume of transactions that should be considered? If so, how would such risks arise from the provision of access?

<ESMA_QUESTION_379>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_379>

Q380: Do you agree that exceeding the planned capacity of the CCP is grounds to deny access?

<ESMA_QUESTION_380>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_380>

Q381: How would a CCP assess that the number of users expected to access its systems would exceed its capacity planning?

<ESMA_QUESTION_381>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_381>

Q382: Are there other risks related to number of users that should be considered? If so, how would such risks arise from the provision of access?

<ESMA_QUESTION_382>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_382>

Q383: In what way could granting access to a trading venue expose a CCP to risks associated with a change in the type of users accessing the CCP? Are there any additional risks that could be relevant in this situation?

<ESMA_QUESTION_383>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_383>

Q384: How would a CCP establish that the anticipated operational risk would exceed its operational risk management design?

<ESMA_QUESTION_384>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_384>

Q385: Are there other risks related to arrangements for managing operational risk that should be considered? If so, how would such risks arise from the provision of access?

<ESMA_QUESTION_385>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_385>

Q386: Given there will be costs to meeting an access request, what regard should be given to those costs that would create significant undue risk?

<ESMA_QUESTION_386>
TYPE YOUR TEXT HERE

<ESMA_QUESTION_386>

Q387: To what extent could a lack of harmonization in certain areas of law constitute a relevant risk in the context of granting or denying access?

<ESMA_QUESTION_387>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_387>

Q388: Do you agree with the risks identified above in relation to complexity and other factors creating significant undue risks?

<ESMA_QUESTION_388>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_388>

Q389: Q: Are there other risks related to complexity and other factors creating significant undue risks that should be considered? If so, how would such risks arise from the provision of access?

<ESMA_QUESTION_389>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_389>

Q390: Do you agree with the analysis above and the conclusion specified in the previous paragraph?

<ESMA_QUESTION_390>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_390>

Q391: To what extent would a trading venue granting access give rise to material risks because of anticipated volume of transactions and the number of users? Can you evidence that access will materially change volumes and the number of users?

<ESMA_QUESTION_391>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_391>

Q392: To what extent would a trading venue granting access give rise to material risks because of arrangements for managing operational risk?

<ESMA_QUESTION_392>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_392>

Q393: Given there will be costs to meeting an access request, what regard should be given to those costs that would create significant undue risk?

<ESMA_QUESTION_393>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_393>

Q394: Do you believe a CCP's model regarding the acceptance of trades may create risks to a trading venue if access is provided? If so, please explain in which cases and how.

<ESMA_QUESTION_394>

TYPE YOUR TEXT HERE
<ESMA_QUESTION_394>

Q395: Could granting access create unmanageable risks for trading venues due to conflicts of law arising from the involvement of different legal regimes?

<ESMA_QUESTION_395>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_395>

Q396: Are there other risks related to complexity and other factors creating significant undue risks that should be considered? If so, how would such risks arise from the provision of access?

<ESMA_QUESTION_396>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_396>

Q397: Do you agree with the conditions set out above? If you do not, please state why not.

<ESMA_QUESTION_397>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_397>

Q398: Are there any are other conditions CCPs and trading venues should include in their terms for agreeing access?

<ESMA_QUESTION_398>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_398>

Q399: Are there any other fees that are relevant in the context of Articles 35 and 36 of MiFIR that should be analysed?

<ESMA_QUESTION_399>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_399>

Q400: Are there other considerations that need to be made in respect of transparent and non-discriminatory fees?

<ESMA_QUESTION_400>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_400>

Q401: Do you consider that the proposed approach adequately reflects the need to ensure that the CCP does not apply discriminatory collateral requirements? What alternative approach would you consider?

<ESMA_QUESTION_401>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_401>

Q402: Do you see other conditions under which netting of economically equivalent contracts would be enforceable and ensure non-discriminatory treatment for the prospective trading venue in line with all the conditions of Article 35(1)(a)?

<ESMA_QUESTION_402>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_402>

Q403: The approach above relies on the CCP's model compliance with Article 27 of Regulation (EU) No 153/2013, do you see any other circumstances for a CCP to cross margin correlated contracts? Do you see other conditions under which cross margining of correlated contracts would be enforceable and ensure non-discriminatory treatment for the prospective trading venue?

<ESMA_QUESTION_403>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_403>

Q404: Do you agree with ESMA that the two considerations that could justify a national competent authority in denying access are (a) knowledge it has about the trading venue or CCP being at risk of not meeting its legal obligations, and (b) liquidity fragmentation? If not, please explain why.

<ESMA_QUESTION_404>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_404>

Q405: How could the above mentioned considerations be further specified?

<ESMA_QUESTION_405>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_405>

Q406: Are there other conditions that may threaten the smooth and orderly functioning of the markets or adversely affect systemic risk? If so, how would such risks arise from the provision of access?

<ESMA_QUESTION_406>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_406>

Q407: Do you agree with ESMA's proposed approach that where there are equally accepted alternative approaches to calculating notional amount, but there are notable differences in the value to which these calculation methods give rise, ESMA should specify the method that should be used?

<ESMA_QUESTION_407>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_407>

Q408: Do you agree that the examples provided above are appropriate for ESMA to adopt given the purpose for which the opt-out mechanism was introduced? If not, why, and what alternative(s) would you propose?

<ESMA_QUESTION_408>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_408>

Q409: For which types of exchange traded derivative instruments do you consider there to be notable differences in the way the notional amount is calculated? How should the notional amount for these particular instruments be calculated?

<ESMA_QUESTION_409>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_409>

Q410: Are there any other considerations ESMA should take into account when further specifying how notional amount should be calculated? In particular, how should technical transactions be treated for the purposes of Article 36(5), MiFIR?

<ESMA_QUESTION_410>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_410>

5.8. Non- discriminatory access to and obligation to license benchmarks

Q411: Do you agree that trading venues require the relevant information mentioned above? If not, why?

<ESMA_QUESTION_411>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_411>

Q412: Is there any other additional information in respect of price and data feeds that a trading venue would need for the purposes of trading?

<ESMA_QUESTION_412>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_412>

Q413: Do you agree that CCPs require the relevant information mentioned above? If not, why?

<ESMA_QUESTION_413>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_413>

Q414: Is there any other additional information in respect of price and data feeds that a CCP would need for the purposes of clearing?

<ESMA_QUESTION_414>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_414>

Q415: Do you agree that trading venues should have access to benchmark values as soon as they are calculated? If not, why?

<ESMA_QUESTION_415>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_415>

Q416: Do you agree that CCPs should have access to benchmark values as soon as they are calculated? If not, why?

<ESMA_QUESTION_416>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_416>

Q417: Do you agree that trading venues require the relevant information mentioned above? If not, why?

<ESMA_QUESTION_417>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_417>

Q418: Is there any other additional information in respect of composition that a trading venue would need for the purposes of trading?

<ESMA_QUESTION_418>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_418>

Q419: Do you agree that CCPs require the relevant information mentioned above? If not, why?

<ESMA_QUESTION_419>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_419>

Q420: Is there any other additional information in respect of composition that a CCP would need for the purposes of clearing?

<ESMA_QUESTION_420>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_420>

Q421: Do you agree that trading venues and CCPs should be notified of any planned changes to the composition of the benchmark in advance? And that where this is not possible, notification should be given as soon as the change is made? If not, why?

<ESMA_QUESTION_421>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_421>

Q422: Do you agree that trading venues need the relevant information mentioned above? If not, why?

<ESMA_QUESTION_422>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_422>

Q423: Is there any other additional information in respect of methodology that a trading venue would need for the purposes of trading?

<ESMA_QUESTION_423>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_423>

Q424: Do you agree that CCPs require the relevant information mentioned above? If not, why?

<ESMA_QUESTION_424>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_424>

Q425: Is there any other additional information in respect of methodology that a CCP would need for the purposes of clearing?

<ESMA_QUESTION_425>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_425>

Q426: Is there any information is respect of the methodology of a benchmark that a person with proprietary rights to a benchmark should not be required to provide to a trading venue or a CCP?

<ESMA_QUESTION_426>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_426>

Q427: Do you agree that trading venues require the relevant information mentioned above (values, types and sources of inputs, used to develop benchmark values)? If not, why?

<ESMA_QUESTION_427>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_427>

Q428: Is there any other additional information in respect of pricing that a trading venue would need for the purposes of trading?

<ESMA_QUESTION_428>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_428>

Q429: In what other circumstances should a trading venue not be able to require the values of the constituents of a benchmark?

<ESMA_QUESTION_429>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_429>

Q430: Do you agree that CCPs require the relevant information mentioned above? If not, why?

<ESMA_QUESTION_430>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_430>

Q431: Is there any other additional information in respect of pricing that a CCP would need for the purposes of clearing?

<ESMA_QUESTION_431>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_431>

Q432: In what other circumstances should a CCP not be able to require the values of the constituents of a benchmark?

<ESMA_QUESTION_432>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_432>

Q433: Do you agree that trading venues require the additional information mentioned above? If not, why?

<ESMA_QUESTION_433>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_433>

Q434: Do you agree that CCPs require the additional information mentioned above? If not, why?

<ESMA_QUESTION_434>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_434>

Q435: Is there any other information that a trading venue would need for the purposes of trading?

<ESMA_QUESTION_435>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_435>

Q436: Is there any other information that a CCP would need for the purposes of clearing?

<ESMA_QUESTION_436>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_436>

Q437: Do you agree with the principles described above? If not, why?

<ESMA_QUESTION_437>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_437>

Q438: Do users of trading venues need non-publicly disclosed information on benchmarks?

<ESMA_QUESTION_438>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_438>

Q439: Do users of CCPs need non-publicly disclosed information on benchmarks?

<ESMA_QUESTION_439>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_439>

Q440: Where information is not available publicly should users be provided with the relevant information through agreements with the person with proprietary rights to the benchmark or with its trading venue / CCP?

<ESMA_QUESTION_440>

TYPE YOUR TEXT HERE
<ESMA_QUESTION_440>

Q441: Do you agree with the conditions set out above? If not, please state why not.

<ESMA_QUESTION_441>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_441>

Q442: Are there any are other conditions persons with proprietary rights to a benchmark and trading venues should include in their terms for agreeing access?

<ESMA_QUESTION_442>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_442>

Q443: Are there any are other conditions persons with proprietary rights to a benchmark and CCPs should include in their terms for agreeing access?

<ESMA_QUESTION_443>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_443>

Q444: Which specific terms/conditions currently included in licensing agreements might be discriminatory/give rise to preventing access?

<ESMA_QUESTION_444>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_444>

Q445: Do you have views on how termination should be handled in relation to outstanding/significant cases of breach?

<ESMA_QUESTION_445>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_445>

Q446: Do you agree with the approach ESMA has taken regarding the assessment of a benchmark's novelty, i.e., to balance/weight certain factors against one another? If not, how do you think the assessment should be carried out?

<ESMA_QUESTION_446>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_446>

Q447: Do you agree that each newly released series of a benchmark should not be considered a new benchmark?

<ESMA_QUESTION_447>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_447>

Q448: Do you agree that the factors mentioned above could be considered when assessing whether a benchmark is new? If not, why?

<ESMA_QUESTION_448>
TYPE YOUR TEXT HERE

<ESMA_QUESTION_448>

Q449: Are there any factors that would determine that a benchmark is not new?

<ESMA_QUESTION_449>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_449>

6. Requirements applying on and to trading venues

6.1. Admission to Trading

Q450: What are your views regarding the conditions that have to be satisfied in order for a financial instrument to be admitted to trading?

<ESMA_QUESTION_450>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_450>

Q451: In your experience, do you consider that the requirements being in place since 2007 have worked satisfactorily or do they require updating? If the latter, which additional requirements should be imposed?

<ESMA_QUESTION_451>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_451>

Q452: More specifically, do you think that the requirements for transferable securities, units in collective investment undertakings and/or derivatives need to be amended or updated? What is your proposal?

<ESMA_QUESTION_452>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_452>

Q453: How do you assess the proposal in respect of requiring ETFs to offer market making arrangements and direct redemption facilities at least in cases where the regulated market value of units or shares significantly varies from the net asset value?

<ESMA_QUESTION_453>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_453>

Q454: Which arrangements are currently in place at European markets to verify compliance of issuers with initial, on-going and ad hoc disclosure obligations?

<ESMA_QUESTION_454>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_454>

Q455: What are your experiences in respect of such arrangements?

<ESMA_QUESTION_455>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_455>

Q456: What is your view on how effective these arrangements are in performing verification checks?

<ESMA_QUESTION_456>

TYPE YOUR TEXT HERE
<ESMA_QUESTION_456>

Q457: What arrangements are currently in place on European regulated markets to facilitate access of members or participants to information being made public under Union law?

<ESMA_QUESTION_457>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_457>

Q458: What are your experiences in respect of such arrangements?

<ESMA_QUESTION_458>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_458>

Q459: How do you assess the effectiveness of these arrangements in achieving their goals?

<ESMA_QUESTION_459>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_459>

Q460: Do you agree with that, for the purpose of Article 51 (3) (2) of MiFID II, the arrangements for facilitating access to information shall encompass the Prospectus, Transparency and Market Abuse Directives (in the future the Market Abuse Regulation)? Do you consider that this should also include MiFIR trade transparency obligations?

<ESMA_QUESTION_460>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_460>

6.2. Suspension and Removal of Financial Instruments from Trading - connection between a derivative and the underlying financial instrument and standards for determining formats and timings of communications and publications

Q461: Do you agree with the specifications outlined above for the suspension or removal from trading of derivatives which are related to financial instruments that are suspended or removed?

<ESMA_QUESTION_461>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_461>

Q462: Do you think that any derivatives with indices or a basket of financial instruments as an underlying the pricing of which depends on multiple price inputs should be suspended if one or more of the instruments composing the index or the basket are suspended on the basis that they are sufficiently related? If so, what methodology would you propose for determining whether they are "sufficiently related"? Please explain.

<ESMA_QUESTION_462>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_462>

Q463: Do you agree with the principles outlined above for the timing and format of communications and publications to be effected by trading venue operators?

<ESMA_QUESTION_463>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_463>

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7. Commodity derivatives

7.1. Ancillary Activity

Q464: Do you see any difficulties in defining the term 'group' as proposed above?

<ESMA_QUESTION_464>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_464>

Q465: What are the advantages and disadvantages of the two alternative approaches mentioned above (taking into account non-EU activities versus taking into account only EU activities of a group)? Please provide reasons for your answer.

<ESMA_QUESTION_465>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_465>

Q466: What are the main challenges in relation to both approaches and how could they be addressed?

<ESMA_QUESTION_466>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_466>

Q467: Do you consider there are any difficulties concerning the suggested approach for assessing whether the ancillary activities constitute a minority of activities at group level? Do you consider that the proposed calculations appropriately factor in activity which is subject to the permitted exemptions under Article 2(4) MiFID II? If no, please explain why and provide an alternative proposal.

<ESMA_QUESTION_467>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_467>

Q468: Are there other approaches for assessing whether the ancillary activities constitute a minority of activities at group level that you would like to suggest? Please provide details and reasons.

<ESMA_QUESTION_468>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_468>

Q469: How should "minority of activities" be defined? Should minority be less than 50% or less (50 - x)%? Please provide reasons.

<ESMA_QUESTION_469>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_469>

Q470: Do you have a view on whether economic or accounting capital should be used in order to define the elements triggering the exemption from authorisation under MiFID II, available under Article 2(1)(j)? Please provide reasons.

<ESMA_QUESTION_470>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_470>

Q471: If economic capital were to be used as a measure, what do you understand to be encompassed by this term?

<ESMA_QUESTION_471>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_471>

Q472: Do you agree with the above assessment that the data available in the TRs will enable entities to perform the necessary calculations?

<ESMA_QUESTION_472>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_472>

Q473: What difficulties do you consider entities may encounter in obtaining the information that is necessary to define the size of their own trading activity and the size of the overall market trading activity from TRs? How could the identified difficulties be addressed?

<ESMA_QUESTION_473>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_473>

Q474: What do you consider to be the difficulties in defining the volume of the transactions entered into to fulfil liquidity obligations?

<ESMA_QUESTION_474>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_474>

Q475: How should the volume of the overall trading activity of the firm at group level and the volume of the transactions entered into in order to hedge physical activities be measured? (Number of contracts or nominal value? Period of time to be considered?)

<ESMA_QUESTION_475>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_475>

Q476: Do you agree with the level of granularity of asset classes suggested in order to provide for relative comparison between market participants?

<ESMA_QUESTION_476>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_476>

Q477: What difficulties could there be regarding the aggregation of TR data in order to obtain information on the size of the overall market trading activity? How could these difficulties be addressed?

<ESMA_QUESTION_477>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_477>

Q478: How should ESMA set the threshold above which persons fall within MiFID II's scope? At what percentage should the threshold be set? Please provide reasons for your response.

<ESMA_QUESTION_478>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_478>

Q479: Are there other approaches for determining the size of the trading activity that you would like to suggest?

<ESMA_QUESTION_479>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_479>

Q480: Are there other elements apart from the need for ancillary activities to constitute a minority of activities and the comparison between the size of the trading activity and size of the overall market trading activity that ESMA should take into account when defining whether an activity is ancillary to the main business?

<ESMA_QUESTION_480>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_480>

Q481: Do you see any difficulties with the interpretation of the hedging exemptions mentioned above under Article 2(4)(a) and (c) of MiFID II? How could potential difficulties be addressed?

<ESMA_QUESTION_481>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_481>

Q482: Do you agree with ESMA's proposal to take into account Article 10 of the Commission Delegated Regulation (EU) No 149/2013 supplementing EMIR in specifying the application of the hedging exemption under Article 2(4)(b) of MiFID II? How could any potential difficulties be addressed?

<ESMA_QUESTION_482>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_482>

Q483: Do you agree that the obligations to provide liquidity under Article 17(3) and Article 57(8)(d) of MiFID II should not be taken into account as an obligation triggering the hedging exemption mentioned above under Article 2(4)(c)?

<ESMA_QUESTION_483>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_483>

Q484: Could you provide any other specific examples of obligations of "transactions in commodity derivatives and emission allowances entered into to fulfil obligations to provide liquidity on a trading venue" which ESMA should take into account?

<ESMA_QUESTION_484>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_484>

Q485: Should the (timeframe for) assessment be linked to audit processes?

<ESMA_QUESTION_485>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_485>

Q486: How should seasonal variations be taken into account (for instance, if a firm puts on a maximum position at one point in the year and sells that down through the following twelve months should the calculation be taken at the maximum point or on average)?

<ESMA_QUESTION_486>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_486>

Q487: Which approach would be practical in relation to firms that may fall within the scope of MiFID in one year but qualify for exemption in another year?

<ESMA_QUESTION_487>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_487>

Q488: Do you see difficulties with regard to the two approaches suggested above?

<ESMA_QUESTION_488>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_488>

Q489: How could a possible interim approach be defined with regard to the suggestion mentioned above (i.e. annual notification but calculation on a three years rolling basis)?

<ESMA_QUESTION_489>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_489>

Q490: Do you agree that the competent authority to which the notification has to be made should be the one of the place of incorporation?

<ESMA_QUESTION_490>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_490>

7.2. Position Limits

Q491: Do you agree with ESMA's proposal to link the definition of a risk-reducing trade under MiFID II to the definition applicable under EMIR? If you do not agree, what alternative definition do you believe is appropriate?

<ESMA_QUESTION_491>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_491>

Q492: Do you agree with ESMA's proposed definition of a non-financial entity? If you do not agree, what alternative definition do you believe is appropriate?

<ESMA_QUESTION_492>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_492>

Q493: Should the regime for subsidiaries of a person other than entities that are wholly owned look to aggregate on the basis of a discrete percentage threshold or on a more subjective basis? What are the advantages and risks of either approach? Do you agree with the proposal that where the positions of an entity that is subject to substantial control by a person are aggregated, they are included in their entirety?

<ESMA_QUESTION_493>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_493>

Q494: Should the regime apply to the positions held by unconnected persons where they are acting together with a common purpose (for example, "concert party" arrangements where different market participants collude to act for common purpose)?

<ESMA_QUESTION_494>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_494>

Q495: Do you agree with the approach to link the definition of economically equivalent OTC contract, for the purpose of position limits, with the definitions used in other parts of MiFID II? If you do not agree, what alternative definition do you believe is appropriate?

<ESMA_QUESTION_495>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_495>

Q496: Do you agree that even where a contract is, or may be, cash-settled it is appropriate to base its equivalence on the substitutability of the underlying physical commodity that it is referenced to? If you do not agree, what alternative measures of equivalence could be used?

<ESMA_QUESTION_496>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_496>

Q497: Do you believe that the definition of "economically equivalent" that is used by the CFTC is appropriate for the purpose of defining the contracts that are not traded on a trading venue for the position limits regime of MiFID II? Give reasons to support your views as well as any suggested amendments or additions to this definition.

<ESMA_QUESTION_497>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_497>

Q498: What arrangements could be put in place to support competent authorities identifying what OTC contracts are considered to be economically equivalent to listed contracts traded on a trading venue? ?

<ESMA_QUESTION_498>
TYPE YOUR TEXT HERE

<ESMA_QUESTION_498>

Q499: Do you agree with ESMA's proposal that the "same" derivative contract occurs where an identical contract is listed independently on two or more different trading venues? What other alternative definitions of "same" could be applied to commodity derivatives?

<ESMA_QUESTION_499>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_499>

Q500: Do you agree with ESMA's proposals on aggregation and netting? How should ESMA address the practical obstacles to including within the assessment positions entered into OTC or on third country venues? Should ESMA adopt a model for pooling related contracts and should this extend to closely correlated contracts? How should equivalent contracts be converted into a similar metric to the exchange traded contract they are deemed equivalent to?

<ESMA_QUESTION_500>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_500>

Q501: Do you agree with ESMA's approach to defining market size for physically settled contracts? Is it appropriate for cash settled contracts to set position limits without taking into account the underlying physical market?

<ESMA_QUESTION_501>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_501>

Q502: Do you agree that it is preferable to set the position limit on a contract for a fixed (excluding exceptional circumstances) period rather than amending it on a real-time basis? What period do you believe is appropriate, considering in particular the factors of market evolution and operational efficiency?

<ESMA_QUESTION_502>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_502>

Q503: Once the position limits regime is implemented, what period do you feel is appropriate to give sufficient notice to persons of the subsequent adjustment of position limits?

<ESMA_QUESTION_503>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_503>

Q504: Should positions based on contracts entered into before the revision of position limits be grandfathered and if so how?

<ESMA_QUESTION_504>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_504>

Q505: Do you agree with ESMA's proposals for the determination of a central or primary trading venue for the purpose of establishing position limits in the same derivative contracts? If you do not agree, what practical alternative method should be used?

<ESMA_QUESTION_505>

TYPE YOUR TEXT HERE
<ESMA_QUESTION_505>

Q506: Should the level of “significant volume” be set at a different level to that proposed above? If yes, please explain what level should be applied, and how it may be determined on an ongoing basis?

<ESMA_QUESTION_506>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_506>

Q507: In using the maturity of commodity contracts as a factor, do you agree that competent authorities apply the methodology in a different way for the spot month and for the aggregate of all other months along the curve?

<ESMA_QUESTION_507>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_507>

Q508: What factors do you believe should be applied to reflect the differences in the nature of trading activity between the spot month and the forward months?

<ESMA_QUESTION_508>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_508>

Q509: Do you agree with ESMA’s proposal for trading venues to provide data on the deliverable supply underlying their contracts? If you do not agree, what considerations should be given to determining the deliverable supply for a contract?

<ESMA_QUESTION_509>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_509>

Q510: In the light of the fact that some commodity markets are truly global, do you consider that open interest in similar or identical contracts in non-EEA jurisdictions should be taken into account? If so, how do you propose doing this, given that data from some trading venues may not be available on the same basis or in the same timeframe as that from other trading venues?

<ESMA_QUESTION_510>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_510>

Q511: In the absence of published or easily obtained information on volatility in derivative and physical commodity markets, in what ways should ESMA reflect this factor in its methodology? Are there any alternative measures that may be obtained by ESMA for use in the methodology?

<ESMA_QUESTION_511>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_511>

Q512: Are there any other considerations related to the number and size of market participants that ESMA should consider in its methodology?

<ESMA_QUESTION_512>

TYPE YOUR TEXT HERE
<ESMA_QUESTION_512>

Q513: Are there any other considerations related to the characteristics of the underlying commodity market that ESMA should consider in its methodology?

<ESMA_QUESTION_513>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_513>

Q514: For new contracts, what approach should ESMA take in establishing a regime that facilitates continued market evolution within the framework of Article 57?

<ESMA_QUESTION_514>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_514>

Q515: The interpretation of the factors in the paragraphs above will be significant in applying ESMA's methodology; do you agree with ESMA's interpretation? If you do not agree with ESMA's interpretation, what aspects require amendment?

<ESMA_QUESTION_515>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_515>

Q516: Are there any other factors which should be included in the methodology for determining position limits? If so, state in which way (with reference to the proposed methodology explained below) they should be incorporated.

<ESMA_QUESTION_516>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_516>

Q517: What do you consider to be the risks and/or the advantages of applying a different methodology for determining position limits for prompt reference contracts compared to the methodology used for the position limit on forward maturities?

<ESMA_QUESTION_517>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_517>

Q518: How should the position limits regime reflect the specific risks present in the run up to contract expiry?

<ESMA_QUESTION_518>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_518>

Q519: If a different methodology is set for the prompt reference contract, would it be appropriate to make an exception where a contract other than the prompt is the key benchmark used by the market?

<ESMA_QUESTION_519>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_519>

Q520: Do you agree that the baseline for the methodology of setting a position limit should be the deliverable supply? What concrete examples of issues do you foresee in obtaining or using the measure?

<ESMA_QUESTION_520>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_520>

Q521: If you consider that a more appropriate measure exists to form the baseline of the methodology, please explain the measure and why it is more appropriate. Consideration should be given to the reliability and availability of such a measure in order to provide certainty to market participants.

<ESMA_QUESTION_521>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_521>

Q522: Do you agree with this approach for the proposed methodology? If you do not agree, what alternative methodology do you propose, considering the full scope of the requirements of Article 57 MiFID II?

<ESMA_QUESTION_522>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_522>

Q523: Do you have any views on the level at which the baseline (if relevant, for each different asset class) should be set, and the size of the adjustment numbers for each separate factor that ESMA must consider in the methodology defined by Article 57 MiFID II?

<ESMA_QUESTION_523>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_523>

Q524: Does the approach to asset classes have the right level of granularity to take into account market characteristics? Are the key characteristics the right ones to take into account? Are the conclusions by asset class appropriate?

<ESMA_QUESTION_524>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_524>

Q525: What trading venues or jurisdictions should ESMA take into consideration in defining its position limits methodology? What particular aspects of these experiences should be included within ESMA's work?

<ESMA_QUESTION_525>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_525>

Q526: Do you agree that the RTS should accommodate the flexibility to express position limits in the units appropriate to the individual market? Are there any other alternative measures or mechanisms by which position limits could be expressed?

<ESMA_QUESTION_526>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_526>

Q527: How should the methodology for setting limits take account of a daily contract structure, where this exists?

<ESMA_QUESTION_527>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_527>

Q528: Do you agree that limits for option positions should be set on the basis of delta equivalent values? What processes should be put in place to avoid manipulation of the process?

<ESMA_QUESTION_528>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_528>

Q529: Do you agree that the preferred methodology for the calculation of delta-equivalent futures positions is the use of the delta value that is published by trading venues? If you do not, please explain what methodology you prefer, and the reasons in favour of it?

<ESMA_QUESTION_529>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_529>

Q530: Do you agree that the description of the approach outlined above, combined with the publication of limits under Article 57(9), would fulfil the requirement to be transparent and non-discriminatory?

<ESMA_QUESTION_530>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_530>

Q531: What challenges are posed by transition and what areas of guidance should be provided on implementation? What transitional arrangements would be considered to be appropriate?

<ESMA_QUESTION_531>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_531>

7.3. Position Reporting

Q532: Do you agree that, in the interest of efficient reporting, the data requirements for position reporting required by Article 58 should contain elements to enable competent authorities and ESMA to monitor effectively position limits? If you do not agree, what alternative approach do you propose for the collection of information in order to efficiently and with the minimum of duplication meet the requirements of Article 57?

<ESMA_QUESTION_532>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_532>

Q533: Do you agree with ESMA's definition of a "position" for the purpose of Article 58? Do you agree that the same definition of position should be used for the purpose of Article 57? If you do not agree with either proposition, please provide details of a viable alternative definition.

<ESMA_QUESTION_533>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_533>

Q534: Do you agree with ESMA's approach to the reporting of spread and other strategy trades? If you do not agree, what approach can be practically implemented for the definition and reporting of these trades?

<ESMA_QUESTION_534>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_534>

Q535: Do you agree with ESMA's proposed approach to use reporting protocols used by other market and regulatory initiatives, in particular, those being considered for transaction reporting under MiFID II?

<ESMA_QUESTION_535>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_535>

Q536: Do you have any specific comments on the proposed identification of legal persons and/or natural persons? Do you consider there are any practical challenges to ESMA's proposals? If yes, please explain them and propose solutions to resolve them.

<ESMA_QUESTION_536>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_536>

Q537: What are your views on these three alternative approaches for reporting the positions of an end client where there are multiple parties involved in the transaction chain? Do you have a preferred solution from the three alternatives that are described?

<ESMA_QUESTION_537>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_537>

Q538: What alternative structures or solutions are possible to meet the obligations under Article 58 to identify the positions of end clients? What are the advantages or disadvantages of these structures?

<ESMA_QUESTION_538>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_538>

Q539: Do you agree with ESMA's proposal that only volumes traded on-exchange should be used to determine the central competent authority to which reports are made? If you do not agree, what alternative structure may be used to determine the destination of position reports?

<ESMA_QUESTION_539>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_539>

Q540: Do you agree that position reporting requirements should seek to use reporting formats from other market or regulatory initiatives? If not mentioned above, what formats and initiatives should ESMA consider?

<ESMA_QUESTION_540>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_540>

Q541: Do you agree that ESMA should require reference data from trading venues and investment firms on commodity derivatives, emission allowances, and derivatives thereof in order to increase the efficiency of trade reporting?

<ESMA_QUESTION_541>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_541>

Q542: What is your view on the use of existing elements of the market infrastructure for position reporting of both on-venue and economically equivalent OTC contracts? If you have any comments on how firms and trading venues may efficiently create a reporting infrastructure, please give details in your explanation.

<ESMA_QUESTION_542>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_542>

Q543: For what reasons may it be appropriate to require the reporting of option positions on a delta-equivalent basis? If an additional requirement to report delta-equivalent positions is established, how should the relevant delta value be determined?

<ESMA_QUESTION_543>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_543>

Q544: Does the proposed set of data fields capture all necessary information to meet the requirements of Article 58(1)(b) MiFID II? If not, do you have any proposals for amendments, deletions or additional data fields to add the list above?

<ESMA_QUESTION_544>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_544>

Q545: Are there any other fields that should be included in the Commitment of Traders Report published each week by trading venues other than those shown above?

<ESMA_QUESTION_545>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_545>

8. Market data reporting

8.1. Obligation to report transactions

Q546: Do you agree with ESMA's proposal for what constitutes a 'transaction' and 'execution of a transaction' for the purposes of Article 26 of MiFIR? If not, please provide reasons.

<ESMA_QUESTION_546>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_546>

Q547: Do you anticipate any difficulties in identifying when your investment firm has executed a transaction in accordance with the above principles?

<ESMA_QUESTION_547>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_547>

Q548: Is there any other activity that should not be reportable under Article 26 of MiFIR?

<ESMA_QUESTION_548>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_548>

Q549: Do you foresee any difficulties with the suggested approach? Please elaborate.

<ESMA_QUESTION_549>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_549>

Q550: We invite your comments on the proposed fields and population of the fields. Please provide specific references to the fields which you are discussing in your response.

<ESMA_QUESTION_550>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_550>

Q551: Do you have any comments on the designation to identify the client and the client information and details that are to be included in transaction reports?

<ESMA_QUESTION_551>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_551>

Q552: What are your views on the general approach to determining the relevant trader to be identified?

<ESMA_QUESTION_552>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_552>

Q553: In particular, do you agree with ESMA's proposed approach to assigning a trader ID designation for committee decisions? If not, what do you think is the best way for NCAs to obtain accurate information about committee decisions?

<ESMA_QUESTION_553>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_553>

Q554: Do you have any views on how to identify the relevant trader in the cases of Direct Market Access and Sponsored Access?

<ESMA_QUESTION_554>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_554>

Q555: Do you believe that the approach outlined above is appropriate for identifying the 'computer algorithm within the investment firm responsible for the investment decision and the execution of the transaction'? If not, what difficulties do you see with the approach and what do you believe should be an alternative approach?

<ESMA_QUESTION_555>
The FIA Associations[51] believe the prescriptive criteria proposed by ESMA on page 454 in Paragraph 82 comprising the process for determining identifiers for algorithms are not appropriate and will add complexity, confusion and potential technical difficulties to the order entry process. Below we set out the reasons we believe the following requirements are not feasible from a technical perspective and set out a suggested alternative:

(i) the requirement that an exclusive designation must be given to each "unique set of code" constituting an algorithm;

[51] This response is submitted jointly on behalf of the Futures Industry Association ("FIA"), Futures Industry Association Europe ("FIA Europe") and the FIA European Principal Traders Association ("FIA EPTA").

FIA is the leading trade organisation for the futures, options and over-the-counter cleared derivatives markets. It is the only association representative of all organizations that have an interest in the listed derivatives markets. Its membership includes the world's largest derivatives clearing firms as well as leading derivatives exchanges from more than 20 countries. As the principal members of the derivatives clearing organisations, our member firms play a critical role in the reduction of systematic risk in the financial markets. They provide the majority of the funds that support these clearinghouses and commit a substantial amount of their own capital to guarantee customer transactions. FIA's core constituency consists of futures commission merchants, and the primary focus of the association is the global use of exchanges, trading systems and clearinghouse for derivatives transactions. FIA's regular members, which act as the majority clearing members of the US exchanges, handle more than 90 percent of the customer funds held for trading on US futures exchanges.

FIA Europe, formerly the Futures and Options Association (FOA), represents some 175 firms involved in the exchange-traded and centrally-cleared derivatives markets – including banks, brokers, commodity firms, exchanges, CCPs, vendors, law firms and consultants. FIA Europe works with its members to maintain constructive dialogue with government and regulatory authorities and deliver high standards of industry practice. FIA Europe, last year, formed an affiliation with FIA under a new structure – FIA Global. Under this arrangement, FIA, FIA Europe and FIA Asia have strengthened their influence on cross-border issues, substantially increasing the coordination and information flow between regions and providing a powerful global voice to express the views of their members. The organisations preserve their ability to deal with legislative, regulatory and market issues in their respective time zones and continue to operate with their own leadership and staff, separate boards of directors and distinct memberships.

FIA EPTA is affiliated with FIA and is comprised of more than 20 firms that trade their own capital in the exchange-traded markets. FIA EPTA members engage in manual, automated and hybrid methods of trading and are active in a variety of asset classes, such as equities, foreign exchange, commodities and fixed income. Members of FIA EPTA are a critical source of liquidity in the exchange-traded markets, allowing those who use the markets to manage their business risks to enter and exit the markets efficiently.

(ii) the same identifier should apply for a specific algorithmic code regardless of the products or markets that the algorithm applies to; and

(iii) an algorithm's designation must be unique over time.

(i) **First**, ESMA states investment firms must give "an exclusive designation to each unique set of code that constitutes an algorithm."

Here, the problem lies in the requirement that an ID apply to "*a unique set of code constituting an algorithm.*" From a developer's perspective, providing a new identifier for each element of "*unique code*" would normally result in a constantly changing and variable code string – in other words, a nearly infinite number of IDs.

Software development is an iterative process. In some cases code may have many independent modular elements and may change in material ways even during the trading cycle. Some trading algorithms are made up of a sum of software sub-parts, which are built to receive and relay data from other correlated markets, or perform other separate calculations to handle complex events. These sub-components of code may have been written by separate developers and have a variation of change different to the 'core' code. Some changes may be material to the trading actions of an algorithm, and some may be meaningless. This makes it extremely difficult to identify whether the overarching algorithm is a unique 'whole' or has changed by means of its sub-parts.

For example, while perhaps not common, some trading computational models based on artificial neural networks (ANNs) are capable of machine learning and pattern recognition. As such, the relevant code may automatically adapt and evolve (as with evolving data or with adaptive configurations) while in operation.

Thus, the sheer number of IDs that would be generated in the market following this approach would border on infinite. Such a requirement will create enormous data pollution – for both firms and regulators – without serving an attainable surveillance purpose. Any designation more granular than a strategy will not be useful to a regulator in analysing abuse, anyway, and will just generate noise.

Moreover, while computers can execute calculations at extreme speeds, they cannot store or write data at the same tempo. The algorithm flagging requirements as currently proposed will not only require firms to store exponentially more data, demanding an unforeseeable increase in processing power compared to what they currently need to operate their trading algorithms; it will also add significant latency to trading and risk management systems. While some observers might not see a problem with slowing markets down, we would like to point out that this effect might threaten their economic utility[52].

We do not believe this is the outcome ESMA intends or has foreseen in requiring a new identifier for each element of "unique code" resulting in a constantly changing and variable code string.

[52] As set out in our response to Question 167 of the Consultation Paper, the ability of market makers to provide agile quote updates reduces risk for the market as a whole by minimising the chance of mispricing, evening out price movements and facilitating faster recoveries from volatility through small, quick steps as opposed to bigger, slower updates. This ensures tight spreads by allowing market makers to respond quickly to changing markets rather than having to rely on wider spreads for managing risks.

We acknowledge that the guidelines released by the Exchange Supervisory Authority of the State of Hessen regarding the German algorithm flagging rules try to avoid this outcome by striking a middle path and requiring changed identifiers when the algorithm "*changes in a material way*."[53]

However, we do not recommend ESMA follow the State of Hessen's approach as a blueprint for an implementation for Europe because "materiality" is a subjective standard that is difficult to maintain without an extensive and inflexible set of guidelines. For example, as discussed earlier, when is a change triggered by a software sub-component a material change to the core code? This would be extremely difficult to determine in a harmonised way. We have been, and remain, concerned that the implementation of the German algorithm flagging rules will prove to be unsustainable, will have a dampening effect on the market, and ultimately overwhelm the relevant regulator with data that it will have trouble storing and making sense of.

Instead, the FIA Associations suggest the use of one identifying number that represents a "*unique strategy*" (not "unique code"), where "*unique strategy*" is defined as "*the software that generates trading actions based on a trading model.*" Each firm should be required to maintain a log of all elements of the software in use at the time of an order and be able to use the single identification number for the unique strategy to provide a reference of that code.

This approach is in line with ESMA's statement that "*a pragmatic solution should be adopted for the identification of algorithms. The investment firm will have responsibility and discretion over how it identifies its algorithms throughout the lifecycle of the algorithm.*"

(ii) Second, ESMA proposes that the same algorithm identifier should apply for a specific algorithm code regardless of the products or markets that the algorithm applies to (82 (iii), page 454).

ESMA hereby explicitly points to the need for a precise definition of the term 'algorithm' and the chain of processes deemed to determine algorithmic trading (see point 1).

However, a volume-weighted average price (VWAP) algorithm used in the cash market might be different from a VWAP algorithm used in the derivatives market.

The FIA Associations therefore recommend following our suggestion to use one identifying number that represents a "*unique strategy*" which implicitly reflects the differences in a specific strategy per product/market.

(iii) Third, ESMA proposed that an algorithm's designation must be unique over time (82 (iv), page 453) and not be used again once the usage of an algorithm discontinued.

Even when our recommendation to use one ID per "*unique strategy*" is followed, we still expect a high number of IDs to be active in markets. Therefore, this uniqueness requirement might encounter potential restrictions in terms of technical capabilities of implementations within trading systems.

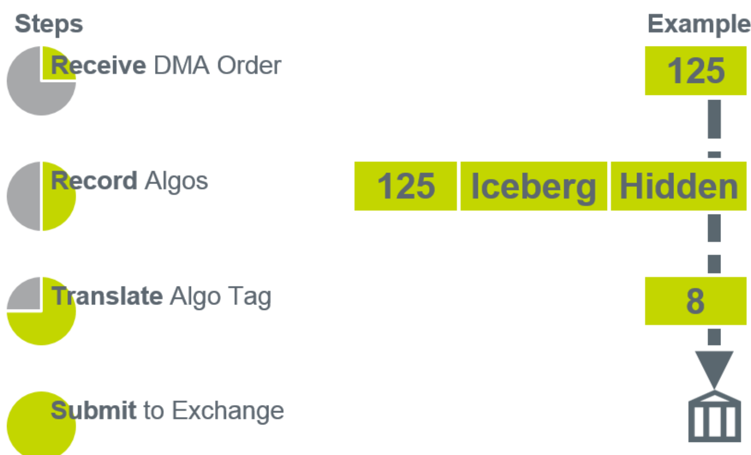
The FIA Associations believe that such uniqueness principle will still be fulfilled as long as the ID being used to identify the discontinued algorithm will be shelved for a period of time (e.g. three months).

[53] Exchange Supervisory Authority of the State of Hessen, Guidelines to the adherence to the requirement of the labelling of trading algorithms, 20 December 2013, p. 5, available at: https://wirtschaft.hessen.de/sites/default/files/media/guidelines_to_the_adherence_to_the_requirement_of_the_labelling_of_trading_algorithms_13-12-20.pdf .

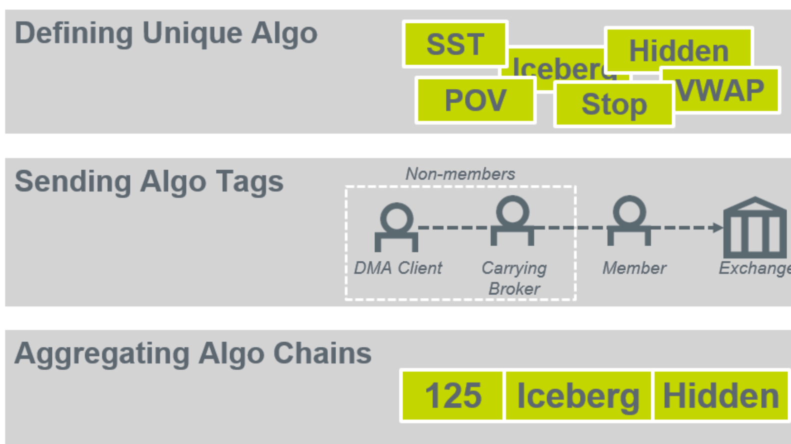
(iv) Finally, above we discuss the methodology for determining an algorithm ID, but equally important are the mechanics of how the market uses this ID in end-to-end order flow, including transaction reporting. The FIA Associations are concerned that uniform implementation of algorithm flagging will be impossible without second level detailing of how this should be harmonised across Europe.

The minimum requirements suggested by ESMA in the discussion paper in the context of transaction reporting could be used as a starting point but should be complemented by additional information about how to flag.

The FIA Associations recommends the method below for aggregating algorithm ID chains into a single identifier to the market and for purposes of transaction reporting, which has already been adopted by some market participants in order to comply with German algorithm flagging requirements.



Source - Fidessa, 2014 International Derivatives Expo (IDX)



Source – Fidessa, 2014 International Derivatives Expo (IDX)

First, the investment firm generating an order will flag that order with a single identifier designating the unique strategy underlying the order. To the extent an algorithm incorporates more than one strategy, this single identifier at firm level will be an aggregate ID representing multiple strategies, for example, EU-REX, hidden, VWAP. Each firm should maintain a log of all elements of the software in use at the time of an order and be able to use the single identification number for the unique strategy to provide a reference of that code.

Second, this order, with a unique ID, goes either directly to the trading venue or via a DEA provider. If the order goes first to a DEA provider, the DEA provider aggregates the investment firm's unique ID with an additional element, creating a new, unique designation to flag the order into the market in a single field.

At every step in the order flow process, a participant maintains a table populated with its unique strategy algorithm ID and sends this populated table on to next participant in the chain, who then aggregates this label into yet a new ID. This method enables order persistence and the labelling of unique permutations of algorithm ID chains, but unlike the German algorithm flagging rules, does not risk generating an infinite number of IDs due to the fact that the initial determinant is at the (useful) level of "unique strategy" rather than "unique code."

With respect to transaction reporting, every investment firm in the order flow process would report its own unique flag.

This solution is relatively easy to implement from a practical perspective, as has been shown by the fact that some market participants have implemented it in a similar fashion already.

The FIA Associations recommend that ESMA issue respective guidelines and recommendations, taking into account the principles we outline above, under Art. 16.1 Regulation 1095/2010 ("ESMA Regulation") in due course.

<ESMA_QUESTION_555>

Q556: Do you foresee any problem with identifying the specific waiver(s) under which the trade took place in a transaction report? If so, please provide details.

<ESMA_QUESTION_556>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_556>

Q557: Do you agree with ESMA's proposed approach to adopt a simple short sale flagging approach for transaction reports? If not, what other approaches do you believe ESMA should consider and why?

<ESMA_QUESTION_557>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_557>

Q558: Which option do you believe is most appropriate for flagging short sales? Alternatively, what other approaches do you think ESMA should consider and why?

<ESMA_QUESTION_558>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_558>

Q559: What are your views regarding the two options above?

<ESMA_QUESTION_559>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_559>

Q560: Do you agree with ESMA's proposed approach in relation to reporting aggregated transactions? If not, what other alternative approaches do you think ESMA should consider and why?

<ESMA_QUESTION_560>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_560>

Q561: Are there any other particular issues or trading scenarios that ESMA should consider in light of the short selling flag?

<ESMA_QUESTION_561>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_561>

Q562: Do you agree with ESMA's proposed approach for reporting financial instruments over baskets? If not, what other approaches do you believe ESMA should consider and why?

<ESMA_QUESTION_562>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_562>

Q563: Which option is preferable for reporting financial instruments over indices? Would you have any difficulty in applying any of the three approaches, such as determining the weighting of the index or determining whether the index is the underlying in another financial instrument? Alternatively, are there any other approaches which you believe ESMA should consider?

<ESMA_QUESTION_563>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_563>

Q564: Do you think the current MiFID approach to branch reporting should be maintained?

<ESMA_QUESTION_564>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_564>

Q565: Do you anticipate any difficulties in implementing the branch reporting requirement proposed above?

<ESMA_QUESTION_565>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_565>

Q566: Is the proposed list of criteria sufficient, or should ESMA consider other/extra criteria?

<ESMA_QUESTION_566>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_566>

Q567: Which format, not limited to the ones above, do you think is most suitable for the purposes of transaction reporting under Article 26 of MiFIR? Please provide a detailed explanation including cost-benefit considerations.

<ESMA_QUESTION_567>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_567>

8.2. Obligation to supply financial instrument reference data

Q568: Do you anticipate any difficulties in providing, at least daily, a delta file which only includes updates?

<ESMA_QUESTION_568>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_568>

Q569: Do you anticipate any difficulties in providing, at least daily, a full file containing all the financial instruments?

<ESMA_QUESTION_569>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_569>

Q570: Do you anticipate any difficulties in providing a combination of delta files and full files?

<ESMA_QUESTION_570>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_570>

Q571: Do you anticipate any difficulties in providing details of financial instruments twice per day?

<ESMA_QUESTION_571>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_571>

Q572: What other aspects should ESMA consider when determining a suitable solution for the timeframes of the notifications? Please include in your response any foreseen technical limitations.

<ESMA_QUESTION_572>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_572>

Q573: Do you agree with the proposed fields? Do trading venues and investment firms have access to the specified reference data elements in order to populate the proposed fields?

<ESMA_QUESTION_573>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_573>

Q574: Are you aware of any available industry classification standards you would consider appropriate?

<ESMA_QUESTION_574>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_574>

Q575: For both MiFID and MAR (OTC) derivatives based on indexes are in scope. Therefore it could be helpful to publish a list of relevant indexes. Do you foresee any difficulties in providing reference data for indexes listed on your trading venue? Furthermore, what reference data could you provide on indexes?

<ESMA_QUESTION_575>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_575>

Q576: Do you agree with ESMA's intention to maintain the current RCA determination rules?

<ESMA_QUESTION_576>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_576>

Q577: What criteria would you consider appropriate to establish the RCA for instruments that are currently not covered by the RCA rule?

<ESMA_QUESTION_577>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_577>

<ESMA_QUESTION_1>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_1>

8.3. Obligation to maintain records of orders

Q578: In your view, which option (and, where relevant, methodology) is more appropriate for implementation? Please elaborate.

<ESMA_QUESTION_578>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_578>

Q579: In your view, what are the data elements that cannot be harmonised? Please elaborate.

<ESMA_QUESTION_579>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_579>

Q580: For those elements that would have to be harmonised under Option 2 or under Option 3, do you think industry standards/protocols could be utilised? Please elaborate.

<ESMA_QUESTION_580>
TYPE YOUR TEXT HERE

<ESMA_QUESTION_580>

Q581: Do you foresee any difficulties with the proposed approach for the use of LEI?

<ESMA_QUESTION_581>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_581>

Q582: Do you foresee any difficulties maintaining records of the Client IDs related with the orders submitted by their members/participants? If so, please elaborate.

<ESMA_QUESTION_582>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_582>

Q583: Are there any other solutions you would consider as appropriate to track clients' order flows through member firms/participants of trading venues and to link orders and transactions coming from the same member firm/participant?

<ESMA_QUESTION_583>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_583>

Q584: Do you believe that this approach allows the order to be uniquely identified If not, please elaborate

<ESMA_QUESTION_584>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_584>

Q585: Do you foresee any difficulties with the implementation of this approach? Please elaborate

<ESMA_QUESTION_585>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_585>

Q586: Do you foresee any difficulties with the proposed approach? Please elaborate

<ESMA_QUESTION_586>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_586>

Q587: Do you foresee any difficulties with the proposed approach? Please elaborate.

<ESMA_QUESTION_587>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_587>

Q588: Would the breakdown in the two categories of order types create major issues in terms of mapping of the orders by the Trading Venues and IT developments? Please elaborate

<ESMA_QUESTION_588>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_588>

Q589: Do you foresee any problems with the proposed approach?

<ESMA_QUESTION_589>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_589>

Q590: Are the proposed validity periods relevant and complete? Should additional validity period(s) be provided? Please elaborate.

<ESMA_QUESTION_590>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_590>

Q591: Do you agree that standardised default time stamps regarding the date and time at which the order shall automatically and ultimately be removed from the order book relevantly supplements the validity period flags?

<ESMA_QUESTION_591>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_591>

Q592: Do venues use a priority number to determine execution priority or a combination of priority time stamp and sequence number?

<ESMA_QUESTION_592>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_592>

Q593: Do you foresee any difficulties with the three options described above? Please elaborate.

<ESMA_QUESTION_593>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_593>

Q594: Is the list of specific order instructions provided above relevant? Should this list be supplemented? Please elaborate.

<ESMA_QUESTION_594>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_594>

Q595: Are there any other type of events that should be considered?

<ESMA_QUESTION_595>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_595>

Q596: Do you foresee any difficulties with the proposed approach? Please elaborate.

<ESMA_QUESTION_596>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_596>

Q597: Do you foresee any problems with the proposed approach? Do you consider any other alternative in order to inform about orders placed by market makers and other liquidity providers?

<ESMA_QUESTION_597>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_597>

Q598: Do you foresee any difficulties in generating a transaction ID code that links the order with the executed transaction that stems from that order in the information that has to be kept at the disposal of the CAs? Please elaborate.

<ESMA_QUESTION_598>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_598>

Q599: Do you foresee any difficulties with maintaining this information? Please elaborate.

<ESMA_QUESTION_599>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_599>

8.4. Requirement to maintain records of orders for firms engaging in high-frequency algorithmic trading techniques (Art. 17(7) of MIFID II)[54]

Q600: Do you foresee any difficulties with the elements of data to be stored proposed in the above paragraph? If so, please elaborate.

<ESMA_QUESTION_600>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_600>

Q601: Do you foresee any difficulties in complying with the proposed timeframe?

<ESMA_QUESTION_601>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_601>

8.5. Synchronisation of business clocks

Q602: Would you prefer a synchronisation at a national or at a pan-European level? Please elaborate. If you would prefer synchronisation to a single source, please indicate which would be the reference clock for those purposes.

<ESMA_QUESTION_602>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_602>

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[54] Please note that this section has to be read in conjunction with the section on the “Record keeping and co-operation with national competent authorities” in this DP.

Q603: Do you agree with the requirement to synchronise clocks to the microsecond level?

<ESMA_QUESTION_603>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_603>

Q604: Which would be the maximum divergence that should be permitted with respect to the reference clock? How often should any divergence be corrected?

<ESMA_QUESTION_604>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_604>

9. Post-trading issues

9.1. Obligation to clear derivatives traded on regulated markets and timing of acceptance for clearing (STP)

Q605: What are your views generally on (1) the systems, procedures, arrangements supporting the flow of information to the CCP, (2) the operational process that should be in place to perform the transfer of margins, (3) the relevant parties involved these processes and the time required for each of the steps?

<ESMA_QUESTION_605>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_605>

Q606: In particular, who are currently responsible, in the ETD and OTC context, for obtaining the information required for clearing and for submitting the transaction to a CCP for clearing? Do you consider that anything should be changed in this respect? What are the current timeframes, in the ETD and OTC context, between the conclusion of the contract and the exchange of information required for clearing on one hand and on the other hand between the exchange of information and the submission of the transaction to the CPP?

<ESMA_QUESTION_606>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_606>

Q607: What are your views on the balance of these risks against the benefits of STP for the derivatives market and on the manner to mitigate such risks at the different levels of the clearing chain?

<ESMA_QUESTION_607>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_607>

Q608: When does the CM assume the responsibility of the transactions? At the time when the CCP accepts the transaction or at a different moment in time?

<ESMA_QUESTION_608>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_608>

Q609: What are your views on how practicable it would be for CM to validate the transaction before their submission to the CCP? What would the CM require for this purpose and the timeframe required? How would this validation process fit with STP?

<ESMA_QUESTION_609>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_609>

Q610: What are your views on the manner to determine the timeframe for (1) the exchange of information required for clearing, (2) the submission of a transaction to the CCP, and the constraints and requirements to consider for parties involved in both the ETD and OTC contexts?

<ESMA_QUESTION_610>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_610>

Q611: What are your views on the systems, procedures, arrangements and timeframe for (1) the submission of a transaction to the CCP and (2) the acceptance or rejection of a transaction by the CCP in view of the operational process required for a strong product validation in the context of ETD and OTC? How should it compare with the current process and timeframe? Does the current practice envisage a product validation?

<ESMA_QUESTION_611>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_611>

Q612: What should be the degree of flexibility for CM, its timeframe, and the characteristics of the systems, procedures and arrangements required to supporting that flexibility? How should it compare to the current practices and timeframe?

<ESMA_QUESTION_612>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_612>

Q613: What are your views on the treatment of rejected transactions for transactions subject to the clearing requirement and those cleared on a voluntary basis? Do you agree that the framework should be set in advance?

<ESMA_QUESTION_613>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_613>

9.2. Indirect Clearing Arrangements

Q614: Is there any reason for ESMA to adopt a different approach (1) from the one under EMIR, (2) for OTC and ETD? If so, please explain your reasons.

<ESMA_QUESTION_614>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_614>

Q615: In your view, how should it compare with current practice?

<ESMA_QUESTION_615>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_615>