EUROPEAN
PRINCIPAL TRADERS
ASSOCIATION

Response by the FIA European Principal Traders Association to the ESMA consultation on MAR

29 November 2019

Introduction

ESMA Questions	FIA EPTA response
Please make your introductory comments below, if any:	The FIA European Principal Traders Association (FIA EPTA) represents 28 independent European Principal Trading Firms (PTFs) that 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. FIA EPTA members support high standards of market integrity and welcome the opportunity to respond to this ESMA consultation on the Review of MAR. We would like to highlight three key elements from our response below: • FIA EPTA members would welcome strengthening the EU regulatory framework for the Spot FX markets. However, FIA EPTA members do not believe that the existing MAR framework would be suited for Spot FX given the fundamentally different characteristics of Spot FX compared to MiFID financial instruments. If European market integrity principles were to be expanded to cover Spot FX, we believe the key concepts of MAR would need to be significantly revised, adapted or removed to take into account the specific product and market structural characteristics of Spot FX, including the global nature of the Spot FX markets.

	• FIA EPTA members have observed that some issuers may act inconsistently in regard to their disclosure requirements under MAR in relation to information that meets the definition of inside information that directly concerns the issuer. In particular, some issuers disclose inconsistently or in an untimely manner information on dividends or upcoming corporate events/actions that may be price sensitive for shares/bonds as well as for related derivatives and ETFs. Also, some issuers contact and provide information to certain analysts with the intention of guiding their forecasts by disclosing inside information. Such practices by the issuer may carry a risk that information is unevenly disseminated or may contain inside information ahead of an official release. FIA EPTA would welcome more comprehensive legislative guidance to be provided in relation to these issues. • FIA EPTA members welcome ESMA's objective to clarify what market practices may constitute legitimate pre-hedging activity in relation to the RFQ markets. In this regard, FIA EPTA members consider that an RFQ will be non-public until the quotes it elicited from market makers become subject to pre-trade transparency. Until that time, the non-public information contained in an RFQ may constitute inside information. Whether there is inside information will depend on the specificness of the RFQ. However, trading on the basis of inside information is prohibited and this should include pre-hedging. In FIA EPTA's view, it is only acceptable to pre-hedge in a limited number of circumstance where a clear risk management rationale is present and the pre-hedging does not impede on counterparty/client interests and general market integrity considerations. FIA EPTA members are concerned that otherwise, pre-hedging may increase slippage costs for investors and undercut market confidence while creating an unlevel playing field with market makers who refrain from pre-hedging. FIA EPTA members would encourage ESMA to provide further guidance in this area. FIA EPTA members would welcome the opportunity to provide further background information to ESMA on these and the other issues raised in our response

3. Scope of MAR

ESMA Questions	**FIA EPTA response**
3.1 Spot FX contracts	
Q1: Do you consider necessary to extend the scope of	Below is a combined response to Questions 1 and 2:

MAR to spot FX contracts? Please explain the reasons why the scope should or should not be extended, and whether the same goals could be achieved by changing any other piece of the EU regulatory framework.	FIA EPTA members agree with ESMA's statement that Spot FX is highly connected to the trading of the financial instruments that are covered by MAR and our members believe there is a need to better regulate and have more robust statutory oversight in the trading of Spot FX. However, FIA EPTA members do not believe that the existing MAR framework is suited for Spot FX given the fundamentally different characteristics of Spot FX compared to MiFID financial instruments. If European market integrity principles were to be expanded to cover Spot FX, we believe the key concepts of MAR would need to be significantly revised, adapted or removed to take into account the specific product and market structural characteristics of Spot FX, including the global nature of the Spot FX markets. FIA EPTA members consider that the existing regulatory regime for Spot FX, which relies on the voluntary Global FX Code, should be strengthened. Consequently, we would encourage ESMA and the European Commission to work with other public authorities in leading third-country jurisdictions globally to target a framework of statutory regulatory oversight of the Spot FX markets. Under such a framework we consider that a separate EU legal instrument for the regulation of Spot FX could be envisioned. Such a separate regulatory regime for Spot FX should adapt the MAR concepts to fit the specific market structure of the Spot FX markets while being more prescriptive than the existing Global Code and ensure effective enforceability of the rules by NCAs while relying on outcomes-based equivalence framework deferring to third-country regulators. Members of FIA EPTA are principal trading firms dealing their own capital who are market makers and liquidity providers in a wide range of financial instruments. FIA EPTA members have a particular interest in eliminating market abuse typologies in Spot FX as they are directly disadvantaged by market participants who utilise these typologies in their trading of Spot FX. FIA EPTA members undertake active and robust firm-level surveillance of all markets in which they operate, and in the process of which they regulatory observe manipulative practices related to Spot FX. FIA EPTA members believe the Spot FX market is particularly vulnerable to manipulative baiting/spoofing strategies which would meet the definition of both points 4(f) ("Momentum Ignition") and 5(e) ("Layering" and "Spoofing") of Annex II Section 1 in the Commission Delegated Regulation (EU) 2016/522. In our experience, both technology providers and bilateral counterparties generally seek to ensure that the trading of Spot FX remains ethical. However, due to Spot FX not being in-scope of a statutory regulatory regime, this market segment currently lacks enforceable market integrity and transparency safeguards. Spot FX trading is predominantly a bilaterally agreed form of

	trading across a large number of globally distributed matching platforms or technology providers. Consequently, there is currently no way for National Competent Authorities to monitor this trading for a number of reasons including: • While some central limit order books (CLOBs) for Spot FX trading do exist, the majority of trading volumes is still being conducted via bilateral agreements, that are not subject to trade reporting requirements; • The globally distributed nature of Spot FX trading platforms means that a trade executed in one jurisdiction can be filled by resting orders on matching engines in a number of other (third country) jurisdictions; • Where Spot FX trading is conducted on a technology provider's platform, those platforms are not in the scope of NCA oversight. We believe that in order to strengthen regulatory oversight of the Spot FX markets a number of other principles would first need to be addressed, such as the following: • To implement structural measures to encourage the trading of Spot FX on regulated trading platforms; • To implement fit-for-purpose trade reporting obligations for Spot FX to provide visibility of Spot FX trading for the entire market; • To implement fit-for-purpose transaction reporting obligations for Spot FX trades; To implement fit-for-purpose market surveillance obligations. The above-mentioned statutory obligations should take into account the global nature of the Spot FX market and consequently will require an outcomes-based equivalence framework deferring to third-country regulators. In order to minimise compliance and administrative costs as much as possible for end-users, we would envision a central reporting and surveillance role for both bilateral and multilateral trading platforms and systems. The above principles would provide greater transparency into the trading of Spot FX and provide NCAs with the visibility that would be required in order for them to monitor trading in Spot FX while mitigating the risk that the Spot FX markets would migrate outside of the EU, which would be a risk if the EU regularly regime develop separately from other developed markets globally

4. Article 5 of MAR – Buy-back programmes (BBPs)

ESMA Questions	**FIA EPTA response**
4.1 Reporting obligations of BBPs	
Q7: Do you agree that there is a need to modify the reporting mechanism under Article 5(3) of MAR? Please justify your position.	FIA EPTA members consider that the current reporting requirements place an onerous burden on corporate issuer to report details of all buy-back related transactions to the NCA of the trading venue on which the transaction was conducted and FIA EPTA members agree that the reporting mechanism should be modified. In practice, issuers do not conduct such buy-back themselves as they do not have the market connections, technology nor expertise required. Rather, the buy-back is conducted by a broker on the issuer's behalf. This further removes the issuer from having control over where the shares are traded and, as the ESMA Consultation Paper notes, the buy-back may be conducted on MTFs or other regulated market operators. The reporting obligation has resulted in issuers requesting that the buy-back only be executed on the involved shares' primary listing venue in order to be able to fulfil their reporting obligation. This prevents the issuer from accessing other liquidity pools at potentially better pricing. As electronic markets have evolved under MiFID II, this places issuers at an unfair disadvantage compared to other market participants who have access to more diverse pools of liquidity via Multilateral Trading Facilities and Systematic Internalisers. This creates an unlevel playing field between issuers and other market participants and as a consequence, issuers are de-facto denied best execution.
Q8: If you agree that the reporting mechanism should be modified, do you agree that Option 3 as described is the best way forward? Please justify your position and if you disagree please suggest alternative.	FIA EPTA members agree that Option 3 would be the best way forward. Reporting the transactions to a single NCA will ensure that transparency is provided into the buy-back programme. This may even increase the transparency as the issuer will not need to be aware of the market that the transactions are executed on and it will ensure that all transactions are recorded by an NCA. Further, this option would give issuers ease of access to larger pools of liquidity and better pricing for the large size of shares that a buy-back normally entails.
4.2 Simplification of the reports for BBPs	
Q9: Do you agree to remove the obligation for issuers to report under Article 5(3) of MAR information specified in	FIA EPTA members agree with the removal of this requirement.

Article 25(1) and (2) of MiFIR? If not, please explain.	
Q10: Do you agree with the list of fields to be reported by the issuers to the NCA? If not, please elaborate.	FIA EPTA members agree with the proposed fields with some exceptions: • field 3: Trading Venue Transaction Identification Code (TVTIC); • field 4: executing entity LEI; • field 7: buyer identification code; • field 12: buyer decision maker code LEI; • field 36: venue (MIC code). We agree that the reporting fields should be harmonised with MiFID II Transaction Reporting. However, there are a large number of trading scenarios that can occur under MiFID II where there is no obligation for the above fields to be passed along the execution chain, ultimately back to the issuer. As a result, there is no formal technological infrastructure set up under MiFID II to facilitate this. Other than a formalised setup, there could be a voluntary FIX protocol established for this, however as the buy-back regime is not widely utilised many brokers will not upgrade their systems to support this and as the regime relates to MAR, an absolute compliance requirement with the specifications should be explicitly mandated. If these fields were required, it would result in the issuer being restricted to a small number of brokers who would only trade on one venue (the primary listing venue). As this is the case now and as noted in our response to the above questions, this would result in the continuance of an unlevel playing field. For example, there are a large number of trading scenarios where a TVTIC would not be passed back to the issuer. An issuer informs their broker that they want to engage in a buy-back in their stock and the broker utilises a range of broker wheels/Smart Order Routers (SORs) to effectively execute the trades in the market which may involve additional brokers in the chain and multiple venues. However, only the market facing firm will be aware of the TVTIC and other order record keeping requirements recording to order record keeping and transaction reporting type fields. There is no infrastructure for each broker within the execution chain to receive the ultimate execution record fields other than price and quantity.
4.3 Transparency of transactions related to a BBP	
Q11: Do you agree with ESMA's preliminary view?	Yes. FIA EPTA members do agree with ESMA's preliminary view. We agree that a report in an aggregated form would be much more beneficial to the public, in particular due to the complexity of today's electronic trading environment.

5. Article 7 of MAR – Definition of "inside information''

<table>
<tr><td>ESMA Questions</td><td>FIA EPTA response</td></tr>
<tr><td>5.1.2 Definition of inside information and its effectiveness in preventing market abuse</td><td></td></tr>
<tr><td>Q13: Have market participants experienced any difficulties with identifying what information is inside information and the moment in which information becomes inside information under the current MAR definition?</td><td>FIA EPTA members are primarily principal trading firms who are market makers and liquidity providers in financial instruments. FIA EPTA members have a particular interest in eliminating insider dealing as they are directly disadvantaged by market participants who, whilst in possession of inside information, improperly use this information asymmetry to deal against market makers' quotes.

FIA EPTA members have observed that some issuers may act inconsistently in regard to their disclosure requirements under Article 17(1) of MAR in relation to information that meets the definition of inside information that directly concerns the issuer:

• Some issuers disclose inconsistently or in an untimely manner information on dividends or upcoming corporate events/actions that may be price sensitive for shares/bonds as well as for related derivatives and ETFs;
• Some issuers contact and provide information to certain analysts with the intention of guiding their forecasts by disclosing inside information. Such "soft-pedalling" practices by the issuer may carry a risk that information is unevenly disseminated or contain inside information ahead of the official release.

Greater detail on the background of these areas of concern is provided below.

1. Issuers improperly disclosing information on dividends and other corporate events

<u>Description of problem</u>

In FIA EPTA members' experience some issuers act inconsistently in appropriately disclosing dividend information and other information relating to corporate events (which may have a potential volatility impact and may affect the pricing of financial instruments or related derivatives and ETFs). Such information on corporate actions may relate to individual listings of companies, as well as for ETFs.</td></tr>
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	This problem can lead to issuers not properly considering whether such information meets the definition of Article 7(1) of MAR and is subject to the disclosure requirement as set out in Article 17(1) of MAR and therefore the improper disclosure of such information by issuers to market participants e.g., on a bilateral telephone call between an issuer's Investor Relations team and a market participant. **<u>Proposal for further guidance to issuers</u>** We note that previously guidance to issuers was published by CESR / ESMA in section 1.15 of CESR/06-562b (link below) - a non-prescriptive list of examples of possible inside information concerning the issuer which included: *"Ex-dividend date, changes in dividend payment date and amount of the dividend; changes in dividend policy"* We would ask that the complete sections 1.15 and 1.16 of this document should be republished in the current MAR Q&A or that it should form part of the revised MAR. https://www.esma.europa.eu/sites/default/files/library/2015/11/06_562b.pdf In addition, question 1 of a previous Q&A (ESMA/2016/419) (link below) provided comprehensive guidance to issuers instructing them to consider any relevant information related to dividend payments and policies as inside information, should this information be likely to have a significant effect on the prices of either the issuer's shares or related derivatives or both. We would ask that this comprehensive existing guidance should be republished in the current MAR Q&A or that it should form part of the revised MAR. https://www.esma.europa.eu/sites/default/files/library/2016-419_qa_market_abuse_directive.pdf Further, we suggest that more comprehensive regulatory guidance be developed for issuers in relation to other types of information that can influence the price formation of equity derivatives, specific examples of which are set out below: ○ Any corporate event timings or new events e.g. earnings, AGM, Sales Releases, Capital Markets Days, conference presentations, data releases; ○ Any corporate action event timings i.e. dividends, stock splits, or the expected launch of a rights issue; ○ Information on possible structure of corporate actions i.e. buyback methods; ○ New product launches.

	Information on the timing and method of such releases are potentially informative to volatility e.g., the date of a company's AGM can affect volatility and dividend timing assumptions – changing it from one week to another can mean that it now falls within a different option's expiry and may hence influence the pricing of that option. Additionally, it is relevant to consider the processing of corporate actions by ETF issuers. We have seen examples of issuers erroneously processing events intraday that affect pricing, for instance by processing a tax reclaim that led to the fund apparently outperforming the index substantially, processing a merger of an underlying share or cancelling an ex-dividend date while trading already commenced. Apart from processing errors, some ETF issuers have changed key product characteristics intraday and have released such essential information inconsistently including information on creation/redemption fees, in some cases announcing such changes not simultaneously to the wider market. We strongly believe that all relevant, foreseeable corporate actions should be announced out of market times only, simultaneously to all market participants, for individual shares/instruments as well as ETPs including ETFs. We strongly believe that ESMA guidance to issuers in this respect would increase awareness of these matters and would assist in ensuring that a high market integrity standard is reached into the future. **2. Selective disclosure by issuers to analysts to guide consensus forecasts** **<u>Description of Problem</u>** We are concerned that some issuers may be disclosing information that appears to meet the conditions of Article 7(1)(a) MAR during the course of: o Analyst and broker conference calls (either 1-1 or group); o Meetings with issuer senior management; o Other corporate access events; and o Briefings by issuer investor relations personnel to investors or shareholders. In certain scenarios this may not be in line with Article 17(1) MAR. In some cases, these breaches may stem from a misinterpretation by issuers on how they are required to make public inside information directly concerning that issuer. Whether by accident or design, some issuers may interpret the words "where applicable" in Article 17(1) of MAR, in reference to disclosure in or through an official appointed mechanism, as making such

	disclosure optional and not having to satisfy the requirements of Article 2 of Commission Implementing Regulation 2016/1055. • **Guidance by issuers** FIA EPTA members have observed in a number of cases that issuers may disclose e information to a small number of analysts, brokers or significant shareholders in order to soften the impact of that information on the price or value of the issuer's financial instruments. Such practices have been observed in a variety of contexts, but particularly via restricted analyst and broker conference calls in the time period leading up to the "quiet period" prior to the release of scheduled earnings. Such guidance could be specifically directed at analysts who have published forecasts that are outliers compared to overall consensus. Selective disclosure of material information (including the "subtle signals" example detailed above), to analysts or a selected group of investors, could potentially be a breach of Article 17(1) MAR but could also to be unlawful disclosure within the meaning of Article 10 of MAR and a breach of the Article 14(c) MAR prohibition if not properly executed in accordance with MAR. For the avoidance of doubt, FIA EPTA members recognise that there may exist legitimate cases, where issuers may address clearly incorrect statements by analysts if this would lead to manifestly erroneous price signals. In such cases, issuers must always refrain from disclosing inside information and rely on publicly available information only. It should be clear that releasing any inside information, inadvertently or deliberately, must be immediately followed by a wide dissemination of such inside information in accordance with MAR. Issuers should also refrain from attempts to influence an analyst via more subtle suggestive signals (e.g. a "nod and wink"). **<u>Proposal for further guidance for issuers</u>** Given the prevalence of incidents that may arise due to incorrect and sometimes unlawful practices by issuers (documented by STORs that have been submitted by our members), FIA EPTA would welcome further legislative guidance to be provided to issuers in this area that clearly sets out how to correctly and timely disseminate the information set out above. We note that the U.S. SEC's Regulation Fair Disclosure (Regulation FD – link below) aims to address the problem of selective disclosure by issuers of material non-public information to analysts, institutional investors and others without concurrently making widespread disclosure. We would welcome similar legislation to be introduced in Europe, requiring (as Regulation FD does) that whenever a public company, or any person acting on its behalf, discloses material non-public information to certain enumerated persons, the company must disclose that information to the public. https://www.sec.gov/rules/final/33-7881.htm

Q14: Do market participants consider that the definition of inside information is sufficient for combatting market abuse?	FIA EPTA members note that there are prescriptive requirements for issuers in MAR setting out when and how they must publicly disclose information that directly concerns them. However, as our response to Q13 above demonstrates, there can be advertent and inadvertent breaches of these requirements by issuers. Where information is improperly disclosed by issuers, it is then incumbent on any market participant who is in receipt of it, either directly from the issuer or from a secondary source, to determine if it meets the definition of inside information (and hence whether they are then bound by the MAR restrictions from using it). This determination is also required by market participants in cases where they are in receipt of information that indirectly relates to issuers or financial instruments. Often the most pertinent determining factor is whether the information meets the non-public test within the definition of inside information. Our members believe that more comprehensive regulatory guidance for market participants is required regarding the determination of when information is considered to be non-public within the definition of inside information. In the absence of clear guidance, some market participants may take inconsistent stances in their determination (if they consider it at all) that could run the risk of non-compliance with MAR. We note the UK FCA handbook (MAR 1.2.12) sets out factors that may be taken into account in determining whether or not information has been made public. FIA EPTA members suggest that these (or similar) factors be included as ESMA guidance in MAR. Guidance on whether information disclosed via social media can be deemed to be public would also be welcomed by our members. In addition, we would also suggest that the non-exhaustive list of scenarios outlined below be also included in ESMA guidance of where any information communicated can be deemed to be non-public: **In relation to issuer communications:** o The CEO of a publicly listed company speaking at a conference that is not open to the public but only to invited guests e.g., clients or members of the media. That is, where a conference is open to any member of the public to attend then any information that is disclosed during the open forums at that conference can be deemed to be public; o A 1-1 or group call or meeting held with a firm e.g. with their Investor Relations, CEO, CFO etc; o A company sending information to the members of a mailing list which is not open for all to subscribe to e.g. only current shareholders may subscribe. **In relation to other communications:**

	○ A broker's message in an Instant Messenger chat in Bloomberg (a blast) that is only sent to their clients; ○ An official communication (e.g., from a government body, regulator, trading venue) that is disseminated in a manner outside of their disclosure policy e.g., where it is selectively disclosed (advertently or inadvertently disclosed to an individual or selected group. ○ A price request that is provided by a counterparty to a broker(s). It continues to be non-public after it is "shopped" to selected market makers; ○ A price request that is sent to a MTF by a counterparty where the MTF does not have pre-trade transparency to the market as a whole at the time of receipt by selected market makers. For the latter two points we refer to our answer to Question 22 below.
5.1.2.1 Inside information for commodity derivatives	
Q20: What changes could be made to include other cases of front running?	FIA EPTA members agree with ESMA's clarification in paragraph 97 of the Consultation Paper that "*front-running behaviours will be relevant for the purpose of insider dealing even when carried out by persons beyond those charged with the execution of orders who had knowledge relating to an order*" and we note that this covers orders in all types of financial instruments. This clarification is useful in confirming that a market maker must consider if they have inside information after receipt of a price request from a broker who is executing an order on behalf of a counterparty. However, we note that in any event, such a counterparty price request could in itself meet the definition of inside information in Article 7(1)(a) of MAR even where it does not relate to the execution of an order (and we note that ESMA makes a similar point in paragraph 101 of the Consultation paper).

5.1.2.3 Pre-hedging	
Q22: What market abuse and/or conduct risks could arise from pre-hedging behaviours and what systems and controls do firms have in place to address those risks? What measures could be	Below be provide a combined response to Questions 22, 23 and 24: 1. FIA EPTA agrees with ESMA that requests for quotes may meet the definition of inside information. We note that trading venues that make use of the RFQ facility normally make RFQs only visible at the time of the request to the market makers who have been asked to respond to the RFQ. Consequently, these specific requests cannot be deemed to be public at the time of receipt and will only become public once the quote(s) by the market maker(s) provided in response to the RFQ have been made pre-trade transparent under the rules of the venue. Pending the

used in MAR or other legislation to address those risks?	application of pre-trade transparency such non-public quoting requests may constitute inside information, in particular, where the size and the side of the trade are “opened” by the client or counterparty (i.e., when the client or counterparty is requesting a one-sided quote for a specific size). 2. By contrast, a request for a two sided quote is unlikely to contain enough specific information to constitute inside information, unless some other specific information is present that was known to the market maker about the counterparty’s or client’s interest at the time the quote was requested (e.g., other information about the client/counterparty or instrument which may allow the market maker to infer the direction of the trade). Additionally, it should be noted that where it is clear that a party (such as an inter-dealer broker) is just seeking information for the purposes conveying pricing to another party who may or may not be interested in trading this is not inside information. CESR previously referred to this activity in its level 3 guidance as “polling”. [1] 3. The issue arises as to what a market participant acting as a market maker can or cannot do when in possession of inside information stemming from an RFQ. In particular, ESMA has questioned whether so-called pre-hedging is acceptable in such circumstances. ESMA notes that it is aware that some market participants appear to justify pre-hedging for risk management purposes, stating that in some cases a broker “having received a request for quote from a client but not yet its firm order, hedges the position that it would have to take where it happened to win the request for quote”. In FIA EPTA’s view, it is only acceptable to pre-hedge in the limited circumstances set out in paragraph 6(a), 6(b) and 6 (c) below where a clear risk management rationale is present and the pre-hedging does not impede on counterparty/client interests and general market integrity considerations. 4. MAR sets out that the “…purpose of this Regulation…is to protect the integrity of the financial market and to enhance investor confidence, which is based, in turn, on the assurance that investors will be placed on an equal footing and protected from the misuse of inside information.”[2] Unless applied in a clearly restricted manner for risk management purposes, ‘pre-hedging’ in the RFQ and “call around” markets may compromise these market integrity objectives for investors and the wider market for the reasons set out below:

[1] Market Abuse Directive, Level 3, Second set of CESR guidance and information on the common operation of the Directive to the market, July 2007, at paragraph 3.8, available at: https://www.esma.europa.eu/sites/default/files/library/2015/11/06_562b.pdf

[2] Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 at recital 24.

	5. Investors often look to achieve price discovery by use of electronic RFQs (on one or more platforms) or by the "call around" market whereby brokers contact one or more market makers and request prices on behalf of investors. A concern for investors is that there may be information leakage during the RFQ process. I.e., the concern that market participants may take advantage of the investor's price requests in order to make trading profits and, in the process, move prices against the investor. For example, were an investor to ask for a price from a number of market makers (either directly or indirectly through an agency or inter dealer broker) and each market maker concluded on receipt of the price request that it was likely that they were going to win the trade and therefore pre-hedged, this could increase price slippage costs for investors and consequently undermine confidence in the market. Where only one market maker were to do this and others not it, would become a self-fulfilling prophecy. I.e., the market maker who had pre-hedged would be moving the price of the hedge against the other market makers, meaning that they would be forced to quote a worse price to the investor thereby ensuring that the party who pre-hedged would win the trade. Such practices may create an un-level playing field and distort competition among market makers. 6. MAR sets out to "avoid inadvertently prohibiting forms of financial activity which are legitimate, namely where there is no effect of market abuse".[3] It recognises that "This may include, for example, recognising the role of market makers, when acting in the legitimate capacity of providing market liquidity." Further ESMA guidance on what constitutes legitimate market making in the context of RFQ trading has not been issued to date. FIA EPTA would welcome the issuance of such guidance. Whilst we believe, as set out above, that pre-hedging where no clear risk management rationale can be evidenced should be clearly prohibited, we consider, by contrast, that the following practices are legitimate market making activities in the context of RFQ trading: a. Where following a request for a price from a counterparty there is an agreed understanding with the counterparty, the market participant agrees with the counterparty to trade at a stated reference price on the basis that the market participant is allowed to hedge in advance of the calculation of that price. This could be pursuant to an explicit agreement at the time of trading or pursuant to an agreed course of dealing between the counterparties. For example, a market participant guarantees that a counterparty can buy at an ETF's NAV on the basis that the participant is allowed to buy the constituents of the underlying ETF or other related hedge ahead of the calculation of that NAV. This practice should be permitted

[3] Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 at recital 29

		because it is done with the consent of the investor and it enables the investor to get a better fill than would otherwise have been available had the market maker not been able to pre-hedge; b. Where following an agreed understanding with a counterparty the market participant indicates that he will trade at a particular price or better if they are allowed to pre-hedge. For example, in the options market an options market maker may agree with a counterparty that they will trade with him at a particular volatility level on the basis that the counterparty agrees that the market participant may execute their “delta hedge” in the underlying instrument before the final options price is determined. This practice should be permitted because it is done with the consent of the investor who, in this case, cares most about the volatility component of the options trade price. Agreeing that the market marker may execute a hedge in the instrument underlying the option enables the investor to get a better fill than would otherwise have been available had the market maker to assume the risk with respect to the price at which the delta hedge could be executed as well as the risk with respect to the volatility component of the options price; c. Where a third country exchange (hereafter “TCE”) permits pre-hedging and the activity is done in conformance with their rules and relates only to orders in contracts traded on that exchange. This, however, would not permit a market participant to use information about orders in instruments admitted to trading on a regulated market to trade in contracts on the TCE in circumstances which otherwise would not be permitted by MAR. For example, a market participant could not use information about an order in a ETF which is admitted to trading in Europe but which has an underlying index which is the S&P 500 to trade in S&P 500 futures on CME other than in accordance with the guidance set out in paragraphs 6(a), (b) and (d) to (i) d. Where following the receipt of an RFQ the market maker continues to update their quotes in line with moves in the displayed market quotes but not based on the information that they have received. This should be permitted in order to ensure the continuity of liquidity provision in the market; e. following receipt of an RFQ which they fill the market maker is free to trade notwithstanding the fact that the trade may not be public as yet. This should be permitted as the market maker has assumed risk

and should be free to hedge that risk. The investor has been filled and cannot be prejudiced by the market makers actions;

f. where following receipt of an RFQ a market maker widens out their quote or pulls their quote to protect themselves against persons who may misuse the information. This should be permitted as a prudent risk management measure for market makers who are particularly exposed to bad behaviour from other market participants because of their requirements to post two-way prices continuously.

g. where following the receipt of a RFQ a market maker is notified that the order has been filled elsewhere the market maker is free to update their prices to reflect the information even though that trade may not have been published. This should be permitted as the investor is filled and cannot be prejudiced by the market maker’s actions. The market maker should be free at that stage to incorporate information regarding the fact that securities have been bought or sold and the volumes and prices of those acquisitions into its liquidity provision activities;

h. where following receipt of an RFQ which is not immediately filled by the market maker a reasonable period of time has passed by such that the counterparty has had a reasonable opportunity to execute the order the market maker is free to update their prices to reflect the information. The reasonableness of the length of time is determined by factors such as the liquidity of the market;

i. where following the receipt of an RFQ which is not immediately filled by the market maker, the market maker receives a RFQ with the opposite direction to the first RFQ, the market maker may improve its price for the second RFQ and may deal whilst having knowledge of the first RFQ. The legitimate activity of a market maker involves provision of immediacy to investors thereby bridging the gap between buyers and sellers. In this case the market maker has improved the price given to an investor using the knowledge that another investor has interest in the opposite direction. The market maker may thereafter also be able to offer to deal with the initial price requestor at a better price than that initially quoted;

11. Competent Authorities, Market surveillance and cooperation

ESMA Questions	FIA EPTA response
11.1.2. ESMA's initial considerations as regards the cross-market order book surveillance framework	
Q66: Please provide your views on the abovementioned harmonisation of reporting formats of order book data. In addition, please provide your views on the impact and cost linked to the implementation of new common standards to transmit order book data to NCAs upon request. Please provide your views on the consequences of using XML templates or other types of templates.	With the number of reporting requirements placed on market participants, we would support a consistent approach to reporting formats. Whilst FIA EPTA members have no strong preference on which reporting template should be enforced, XML templates are already in place for other forms of reporting and would therefore be consistent.
Q67: Please provide your views on the impact and cost linked to the establishment of a regular reporting mechanism of order book data.	The introduction of recent regulation has seen the industry make significant strides towards comprehensive transaction reporting and order record keeping. Whilst this requirement has greater impact on trading venues rather than investment firms, it is our view that introducing additional reporting would be a sub-optimal outcome which could increase complexity. NCAs are able to attain the required order data from each other and without evidence of this being an ineffective process, does not require changing.
Q68: In particular, please: a) elaborate on the cost differences between a daily reporting system and a daily record keeping and ad-hoc	As per the answer above, we would favour maintaining the order record keeping and ad-hoc transmission mechanism.

transmission mechanism; b) explain if and how the impact would change by limiting the scope of a regular reporting mechanism of order book data to a subset of financial instruments. In that context, please provide detailed description of the criteria that you would use to define the appropriate scope of financial instruments for the order book reporting.	

12. Sanction and measure

12.2 Cross border enforcement of sanctions	
Q71: Please share your views on the elements described above.	FIA EPTA supports cross-border enforcement of sanction to ensure optimal compliance with European market integrity rules