FIA EPTA response to the German Ministry of Finance Consultation on MiFID II/MiFIR

15 March 2019

Introduction and executive summary

The FIA European Principal Traders Association (FIA EPTA) represents 28 independent European Principal Trading Firms (PTFs) which deal on own account, using their own money for their own risk, to provide liquidity and immediate risk-transfer in exchange-traded and centrally-cleared markets for a wide range of instruments, including shares, options, futures and ETFs. As market makers and liquidity providers our members contribute to efficient, resilient, and high-quality secondary markets that serve the investment and risk management needs of end-investors and corporates throughout the EU. Our members are active participants in the German market, in particular on Eurex Exchange, the Frankfurt Stock Exchange (Xetra) and Equiduct/Boerse Berlin. Moreover, our members are important sources of liquidity for German institutional investors accessing liquidity pools across Europe.

FIA EPTA supports transparent, robust and safe markets with a level playing field for all appropriately regulated market participants. We have consistently been supporting the aim of the market structure reforms laid out in MiFID II/MiFIR. FIA EPTA welcomes the opportunity to respond to the consultation by the German Ministry of Finance on the implementation experiences of MiFID II in its first year of its application. We stand ready to support the Ministry with any further information which it would require.

Overall, we believe MiFID II/MiFIR has had a positive impact on European financial markets and has contributed to making markets more efficient, resilient and transparent. When looking at how to further improve the legislative framework we believe it is imperative to have these guiding principles in mind.

Our response suggests changes we believe would further improve the MiFID II/MiFIR legislative framework in achieving the aims and aspirations originally set out. Our response reflects upon key high-level policy issues, followed by more granular examples of the interaction and functioning of the MiFID II/MiFIR regime for various product groups and requirements. We use empirical evidence to underline our position. More specifically, our response identifies five areas where we consider improvements are needed**: (i) transparency, (ii) open-access, (iii) market structure; (iv) market microstructure; and (v) market data**, as summarised below:

Transparency

Implementation issues relating to the MiFID II transparency regime have frustrated the overall objective of increasing market transparency. FIA EPTA members have seen issues in relation to several different financial instruments:

Non-equities

- The concept of "traded on a trading venue" (ToTV) is being interpreted too narrowly;
- Of the instruments that are being considered ToTV at the moment, most are eligible for waivers and deferrals from transparency requirements. This undermines the objective of increasing transparency;
- Poor publication practices of trading venues and Approved Publication Agreements (APAs) hinder the ability for market participants to access data.

Shares

- Issues with the quality and consistency of post trade reporting remain.

Exchange Traded Products (ETFs/ETCs/ETNs)

- The classification of Exchange-Traded Notes (ETNs) as non-equities ('bonds') rather than as equity-like instruments leads to confusion and unnecessarily reduces transparency and liquidity for these instruments under MiFID II.

Equity and non-equity options

- There is no set process for notional amounts to get converted to a lot size for the purpose of the LIS thresholds;
- The model used for determining the LIS threshold value for fixed income options is substantially different to the approach taken for index and equity options;
- Currently, options trading venues are allowed to have delayed publications for up to 2 days where 1 day would be more appropriate.

Structured products

- Listed structured products suffer from a lack of transparency and are subject to significant conflicts of interest, while being too complex for retail investors to price correctly. Such structured products cause significant and endemic losses making them inappropriate for retail investors.

Open access

MiFID II/MiFIR establishes open and non-discriminatory access provisions for trading venues but implementation issues exist across asset classes. Important fixed income markets, such as for government bonds, remain inaccessible for non-bank liquidity providers, due to discriminatory access criteria employed by certain trading venues.

Market structure

There is an inconsistency across the EU with respect to the application and interpretation of the Share Trading Obligation (STO) as set out in Article 23 of MIFIR. Under the current design of the STO, double listing practices of third country equities by certain European trading venues lead to a situation where investment firms are de-facto prohibited from trading the more liquid shares in the original third-country listing venue.

Market microstructure

The practical implementation of the market making registration requirements and order-to-trade ration rules by trading venues has varied. Certain practices are at odds with the regulatory intention of MiFID II and should be reconsidered.

Market data

We witness several adverse issues with regard to the access to and pricing structures to market data from exchanges and data vendors creating tensions with the MiFIR obligation to make data available on a reasonable commercial basis and in a non-discriminatory manner.

1. Transparency

FIA EPTA strongly supports MiFID II's objective to increase pre- and post-trade transparency for end investors in both equities (MiFIR Articles 3, 6, 14, and 20) and non-equities (MiFIR Articles 8, 10, 18, and 21) asset classes. Increasing transparency leads to increasing liquidity, competition, and market resiliency, reducing systemic risk and information asymmetries, and assists investors in achieving best execution. Unfortunately, several implementation issues relating to the MiFID II transparency regime are impeding the overall objective of increasing market transparency. We detail those implementation issues with different products below and would welcome the Ministry to address them as a matter of priority with the European Commission, the relevant German competent authorities and/or ESMA.

Non-equities

The current experience with the MiFID II transparency regime for non-equities is that it has failed to meaningfully increase transparency for end-investors. Increased pre-trade and post-trade transparency in these historically opaque markets is designed to increase competition, liquidity and counterparty diversity, reduce systemic risk, and facilitate best execution. These objectives are important to continuing to expand EU capital markets, including improving government bond markets. Below, we provide the three main reasons for this outcome, and potential solutions:

The concept of "traded on a trading venue" (ToTV) is being interpreted too narrowly. The ToTV concept seeks to assess which off-venue derivatives are substantially similar to derivatives traded on trading venues. At the moment, nearly each of the 48 reference data fields in RTS 23 (which details data standards and formats for financial instrument reference data) is required to match in order for an off-venue transaction to be considered equivalent to an on-venue transaction and therefore subject to the MiFID II transparency regime. Data quality issues and a lack of validation rules around certain reference data fields are resulting in almost all off-venue transactions being considered out-of-scope for transparency at the moment. For example, according to data from ANNA-DSB, only ~2% of all OTC ISINs have been reported to the ESMA's Financial Instrument Reference Data System (FIRDS), highlighting that the vast majority of the OTC derivatives market remains out-of-scope and opaque.[1]

We would recommend that the concept of ToTV either be re-interpreted or removed. The ESMA Opinion for derivatives[2] should be revised in order to ensure more trading volume is subject to the MiFID II transparency regime. Regulators should assess the percentage of trading activity in a specific asset class that is considered ToTV on a regular basis.

[1] See https://www.anna-dsb.com/2018/05/04/firds-data-analysis-for-april-2018/. We note that the sheer volume of ISINs being created for derivatives (see https://www.anna-dsb.com/2019/02/07/monthly-dsb-metrics-review-january-2019/) also creates difficulties for market participants with respect to determining whether a specific instrument is in-scope for transaction reporting and transparency requirements. We recommend removing the "Expiry Date" field from the ISIN in order to reduce the number of ISINs being created for derivatives.

[2] ESMA Opinion on "OTC derivatives traded on a trading venue" (22 May 2017) at paragraph 11, available at: https://www.esma.europa.eu/sites/default/files/library/esma70-156-117_mifir_opinion_on_totv.pdf.

Too many waivers and deferrals. Of the non-equities instruments that are being considered ToTV at the moment, most are eligible for waivers and deferrals from transparency requirements. This undermines the objective of increasing transparency, as liquid non-equities instruments are exempted from pre-trade transparency and are provided with four-week deferrals from post-trade transparency.

> We would recommend assessing the percentage of trading volume that is currently eligible for each exception and recalibrate the regime accordingly. For example, OTC derivatives subject to the EMIR clearing obligation are highly liquid and should not be eligible for complete exemptions from pre-trade transparency or four-week deferrals from post-trade transparency.
> In addition, size specific to the instrument (SSTI) thresholds should be increased to expand the scope of the transparency regime. The post-trade deferral regime should be simplified by reducing the number of available options and removing the extended deferral of four weeks, which is far too long a delay for instruments that are traded on trading venues.

Poor publication practices of trading venues and Approved Application Agreements (APAs). With respect to the few transactions that are currently subject to MiFID II transparency requirements, APAs and trading venues are making it difficult to access the transparency data free of charge 15 minutes after publication as required under MiFID II. With only delayed, fragmented, and inconsistently formatted data provided by APAs and trading venues, market transparency goals remain unfulfilled and market participants are compelled to purchase expensive data packages from the APAs and trading venues. ESMA issued guidance on this topic in November 2018[3], but it has yet to be fully implemented.

> We would recommend to ensure that the ESMA guidance is implemented in a consistent manner, as investors are unable to benefit from the MiFID II transparency regime without access to the available data. We would also recommend that regulators consider ways to consolidate the available market data as no consolidated tape provider (CTP) has emerged for non-equities.

Shares

FIA EPTA supports the spirit of MiFID II to promote transparency, move trading from OTC markets to regulated trading venues and systematic internalisers, and to differentiate between bilateral and multilateral trading activity to safeguard the price formation process on transparent regulated venues and deliver a level playing field. However, we consider that the application and framework for post-trade transparency for equities would need further scrutiny:

Issues with the quality and consistency of post trade reporting. The prevalence of systematic internalisers (SIs) and investment firms trading OTC, make it difficult to assess whether MiFID II has succeeded to meaningfully increase transparency in equities for end investors. Specifically, relatively high volumes of trade reports by systematic internalisers that are being flagged as "non-addressable liquidity", show 60.4% and 24.9% of systematic internaliser trade reports (by notional) being flagged this way (taking trade reports in instruments in the DAX 30 as examples)[4].

[3] ESMA, General Q&As on transparency topics (Chapter 2, Q&A 10, last updated on 14 November 2018), available on pp. 24-26 at https://www.esma.europa.eu/sites/default/files/library/esma70-872942901-35_qas_transparency_issues.pdf.
[4] Data for 13/11/18 and 19/02/19 sourced from Bloomberg LLP and is based on OTC trades reported to Cboe's BXTR APA service in the instruments' primary listing currency.

FIA EPTA members recognise that this is a highly technical area and would call for further broad regulatory engagement with the industry to ensure the MiFID II/MiFIR regime delivers clear and unambiguous requirements that meet the needs of all users and stakeholders in EU equities markets.

Inconsistencies in the application of the "TNCP" flag. We note that there is now a difference between the Level 2 and Level 3 text in respect of the reporting of give-ups and give-ins, in particular for the purposes of reporting transactions not contributing to the price discovery process (TNCP) under Article 23 of MiFIR

We would recommend that more emphasis should be placed on ensuring consistency in post-trade reporting.

Exchange Traded Products (ETFs, ETCs, ETNs)

In regard to the application of pre- and post-trade transparency for Exchange Traded Products under MiFID II, we are of the opinion that some elements require attention to ensure an outcome that is more consistent with overall MiFID II transparency objectives:

The classification of Exchange-Traded Notes (ETNs) as non-equities ('bonds') rather than as equity-like instruments leads to confusion and impracticalities. An ETN is an Exchange-Traded Product that is structured as a note (issued by a financial institution), the value of which tracks an underlying asset – often a basket of commodities, bonds or other financial instruments. While the legal structure is a note, these ETNs trade like, and should have the same transparency obligations as, equity-based Exchange-Traded Products (like ETFs). While some trading venues classify ETNs, correctly, as 'equity-like', the ESMA FIRDS system classifies some ETNs as bonds. This reduces the transparency and liquidity of such ETNs, negatively impacting the ability of end-investors to efficiently use these instruments for investment and risk management purposes.

We would recommend classifying all Exchange-Traded Products, including ETNs, as equitylike instruments, in order to do right to the products' characteristics in terms of constituents, and trading behaviour.

Equity and non-equity options

We consider that certain areas of the framework for establishing uniform transparency requirements for option derivative instruments under MiFID II has fallen short. The way in which the transparency requirements under RTS 2 have been implemented has resulted, in some instances, in negative impacts for the liquidity in certain options segments, which are detrimental for end-investors. We have identified a number of such areas where greater clarity or a revision of the Level 2 text would be required in order to more fully achieve the objectives for the MiFID II transparency regime for listed derivatives:

Lack of harmonisation in the conversion of the MiFIR LIS threshold to lot size leads to an unlevel playing field. Under RTS 2 (Annex, table 6.1 for stock and index options), large-in-scale (LIS) pre-trade transparency thresholds are determined based on the average daily notional amount (ADNA) of each unique ISIN. The LIS thresholds are published in terms of *notional*. However, exchanges determine the minimum thresholds for off-order book trading in terms of a number of *lots* (i.e., number of options contracts). As there is no set process for how these notional amounts are being converted to a

lot size, this has led to a subjective and fragmented implementation of the transparency rules by trading venues. One pan-European derivatives exchange, for example, has used this ambiguity in the conversion from notional to lot size to define lower block trade sizes so that this exchange can attract trading volume to the detriment of other exchanges, such as Eurex Exchange in Germany. A proposed solution for this would be for ESMA to specify how to convert the pre-trade transparency notional amounts to a lot size.[5]

We recommend the creation of a methodology by ESMA to convert the LIS notional to a lot block trade size to generate consistency across exchanges so as to safeguard a harmonised European transparency regime for option derivative instruments.

The LIS adjustment process for options needs to be improved. Currently, derivative exchanges have fixed lot size levels above which participants can avail of a pre-trade transparency waiver. With these fixed lot size levels, if the underlying stock moves down by a large enough amount, it can mean that trades can avail of a pre-trade transparency waiver while being below the LIS notional outlined in RTS 2.

We would recommend that lot size levels should be reviewed on a quarterly (rather than yearly) basis, and the lot sizes should be adjusted accordingly where needed.

Discrepancies between LIS and ADNA levels for options needs to be addressed. When looking at the average daily notional amount (ADNA) buckets in table 6.2 in RTS 2 (see annex to our response), the first bucket is 20 times larger for index vs stock options. We would have expected the relevant LIS value to also be larger but this is not the case. Consequently, for index options a very small trade size can already avail of the pre-trade transparency waver. This is evident with a number of index options listed in Germany and in other Member States. One example are STOXX Europe 600 Sector Index Options traded on Eurex Exchange, such as the STXE 600 BANKS PR.EUR (Eurex code: OSTB), where the minimum trade that could avail of the pre-trade transparency waiver is 4 lots if Eurex Exchange were to match the ESMA LIS level. This represents a mismatch, as the product is quoted in the order book in 50 lots. This is creating a lack of transparency in this market and for other index options that fall in this first tier. The notional sizes for index options are often very large and so applying the same size as the single stock options means exchanges are able to set very low block trade thresholds, which is at odds with the objectives for the MiFIR transparency regime.

We would recommend a coherent review by ESMA of the threshold values for the first bucket, increasing these to be more aligned with the ADNA buckets.

Inconsistent modelling for determining the LIS threshold value for different types of option products should be addressed. The model used for determining the LIS threshold value for fixed income options is substantially different to the approach taken for index and equity options: Using the 70th percentile approach for fixed income options has almost the opposite effect to using the ADNA number for index and equity options. This discrepancy has created a current situation in the Bund and the Schatz options where the less liquid Schatz options have a LIS block trade size of 1250 lots, compared

[5] An appropriate method for the conversion from notional to lot size would be as follows:
Lot size LIS value = [(LIS pre-trade threshold) / (underlying spot price * multiplier * EUR FX conversion)]

to 100 lots for Bund options which trade 225% more than Schatz options.[6] Products with an active order book will therefore have a *lower* block trade threshold as a higher number of smaller trades get executed in the order book. This is the opposite from what would be the expected outcome, as normally less liquid products will tend to trade more off-order book in larger trade size meaning that the block trade size will be larger.

We would value a review of the appropriateness of the 70th trade size percentile over the ADNA method for fixed income options, as in practice this method results in less transparency than intended with the introduction of MiFID II.

Undue transparency deferrals for options trading venues. While the vast majority of all trading venues publish trades within one day, options trading venues are allowed to have delayed publications for up to 2 days. Such long deferrals unnecessarily reduce transparency and are detrimental for the overall quality of price formation and are not in the interest of end-investors.

We consider that 2-day delayed publication is not needed and should be reconsidered as this goes against the MiFID II/MiFIR transparency objectives.

The "market-cross" model unduly reduces pre-trade transparency for flex options. We consider that the "market-cross model" developed by one of the pan-European derivatives exchanges goes against pre-trade transparency rules for sub-LIS trades, to the detriment of the wider market and other trading venues that list comparable products. Flex options are products where the parameters such as the strike maturity day can be selected by the user (investor). This exchange has developed a crossing mechanism for flex options where products with no active order book can get executed in sizes below the LIS threshold without the wider market being able to interact with that trade. We consider that under such circumstances no meaningful pre-trade transparency is being provided, even though this would be required for sub-LIS trades. Consequently, the market-cross model allows for options listed on that venue to be de-facto executed in the dark below the LIS threshold applied on other venues such as e.g., Eurex Exchange, hurting liquidity on these other markets.

In situations where alternative execution models are developed to execute pre-arranged trades, trades which are below LIS should be available for trading by other participants. Trading venues should ensure that all trading members should be able to interact with those orders which are below LIS.

Structured products

Listed structured products are not suitable for retail investors as they are highly complex, non-transparent, subject to conflicts of interest and cause significant and endemic losses. FIA EPTA greatly welcomes MiFID II's objectives to increase investor protection. We strongly support ESMA's recent product intervention measures to address investor protection risks posed by binary options and certain Contracts for Differences (CFDs). However, we believe retail investors also deserve protection against certain types of leveraged, listed structured products that are insufficiently transparent and deliver sub-optimal results for retail investors.[7] These include structured products such as

[6] Eurex 2018 data

[7] For more information, see also these reports on structured products undertaken for/by the FCA in the UK:

sprinters, turbos, speeders and warrants. These products are all characterized by significant conflicts of interest: quotes are provided by only one market maker which is affiliated with the issuer of the product. In the absence of competition by other liquidity providers, these market makers have full discretion to set spreads and pricing rules in a manner that disadvantages the retail clients who are at the other side of the trade. In practice, we consider that these structured products are comparable to CFDs in the sense that retail investors are consistently at the losing side, while profits flow in a disproportionate degree to the issuer who is also essentially the counterparty to the retail investors.

For all such products it is doubtful whether they are sufficiently transparent for retail investors to make well-informed investment decisions. These products are so complex that prospectus or PRIIPs disclosures are not sufficient to adequately inform them of the associated risks of these products.

We recommend a comprehensive review of listed structured products in order to assess whether these products are fit-for-purpose for use by retail investors, focusing in particular on conflicts of interest on the part of the issuers of these products which disadvantage retail investors. We believe that product intervention measures under MiFIR Articles 40 and 42, either at ESMA or national competent authority level, would be warranted.

2. Open access

FIA EPTA welcomes the open access provisions and clear requirements in MiFID II to ensure that investment firms all have the same opportunities of joining or having access to regulated markets and other types of trading venues.[8] However, in practice we still observe significant implementation issues across asset classes where the MiFID II objectives of establishing an open market structure have not yet been achieved:

Important fixed income markets, such as the government bond markets, to this day remain inaccessible for non-bank liquidity providers. This is due to discriminatory access criteria employed by trading venues, such as having to be a self-clearing member or a primary dealer (i.e., a bank). This means that, for an important part of the fixed income trading universe, non-incumbent parties cannot interact with trading flow, which makes such flow less liquid, less competitive, and less transparent. These types of discriminatory access criteria are inconsistent with MiFID II requirements as clearly stated by ESMA.[9]

We note that MiFIR requires the Commission to submit a report to the European Parliament and to the Council reviewing the interoperability provisions in Article 36 of the Regulation by 3 July 2019. We would welcome the Ministry's attention to these concerns and for regulators to consider other barriers that may undermine non-discriminatory access, such as the U.S. CFTC is currently doing with respect to the practice of "post-trade name give-up" in the cleared OTC derivatives markets.[10]

https://www.fca.org.uk/publication/research/structured-products-consumer-research.pdf
https://www.fca.org.uk/publication/thematic-reviews/tr15-02.pdf
[8] As specified in Recitals 14 and 107 and Articles 18(3) and 53(1) MiFID II.
[9] ESMA Q&A on MiFID II and MiFIR market structure topics, Section 5.1, Question 3, available at: https://www.esma.europa.eu/sites/default/files/library/esma70-872942901-38_qas_markets_structures_issues.pdf
[10] https://www.cftc.gov/sites/default/files/2018-11/2018-24643a.pdf

Exclusion of certain trading strategies based on trading capacity. In equities, at least one pan-European multilateral trading facility applies a market model that excludes trading by certain firms based on their trading capacity (trading as principal) depending on the type of trading strategy they operate (undertaking liquidity-removing trades). This venue offers trading in the constituents of the Deutsche Boerse AG German Stock Index DAX, amongst other major European indices. These restrictions distinguish between the order flow of participants, denying investors executions, and creating a tension with MiFID II's non-discriminatory access provisions.

Article 53(1) of MiFID II requires regulated market to establish, implement and maintain transparent and non-discriminatory rules, based on objective criteria, governing access to or membership of the regulated market. In ESMA's Q&A on Market Structure Issues, on the topic of objective criteria ESMA states: "One of the benefits of more on-venue, pre-trade transparent trading is to broaden access to liquidity for market participants. In order for these benefits to be fully realised, it is important that trading venues do not have restrictive criteria governing their access, which place unreasonable restraints on certain market participants' access to particular liquidity pools." Under paragraph d) of Answer 3 (p. 37) of the Q&A, ESMA states that "Regulated markets should not impose restrictions on the number of participants that a participant can interact with," while emphasizing that the examples given are not an exhaustive list of arrangements which are non-objective and discriminatory.[11]

We would suggest to assess such access requirements – in particular the restriction that proprietary traders cannot operate liquidity-removing strategies – against the requirements of Article 53(1) of MiFID II.

3. Market Structure

Share Trading Obligation and Equivalence

Inconsistent interpretation and application of the Share Trading Obligation (STO). FIA EPTA believes there is an inconsistency across the EU with respect to the application and interpretation of the Share Trading Obligation as set out in Article 23 of MiFIR. The legislative intent of the Share Trading Obligation was to move more over-the-counter trading in shares onto platforms providing market transparency (i.e., regulated markets, multilateral trading facilities (MTFs) and systematic internalisers). FIA EPTA does not believe the legislative intent was to apply the STO to EU investment Firms' trading of third country shares in their "home" markets (regardless of whether that was on- or off-exchange). It is common in multiple EU jurisdictions for Trading Venues to make significant numbers of third country shares available to trade on their markets. As written, Article 23 brings regular trading of these instruments by investment firms into the scope of the STO. Liquidity on these listings tends to be poor when compared with the "home" third-country jurisdiction and it is clearly harmful to EU investment firms and end-investors that rely on them to have to execute client orders within the EU or on a limited sub-set of equivalent third-country markets. A similar set of issues can apply to instruments representing genuine dual listings and EU investors and investment firms should not be restricted from trading third-country listings of EU shares where that represents their ultimate investment decision.

We would recommend the STO to be reworked to allow legitimate trading in third-country markets unless the sole intent is to avoid EU regulation.

[11] https://www.esma.europa.eu/sites/default/files/library/esma70-872942901-38_qas_markets_structures_issues.pdf

Uncertainty regarding the equivalence regime creates disadvantages for EU investors. We observe that the MiFID II equivalence regime, particularly in the context of the STO, creates significant uncertainties for investment firms and EU investors. This has been demonstrated recently in the case of the time-limited equivalence decisions in respect of SIX Swiss Exchange as well as in the context of Brexit and the potential exclusion of EU investment firms from accessing the London Stock Exchange. We are concerned that unduly delayed or politicised decisions will have adverse consequences for EU investors, as well as firms, which need legal certainty. We are also concerned about the higher costs and lower investment returns for European end-investors if they are not able to access key third-country liquidity pools for dual listed instruments. In such instances, European end-investors face higher explicit and implicit trading costs, for example because they can only trade at EU exchanges that have thinner liquidity for these EU-listed third-country shares, forcing investors to trade at wider spreads and with greater market impact. Also, the absence of a timely equivalence assessment will deny European investors the benefit of competition between exchanges or of clearing interoperability.

FIA EPTA considers that equivalence decisions should be timely and based on a clear and objective legal-technical review of the market conduct rules of the relevant non-EU jurisdiction. We would appreciate the Ministry's support in this regard in encouraging the European Commission to prioritise EU end-investors' economic interests in how the Commission approaches its equivalence decisions.

Periodic auctions

FIA EPTA is agnostic about the advent of periodic auction systems as such, and we welcome any form of meaningful market model innovation that is able to compete on its own merits with other market models. As a whole, our membership does not at this point in time (only one year into MiFID-II) have a strong opinion about periodic auction systems, given the small market share they have attracted and the fact that these trading protocols are still in their infancy in Europe and have a very limited track record so far.[12]

While periodic auctions are a small percentage of the current market volume, we nevertheless view them in the context of execution protocols that have gained in popularity post-MiFID II. We have observed that these execution protocols have emerged as alternatives to central limit order book (CLOB) activity with varying degrees of (1) transparency, (2) multilaterality, and (3) contribution to price formation.

We believe it is essential that periodic auction systems offer meaningful levels of transparency, multilaterality, and contribution to price formation. We believe markets are healthiest when policy sets the stage for fair competition across the widest possible set of diverse market participants. FIA EPTA believes that transparency, open access and competition, rather than any undue regulatory advantages or burdens, should determine the appropriate balance between central limit order books and other types of market models.

As such, FIA EPTA believes that the level of trading activity on other execution protocols, including periodic auctions, should be grounded in transparency and set by fair competition, in compliance with the requirements of MiFID II. FIA EPTA encourages regulators to continue to study the influence of various execution protocols (if any) on the critical price discovery function of exchanges.

[12] For more detail please refer to FIA EPTA's response to ESMA's Call for Evidence on periodic auctions: https://epta.fia.org/articles/fia-epta-comments-esma%E2%80%99s-call-evidence-periodic-auctions

4. Market Microstructure

Order-to-trade ratios

The prescriptive order-to-trade-ratio (OTR) regime introduced by MiFID II is harmful for EU markets. The OTR regime under Article 48(6) MiFID II, further specified in RTS 9, acts to hamper liquidity provision during times of high market volatility by forcing market makers to quote wider than they otherwise might so as to manage their OTR. Many EU venues had well-functioning OTR regimes in place ahead of MiFID II, which were well-tailored to the nature of the trading venue and the type of financial instrument being traded. These previously existing OTR regimes were changed as a consequence of MiFID II and have been superseded by a less adaptive regime that is less suitable to take into account the specific characteristics of each market and product.

For example, with the introduction of MIFID II, Eurex Exchange in Germany moved to monitor OTRs on a daily basis rather than over the course of a month as had previously been the case. Moving to daily monitoring has led to a restrictive OTR practice which also has the effect of reducing market liquidity during stressed market conditions, as participants run the risk of breaching OTRs if they quote outside the market making spreads. This means that if the market becomes more volatile, participants will have to quote wider in order to reduce the frequency of quote updates which lead to higher OTR numbers. Quoting wider spreads, however, has a negative impact on the quality of the liquidity that market makers are able to offer to the market. If participants' quoting behaviour were still to be aggregated over the period of a month, this would allow for better management and smoothing of the OTR levels, allowing market makers to continue to provide better liquidity during stressed market conditions.

We would recommend having a general obligation on trading venues to implement an OTR regime on their venue but to allow trading venues to design a bespoke regime that is appropriate for their markets and products.

Market making

FIA EPTA's members are very strongly committed to efficiently provide liquidity to markets and end-investors on a continuous basis; this is the core mission of principal trading firms. In this regard, we have consistently supported the market making requirements as laid down in Articles 17(3) and (4) and 48(2) and (3) of MiFID II and further specified in RTS 8. However, we note that the practical implementation of the market making registration requirements by trading venues has varied. Certain venues have introduced significantly burdensome administrative procedures for registering as a market maker and there are also cases with wide variations in approach across trading venues within the same exchange group.

Comparable quote size restrictions may unduly reduce liquidity provision. The current requirement for a registered market maker to maintain two-way quotes of comparable size is being interpreted differently by trading venues across the EU and in some cases prohibits or penalises market makers who are providing more liquidity on one side of the market while still maintaining a two-sided quote above the minimum size obligation. Such quote size imbalances are a normal part of market making activity and reflect market makers responding to supply and demand as well as managing their own inventory and market risk; we do not believe it is in the spirit of the legislation to prevent such liquidity provision.

OTR monitoring should be undertaken by trading venues rather than firms. Article 48(3) requires trading venues to monitor and enforce compliance by investment firms of the requirements of the market making agreements they have with the venue. We note, however, that multiple trading venues have in practice pushed the monitoring obligation back to their members, rather than carrying this out themselves. This creates an administrative burden for firms and is in our view not the regulatory intention of Article 48.

We would welcome a more consistent application of the MiFID II market making requirements across trading venues; in light of the various divergent practices, we would welcome additional supervisory guidance to be provided to trading venues by either national competent authorities or ESMA.

Access to market making schemes should be open, transparent, and non-discriminatory. Additionally, we also observe issues with trading venues restricting access to market making schemes and not making details of these schemes or the corresponding incentives or requirements readily available to all interested market participants. We note further that certain trading venues have tended to favour incumbents and prevent access to a market making scheme unless an existing participant ceases to participate in it.

We believe that such behaviour restricts competition in European capital markets and is not in the interest of end-investors, who are disadvantaged if additional and/or more efficient firms are precluded from participating in relevant market making schemes. We believe such practices to be conflicting with the requirements for fair and non-discriminatory market making schemes laid down in Article 7 of RTS 8. Also relevant in this context are the requirements for non-discriminatory fee structures as laid down in Article 48(9) MiFID II and further specified in RTS 10, which notes in its Recital 5 that "[t]rading venues should … use objective criteria when determining rebates, incentives and disincentives", which should encompass any incentives provided for in market making schemes.

We would welcome additional supervisory attention to ensure that trading venues' market making schemes and associated incentives are made available to firms based on their performance against each scheme's objective criteria and that access should be transparent and non-discriminatory, and should not be restricted, therefore, based on historical factors or prior participation.

Speedbumps

Speedbumps may create potential conflicts with MiFiD II. Some EU exchanges have recently proposed to implement asymmetric speed bumps, also called passive liquidity protection mechanisms. One example is the Eurex Exchange in Germany. Such exchanges argue that market participants will add more liquidity to markets where speedbumps are implemented. FIA EPTA believes speedbumps have the potential to conflict with important aspects of MiFID II, including impacting on pre-trade transparency and fair and orderly trading, consistency with non-discriminatory access, best execution, and access to market data. With some European exchanges experimenting with speedbumps, it will be of important that the parameters for evaluating the effectiveness of these mechanisms are well defined and critically reviewed.

We would suggest that exchanges roll out speedbumps only on a pilot basis on a limited number of illiquid instruments which would allow for data comparisons to a control group without a

speedbump. Such speedbump pilots should time-limited and subject to a clear evaluation methodology. Relevant data should be shared with market participants so as to ensure a transparent process.

We would recommend close regulatory scrutiny of any newly proposed market models with speedbump-like features, in light of the MiFID II objectives of ensuring an orderly, non-discriminatory and transparent market. We would suggest, further, that a key supervisory and policy consideration for assessing speedbump-like mechanisms is the impact these may have on the overall quality and complexity of European market microstructure.

Further, it would be helpful for ESMA to provide clear guidance on speedbumps. This will assist with achieving regulatory convergence across the EU with respect to these novel questions, which is important to ensuring a level playing field for both trading venues and market participants.

5. Market Data Issues

FIA EPTA members are strongly concerned about the accessibility to market data provided by exchanges and data vendors.[13] While high-quality market data is arguably important to liquidity providers, the current cost structures, price increases, and aggressive commercial tactics make market data prohibitively expensive and increasingly inaccessible for all but the few firms that find a valid business reason to procure such data. This hampers competition, price formation and transparency and is detrimental to overall market quality and competitiveness.[14]

Through very significant investments in people and technology, FIA EPTA's members contribute strongly to the quality of price formation in European markets, lowering trading and search costs for end-investors. As market makers and liquidity providers across a very large number of markets and instruments, FIA EPTA's members generate significant quantities of information-rich pricing and other market data, which reflect our members' intellectual property. This data flows through the systems of exchanges and is disseminated to market data vendors; both then use the control they have over these data flows to sell the data back at high cost to the same population which had originally created it. Market participants cannot do but to procure this essentially self-generated data, as not doing so would come at the expense of de-facto exclusion from trading on a specific market.

Our more specific concerns are set out below, as follows:

Market data is not made available at a reasonable price. Article 12 of MiFIR and RTS 14 provide that market data should be available on a reasonable commercial basis, in a disaggregated/unbundled fashion. Contrary to MiFID II's intentions, however, the price of market data has risen approximately 20% year-on-year over the last 3-5 years, while sets of market data that were grouped in sensible packages are now being offered in more expensive, recombined packages that contain irrelevant data while charging for it. In addition, users are required to pay multiple (up to four) times for the same market data, which (as noted above) has been created by the same market participants in the first place. In view of our observations of how market data has become a profit center for exchanges and market data vendors, we are not convinced by the argument, proposed by some, that market

[13] This subject has been evidenced extensively in the US; we would echo many of the same concerns as recently expressed by U.S. market participants in the context of the SEC review of market data issues; see for example: http://www.projectinvested.com/market-data/

[14] These developments are further analysed in a useful recent study by Copenhagen Economics, which may be a useful starting point for the Ministry to further form an opinion on this matter: https://www.copenhageneconomics.com/publications/publication/pricing-of-market-data

data has merely become more expensive because it has to comply with more onerous MiFID II standards.

Market data agreements are opaque. The terms of market data agreements are often opaque which leads bona fide users at risk of having to pay substantial retroactive bills if they cannot agree with market data auditors on use parameters. FIA EPTA members have observed that vendors cancelled current market data contracts, to revert with new contracts and pricing mechanisms that were a multiple (10-fold and up) of the previous contract, without any discernable change in product. Our members see similar trends with regard to basic reference data, index data and other public data (including those provided by APAs in spite of the requirement to make this data freely available after 15 minutes.

Multiple charges apply for the same service. New market data agreements separately charge for off-screen (algorithmic) and on-screen use, once more for reference in e.g., Bloomberg, and once more for use in mandatory market abuse monitoring. Some exchanges have attempted to charge additionally for the use of market data packages for risk/compliance purposes (which firms had already purchased for trading purposes). This was done on the back of RTS 6 requirements for firms to have adequate risk controls (which require real-time data).

Fee increases specifically target systemic internalises and MTFs. We also note that certain trading venues have also leveraged MiFID II and the additional execution venues and market models it has created to generate new revenue streams from their existing market data packages. Most primary equities markets have now introduced or modified their fee schedules to charge significant incremental fees specifically targeting systematic internalisers and certain market models operated by MTFs. These fee increases are material and in some cases represent increases in excess of 50% in firms' fixed market data bills.

FIA EPTA questions whether trading venues and vendors are acting within the spirit and requirement for market data to be made available on reasonable commercial terms under MiFID II. We are concerned that such practices hurt innovation and competition within EU capital markets. We consider that such practices should be closely monitored, and where necessary addressed, by the regulator. We would strongly welcome any support by the Ministry to alleviate these concerns.

Annex: discrepancies between LIS and ADNA levels

Table 6.2

Equity derivatives – pre-trade and post-trade SSTI and LIS thresholds for sub-classes determined to have a liquid market

Asset class - Equity Derivatives							
Sub-asset class	**For the purpose of the determination of the pre-trade and post-trade SSTI and LIS thresholds each sub-asset class shall be further segmented into sub-classes as defined below**	**Transactions to be considered for the calculations of the thresholds**	**Pre-trade and post-trade SSTI and LIS threshold values determined for the sub-classes determined to have a liquid market on the basis of the average daily notional amount (ADNA) band to which the sub-class belongs**				
			Average daily notional amount (ADNA)	**SSTI pre-trade**	**LIS pre-trade**	**SSTI post-trade**	**LIS post-trade**
				Threshold value	**Threshold value**	**Threshold value**	**Threshold value**
Stock index options	a stock index option sub-class is defined by the following segmentation criteria: **Segmentation criterion 1** - underlying stock index	calculation of thresholds should be performed for each sub-class considering the transactions executed on financial instruments belonging to the sub-class	**< EUR 100m ADNA**	EUR 20,000	EUR 25,000	EUR 1,000,000	EUR 1,500,000
			EUR 100m <= ADNA < EUR 200m	EUR 2,500,000	EUR 3,000,000	EUR 25,000,000	EUR 30,000,000
			EUR 200m <= ADNA < EUR 600m	EUR 5,000,000	EUR 5,500,000	EUR 50,000,000	EUR 55,000,000
			ADNA >= EUR 600m	EUR 15,000,000	EUR 20,000,000	EUR 150,000,000	EUR 160,000,000

Asset class - Equity Derivatives							
Sub-asset class	**For the purpose of the determination of the pre-trade and post-trade SSTI and LIS thresholds each sub-asset class shall be further segmented into sub-classes as defined below**	**Transactions to be considered for the calculations of the thresholds**	**Pre-trade and post-trade SSTI and LIS threshold values determined for the sub-classes determined to have a liquid market on the basis of the average daily notional amount (ADNA) band to which the sub-class belongs**				
			Average daily notional amount (ADNA)	**SSTI pre-trade**	**LIS pre-trade**	**SSTI post-trade**	**LIS post-trade**
				Threshold value	**Threshold value**	**Threshold value**	**Threshold value**
Stock options	a stock option sub-class is defined by the following segmentation criteria: **Segmentation criterion 1** - underlying share	calculation of thresholds should be performed for each sub-class considering the transactions executed on financial instruments belonging to the sub-class	**< EUR 5m ADNA**	EUR 20,000	EUR 25,000	EUR 1,000,000	EUR 1,250,000
			EUR 5m <= ADNA < EUR 10m	EUR 250,000	EUR 300,000	EUR 1,250,000	EUR 1,500,000
			EUR 10m <= ADNA < EUR 20m	EUR 500,000	EUR 550,000	EUR 2,500,000	EUR 3,000,000
			ADNA >= EUR 20m	EUR 1,000,000	EUR 1,500,000	EUR 5,000,000	EUR 5,500,000