15 March 2019

# Final ISDA/ FIA/ GFXD/ GFMA Commodities working group response to German Ministry of Finance

## Consultation on MiFID II/ MiFIR

ISDA, FIA, GFXD and the GFMA Commodities WG (hereinafter the Associations) welcome the opportunity to respond to the consultation launched by the German Ministry of Finance on the outcomes of the MiFID II/ MiFIR full implementation after one year of experience and in the view of the future report that the European Commission will publish in March 2020.

The implementation of MiFID II/ MiFIR has been one of the most ambitious implementation exercises carried out by the industry in the past few years due to MiFID II/R overhauling existing regimes and addressing all investment services in all asset classes.

The constant dialog between the Associations and National Competent Authorities (NCAs) and ESMA has been helpful and has enabled both markets participants and regulators to understand and apply the legislative and regulatory framework. In this respect the various ESMA Q&As, opinions and consultations have been of significant importance.

Members of the Associations have been operating under MiFID II/ MiFIR rules and requirements for over a year now and have an understanding of where the legislation has worked well and where clarification or re-calibration would be appreciated.

## EXECUTIVE SUMMARY

- MiFID II/R has always been the cornerstone of the EU financial legislation for the following reasons:
  - MiFID II/R defines the conditions upon which investment firms are licensed to provide investment services and the content of conduct of business rules they have to comply with;
  - MiFID II/R defines trading venues and the conditions upon which trading venue operators can provide services;
  - MiFID II/R defines financial instruments and covers all asset classes accessible to wholesale and retail investors.
- The Associations consider that it remains questionable whether MiFID II/ MiFIR has met its objectives in increased and effective transparency. Market participants have constantly reported outstanding problems associated with the implementation of data and reporting rules and calibration of transparency since the full application date of the framework. Although NCAs and ESMA have been provided with feedback about all these deficiencies, the Associations note that no re-calibration has been seriously considered so far to make the regime more effective and based on an appropriate cost-benefit analysis.
- The Associations strongly believe that the focus of the review should be to simplify the rules, to increase the efficiency of the requirements and to reduce disproportionate costs and burdens imposed by the current MiFID II/R framework. Some of these suggested clarifications or simplification would require changes to the level 1 texts whereas others can be done through a revision of level 2 measures (Regulatory Technical Standards or Implementing Technical Standards) or level 3 Q&As.
- The Associations strongly believe that the approach should be a 'Refit' of MiFID II/ MiFIR and that a complete re-write of the existing legislation would be inappropriate. Not only has MiFID II/R been implemented relatively recently but the industry, as well as regulators, are currently facing considerable uncertainty and implementation challenges associated with Brexit. As an example, where the framework is based on EU metrics (e.g. the systematic internaliser regime or calibration of the transparency regime), ESMA should concentrate on the impact of Brexit and the calibration of rules once UK data is no longer included in the calculation of the EU metrics.
- The Associations also have strong concerns that the European legislation does not provide a horizontal approach to regulatory reporting. The co-existence of many different overlapping and sometimes inconsistent reporting regimes (MiFID II/R, Short Selling Regulation (SSR), Securities Financing Transactions Regulation (SFTR), Regulation on Wholesale Energy Market Integrity and transparency, (REMIT) is considered an area where European policy makers should seek a more harmonised regulatory framework in line with the European Commission's commitment to better regulation. The Associations support the EC's Fitness Check on Supervisory Reporting that was launched in December 2017 and believe it would be sensible for any adjustments to MiFID II/R reporting to be coordinated with any plans that the EC has under the Fitness Check on Supervisory Reporting.
- The Associations recommend the recognition of equivalence between EU and UK financial services rules and trading venues after Brexit as critical for the continuity of financial services activities. The UK has on-shored EU financial legislation and aims to remain aligned to the existing EU framework. When considering new legislative proposals, both the EU policy makers and the UK authorities will need to pay attention to the risk of misalignment between both regimes.
- More specifically, the Associations support improvements to the existing framework. Data and reporting, mandatory systematic internaliser regime, transparency and equivalence of trading venues are the main areas of concerns for the Associations' members. The other areas where re-calibration or clarifications would be deserved include the treatment of packages under the transparency regime

and the derivatives trading obligation, the commodity derivatives position limits and hedging exemption, the costs and charges rules and the consolidated tape for non-equity financial instruments.

## SPECIFIC COMMENTS

## 1. Data and Reporting Issues

As a general comment, the Associations strongly believe that more harmonised approach to reporting across regimes is required.

The same trading event can be reported differently between MiFID II/R and EMIR, for example a partial termination is reported differently between the two regimes. Also, there are overlaps between the various regulatory regimes in Europe. All existing reporting regimes – EMIR, MIFID, REMIT, SSR, SFTR – should be reviewed holistically by the European Commission in order to bring consistency and avoid overlap and duplication.

In its response to the European Commission's Fitness Check of supervisory reporting requirements, ISDA and FIA raised key supervisory reporting issues[1]:

- Report once/ permission access to data once: Firms would produce a single dataset which the relevant regulators could 'cut' to suit their particular objective;
- Alignment across jurisdictions: harmonisation on the basis of CPMI, IOSCO and FSB work undertaken for the Unique Trade Identifier (UTI), Unique Product Identifier (UPI) and Common Data Elements (CDE);
- Global harmonisation of UTI, UPI and CDE of OTC derivatives reported to trade repositories and harmonisation of data requirements;
- Single-side reporting: derivatives transactions, matched via confirmation and reconciliation processes, should only be reported once to supervisors, by one party, not twice; this system is already practiced in major jurisdictions such as the US and Canada;
- Early engagement with the industry in order to identify data sets and data sources and to craft a solution before making fundamental policy decisions about how and what to report;
- Flexibility in the sense that regulation should adapt to market developments or problems; in this respect changes to Regulatory Technical Standards is a long and difficult process;
- Phased implementation.

The Associations note that MiFID II reporting is driven by data. In order for reporting to be consistent and accurate across all submitting parties, reference data must itself be consistent and equally available to all market participants. There is currently a lack of a single golden source of reference data which increases the risk of inconsistent reporting. Recognition of a single golden source for reference data would enable market participants to work from the same data and be confident that the same data is being applied consistently by all reporting parties.

While there are currently some ambiguities in the data specifications to be input into FIRDS, which can lead to inaccurate reference data being held, FIRDS would still be best placed to be treated as a golden source of reference data.

[1] See https://www.isda.org/2018/03/21/isda-responds-to-ecs-supervisory-reporting-requirements-fitness-check/ and https://fia.org/articles/fia-submits-response-european-commission%E2%80%99s-fitness-check-supervisory-reporting

### *Market data*

Market data is a highly valuable tool that supports the efficiency of a trading eco-system as it helps firms and investors to make investment and hedging decisions and to facilitate transparency in the market. MiFID II/R has increased the need to consume market data, for example, in order to satisfy and monitor for best execution.

The production of high-quality market data, delivered through reliable, timely and efficient channels to data vendors and end users, therefore makes an important contribution to market efficiency. Non-discriminatory access to market data allows for a balancing of asymmetry of information between market participants.

The Associations have observed the rising cost of market data in the EU over recent years. According to a recent study[2], market data cost from exchanges is five times higher in the EU than in the US for Level 1 data (top of the order book data such as best bid/ask). Steven Maijoor, Chairman of ESMA, stated in a speech on 21 June 2018 that *"Following the application of MiFID II, we were made aware of substantial increases in the costs of market data, reaching at times up to 400% compared to prices charged prior to 3 January 2018."*[3]

MiFID II aimed to address the issue of market data costs by putting in-place the concept of 'reasonable commercial basis' (RCB). The RCB principle refers to the provision of market data at fees that are based on a reasonable relationship to the cost of producing and disseminating that data. However, it is important to note that data vendors / distributors are not currently regulated (unlike data providers such as Exchanges, who are regulated under MiFID).

The Associations urge policymakers to assess compliance with 'reasonable commercial basis' as well as assess the existing licensing and fee disclosure issues, and how transparent are the cost methodologies of data production to users.

The ability to use market data is determined by data usage licenses. The data usage licenses offered by trading venues should continue to evolve in parallel with evolving customer use cases and not limit the ability of end-users to use market data. In order to make investment decisions, firms need to be able to analyse data.

### *Reliability and accuracy of FIRDs*

The ESMA portal has been interrupted multiple times and ESMA has not always proactively communicated on issues encountered. This has left firms in the dark as to when / if the data needed for MiFID II/R reporting that day would be available.

The FIRDS file has intermittent availability, disappearing from the portal. This causes significant difficulties in processing the file. Where such issues arise, the support model provided by ESMA is difficult to access, and where emails or calls are responded to, responses can often be generic and do not address the specific concerns. FIRDS outages have a major impact on investment firms' ability to

[2] 2018_November_Copenhagen_Economics-Report – 'Pricing of Market Data', see graph on page 34.
[3] mifid_ii_implementation_-_achievements_and_current_priorities_s.maijoor_fese_convention_21June2018.

comply with MiFID II/R, and are a barrier to an effective transparency framework and have consequential impacts throughout the system. For example, if FIRDS is down an ARM (Approved Reporting Mechanism) cannot validate ISINs for the purposes of transaction reporting.

Regarding the quality of FIRDS data, a number of entries in FIRDS have characteristics missing which makes it hard to identify the instrument. Members have also observed instances where firms have independently verified reference data for in-scope instruments (e.g. ISINs on newly issued bonds; reference data attributes associated with ISINs issued by ISIN issuing bodies such as ANNA) but only to see their submissions using this reference data being rejected from NCA systems, which results in re-reporting of information as and when the data in FIRDS is updated. Furthermore, there are large numbers of ISINs, often involving multiple ISINs for economically comparable products. As this data is the basis for ToTV with ToTV being the basis for transparency, and transparency being based on ISIN which is the instrument identifier, this makes it very difficult for end-users and investors to decipher transparency for OTC derivatives.

A political decision was made to use ISINs for the identification of derivatives. The Associations consider that the UPI is more meaningful than ISINs to genuinely identity derivatives. However, should the ISINs still be the reference used for the identification of derivatives under MiFID II/R, The Associations would support improvements to ISIN generation to reduce the instances of multiple ISINs for comparable products. As an example, if rates products were to reference the tenor of a swap instead of the maturity date, the number of ISINs required for what would essentially be the same swap product will be greatly reduced. While the tenor was introduced in ESMA's Q&A from 26 September 2018, the tenor was introduced in addition to maturity date, meaning that this will result in more ISINs, not less. We believe that this example gives support to the view that ESMA should reassess the criteria for generating ISINs.

Similar problems arise in respect to the creation of ISINs for energy commodity derivatives. The attributes and financial instrument reference data required for the creation are not sufficiently granular. As a result, very different commodity derivatives (with different liquidity/delivery zone etc) may be captured by the same ISIN code. Additional attributes and clarification are key not only to reduce the number of ISINs, but also to improve consistency and quality thereof.

### *Disclosure of identifiers*

Publication of SI MIC codes and LEIs in publicly available reference data remain a concern because SIs trade on risk, unlike multilateral trading venues, and therefore need some anonymity to be able to provide important liquidity sources to the market.

The reference data reporting regime under MiFID II is designed to collect instrument reference data. However, the data collected about instruments currently includes information identifying the counterparty, and this data is currently made publicly available to all users that consume FIRDs data. Even with no price or volume data, this substantially increases the risk of a SI not being able to trade at market terms and may affect the ability for Sis to provide vital liquidity, which ultimately affects end users. In contrast, the transparency framework in MiFID II/R does not require the identity of the trading counterparties to be disclosed in the transparency data, which recognises the important role that SIs play in the market in providing alternative sources of liquidity. We would urge legislators to consider changing the reference data reporting requirements so that the identity of the SI is not disclosed publicly in the FIRDS file.

The Associations believe it is important to work towards a solution for reporting of personal information for natural persons. Currently, sensitive information including surnames, dates of birth and national identifiers (i.e. raw personal data) must be disclosed in MiFID II/R transaction reports and kept in firms' and trading venue records. This information is shared amongst multiple entities, for example, ARMs and trading venues. The large volumes of raw personal data that is being transferred between market participants exposes them and their data transmission arrangements to increased risk of cyber security threats and increases the risk of identity theft for the natural persons whose personal information is being reported or kept for the purposes of the MiFID II/R order record keeping requirements.

While we recognise the personal identifiers specified in the MiFID II/R technical standards were the best available solutions at the time, it would be beneficial if a unique universal identifier was developed as a longer-term solution. This would help to mitigate the concerns around sharing raw personal data, as well as assist regulators by creating a reliable and persistent form of identification which would not change over time (e.g. if passport numbers changed). We note that an ISO Study Group has been established to consider the creation of an ISO standard for the identification of natural persons (similar to a LEI for natural persons). The Associations would like to recommend that policymakers monitor ISO's work and consider potentially endorsing such an ISO standard in the future.

***Usefulness of reportable information***

Transaction reports under MiFID II are much more detailed;  however some of the information that market participants need to report does not always fully reflect the economic features of a product that we think would be critical for a regulator to monitor.

For instance, regarding reporting of Equity Swaps, ESMA Guidelines in relation to the submission of transaction reports pursuant to Article 26 of MiFIR (the "Guidelines", dated 10 October 2016), set out examples of how to report different types of instruments under RTS 22 and Examples 107-112 show a number of examples of how to report Equity Swaps. In each example, the field 'Price' is populated with the 'spread paid/received in addition to the underlying interest rate' (the "Spread").

The Associations note that the negotiated Spread is the appropriate price to report for certain types of Equity Swap orders where Spread is the price forming feature, and will allow regulators to monitor the price that investment firms are charging clients to finance the synthetic equity position. However, we have concerns that that for other types of Equity Swap orders, where the price forming feature is the initial equity price, and the Spread is pre-agreed in the Master Confirmation, if the initial equity price is not reported, regulators may not be able to identify the reference prices that the synthetic equity positions were entered into or closed out at.

## 2. Mandatory Systematic Internaliser (SI) regime

The Associations recognise that the policy objectives behind MiFID II/R's SI regime is to apply a level playing field between trading venues and SIs by requiring greater price transparency in relation to OTC trading of venue traded instruments with the ultimate aim of encouraging trading of these type of instruments on trading venues. Therefore, the concept of an SI is to be understood in the framework of the transparency rules, which we note applies only to instruments that are traded on a trading venue (ToTV).

MiFID II SI regime consists of:

- the **mandatory** regime where an investment firm becomes an SI on a product when some pre-set limits for a frequent and systematic basis and for a substantial basis are both crossed,

  and

- the **optional** regime where an investment firm can choose to opt-in in any financial instrument.

The focus of the below section is primarily focused on the mandatory SI regime and derivatives. The Associations suggest amendments to the framework to more closely align the way the SI regime operates in practice to the fundamental policy objectives behind the SI regime.

Under article 4(1)(20) of MiFID II, an SI is an investment firm which, on an organised, frequent, systematic and substantial basis, deals on own account when executing client orders outside a Regulated Market, an MTF or an OTF. The frequent and systematic part is measured by the number of OTC trades in the financial instrument carried out by the investment firm on own account when executing client orders.

The substantial criteria is measured by:

a) the size of the OTC trading carried out by the investment firm in relation to the total trading of the investment firm in a specific financial instrument
   or
b) the size of the OTC trading carried out by the investment firm in relation to the total trading in the European Union in a specific financial instrument.

The Associations note that becoming a mandatory SI for derivatives triggers various requirements that come in addition to the reporting of transactions under RTS 22 that is applicable to all investment firms:

- Transparency requirements under RTS 2 for SI trading ToTV products;
- Supply of financial instruments reference data (FIRDS) under RTS 23 if instruments are uToTV[4] only (and not ToTV).

In order for an investment firm to determine whether they are a mandatory SI in a financial instrument, they must undertake two steps:

- Calculations based on the pre-set limits;
- Final determination of SI status at a class of instrument level once the obligation is triggered as a result of the calculations.

[4] uTOTV means:
- financial instruments where the underlying is a financial instrument admitted to trading or traded on a trading venue or
- financial instruments where the underlying is an index or a basket composed of financial instruments admitted to trading or traded on a trading venue.

### *Mandatory SI assessment (Calculations)*

As stated above, the policy objective behind the mandatory SI regime is to encourage execution of venue-traded instruments on trading venues. Therefore, the mandatory SI assessments are focused on identifying investment firms' trading activity that meets the SI criteria in instruments that are traded by trading venues. As transparency applies only to ToTV instruments[5], the scope of the mandatory SI assessment should also only apply to ToTV instruments. Only this interpretation supports the original policy objective behind the mandatory SI regime. The Associations would welcome changes to interpretative guidance on this point and, if required, changes to the legislative framework to achieve this aim.

Under Article 22 of MiFIR, only trading venues, APAs and CTPs are required to submit data on which ESMA bases its transparency calculations. The scope of these is necessarily limited to those instruments to which the transparency obligation applies (i.e. ToTV instruments).

In addition, ESMA noted in its Q&A on transparency (Section 7 Systematic Internaliser, Q11[6]) that it would only publish data on ToTV instruments for the purposes of the SI assessment. ESMA also confirmed that types of transactions that were not subject to transparency should also be excluded from the SI assessment (Section 7 Systematic Internaliser, Q3[7]).

Applying the mandatory SI assessment to instruments that are not ToTV ultimately does not provide comparable information because these instruments are, by their nature, not traded on any trading venue. If any of these instruments are later traded on any trading venue, then it would then be appropriate to apply the mandatory SI assessment to those instruments at that time.

We would further suggest that the final determination of SI status should also be limited to those instruments that are TOTV in the relevant class of derivatives or class of financial instruments as this would be more consistent with the primary policy objective for the reasons discussed above.

The Associations also note that there are different interpretations for the scope of application of the mandatory SI calculations across the industry and between NCAs. Some NCAs consider that ToTV only have to be deemed SI when thresholds are exceeded whereas other NCAs consider that u-ToTV also have to be deemed SI when thresholds are exceeded within a group of instruments containing both ToTV and uToTV instruments i.e. for example a sub-class of derivatives. This creates uncertainties and confusion.

### *Obligations triggered by the mandatory SI regime – Supply of reference data*

The Associations acknowledge that limiting the scope of application of the SI regime to only ToTV instruments will affect reporting of uToTV reference data to FIRDS under RTS 23 because only

---

[5] Under Article 22 MiFIR, only Trading Venues, APAs and CTPs are required to submit data on which ESMA bases its transparency calculations. The scope of these is necessarily limited to those instruments to which the transparency obligation applies (i.e. ToTV instruments).

[6] ESMA's Q&A transparency, Section 7 – the Systematic Internaliser regime – Question 11 pages 60-61: *ESMA is only publishing information on ToTV instruments for determining whether an investment firm meets the thresholds to be considered as a systematic internaliser*.

[7] ESMA's Q&A transparency, Section 7 – the Systematic Internaliser regime – Question 3 pages 53: *Article 13 of RTS 1 and Article 12 of RTS 2 exempt investment firms from reporting certain types of transactions for the purposes of post-trade transparency. ESMA is of the view that those types of transactions should not be part of the calculations for the purposes of the definition of the systematic internaliser regime, both for the numerator and the denominator of the quantitative thresholds.*

investment firms that have opted into being SIs for uToTV instruments will have the obligation to report reference data under RTS 23[8].

Under RTS 23, trading venues have responsibility for reporting reference data in relation to instruments traded on a trading venue and SIs have responsibility for reporting reference data in relation to uToTV instruments. However, we would urge legislators to carefully consider whether the reference data in relation to uToTV instruments that NCAs are receiving ultimately supports the original policy objectives of the reference data reporting regime.

The Associations note that FIRDS aims to help NCAs in their effective monitoring of the markets by standardising instrument reference data, notably using ISINs for the identification of derivatives products.

Beyond the difficulties associated with the use of ISINs (See Section 1 on Data and Reporting), the Associations note that with or without u-ToTV instruments FIRDS will never mirror the entirety of the scope of instruments that NCAs have to monitor for the reason that u-ToTV instruments that are not traded by SIs will not be part of it. In contrast, the universe of products that trading venues can submit reference data for is finite: all trading venues must submit reference data in relation to instruments traded on their platforms so the data in FIRDs will reflect the full scope of instruments that are traded by a trading venue.

We consider that the transaction reporting regime under RTS 22 already provides NCAs with good information to support its market monitoring objectives for three reasons. Firstly, the reporting of transaction includes the same data fields as under RTS 23. Secondly, all u-ToTV instruments are covered there so NCAs and ESMA have the full picture. Thirdly, the transaction reporting under RTS 22 relieves some of the concerns that the Association have regarding the use of the ISIN for derivatives[9].

The Associations strongly believe that the application of the reference data reporting obligation to uToTV is posing unsolvable practical issues without giving the full picture to NCAs and ESMA. As the policy objective of collecting reference data under RTS 23 is to support NCA's market monitoring responsibilities, incomplete data which is not comparable does not ultimately support that policy objective[10].

For all these reasons, the Associations would strongly support the following clarifications at level 3 (ESMA Q&A) and any other necessary changes to the legislative framework for the purpose of the review of MiFID II/ MiFIR:

- The SI mandatory regime is to apply to ToTV instruments only.

The Associations would also like to emphasize:

- the ability for investment firms to opt into the optional SI regime for any financial instrument, whether they are ToTV, uToTV or any other OTC instrument; and
- the ability for investment firms to be SIs under both the mandatory SI regime as well as the optional SI regime.

[8] In contrast, it is clear that RTS 2 (transparency) applies to ToTV instruments only and that RTS 22 (transaction reporting) applies to ToTV AND uToTV instruments irrespective of their SI classification.

[9] The reporting through FIRDS involve the generation of ISINs whereas the transaction reporting does not, which means that an SI u-ToTV would require the generation of an ISIN whereas the identical non-SI u-ToTV would not.

[10] Also, recital 33 of MiFIR focuses on trading venues' obligation for supplying reference data to support NCA's market monitoring objectives. It is logical then to consider that the original scope of the RTS 23 reporting regime was intended for ToTV instruments.

## 3. Transparency Regime

MiFIR has introduced a harmonised pre-trade transparency regime for certain financial instruments traded on a trading venue, including derivatives. According to MiFIR article 8, trading venues shall publish information about current bid and offer prices and the depth of trading interests at those prices advertised through their systems.

However, the same provision recognises that certain exemptions from the general requirement to publish pre-trade transparency data are necessary to preserve an orderly price discovery process and to allow nascent and niche markets to develop. These exemptions are respectively implemented through pre-trade transparency waivers for transactions above a certain volume threshold (Large in Scale waiver or 'LIS') and transactions in instruments classified as illiquid, regardless of their volumes (Illiquid Instrument waiver or 'IL').

The implementing Regulation 2017/583 ("RTS 2") sets out the methodology for calculating LIS thresholds and determining illiquid instruments. With regards to LIS, the calculation is based on a threshold floor expressed in notional trade value in a given sub-asset class and the trade size below which lies the percentage of transactions corresponding to the trade percentile specified by the RTS for that sub-asset class. The IL thresholds are determined on the basis of the average daily trade notional amount and the average daily number of trades as specified by RTS 2 for a given sub-asset class.

The Associations believe that currently the transparency regime is not calibrated correctly to match the economic characteristics of the products that are actually traded and that this could significantly impair liquidity in those markets. We have listed a number of specific issues to illustrate this (**please see the annex**). ISDA has written a number of papers/letters on issues regarding the transparency regime that the Associations would be happy to share with you. -

### *Post-trade transparency requirements and deferrals for non-equity instruments*

In addition, the Associations note that the post-trade transparency requirements for non-equity leave it to national competent authorities (NCAs) to choose between various options on extended deferrals for large trades in bonds and derivatives.

As a result, NCAs have adopted different types of deferrals of varying publication requirements and duration. Such an uneven approach to post-trade transparency has led to inefficiency in the market and substantial implementation costs borne by market participants and by investors ultimately, depending on their location.

The Associations suggest harmonising the regime for waivers and deferrals so that all investment firms can benefit from the same extended deferrals across all EU countries. Extended deferrals are critical to protect liquidity and allow hedging of risk. An alignment across NCAs is essential to ensure a level playing field across the EU and avoid a fragmentation of liquidity.

## 4. Trading Obligation – Equivalence between Trading Venues

For the purpose of the trading obligation under MiFID II, third-country trading venues may be considered as regulated markets for shares and derivatives under MiFIR (Art. 23 and 28(4)) if the Commission considers the third-country is equivalent.

So far, the European Commission has adopted one equivalence decision for the derivatives trading obligation, concerning the United States. The decision recognises certain trading venues authorised by the US CFTC as eligible for compliance with the trading obligation for derivatives. According to the European Commission, the decision ensures that 'EU counterparties can trade the derivatives instruments that are subject to the trading obligation, such as interest rate swaps and index-based Credit Default Swaps (CDS), on CFTC-authorized Designated Contract Markets and Swap Execution Facilities in the US'.

The Associations strongly believe that the equivalence determination for non-EU trading venues, particularly non-EU regulated markets and MTFs, is essential for the good functioning of financial markets and to avoid fragmenting markets.

The Associations believe that rather than a full equivalence based on a line-by-line analysis of rules applicable in the EU and in the home jurisdictions of the trading venue, the determination should be based on a risk based-approach. Applying the derivatives trading obligation (DTO) without a sound equivalence regime would lead to the situation where market participants are using well-established regulated markets outside of the EU but may not be compliant with the DTO if these markets are not deemed equivalent to EU markets.

When it comes to derivatives markets in particular, the Associations note structural differences with equity markets as derivatives markets are purely wholesale and global by nature.

Without equivalence, end-users of derivatives would need to have multiple and duplicative compliance systems, which would lead to fragmentation of market liquidity and cost increases. As an example, there is no concept close to the OTF category in any jurisdictions outside the European Union. Full alignment of rules would mean that no EU OTF would ever get any equivalence decision in any other jurisdiction, particularly in the US.

The Associations note that in general, the approach to equivalence and deference should differ depending on whether the rules in question are designed to mitigate systemic risk such as central clearing, collateral (margining), risk-mitigation techniques other than margining, i.e. timely confirmation, portfolio compression, portfolio reconciliation, mark-to-market valuation, dispute resolution, versus rules for non-systemic risk activities (such as trading rules, conduct of business rules, public reporting), where deference to third country regulatory regimes should be given. We note that this is consistent with the remarks by CFTC Chairman Christopher Giancarlo in September 2018 where he observed that reforms that are address particular market and trading practices (e.g. transparency, trade execution methodologies and trading platform design) should be permitted to be tailored to local trading conditions.[11]

## 5. Treatment of packages under the Transparency regime and the Derivatives Trading Obligation (DTO)

The Associations note that there is a misalignment between level 1 texts and ESMA's interpretation regarding the treatment of packages.

The intention of the co-legislators was to assure that package orders are treated as a whole and that consequently MiFID obligations shall not apply to any component of the package order separately.

With regard to the transparency regime and the derivatives trading obligation, ESMA introduced uncertainty.

[11] Remarks of Chairman Christopher Giancarlo to the City Guildhall, London, 4 September 2018: https://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo52

The associations consider that the co-legislators have to reiterate clearly that packages are treated as a whole.

The Annex II to the present response includes an ISDA paper that discusses the problems currently associated with the packages regime.

## 6. Commodity derivatives position limits – new/illiquid contracts and hedging exemption

Article 57 of MiFID II and ESMA RTS 21 introduced the Commodity derivatives position limits regime under MiFID II.

The Associations note the position limits regime was unprecedented in the EU and that after only one year of experience it is difficult to form conclusions on its effectiveness and relevance. However, the Associations have noted that the general regime has not raised major issues so far.

The main concern that the Associations have is about the specific treatment of new contracts and particularly the de-minimis threshold.

Under RTS 21, ESMA has established a specific regime for new and illiquid contracts for the purpose of calculations of position limits. Article 15 of RTS 21, states that new contracts traded on a trading venue with a total combined interest in spot and other months not exceeding 10,000 lots over a consecutive three-month period shall be set a limit of 2,500 lots.

The Associations note that some NCAs have interpreted this requirement to mean that on day 1 of a new commodity derivative, a limit of 2,500 lots would apply. In some instances, market participants have raised that this limit too restrictive to allow a new contract to develop into a liquid instrument. Further, there was at least one occasion where a venue had to amend a number of commodity derivative contracts. Market participants had to make changes to several hundred transactions to implement the required changes. Another option would have been to terminate the old derivatives and offer new contracts with the new specifications, which would have been less of an administrative burden on market participants. However, the venue felt they were unable to create new contracts, as those new contracts would have attracted the 2,500-lot limit, and thus a lower position limit than the limit for the existing contracts.

And whilst in theory, in line with ESMA Q&As on 'commodity derivative topics', NCAs can use different derogations for illiquid markets which have an open interest between 5.000 and 10.000 lots, these remain difficult to apply in practice in a meaningful manner and are often not sufficient to mitigate the negative impact of disproportionately low position limits.

Any increase of the limit under the available derogation will need to be substantial in order to provide sufficient relief to market participants close to the limits and prevent unreasonable restrictions on trading activity in fast growing markets. An increase of a given position limit with for example 500 lots will only have a very limited impact, effectively allowing market participants close to the limit to trade an additional lots equivalent of four Calendar or eight Season contracts. Additionally, NCAs tend to reserve the use of the derogation for cases for which the exchanges can bring forward other arguments than the fact that the contract is illiquid and needs room to grow, while this is one of the most critical arguments that apply to all contracts coming closer to 10.000 lots.

Once the position limit is nearly reached, market participants will withdraw from the market, often switching to another trading venue outside of the MiFID II regime, thereby leaving the NCA no time to adjust the limit upwards. Furthermore, in relation to newly launched contracts, it is not unusual that only one participant sits on the buy or sell side of the market. In such cases, even a fifty percent limit is not sufficient to allow the market to further develop.

The Associations recommend the following approach to the application of the position limits regime to new contracts:

ESMA should consider revisiting RTS 21 to allow a review period for new contracts (3 months, 6 months, 9 months, depending on the contract) during which no position limit is set. This would allow the concerned NCA to review the development of the contract and to determine a position limit appropriately calibrated regarding the needs of the market.

This is supported by the policy objective of the MiFID II as expressed in its implementing RTS 21 which provides that "Position limits should not create barriers to the development of new commodity derivatives and should not prevent less liquid sections of the commodity derivative markets from working adequately".

New and nascent products normally constitute a minor share of commodity markets. Moreover, such contracts are unlikely to influence such price movements in the underlying physical commodity markets that could negatively impact consumers. Thus, the suspension of position limits for such contracts would not pose any risk to the transparency and functioning thereof. Rather, attracting more volume to regulated venues would contribute to a more transparent trading environment.

Please also see our alternative proposals for the recalibration of position limits in the Annex.

***Hedging exemption from position limits***

Non-financial firms (NFCs) can apply for a hedging exemption from position limits for defined commodity contracts traded on trading venues. We believe that firms should be granted a hedging exemption without the imposition of a quantitative limit to this exemption, in other words, all hedging activity in a contract for which an exemption has been granted by an NCA should be exempt. However, some NCAs impose quantitative limits to the hedging exemption, which causes unnecessary implementation burden, because NFCs must then apply for a new exemption every time they breach the set limit if they have a larger hedging need, for example because of their increased power production. This quantitative limitation is not necessary as NCAs can monitor the use of the hedge exemption on the basis of the data they receive under the position reporting regime.

## 7. Costs and charges rules

The Associations have observed that there are differences in interpretation amongst firms regarding the interpretation of what constitutes an 'ongoing relationship' in relation to execution services as well as on other issues such as how fair value should be calculated.

For example, whilst ESMA has published Q&A regarding the term 'ongoing relationship, there is ambiguity in the industry as to what ESMA means when it refers to a 'trading account' and to an 'executive investment service'. In addition, although the PRIIPs methodology refers to using 'fair value' to calculate costs, there is no EU wide definition or guidance on what constitutes fair value.

It is also to be noted that some clients (professionals and eligible counterparties) are not interested in receiving the costs and should be able to opt out.

The Associations believe that harmonisation and convergence across the EU would be beneficial to investment firms and to the benefit of end clients. Therefore, the Associations suggest that it may be appropriate to carry out further consultation with the industry on the topic of costs and charges in order to facilitate consistency amongst firms. This in turn, will help enable comparability for end investors willing to receive that information when comparing the costs and charges disclosed to them by different firms.

## 8. Consolidated tape

Article 65(8)(c) of MiFID II, articles 6 and 20 of MiFIR and ESMA RTS 14 set out the regime applicable to the consolidated tape for non-equity financial instruments.

In theory, a consolidated tape should be established for non-equity instruments by September 2019.

However, the Associations estimate that it is very unlikely that a Consolidated Tape Provider (CTP) will be able to provide market participants with an exhaustive consolidated tape and as of today, the Associations have not identified any potential CTP for non-equity instruments.

There are two main reasons to explain why, based on the current rules, a CTP will be unlikely to be able to consolidate data on non-equity instruments.

Firstly, MiFID is not incentivising this ‘service’. For potential CTPs, not only is the process of establishing the consolidated tape burdensome and expensive, but it implies the obligation to update it and adapt to market changes (e.g. connecting to any new trading venues or new APAs that are established ) and introduces accountability regarding the accuracy of the consolidated tape.

Secondly, most trading venue operators only provide market data at a high cost, which makes providing a CTP service un-economic, as this would mean that the CTP would also have to charge a high price for the consolidated tape.

The Associations have also raised that there is no clarity in the texts as to when a firm can claim to be a CTP.

Generally, MiFID II does not provide sufficient clarity on when and how trading venue operators should share data for the purpose of a pan-European consolidated tape. The risk associated with being a CTP compared to the lack of any ability to force operators to share data is a strong disincentive.

In the absence of any changes in the framework, the Associations do not expect any sufficiently reliable consolidated tape to exist in non-equity.

The Associations recommend that EU policy makers create the appropriate incentive for CTPs and calibrate the obligation for trading venue operators and APAs to share data.

**About ISDA**

Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 900 member institutions from 70 countries. These members comprise a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's website: www.isda.org. Follow us on Twitter @ISDA.

**About FIA**

FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in Brussels, London, Singapore and Washington, D.C. FIA's membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from more than 48 countries as well as technology vendors, lawyers and other professionals serving the industry. www.fia.org.

**About GFXD**

The Global Foreign Exchange Division (GFXD) of the Global Financial Markets Association (GFMA) was formed in co-operation with the Association for Financial Markets in Europe (AFME), the Securities Industry and Financial Markets Association (SIFMA) and the Asia Securities Industry and Financial Markets Association (ASIFMA). Its members comprise 25 global foreign exchange (FX) market participants,[12] collectively representing around 85% of the FX inter-dealer market.[13] Both the GFXD and its members are committed to ensuring a robust, open and fair marketplace and welcome the opportunity for continued dialogue with global regulators.

**About GFMA Commodities WG**

The Commodities Working Group of GFMA focuses on regulatory issues specific to banks operating in the financial and physical commodities markets. The CWG's work centers around the creation of a more level regulatory playing field for the commodity markets, advocating consistency and avoiding duplication among legislative measures.

[12] Bank of America Merrill Lynch, Bank of New York Mellon, Barclays, BNP Paribas, Citi, Credit Agricole, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JP Morgan, Lloyds, Mizuho, Morgan Stanley, MUFG Bank, NatWest Markets, Nomura, RBC, Scotiabank, Société Générale, Standard Chartered Bank, State Street, UBS, Wells Fargo and Westpac.

[13] According to Euromoney league tables.

## Annex I – Transparency regime
## Examples of areas where the transparency regime should be re-calibrated

- **ToTV**

There are still a number of areas where ESMA's ToTV ("traded on a trading venue") Opinion is open to interpretation, and firms are taking different approaches. Markets participants expect clarity on the timing of the ToTV assessment and the treatment of derivatives with additional terms not reflected in reference data. It is noted that transparency will be meaningless and likely to be misleading regarding non-standardised OTC derivatives instruments that are deemed to be TOTV (due to them sharing the same reference data that a trading venue reports for a standardized instrument) but include additional price forming terms that significantly alter the product and are not reflected in such reference data. Clarity on these issues would be very welcome, as currently different approaches are being taken by firms and regulators alike.

ISDA has written a number of papers on this topic that the Associations would be happy to share with you.

- **Equity derivatives liquidity classes.**

RTS 2 Annex 1 Table 6.1, defines all contracts in the equity derivatives options and futures/forwards sub-asset classes as "liquid" , irrespective of time to maturity or any other segmentation criteria.

ESMA has argued that: (i) to do otherwise would be to undermine current levels of pre-/post-trade transparency; and (ii) the trading in options/futures/forward contracts is already characterised by high pre-/post-trade transparency.

This approach is problematic for the following reasons:

. it is not aligned with MiFIR Level 1 which defines a liquid market as being "where there are ready and willing buyers and sellers on a continuous basis" and requires it be assessed on the basis of average frequency and size of the transactions criteria;

. it over estimates the pre-trade transparency that already exists. No pre-trade transparency previously exists for contracts within these sub-asset classes that are traded OTC, and a majority of listed equity options/futures contracts on exchanges are only available for block trading rather than being on platforms with pre-trade transparency;

. it overstates the risk that a more granular approach would undermine current levels of transparency – where transparency previously exists for a contract type within a sub-asset class, there is no reason to believe that it would reduce if pre-trade transparency is not mandated for every contract type under that sub-asset class;

. it gives insufficient consideration of the consequences for the financial markets and to end users; liquidity will likely fall and hedging costs for end users will increase if pre-trade transparency is mandated on contract types that are not actually liquid.

ISDA has written a paper on this topic that the Associations would be happy to share with you.

- **Interest rate options – SSTI/LIS thresholds**

  There have been conflicting messages regarding the scope of the IR Options sub-asset class in RTS 2. It is unclear if this covers listed IR Options or listed IR Options and OTC options that are ToTV (noting that there is a separate sub-asset class for swaptions).

  In the context of OTC IR options, the transitional transparency calculations for the SSTI and LIS thresholds for IR options are extremely high, in the billions of Euros. We assume the calculations have only used data from listed options as opposed to OTC IR options, OTC IR options being very different products that trade at much smaller sizes. If the sub-asset class is interpreted to mean IR options and OTC IR options that are ToTV, the transparency calculations need to be re-run using a more representative sample, to avoid significantly impairing liquidity in those markets as a result of the thresholds as they stand.

- **Credit default swap maturity buckets**

  The specified 'time to maturity bucket' in the TTC appears to be inconsistent with the RTS2 additional qualitative liquidity criterion for this sub-asset class (Table 9.1 of RTS2). The RTS2 additional qualitative liquidity criterion for Index CDS states that:

  The underlying index is considered to have a liquid market:

  (1) during the whole period of its 'on-the-run status',

  (2) for the first 30 working days of its '1x off-the-run-status'.

  The market treats a 5-year 'on-the-run' Index CDS as any maturity from 5.25 to 4.75 years – the market moves to a new 'on-the-run' contract every 6-months (on each 20th March and September). For example, on 1st April 2019, the current 'on-the-run' 5-year Index CDS contract mature on 20 June 2024. Then on 20 September 2019, firms switch to trading contacts maturing on 20 December 2024 and this remains the 5-year 'on-the-run' contract until 20 March 2020, at which point firms switch to trading contracts maturing on 20 June 2025. Therefore on the 20th September 2019, the 5-year 'on-the-run' Index CDS will have a time to maturity of 5.25 years.

  This concept of 'on-the-run' status is consistent with how "5Y Tenor" is defined for the purpose of the Clearing Obligation, and is allowed for in Table 9.1 of RTS2. If the "4Y_5Y" time to maturity bucket specified in the TTC is determined to mean each contract where the Scheduled Termination Date is within 4 to 5 years of the Trade Date, then the period of highest liquidity (the first few weeks following the roll date – which will fall between 5.25 and 5 years following the Trade Date) will not be in-scope.

  ESMA clarified that the instructions on how to calculate the time to maturity buckets given in the templates for the data collection on non-equity instruments, were based on ISDA's suggestions in order to take into account the additional 0.25 year period.

  The Associations note, however, that whilst the full period of the 'on-the-run series' is captured by the formula set out in the data collection template, the entire period of the '1x off-the-run-status' is also captured. This is not consistent with part (2) of the additional qualitative liquidity criterion in Table 9.1 of RTS 2, which states that:

  "The underlying index is considered to have a liquid market:

  (1) during the whole period of its 'on-the-run status',

  (2) for the first 30 working days of its '1x off-the-run-status'".

  The Associations note that trading of Index CDS on an Index series that is immediately prior to the current 'on-the-run' version and outside of the first 30 working days of such status is likely to be significantly different in character compared to trading in the first 30 working days of such status. Whilst trading in the first 30 working day period would largely constitute rolls to the current on-the-run series, trading after the first 30 working days is likely to be much more bespoke and illiquid and comprise of compression trades etc. ISDA notes that, although the trading convention of Index CDS is aligned with the dates that an Index moves from one version to the next (as described under above), the time to maturity of an Index CDS should not be conflated with the on-the-run status of the particular Index series that the CDS is traded on. A new Index series is comprised of different components compared to the previous series and therefore the market treats CDS on a new Index series as a separate instrument compared to CDS on the previous series. Any formula that calculates the number of days from execution to maturity cannot determine the status of the particular Index series that the CDS is traded on.

Potential consequences of including such Index CDS that are traded outside of the first 30 working days of the relevant series '1x off-the-run-status' in transparency calculations for sub-classes determined to have a liquid market, is that SSTI/LIS threshold levels are likely to be skewed.

It is essential that the SSTI/LIS post-trade thresholds are calibrated correctly to ensure that end users can continue to transact in large trade sizes. If set too high, very large trades will be subject to real time transparency and market makers may be unable hedge and unwind their positions. This will ultimately result in a reduction of liquidity and wider spreads at the expense of end-users. ISDA notes that SSTI and LIS post-trade thresholds specified in the TTC for ITRAXX Europe 5Y Index CDS are set at EUR 175,000,000 and EUR 225,000,000 respectively, however the equivalent threshold for this instrument under U.S. regulations is significantly lower (the CFTC block threshold is USD 110,000,000).

- **Post-trade transparency 'price' for CDS**

  RTS2, Annex II Table 2, gives descriptions of the details of transactions to be made available to the public for the purposes of post-trade transparency. For credit default swaps (CDS) the description given for the details to be published for 'price' is "the coupon in basis points". Standard single name and index CDS trade with fixed coupons. For example, investment grade single name CDS trade at 100 basis points and high-yield single name CDS trade at 500 basis points. An upfront payment amount is exchanged on trade date +3 representing the difference between the fixed coupon and the agreed spread. ISDA notes that for such types of standard CDS, transparency on the "coupon in basis points" without the upfront payment amount will be unlikely to give meaningful transparency.

- **Post-trade transparency 'price' for Equity Swaps/Portfolio Swaps**

  ISDA also note that transparency on 'price' for Equity swaps and Portfolio Swaps using the spread paid/received in addition to the underlying interest rate (as described above) will be unlikely to give meaningful transparency for types of Equity Swap and Portfolio Swap orders where the price forming feature is the initial equity price, and such spread is pre-agreed in the master confirmation.

  ISDA has written a paper on this issue that we would be happy to share with you.

- **Commodity derivatives – pre-trade transparency**

  With respect to commodity derivatives, the RTS 2 methodology has proven difficult in practice. Calculations based on insufficiently granular sub-asset classes, besides arbitrarily selected and inappropriately calibrated parameters, result in disproportionately low LIS thresholds for highly liquid products and overly high thresholds for developing markets. This is an issue in most commodity markets and even if the below examples are mainly focused on the energy sector, other commodities would require re-calibration of the thresholds.

Trading venues and market participants are also challenged by the fact that LIS thresholds are set in Euros instead of lots. Using lots has been the standard in the market for similar threshold calculations pre-MiFIR. The circumstance that LIS thresholds are currently based on historical Euro trade values and not the number of traded lots in a particular sub-asset class result in disproportionate LIS thresholds that ignore the actual underlying trading behaviour.

For example, the LIS threshold for highly-liquid *ICE Futures Europe Gasoil Futures* calculated under the current RTS 2 methodology is equal to 10 lots compared to the 100 lots minimum block threshold applied before the introduction of MiFIR. In contrast, in far less liquid products such as *ICE Futures Europe Rotterdam Coal Options*, only trades above 50 lots would be considered LIS as compared to the 5 lots block threshold pre-MiFIR.

Furthermore, the new methodology has led to a significant number of niche and nascent products being incorrectly classified as liquid, and thus becoming subject to significantly broader transparency requirements, which were previously reserved for developed markets.

The current market practice in the electricity market with broker systems is such that energy brokers offer clients clearing of exchange traded blocks at multiple venues. The trades are concluded outside the market but according to market rules. These blocks represent a large part of the total traded and cleared market (for the Nordic power markets it is approximately 50%). For example, the LIS threshold for a liquid Nordic power monthly contract is estimated to be 26 lots compared to an average order book lot of 5.4 (trade value = EUR 142,000) and 13 (EUR 263,000) lots for blocks. Too high LIS thresholds may lead market participants to revert to more bilateral trading (e.g. OTC and origination) outside transparent and supervised venues and outside CCP clearing. This increases market concentration and leads to less competition and ultimately lowers the social welfare gains of an efficient price discovery.

As it currently stands, the MiFIR pre-trade transparency regime has a materially adverse impact on commodity derivatives markets by:

- Preventing pre-negotiated trades to be submitted to exchanges, thereby limiting the ability of market participants to hedge their commercial exposures;
- Forcing the trading activity to move away to the non-cleared OTC space, thereby limiting transparency and undermining the price discovery process as well as limiting the possibility of physical delivery to take place under the exchange rules;
- Limiting the number of cleared trades and therefore increasing systemic risk and market concentration;
- Preventing nascent commodity derivatives markets from developing;
- Pushing small and medium sized members towards more bilateral (OTC) trading, ultimately resulting in more direct trading with the large(r) producers, often referred to as origination business.

This goes against the MiFID II/MiFIR’s policy objectives.

***The rationale of exchange-operated trade registration facilities***

As a general principle, the Associations believe that financial markets benefit from a high degree of transparency in a multilateral environment. It maximises market participation and enables the matching of buying and selling interests in a manner which is conducive to forming competitive prices. At the same time, and in respect of commodity derivatives markets, there is a need for a calibrated approach to transparency in recognition of the fact that some forms of trading activity cannot easily be accommodated in a fully transparent central order book environment:

If pre-trade transparency rules were to be applied to trade registration, the thresholds should be set in such a way as to encourage as much trading volume as possible to be executed through the central order book, taking into account a realistic assessment of the characteristics of the market and the liquidity in this order book.

Registered trades, and their accompanying rules and procedures, should be designed to support and complement orderly markets.

Typically, a market is suitable for the introduction of trade registration where it:

(i) Offers a way to wholesale market participants in which to create or extinguish substantial positions without introducing disruptively large orders into the central order book. The use of an exchange's trade registration facility in those circumstances enables such participants to avoid an execution delay and/or a price slippage by executing large orders outside the central order book. Such business is executed under the exchange's rules and is subject to specific minimum volume thresholds as well as strict pricing parameters which are designed to ensure that registered trades are concluded at a fair market value;

(ii) Supports the development of new or nascent on-exchange markets by providing an alternative to OTC trading. This creates a pool of open interest to support the transition of further trading from an OTC environment to an exchange environment;

(iii) Enables market participants to pre-negotiate substantial trades against markets or settlements that would have otherwise to be traded directly in the relevant period, with the associated commercial and compliance risks.

***Proposed solutions to the described challenges***

**Option 1: replacing the current methodology set out in RTS 2 with a product-specific approach**

The Associations propose that the RTS 2 is amended in the following way: the current methodology for setting LIS thresholds should be replaced by a more appropriately tailored and market-based approach. Specific thresholds should be set by the relevant NCAs in cooperation with trading venues with regards to instruments these venues admit to trading.

The proposed approach to determining thresholds and rules for registered trades would depend mainly on:

- The current liquidity in the contract;
- The commercial activity that underpins trading in the central order book (including the average lot size or the most frequently traded lot size).

For example, in the case of a highly liquid instrument, such as the *ICE Futures Europe Brent Futures* contract, whilst approximately 600,000 to 900,000 lots are traded each day, the average trade size is only 2.4 lots and the number of lots at the best bid or offer is typically 30 or 40 lots. This means that an order of e.g. 1,000 lots is too large to be placed into the central order book since it would have a significant price effect, whether it is executed or not. Brent, moreover, is a futures contract used to hedge entire cargoes of oil in sizes of 600 lots or more. There is substantial appetite for such large trades. The size of a block trade permitted in liquid contracts is thus driven by what size of order would disrupt the central order book and by whether the underlying physical trade would be likely to give rise to orders of such size.

In less liquid and illiquid contracts, it is probable that the market will even have difficulties in absorbing orders of a modest size. A more nuanced approach is therefore needed. Market participants would consider which size of an underlying physical trade might require a futures hedge. For example, Fuel Oil contracts are not liquid in the central order book, but Fuel Oil itself is typically traded in tranches of 5,000 to 10,000 tonnes in the physical market. To enable a futures hedge to be executed on-exchange, the permitted block trade size should be equivalent, i.e. 5 lots. This adds to the open interest in the exchange contract, some of which is subsequently extinguished in the central order book which means that there is enough activity in the instrument for other market participants to offer or bid on-screen.

In addition, many contracts are traded as bundles – for example:

i. A margin strategy will involve buying crude and selling gas oil, jet, and naphtha against it;
ii. A seasonal hedge may involve buying all six months of the summer and selling all six months of the winter;
iii. In the Nordic power market, a full hedge of the bidding zone will consist of a liquid system contract and an illiquid classified Electricity Price Area Differential (EPAD) contract.

In these cases, the Associations consider all the components to be a single reported trade as they share a common economic purpose and thus allow the size of each component to be added in order to meet the threshold.

**Option 2: re-calibrating the LIS and IL parameters for commodity derivatives**

The Associations believe that acknowledging the long-standing and well-established practice of setting minimum thresholds for registered trades and determining liquid markets through exchanges would be the most appropriate way of revising RTS 2. However, we would also welcome a less comprehensive amendment, focusing on energy derivative markets, as a short-term measure in order to mitigate at least some of the negative effects the inappropriately calibrated MiFIR pre-trade transparency regime.

As mentioned above, the overly restrictive thresholds and improper classification of niche and nascent markets as liquid result inter alia from the inaccurately set parameters for LIS and IL waivers. These parameters should be recalibrated as follows in order to better reflect the underlying characteristics of energy markets.

**Proposal for revised thresholds for energy commodity derivatives and emission allowances derivatives**

| | **IL waiver (Table 7.1 Annex III, RTs 2)** | | **LIS waiver (Table 7.2, Annex III, RTS 2)** | |
|---|---|---|---|---|
| | **Average daily number of trades** | **Average daily notional amount (ADNA)** | **LIS percentile** | **LIS, notional value of a trade** |
| **Current value** | 10 | 10,000,000 | 70 | 500,000 |
| **Proposed value** | 100 | 100,000,000 | 30 | 50,000 |

| | **IL waiver (Table 13.1 Annex III, RTS 2)** | | **LIS waiver (Table 13.2, Annex III, RTS 2)** | |
|---|---|---|---|---|
| | **Average daily number of trades** | **Average daily notional amount (ADNA)** | **LIS percentile** | **LIS, notional value of a trade** |
| **Current value** | 5 | 150,000 tons of CO2 equivalent | 70 | EUA as underlying: 50,000 tons/other underlying: 25,000 tons |

| | | | | |
|---|---|---|---|---|
| **Proposed value** | 100 | 150,000 tons of CO2 equivalent | 30 | EUA as underlying: 50,000 tons/other underlying: 25,000 tons |

Please note that the proposed suggested thresholds have been based on the assumption that the liquidity assessment is conducted per financial instrument per venue.

## Annex – Commodity position limits - Proposals for re-calibration

The Associations believe that position limits for new and less liquid contracts should be temporarily suspended in order for these contracts to be able to develop (see above). However, should such a change not be immediately possible, the Associations recommend that the current provisions are nonetheless adjusted in order to mitigate their adverse negative impact on the development of markets in commodity derivatives.

We propose that the current *de minimis* limit for illiquid markets is increased to 5 000 lots to better accommodate the nature of fast growing contracts. Such an approach would ensure that (1) the development of contracts is not curbed by an overly restrictive limit once open interest grows closer to the 10.0000 lots upper range of the illiquid markets category and (2) the overall framework becomes less dependent on unreasonably high levels of flexibility required from NCAs in terms of re-classifying markets and re-calibrating applicable limits on a near real-time basis.

For contracts between 10.000 lots and 20.000 lots or "less liquid contracts" the Associations propose that the current derogation for the position limit should go up to 50% and be transformed into a default approach from which derogations could be envisaged if needed.

Furthermore, the Associations would recommend to explicitly allow NCAs to base their calculation on anticipated growth in open interest.

### Examples and further background

In order to provide for a workable regime for growth markets, and given that NCAs cannot set position limits on the basis on anticipated open interest growth, NCAs need to be able to process near instant updates to the categorisation of markets and re-adjust the applicable limits as open interests in a market increases. This is especially true for markets that experience strong increases in open interest in a small period of time. Markets with initially relatively low levels of open interest can develop into liquid markets in a matter of months, weeks or even days. In order for a limit not to impede the development of fast-growing markets:

- The growth of open interest in a given market requires a timely reclassification of this market under the position limits regime (for example from 'illiquid' to 'less liquid') in order to allow the position limit to be adjusted to a workable level, before it becomes unnecessarily restrictive. The use of administrative acts to implement or adapt position limits, as required by some Member States' national legislation, is an example of how inflexible requirements can hamper the ability of NCAs to adapt to the fast pace with which contracts can grow.

- It is essential that NCAs take an adequate approach with regard to the time period they take as a basis to calculate open interest for the purposes of setting a position limit and classifying a market. Not looking at the right time period could result in relatively frequent requests to NCAs for adjustments of the limit, as the newly set limit could be reached with only a limited amount of transactions in a fast-growing market.
- In certain cases, such as the transition to a new benchmark, it would even be desirable for NCAs to be able to categorise markets and set limits based on anticipated growth in open interest. One example is the German bidding zone split which triggered EEX to split the German/Austrian Phelix benchmark power contract into a German Phelix power contract and Austrian Phelix power contract.

In practice it has proven to be impossible for NCAs to reclassify markets and recalibrate the applicable limits and in a manner that would prevent a negative impact on the development of fast-growing markets.

### Inaccurate reflection of physical markets

Moreover, for some commodity derivatives, the characteristic of the underlying physical market is such that an effective hedge can only be achieved by trading a specific number of lots. Such a number cannot be traded without exceeding the limit. Yet, under the current MiFID II provisions, the limit cannot be raised without sufficient increase of the open interest.

In example, the recently launched *ICE Futures Europe TD20 West Africa to UK-Continent (Baltic) Future* has grown significantly over the past few months, reaching over six thousand lots of open interest. The contract is a Suezmax crude route, West Africa to UK Continent for tankers sized on average 130,000 MT (DWT). The biggest positions exceeding 1.9k lots are held by commodity traders, some of which are located outside of the EU and do not hold hedging exemptions. Companies with Suezmax types of tankers fleets tend to hedge calendar years forward, fleet sizes up to 20 tankers and above.

To hedge a fleet of ten tankers on a year forward basis - the trade size will be (either as a single trade or done in a sequence of multiple smaller trades for the same Calendar Year tenor, keeping positions open throughout expiry):

**130 lots * 12months * 10 tankers = 15,600 lots** to hedge freight rates exposure for a single Calendar year (i.e Cal 2019 trade)

With fast growing trading volumes in wet freight, companies are now seen extending hedges down the curve, trading to cover Cal19 / Cal20 and even Cal21 tenors that we are now seeing in a VLCC TD3C route (Arab Gulf to China crude route). International Maritime Organization's regulation going live in 2020 has been a significant factor behind the longer-dated hedges as companies are seeking certainty and stability of "locked in" freight levels that are expected to become volatile as the new sulphur caps for bunker fuel will start affecting the cost of shipping from January 2020.

Since the traders active in TD20 have indicated the business need to hedge multiple calendar years forward in TD20 route that would result in tripling trading volumes in the traded volume calculation scenario above, with potential volumes amounting to 46,800 lots.

However, the growth of the contract is restricted by the current *de minimis* position limit of 2.500 lots. Further development of this contract requires dynamic changes of the current limit to a much higher limit based on the open interest.

## Annex II – ISDA paper on the treatment of packages under the MiFID II framework

ISDA | Safe, Efficient Markets

### Introduction

1. ISDA understands that pre- and post-trade transparency is intended to improve transparency, particularly in non-equity markets. ISDA also understands that pre-trade transparency is intended to reflect prevailing market conditions and value of financial instruments, and post-trade transparency is intended to make public the economic terms on which financial instruments have been traded at a given point in time. It is not clear that the approach being taken to transparency for packages achieves these goals.
2. ISDA considers that optimal transparency is not best served by the reporting of every single transaction, but instead should focus on the accurate and timely publication of data reflecting prevailing market conditions. Indeed, there are a number of exemptions from transactions being reported for transparency purposes, which are intended to prevent misleading information about current market conditions being included with the pre and post trade transparency information. For example, SFTs are excluded, as they do not represent price-forming transactions.
3. The rules applying to packages in MiFID II provide a foundation on which the transparency rules can be applied. However, there are limited details set out in the Level 1 and Level 2 text itself, particularly in relation to systematic internalisers (SIs), so Q&A are essential to assist achieving a consistent approach to the application of the packages regime. They also play a critical role in establishing a framework that supports the policy rationales of the European legislature, including minimising undue market, operational and execution risk for market participants.
4. The rules applicable to packages across various parts of the MiFID II framework are not always consistent. In particular, although we note that some of the Level 2 rules apply obligations on a component basis, the Level 3 guidance diverges from the Level 1 principle that, for pre-trade transparency, packages should be treated as a whole. Such inconsistencies ultimately affect the quality of the transparency data that is produced by market participants, as the information reported may not be representative of actual trading activity. It will therefore also affect the usefulness of data for end-users of financial services and may impact the ability of regulators to fulfil their supervisory functions.
5. This paper seeks to highlight some of the key areas where these issues arise, in particular, where we believe that ESMA/NCAs have the ability to provide vital clarity through their policy and supervisory activities. Our underlying principle is that transparency data should accurately represent prevailing market conditions and trading activity that has taken place. We note that this approach prioritises accurate transparency rather than the quantitative amount of transparency available in the market. We believe that "less" transparency may sometimes be positive if it means that the transparency available is more accurate overall.

## Pre- and post-trade transparency: Package level or component level?

### Pre-trade transparency

6. Article 18(11) of MiFIR states that *"(i)n respect of a package order and without prejudice to paragraph 2, the obligations in this Article shall only apply to the package order* ***as a whole*** *and not to any component of the package order separately.* [emphasis added]". Question 4(c) in Section 4 of ESMA's Transparency Q&A recognises this, stating that "*(f)or pre-trade transparency obligations to apply at package order level, including for an exchange for physical, an investment firm must be a systematic internaliser in all financial instrument components of the order.*" However, it goes on to say that "*(w)here an investment firm is prompted for a quote for a package order for which it is a systematic internaliser only for some components, the investment firm can decide either to provide a firm quote for the whole package or only for the components for which it is a systematic internaliser.*"

7. It is not clear if this additional sentence means that, if the investment firm is not a systematic internaliser in all components of the package order, it:

   a) <u>can voluntarily</u> provide a firm quote on the whole package, or for the components on which it is a systematic internaliser; or

   b) <u>must decide either to</u> provide a firm quote for the whole package, or only for the components for which it is a systematic internaliser.

8. Both interpretations introduce the concept that the components of packages should be subject to pre-trade transparency in their own right. ISDA is concerned that this:

   a) is contrary to Article 18(11) of MiFIR; and

   b) treats swap instruments which have been executed as part of a package as individual trades for transparency purposes. This has the potential to be highly confusing and misleading to the market.

9. If executed as part of a package, the price of the swap component is likely to be off market (reflecting the different risk and characteristics of a package trade compared to a single component trade). However, if the investment firm provides pre-trade transparency on a component it may be doing so without being able to properly identify that the price provided is not representative of the currently tradable price. In order to provide the end client with meaningful transparency, the investment firm may end up needing to provide two prices: one to fulfil its MiFID II pre-trade transparency obligations and one to reflect the price at which it is willing to trade the package as a whole.

10. This can be seen particularly in the case where the derivative component is subject to the trading obligation and the investment firm cannot execute the trading obligated component through a trading venue and flag that it was agreed as part of a package trade. The trading obligated component may be subject to pre-trade transparency by the trading venue, despite the economic trade (the package) already having been agreed. This pre-trade transparency may be additional to the pre-trade transparency applied to the actual trade – the package – or may apply even though the package itself was not subject to pre-trade transparency. Beyond this being convoluted and confusing for the participants in the trade, when done on any scale this leads to highly convoluted pre-trade transparency information, mixing off-market trades with at-market trades in publicly available pre-trade transparency data.

11. The concept underlying a package is that the components are in some way linked, and it is beneficial to the end user to trade the different components in one transaction. These benefits are likely to extend to favourable pricing compared to if the components were traded separately. Providing

transparency on individual components of packages would therefore be very misleading unless there is a robust way of informing users of the data that those components were executed as part of a package, and so the transparency is not representative of the prevailing market conditions for outright trading in those financial instruments. Indeed, RTS 2 does not envisage flagging components separately without being flagged as a package for post-trade transparency, and article 18(11) of MiFIR is clear that pre-trade transparency should be on the package as a whole. It is therefore unclear where the basis for providing transparency on components separately has emerged from.

12. ISDA and its members believe that an interpretation that is open to ESMA/NCAs which is consistent with Article 18(11) of MiFIR is that SIs should only provide pre-trade transparency in relation to a package where it is a an SI in all components of a package. This would ensure that transparency provided is representative of the prevailing market conditions for the type of transaction that has actually taken place. ISDA suggests that it would be useful for the Q&A to be clarified so that it is clear that any quotes provided by SIs either on components or on the whole package (if they are not SIs in all components of a package) are purely on a voluntary basis (albeit noting the concerns set out above).

**Post-trade transparency**

13. ISDA recognises that the post-trade requirements in relation to packages are largely set out in the Level 2 text and as such, ESMA may not have the mandate to change much of the requirements in relation to post-trade transparency. However, ISDA believes that ESMA does have the mandate to adopt a more functional interpretation in some areas of post-trade transparency.

14. Helpfully, RTS 2 introduces a package flag for post-trade transparency, ensuring that package transactions are appropriately identified as such in post-trade transparency data. This assumes that all components are flagged together, by the same entity/party to the trade, after the transaction has been agreed. It also relies on an assumption that if something is traded as a package it can be treated as a package under MiFIR (which, as explored below, might not be the case according to ESMA Q&A which states that a package cannot contain an equity or non-ToTV component). Should this not be the case, the transaction would not be able to be treated as a package in post-trade transparency reporting, despite both counterparties agreeing that this is the case.

15. Question 4(f) in Section 4 of ESMA's Transparency Q&A notes that meaningful transparency can only happen if all the components are reported by the same party. However, an investment firm cannot always reconcile the practical outcomes of question 4(f) and question 4(g) in Section 4 of ESMA's Transparency Q&A where packages are executed on different execution venues (in particular where there are components traded on and off venue). Further, article 7(8) of RTS 2 suggests that the same deferral should apply to all components of a package, but it is not clear how this can be practically applied where the package is executed part on-venue and part OTC, as the counterparts/trading venue would not know what the other participants are dong.

16. This inconsistency can be resolved by adopting an interpretation that packages should only be subject to transparency when the packages and all of its components are traded on the same execution venue. If a package is comprised of components that are traded both off venue and on venue, the on-venue components will be reported by the trading venues and the off venue components will be reported by the investment firms. As ESMA notes in its answer to question 4(g), MiFIR is silent on the execution venue of a component of a package so it would be open for ESMA to propose that transparency in relation to packages only applies where they are executed on the same venue. Adopting this interpretation would mean that the only packages subject to post-trade transparency would be those that are wholly executed on the same trading venue or wholly executed OTC and in each case, there would be one party that is responsible for post-trade transparency. This would be consistent with the

principle proposed by ESMA in question 4(f) that one party should report all the components of a package.

17. We note that it would be preferable if a package could be flagged by a trading venue, including where the components were executed outside of the trading venue and then an individual component is subsequently executed through the venue (ie. a pre-arranged/negotiated trade). In this scenario the executing firm would need to inform the trading venue that the relevant component was executed as part of a package. We note, however, that from a trading venue's perspective the Level 1 and 2 require the trading venue to apply regulatory requirements to the trades that are executed on their venue, and do not allow trading venues to apply discretion based on any trading activity that has taken place in advance of an instrument being sent for execution on that trading venue. Therefore, the trading venue would be legally required to apply requirements such as pre-trade transparency, post-trade transparency, any deferrals, best execution statistics analysis etc., on the basis of the trading that has taken place on the trading venue – i.e. the individual component executed on the venue, and not the package as a whole. In the absence of Level 1 and 2 change, therefore, we note that a package being flagged by a trading venue where only one component is actually executed on that venue is not currently possible.

### Deferrals

18. Enhanced deferrals that are available for sovereign debt are not available if traded as part of a package. There should be a consistent approach to the general principle proposed by ESMA that if one component is eligible for a deferral, the whole package qualifies for the deferral. In the case of enhanced deferrals for packages with sovereign debt components that would be eligible for an enhanced deferral, the enhanced deferral should be available to all components of the package, where applicable.

### Conditions on the components of a package

19. Packages trade as a combination of components that are linked to each other, to hedge a risk that a specific end user is exposed to. This does not consider the specific regulatory treatment of the individual components of the package – this is a commercial consideration driven by the economic requirements of the end-user.

20. Treatment of packages with an equity component**:** Question 4(b) of Section 4 of ESMAs' Transparency Q&A[14] states that package orders and transactions cannot contain an equity component (for example, an equity EFP, or a basis trade). This appears to be based on an interpretation that the waivers in Article 9 of MiFIR only apply to non-equity instruments. ISDA and its members note that the equities transparency regime does not have a package flag for post-trade transparency. However, neither the definition of a package order or a package transaction specify conditions on the nature of the components that a package contains, other than that a package order and package transaction must contain two or more financial instruments.

21. Treatment of packages with a non-ToTV component**:** Similarly, question 4(h) of Section 4 of ESMA's Transparency Q&A states that package orders and package transactions can only contain instruments that are ToTV, citing the definitions in Article 2 of MiFIR. However, there is no stipulation in the Article 2 definitions that all the components of a package must be ToTV in order for it to be considered a package under MiFIR. Rather, these definitions only specify that a package order or transaction must contain two or more financial instruments – the fact that a package contains a non-ToTV component

[14] https://www.esma.europa.eu/document/qa-mifid-ii-and-mifir-transparency-topics-0

should not prevent the package from being considered as such under MiFIR. An example of such a package would be a swap against a primary issuance bond.

22. The view of ISDA and its members is that the ToTV criteria should be used to determine whether transparency is owed rather than used to determine what packages can be considered to be packages under MiFIR. We support the view that the transparency requirements for non-equity instruments only apply to packages for which all components are ToTV, and packages which do not contain an equity component. However, we query how this links to the definition of what is or is not a package under Article 2.

23. The interpretations provided in the Q&A have material practical implications on the trading of affected packages. Most apparently, if packages are not permitted to be defined as a package under MiFIR this requires the equity or ToTV component(s) to be subject to transparency requirements on a component basis. As discussed above, this has the potential to lead to highly misleading transparency on these trades, as they are not able to be flagged as a package trade in transparency data.

24. Requiring pre-trade transparency on the components of a package individually would create transparency on "more" instruments, but transparency on those instruments would not be representative of the economic conditions of the trade, or of the individual component financial instruments on which transparency is being provided. Such transparency would, from the perspective of a consumer of the transparency data, be treated the same as instruments that are not executed as part of a package, therefore diluting and compromising the quality of transparency data overall. There is a risk that such incorrect regulatory transparency on components of packages could mislead end users to entering in to trades based on a belief that that market is moving, when in fact the most recent quotes published in regulatory transparency data for a given financial instrument were executed as part of a package. So in fact the quotes in the transparency data were off-market – i.e. not reflective of prevailing market conditions in that instrument on an outright basis – but there is no way for the end-user (or any other consumer of the data) to know this.

25. This also introduces complications when a package contains a component subject to the trading obligation for derivatives (DTO). Where a package contains a non-TOTV or equity component the DTO component may not be able to be considered as part of a package, and so would need to be considered as an individual trade under the DTO, not being able to be considered under ESMA's Opinion on the application of the DTO to packages. Further, this interpretation makes providing a quote to a client highly complex, with multiple different quotes being given to fulfil regulatory obligations, none of which reflect the economic realities of the trade.

26. As noted above, an interpretation that we believe is open to ESMA/NCAs and is consistent with the Level 1 principle for pre-trade transparency that packages should be treated as a whole is to require transparency where all components are traded on the same execution venue and for SIs, only where the firm, is an SI in all the components.

27. We note that whilst it appears that fewer packages trades will potentially be made transparent if the above alternative interpretation is followed, for the reasons we have discussed above "more" transparency is not necessarily better or more useful transparency. The consequence of the current packages framework limits the quality of the transparency for end users in all instruments, irrespective of whether or not they are traded as part of a package. We note that whilst there is no transparency on packages that are excluded from pre-trade transparency, they may be subject to post-trade transparency. The difference in scope mirrors exactly the much larger scope of instruments subject to post-trade transparency vs pre-trade transparency when trading instruments individually. We note that ESMA can always reserve the right to revisit the Q&A should any avoidance behaviour develop.

    We also note that ESMA's interpretation of the the Level 1 rules require SIs to quote in circumstances where they would not have to if they were trading the components individually, which potentially exposes them to additional risk. The additional risks that are placed on SIs as a result of this interpretation should be considered against the principle that any interpretation adopted should not place additional obligations on firms that they would not otherwise have if the components of a package are traded individually. Question 4(e) of ESMA's Transparency Q&A notes that packages qualify for a pre-trade transparency waiver under Article 9(1)(e)(iii) only if all the components are above SSTI. However, if waivers are considered in the context of trading instruments individually, SIs do not need to rely on the SSTI waiver in Article 9(1) (b) because of Article 18(10) which requires SIs to quote only if an instrument is traded at or below SSTI. ESMA's interpretation in Question 4(e) diverges from the approach to transparency for individual instruments. ISDA's view is that it would be more consistent with the existing MiFIR transparency framework and support the aim of providing meaningful transparency data to the market if SIs are only required to provide pre-trade transparency if all the components of a package are traded above SSTI.

### Treatment of packages under the trading obligation for derivatives

28. In March 2018 ESMA published an Opinion outlining the interaction between the trading obligation for derivatives (DTO) and package orders.[15] This was very welcome clarity. Paragraph 14 of the Opinion states that, "*only where it is feasible to trade components of a package that are subject to the TO on a trading venue without creating undue operational or execution risk, those components need to be concluded on a trading venue.*" The Opinion then clarifies that in ESMA's view, the trading obligated component of a package should be executed through a trading venue in the following circumstances:
    - All components of the package are subject to the TO;
    - At least one component is subject to the TO and all other components are subject to the clearing obligation for derivatives (CO);
    - At least one component is an IRS subject to the TO and all other components are government bonds denominated in the same currency ('spread overs').
29. The second category is likely to capture all swaps that fall in to the first category, as a general pre-condition of being subject to the trading obligation is that the swap is subject to the clearing obligation. We do not envisage significant issues as market participants implement the Opinion for the first two categories.
30. The third category is less straightforward. It is clear from the Opinion that the bond component does not need to be executed through the venue, only the trading obligated component. Further, it is clear that the use of pre-arranged/negotiated trades is permitted, subject to the conditions in Section 5 question 11 of ESMA's Transparency Q&A. However, as such packages need to be traded across multiple trading desks (the government bond desk and the swaps desk) and the pricing of the package needs to be agreed across those desks, this is a more significant implementation build. It requires automated processes to ensure that if the package transaction is agreed OTC, the swap(s) subject to the DTO are then executed through a trading venue. This also requires systems and compliance training for traders, and updates to Terms of Business to ensure that clients are aware that they need to send an RFQ-1 through the venue after a package trade is agreed OTC. Accordingly, market participants are likely to need longer to comply with this aspect of the Opinion.
31. As noted above, ISDA and its members believe that an interpretation that is open to ESMA/NCAs is for pre-trade transparency to apply where components are all executed on the same execution venue. This would be consistent with the policy objectives of the transparency framework of MiFID II as well as acknowledging that packages of financial instruments should have their own unique transparency regime (supported by the fact that the European legislature made amendments to the Level 1 and Level 2 text specifically recognising this in the "Quick Fix" Regulation). This will ultimately result in

[15] https://www.esma.europa.eu/press-news/esma-news/esma-clarifies-treatment-packages-under-mifir%E2%80%99s-trading-obligation-derivatives

more meaningful data for end users of financial services and for ESMA/NCAs to carry out their supervisory responsibilities.

### Treatment of packages under the trading obligation for derivatives: The "undue risk criteria"

32. Finally, we note that the Opinion on the treatment of packages and the trading obligation states that "only where it is feasible to trade components of a package that are subject to the TO on a trading venue without creating undue operational or execution risk, those components need to be concluded on a trading venue" (we herein refer to this as the "undue risk criteria"). The Opinion then continues to outline the three types of package where this scenario applies.

33. It is unclear, however, if this is an overarching condition that must be met, or is the condition which ESMA considers will always be met in the three types of package listed. ISDA considers that in the vast majority of cases for the packages falling under the first two criteria that condition will be met. There are, however, a minority of cases, such as a EUR denominated swap against an illiquid EUR sovereign bond, that it might not be met. This would also be the case for an asset swap where the swap component is below LIS – under which case it would not be able to be executed as a pre-arranged/negotiated trade. ISDA suggests that in this small minority of cases investment firms could be able to use their judgement to determine whether this condition has not been met, and so whether the particular package falls under the Opinion. However, this would benefit from clarification by ESMA.

## Conclusion

- For pre-trade transparency, transparency should be provided on the package as a whole (not on an individual component basis).
- For pre-trade transparency, SIs should only provide pre-trade transparency in relation to a package where it is a an SI in all components of a package.
- Packages should only be subject to transparency when the packages and all of its components are traded on the same execution venue.
- Packages with non-ToTV and/or equity components should not be precluded from being treated as packages under MiFIR. Doing so could result in individual components of package trades being subject to transparency on an individual component basis, without any way of flagging that the quote/trade was part of a package.
- ToTV should be used as the criteria to determine whether transparency obligations apply to a package rather than determining whether a package is a package for MiFIR purposes.