European Commission public consultation on the review of the MiFID II/MiFIR regulatory framework

Brussels, 18th May 2020

Section 1. General questions on the overall functioning of the regulatory framework

Question 1. To what extent are you satisfied with your overall experience with the implementation of the MiFID II/MiFIR framework?

☐ 1 - Very unsatisfied
☒ 2 - Unsatisfied
☐ 3 - Neutral
☐ 4 - Satisfied
☐ 5 - Very satisfied
☐ Don't know / no opinion / not relevant

Question 1.1 Please explain your answer to question 1 and specify in which areas would you consider the opportunity (or need) for improvements:

5000 character(s) maximum
including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

While MiFID I introduced more competition in equity markets, MiFID II was meant to strengthen the price formation process by increasing transparency and ensuring that entities, carrying out the same activity, would be regulated in the same way. This was important not only to ensure fair competition but also for investor protection, legal clarity and market integrity.

However, MiFID II continues to allow the growth in off—exchange trading and has unintendedly facilitated a proliferation of Systematic Internalisers (SIs) to the detriment of the price formation process. This increased market fragmentation further diminished transparency. As a result, the share of price forming lit trading activity has decreased to the detriment of issuers and investors.

Securing the right market structure for European public capital markets will continue to deliver price formation thereby serving companies and investors. A well-functioning price formation process is key to the stability and resilience of public capital markets and has a positive impact on the cost of capital for the broader economy.

Periods of crisis, as the current one caused by Covid-19, demonstrate that, at times of high uncertainty, more trading volumes go to the Regulated Market (as a safe, transparent and robust trading venue where core price formation takes place), instead of through a bank or anonymous execution venues. At times of uncertainty, transparency is highly appreciated by all market participants, as it provides financial stability, integrity and fairness. This type of event (which was also witnessed after the 11th September attacks or the Lehman Brothers' crash in 2008) shows the high value of transparent trading versus dark or less regulated trading. During the current crisis, financial infrastructure has performed well and demonstrated resilience. Central banks and governments have reacted swiftly to inject liquidity, but when solvency is lacking, the transformational capacity of banks can only work to a certain extent. Equity is needed to buffer exogenous shocks.

The lessons learnt should provide the basis for all measures that should be implemented in particular with a view to strengthening price formation. This will be needed more than ever so that public equity capital markets can perform to the best of their abilities in helping businesses weather the crisis and refinance their growth once the crisis has subsided.

Exchanges allow companies to raise capital by listing on public markets and thereafter to be traded in the marketplace by investors. Europe needs a market architecture that funds the economy in the most inclusive and fair way. One of the key activities of stock exchanges is organising the activity on primary markets, especially for SMEs. This includes education, promotion, marketing of issuers and communication with banks. Without exchanges' support, there would be no kind of SME market in certain EU countries. MTFs, SIs and OTC can free ride on the primary market function of exchanges as well as the price formation in secondary trading.

In reviewing MiFID II, the key focus for equities should be to adjust market structure and transparency provisions (i.e. limit SI trading to above LIS waiver) to support price formation.

In addition, the development of a consolidated tape can, if structured in the right way, support price formation in a cost-effective manner without creating negative policy implications for investors. This translates into an end of day "Tape of Record" consolidated tape (TOR). Guaranteeing high quality, reliable and consistent flagging of SI and OTC trades is also key to delivering a CT that can be considered meaningful. A TOR would be significantly less complex and less costly to set-up and would provide a comprehensive overview of overall liquidity within the EU on an instrument level.

Certain other provisions in MiFID II/R have had unintended consequences and increased the regulatory burden. For instance, MiFID II has accelerated the reduction in equity research focussing on smaller issuers. A growing number of SMEs are paying independent research providers to write research and take the initiative in approaching investors directly.

When it comes to derivatives trading, capital markets with deep pools of liquidity across different market segments act as a strong stabilisation force in times of crisis. In critical market situations, liquidity in bilaterally-traded products does not allow for efficient risk management, so market participants turn to ETDs – the 'flight to quality' principle. Any fundamental and experimental market structure change (such as the MiFIR provisions on 'non-discriminatory' access for ETDs) should not be implemented, unless a quantitative financial stability impact is conducted to carefully assess all possible negative effects on the financial stability and competitiveness of the EU27.

For commodity derivatives, the objectives to improve transparency and reduce volatility have not fully materialised with the implementation of the position limits and pre-trade transparency regimes. To solve these issues, we would suggest a fundamental review of the scope with the aim of moving towards a more proportionate and efficient position limit regime. This can be achieved by focusing its application to 'critical' contracts only.

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Question 2. Please specify to what extent you agree with the statements below regarding the overall experience with the implementation of the MiFID II /MiFIR framework?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
The EU intervention has been successful in achieving or progressing towards its MiFID II /MiFIR objectives (fair, transparent, efficient and integrated markets).		X				
The MiFID II/MiFIR costs and benefits are balanced (in particular regarding the regulatory burden).		X				
The different components of the framework operate well together to achieve the MiFID II/MiFIR objectives.		X				
The MiFID II/MiFIR objectives correspond with the needs and problems in EU financial markets.		X				
The MiFID II/MiFIR has provided EU added value.		X				

Question 2.1 Please provide qualitative elements to explain your answers to question 2:

5000 character(s) maximum

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FESE fully agrees with the overall aim of MiFID II/MiFIR to increase transparency, foster investor protection and improve the price formation process to the benefit of the economy and society as a whole. However, these objectives have not, as anticipated, materialised with its implementation.

When assessing the impact of MiFID II, we have observed a growth in dark trading, consequently weakening the basis of price formation and the very basis of the equity ecosystem in Europe. Policy makers must reflect on the most appropriate market structure enforcement, to allow a robust price discovery mechanism. A liquid and transparent pool which forms prices is key for the well-functioning of capital markets and for end-investors. Exchanges provide reference prices to all market participants including those that do not contribute to the price formation process. In the absence of policy action, price formation on public markets may become non-viable in the long-term, leading to the re-emergence of dealer markets with higher risk to systemic stability, higher cost and less transparency. Investor confidence must remain a key priority for the next regulatory plan and to achieve that, investors should be reassured that capital markets remain open, well-regulated, transparent, and fair.

Analysis of the evolution of EU equity and non-equity market structure reveals that policy measures to bring trading out of the dark have not been as successful as originally expected. Public equity and non-equity markets with deep pools of high-quality liquidity are a crucial component of healthy capital market ecosystems as well as an important contributor to competitive, transparent and stable EU financial markets. Based on this, we believe more needs to be done to ensure the transparency objectives of MiFID II can be fulfilled. FESE therefore calls for increased reflection on the appropriate application and subsequent enforcement of existing rules.

Question 3. Do you see impediments to the effective implementation of MiFID II/MiFIR arising from national legislation or existing market practices?

☐ 1 - Not at all
☐ 2 - Not really
☐ 3 - Neutral
☒ 4 - Partially
☐ 5 - Totally
☐ Don’t know / no opinion / not relevant

Question 3.1 Please explain your answer to question 3:

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Yes, FESE has observed impediments to the effective implementation of some MiFID II/MiFIR rules.

Flagging of SI trades at an EU level is not done in a consistent manner. More than two years after the MiFID II implementation, the flagging is still very unclear. We would urge ESMA to address this issue. A broader implementation of the Market Model Typology (MMT), which currently ensures consistency of exchange data, would be part of the solution. The extension of the MMT would promote enhanced data consistency and contribute to increased regulatory oversight of SI activity. In addition, we believe that ESMA should review how SIs operate by looking more deeply into the transactions they conclude and report. One important concern is riskless trading: hubs that have the potential to link SIs and counterparties should be monitored to guarantee that they always work on a bilateral basis. If they operate an internal matching system, they must operate an MTF, in line with the MiFID II framework. Such activities must be monitored as there is the risk that they facilitate trading on a multilateral rather than bilateral basis. This would clearly be in violation of the legislation and to the price formation process.

In line with the issues raised by ESMA in their consultation paper on the transparency regime for equity instruments, Frequent Batch Auctions (FBAs) should be defined separately from periodic auctions as currently described in RTS 1. The specificities of FBAs compared to traditional auctions are listed by ESMA in the final report on their Call for Evidence on periodic auctions. The latter resulted in the Opinion on FBAs (ESMA70-156-1355), as well as a Q&A on the tick size regime to apply for periodic auctions (ESMA Q&A on MiFID II and MiFIR market structures topics). We have observed that the Level 3 Guidelines are applied differently across EU jurisdictions with for example some NCAs having forbidden midpoint order pegging as opposed to other jurisdictions where the Level 3 guidelines have not been applied. Although we understand that Level 3 regulation is not mandatory, we also notice distortion to the benefit of some players. In this instance we advise moving the Level 3 measures to Level 2 to avoid competition distortions.

Furthermore, the MiFID II tick size regime applying to shares, DRs and certain ETFs (RTS 11) is not applied uniformly across trading venues. This situation results from technical issues as well as differing interpretations of the regulation across national jurisdictions. Due to the complexity of the regime, and the fact that it is based on the FITRS database which still contains errors (whilst realising that Competent Authorities may not have the full view), exchanges need to make daily adjustments to their systems, regularly question information published and spend a significant amount of resources ensuring that all trading venues apply the same values for the Average Daily Number of Transactions (ADNT) for the determination of the tick sizes. It is necessary, especially now that in June 2020 at the latest, SIs are also subject to the tick size regime, that ESMA engages with trading venues to take their input and clarify some points in the interpretation of the regulation at Level 3 and that technical issues are solved as quickly as possible. We would like to underline as well that not respecting the tick size regime creates competitive distortion which, even if temporary, should be avoided.

Question 4. Do you believe that MiFID II/MiFIR has increased pre- and post-trade transparency for financial instruments in the EU?

☐ 1 - Not at all
☒ 2 - Not really
☐ 3 - Neutral
☐ 4 - Partially
☐ 5 - Totally
☐ Don’t know / no opinion / not relevant

Question 4.1 Please explain your answer to question 4:

5000 character(s) maximum
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FESE believes that the level of transparency could still be improved. **Only large orders for equity and equity-like instruments should be exempt from pre-trade transparency requirements**. Pre-trade transparency leads to a more efficient price formation process by distributing price signals more rapidly to the market. Hence, all standard orders that are below LIS compared to the normal market size, and for which the necessary liquidity is available on a trading venue, should be subject to full transparency requirements. Therefore, FESE is in favour of repealing the Negotiated Trade and Reference Price waivers and consequently the DVC mechanism.

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When it comes to **pre-trade transparency requirements for SIs** the current minimum quoting size of 10% of the SMS is too low. Instead, we recommend they should quote at a minimum €10,000 on each side. FESE is of the view that extending the transparency obligations under the SI regime to illiquid instruments would be an improvement compared to what is in place under the current framework. However, this is less relevant if SI activity is restricted to above LIS only.

With regard to ETFs, FESE would follow ESMA's proposal to increase the pre-trade LIS threshold for ETFs to €5m as the current level is too low. Additionally, we would urge ESMA to complement this measure with additional steps to further promote transparency for on-venue trading of ETFs. Regarding post-trade transparency, FESE would generally agree with ESMA's proposal to increase the applicable deferred publication threshold to align the proportion of deferred transactions more closely with equities. We would also request real-time publication for transactions that are below €20m.

In addition, due to a significant shift of trading volumes in **ETFs from lit order book trading systems to RFQ trading systems** following the introduction of MiFID II/MiFIR, we suggest considering the implementation of a pre-trade transparency regime for RFQ trading systems similar to that for lit order book trading systems. This would require the publication and dissemination of each quote submitted in response to a sub-LIS RFQ immediately after the reception of the quote by the RFQ trading system.

With regard to shares and DRs, FESE agrees with the principle of deferral of publication for large transactions and would also not see any reason to amend the current conditions for deferred publications for those instruments. The analysis conducted by ESMA shows that only a very small portion of trades benefits from deferred publication, justified by their large size; this means that the deferral regime as currently defined has delivered on its objectives to protect large trades while maintaining a high level of transparency.

With reference to OTC transactions for equities and equity-like instruments, FESE agrees with ESMA's conclusion on the level of post-trade transparency and that there is no reason for different thresholds for OTC and on-venue transactions. Rather, we are of the view that trading OTC does not mean that post-trade transparency should be minimal.

With regard to publishing post-trade information in general, FESE believes that a 1-minute delay is not sensible for electronic order book systems and fully supports the ESMA Q&As from October 2017 stating that transactions should be published 'as close to real time as technically possible'. Please note that, if that proposal is followed, the time stamps for trading venues and other execution venues should be aligned in RTS 1 / RTS 2, as current requirements differ (e.g. milliseconds vs. seconds). In addition, these differences have a detrimental effect on any data aggregation. We also believe that the maximum delay should be equal for all execution venues including SIs.

Regarding the **transparency of bonds**, while MiFID II introduced transparency requirements for trading in bonds, it is evident that it has not achieved the objectives. This is acknowledged by ESMA in its recently published consultation (70-156-2189) indicating its analysis has concluded that "*the level of pre-trade transparency in non-equity markets remains limited following the application of MiFID II*" and "*the overall level of real-time post-trade transparency appears to be very limited*". We suggest that the transparency regime should be amended and simplified and in particular, it is important that the criteria for assessing the liquidity of bonds needs to change so as to increase the number of bonds that are deemed liquid and therefore subject to the transparency requirements. This should result in the bonds that actively trade and are most liquid falling within scope of the transparency requirements, and therefore this trading activity should be visible in the market and the benefits of clear price formation process can be achieved.

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Question 5. Do you believe that MiFID II/MiFIR has levelled the playing field between different categories of execution venues such as, in particular, trading venues and investment firms operating as systematic internalisers?

☐ 1 - Not at all
☒ 2 - Not really
☐ 3 - Neutral
☐ 4 - Partially
☐ 5 - Totally
☐ Don't know / no opinion / not relevant

Question 5.1 Please explain your answer to question 5:

5000 character(s) maximum
including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

MiFID II/MiFIR has not levelled the playing field between trading venues and SIs in the equities and equity-like space. Although broker crossing networks were banned with the introduction of MiFID II/MiFIR, the rules for the SI regime were only slightly modified, meaning that SIs still hold a competitive advantage compared to trading venues (see also our responses to Q25 and Q26). When it comes to pre-trade transparency requirements the current minimum quoting size of 10% of the SMS is very low. The threshold only increased by €250 to €1,000 compared to MiFID I, which is effectively meaningless for increasing transparency. Regarding instruments in scope, currently all illiquid instruments are excluded from any pre-trade transparency requirement for SIs. On the contrary, illiquid instruments are in scope for pre-trade transparency for all trading venues unless a waiver from pre-trade transparency is used. FESE believes that an extension of the transparency obligation for SIs to illiquid instruments would be an effective way to improve market transparency and level the playing field between on-venue and SI trading. We are not of the view that such new requirements would be overly burdensome for SIs, they would effectively foster lit trading and overall transparency.

Furthermore, we believe that ESMA should review how SIs operate by looking more deeply into the transactions they conclude and report, e.g. riskless trading. Crucially, MiFID II does not specify any operational details for the SI business model. This is in contrast with the details MTFs and Regulated Markets need to fulfil. Hence, we suggest establishing a level-playing field in terms of the description of the business model and how regulatory compliance is maintained.

In addition, we notice that there is no level-playing field with regard to flagging of SI trades at an EU level. More than two years after MiFID II was introduced, flagging remains very unclear and inconsistent. This could be solved thanks to a broader implementation of the Market Model Typology (MMT) which currently ensures consistency of exchange data as highlighted in Q3.1. That said, we believe the most effective way to minimise the shortcomings of the SI regime (inconsistent flagging of trades and the question of riskless principal trading being based on a bilateral relationship) and create a more level-playing field with trading venues would be to restrict SI activity to trading above LIS only. FESE believes that such restrictions to the SI regime are necessary in order to increase transparency, strengthen overall price formation and promote a level playing field between trading venues and SIs. Above LIS trading would thereby constitute a legitimate dark space in which trades across bilateral execution venues and multilateral trading venues are not subject to pre-trade transparency and would benefit from delayed post-trade transparency.

FESE also sees an unlevel playing field between SIs and multilateral venues active in non-equity instruments. Bonds and securitised derivatives trading are still opaque and there was no increase in transparency triggered by MiFID II compared to MiFID I. This is the case

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for SI trading where there is seemingly no pre- and post-trade transparency available. Transparency is established by SIs via proprietary means, via their websites, via ECN-like networks or has not to be established at all (for illiquid bonds).

For bonds and securitised derivatives, we would recommend using the €100,000 denomination threshold to delineate lit (RM, MTF and OTF) trading from dark (OTC and SI) trading. Prohibiting trades in instruments with denominations below €100,000 to be executed via SIs could trigger a shift of (retail) bond trading to lit venues (RMs, MTFs and OTFs) compared to the current market structure where the major part of bond trades are executed in the dark ((1) OTC between banks or (2) between retailers and SIs). Trading at and below the €100,000 threshold on transparent multilateral venues would reduce market fragmentation and increase liquidity and pre- and post-trade transparency, in particular for retail investors. We suggest that this level applies to both non-liquid and liquid products. The delimitation based on the €100,000 denomination threshold would be consistent with the threshold used for the wholesale disclosure regime defined by the Prospectus Regulation. Furthermore, this threshold would also be in line with the one currently used for the calculations to determine whether a bond is liquid or not. For securitised derivatives, this delimitation would simplify the fragmented execution landscape. We expect that investors – especially retail investors – would profit from the change as it would allow for a better interaction on multilateral markets.

Question 6. Have you identified barriers that would prevent investors from accessing the widest possible range of financial instruments meeting their investment needs?

☐ 1 - Not at all
☐ 2 - Not really
☐ 3 - Neutral
☒ 4 - Partially
☐ 5 - Totally
☐ Don't know / no opinion / not relevant

Question 6.1 If you have identified such barriers, please explain what they would be:

5000 character(s) maximum

including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

Retail investors' access to classic corporate or bank bonds is increasingly limited due to regulation. This is due to the inclusion of classic bonds in the PRIIPS regulation and the increasing number of bond issues availing of the wholesale bond regime for qualified investors with reduced requirements under the Prospectus Regulation, as well as new provisions for product governance defined in the "Guidelines on MiFID II product governance requirements" further reduce retail investors' possibilities to invest in classic bonds.

FESE believes that point 1 of Art. 4 of the PRIIPs Regulation (Regulation 1286/2014), which defines the scope of the regulation, is not sufficiently precise in order to unambiguously assess whether a product qualifies as a packaged retail investment product ("PRIIP"). This has led to uncertainty regarding bonds and to (potentially) the false inclusion of classic corporate and bank bonds into the scope of the regulation.

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Current interpretation of the PRIIPs Regulation by regulators and the market results in the inclusion of:

- Corporate and bank bonds with a call option for the issuer where the amount to be paid back is not fixed but is depending on parameters defined in the prospectus, and
- Corporate and bank bonds with a floor or a cap for the variable coupon.

Consequently, these bonds cannot be accessed by retail investors unless the issuer of the bond publishes a KID. However, this is not realistic as the issuers of these corporate bonds are:

Non-European firms like Apple or Amazon which do not explicitly market their bonds to European retailers and therefore do not publish a KID in Europe, or

- European firms like Daimler or Bayer which do not want to take the risk associated with the publication of a KID. The industry standard is that issuers sell their bonds to their bank consortium and have no further interest in the reselling of these bonds by the banks in particular to retailers.

As a result, European retailers are not able to invest in about 50% of the corporate bonds market.

The product governance obligations under MiFID II for the product life cycle put a number of requirements on investment firms which manufactures financial instruments for sale to end clients ("manufacturer") and on investment firms offering products to end clients ("distributors"). Some requirements have introduced significant administrative burden on manufactures and distributors alike without ensuring a higher level of investor protection. There are Level 3 measures which offers certain exemptions for the non-advised client business and these rules should be taken into account in the MiFID II /R Level1 Review. This is further explained in Q 46.1.
However, regulators should ensure that the target market definition is not adversely used by issuers to prohibit retail investors from investing in products like classic bonds that otherwise suit them.

Question 6.1 Please explain your answer to question 6:

5000 character(s) maximum
including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

FESE concurs with the ESAs´ view, as expressed in the letter by the Joint Committee to the European Commission (19th July 2018), that the scope of the regulation has led to uncertainty and to negative consequences for the functioning of financial markets and affected access by retail investors as well as the liquidity of these markets.

We also observed that the number and overall volume of low denomination issuances by non-financial corporates decreased, while at the same time retail investors faced difficulties to trade corporate and bank bonds (for further detail, see the FESE position paper 17 September 2019, https://fese.eu/app/uploads/2019/09/190917-PRIIPs-Regulation-Impact-on-retail-investors-access-to-corporate-bonds.pdf).

Therefore, we ask regulators for more guidance and clear criteria on whether a bond should be classified as PRIIP and if classic bonds at all should be defined as PRIIP. We propose to assign the ESAs the competence to define such criteria via a change of the Level 1 text to foster a uniform application of the regulation.

When defining the scope of the PRIIPS regulation for bonds ESA should consider the following:

- *The objective of the PRIIPS regulation is to cover products "manufactured" by the "Financial Services Industry" to provide investment opportunities to retail investors (recital 6 of PRIIPS regulation).* Issuers like Apple, Amazon, Daimler or Bayer cannot be considered as part of the financial services industry. Therefore, we conclude that bond issues of these firms cannot be in scope of the PRIIPS regulation. *Recital 6 of the PRIIPS regulation states: "PRIIPS are defined as products where the amount repayable to the retail investor is subject to fluctuation because of exposure to reference values, or subject to the performance of one or more assets which are not directly purchased by the retail investor.* For all those products, investments are not of the direct kind that is achieved when buying or holding assets themselves. Instead these products intercede between the retail investor and the markets through a process of packaging or wrapping together assets so as to create different exposures, provide different product features, or achieve different cost structures as compared with a direct holding." *Additionally, recital 7 of the PRIIPS regulation states: "Assets that are held directly, such as corporate shares or sovereign bonds, are not PRIIPs, and should therefore be excluded from the scope of this Regulation".*

Considering recital 6 and 7 the regulation clearly excludes "classic" bonds from the PRIIPS regulation as no service provider "intercedes" between the retail investor and the issuer of a bond. "Classic" bonds are clearly held directly by retail investors. There is no differentiation possible between a sovereign bond held by a retail investor or a classic bank or corporate bond held by a retail investor. Corporations and banks lend money from investors (including retail investors) using classic bonds to finance their undertakings as do states to finance their infrastructure or welfare.

Furthermore, a call option with a non pre-defined payback amount or a floor/cap of a variable coupon cannot be the single basis for the definition of a corporate or bank bond as a PRIIP. These attributes of a bond are also used by issuers of sovereign bonds like Portugal (e.g. PTOTVHOE0007), Austria (e.g. XS0212688013) and the German state owned "Erdölbevorratungsverband" (e.g. DE0005502462). We see no reason why a corporate or a bank bond issuer must publish a KID and a state does not if these bond attributes lead to the requirements for issuers to "make additional information available, in particular to enable comparisons between different ways of packaging investments" (recital 6 of PRIIPS regulation).

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PART ONE: PRIORITY AREAS FOR REVIEW

I. The establishment of an EU consolidated tape

CTP - Part 1 (Current state of play)

1.1. Reasons why the CTP has not emerged

Q7: What are in your view the reasons why an EU consolidated tape has not yet emerged?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
Lack of financial incentives for the running a CT					X	
Overly strict regulatory requirements for providing a CT			X			
Competition by non-regulated entities such as data vendors					X	
Lack of sufficient data quality, in particular for OTC transactions and transactions on systematic internalisers					X	
Other					X	

Please specify what are the other reasons why an EU consolidated tape has not yet emerged?

FESE believes that difficulties in identifying a valid regulatory use case is the main reason as to why an EU consolidated tape, as defined by MiFID II/MiFIR, has not yet emerged. Furthermore, the viability and potential attractiveness of a CT ultimately depends on the existence of a valid business case. A convincing use case is particularly important to ensure that the tape does not add cost to the industry (i.e. infrastructure and maintenance costs) without any clear benefits, which would make it a disproportionate intervention.

A real-time consolidated tape will create a lot of costs for market users. Several market participants (namely some brokers and sell-side firms) have voiced concerns in this respect. In such a scenario, it is worth asking whether a real-time CT would lead to significant costs for little benefit. The implementation of data disaggregation constitutes an instructive precedent in that regard, with significant implementation costs and additional complexity in terms of managing data, and an extremely low take-up by end users.

FESE is sceptical regarding some of the purported use cases of a real-time consolidated tape. Nevertheless, it is important to underline that exchanges see a case for a tape of record that could be used as an ex-post instrument to inform best execution choices and the control of execution.

The impact of the UK's departure from the EU must also be factored into the assessment. In our view, the relevance of a CT without UK data is questionable. It is difficult to conceive mechanisms to include UK data, notably via voluntary mechanisms, post Brexit. As such, the value of an EU27 CT, particularly real-time, would be weakened. Although, it is difficult to see third country venues contributing data under an EU regulated CT regime, in the case where EU firms would execute EU instruments outside the EU these transactions should be published under the APA regime in the EU, allowing for the information to be included on the EU CT, even if this is not current practice.

In our view, the creation of a tape of record would represent a more cost-effective solution, avoid latency issues and deliver clear value to the market and investors: notably, a means for them to analyse execution quality.

Q7.1: Please explain your answers to question 7

Policy makers may be tempted to believe that a consolidated tape, by increasing transparency, will fix the current market structure issues in the EU. A consolidated tape, however, is no substitute for adequate market structure and rigorous enforcement of rules.

A pre-condition for any reliable CT is the improvement of off-venue data quality as well as coverage of all execution venues. The main underlying issue for the absence of a commercial EU tape is the lack of quality of data reported by SIs and OTC operators, and the reluctance of data vendors to aggregate such inferior data with highly reliable data as, if they were doing so, the full set of data would become unreliable. However, data vendors provide quasi-consolidated tapes already today even if, they are not yet fully comprehensive due to such data quality issues. In addition, MIFID II/MiFIR does not provide specific information on the role and purpose of a CTP which is also one of the reasons that no CTP has yet emerged across the vendor community.

In order to improve off-venue data quality FESE advises, amongst other improvements, to implement the Market Model Typology (MMT) across all trading venues and execution mechanisms, as well as OTC trades. It can be observed that the quality, reliability, and consistency of flagging of SI and OTC trades is currently the biggest issue preventing transparency. Incorrect classification and flagging of transactions are widespread. In many cases, unclear reporting requirements lead to either an over reporting or under reporting of transactions whilst disagreements regarding the nature of an instrument (equity, bond or derivative) can lead to wrong deferrals or publications.

Looking at the current use of market data, the benefit of the tape and its potential use cases remains unclear especially considering the fact that different firms have different needs. Smaller firms focusing on a subset of the EU market will not have a use for all the data contained in the EU CT and would need to filter out the data that is relevant for them. Filtering the EU CT will be costly and add latency, meaning that such firms would be better off using their current market data solutions rather than the EU CT. Bigger firms may also see a benefit in continued use of their current market data solutions that allow them to access individual trading venues and execution mechanisms with ultralow latency, to execute at the best prices available on the various execution venues and mechanisms.

It is worth noting that if data quality, consistency and reliability of SI and OTC data is improved, data vendors will be in a position to consolidate the full range of data on existing trading venues and execution mechanisms thus providing full transparency in the European space.

Q8: Should an EU consolidated tape be mandated under a new dedicated legal framework, what parts of the current consolidated tape framework (Article 65 of MiFID II and the relevant technical standards (Regulation (EU) 2017/571)) would you consider appropriate to incorporate in the future consolidated framework?
Please explain your answer

The creation of a tape of record (TOR) would be more appropriate and is more likely to meet market participants' needs than a "as close to real-time" tape. While several market participants are calling for a real-time tape, the cost of providing it (e.g. infrastructure cost and maintenance cost) and its inherent latency issues puts a viable use case into question. A TOR would be a more cost-effective solution and deliver clear value to the market and investors: a means for them to analyse execution quality or use the data for valuation purposes. This option would require an amendment to MiFID II.

FESE would strongly caution against amending the current CT framework to include pre-trade data (please see response to question 15.1).

In light of the challenges outlined in Qs 7 and 7.1, FESE believes that a TOR would be a sensible and an attractive alternative to what is provided for by the current CT framework. A TOR would consolidate and disseminate the details of all transactions that have taken place in these markets during the trading session.

These details would include, among others: the hour, price and volume of each individual transaction. This information is very useful for investors as it allows them to analyse the performance of each instrument during the trading session and carry out compliance checks. Importantly, it would allow for the assessment of execution quality. Data could also be used from predictive analytics on liquidity developments in different trading venues and the market, identification of liquidity risk end of day pricing used to calculate Net Asset Valuation for mutual funds and ETFs, and other.

Advantages of a TOR vs a real-time CT:

- Information already available: this information is already being generated by trading and execution venues under MiFIR.
- Infrastructure cost: The CT would be able to receive, process and disseminate the information without having to make a large investment in IT infrastructure;
- Maintenance cost: the cost of maintaining an IT infrastructure that receives and processes plain text files once a day is a small fraction of the cost of an IT infrastructure that has to receive, process and disseminate information via data feeds on a real-time / delayed basis;
- Compliance checks: the information consolidated by the tape of record may include additional information compared to a real-time / delayed CT (e.g. block trades information, amendments and cancelations, etc.);
- No latency issues: the latency issues would be non-existent given that the information is not provided real-time.

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The pre-requisite to consolidation of aggregated and comprehensive data in any form is: (i) resolution of non-trading venue data quality, consistency and reliability issues, and (ii) the application of MMT to all market participants. Any review of MiFID II/MiFIR, should include provisions to this effect.

If a real-time CT is ultimately mandated under a new dedicated legal framework, FESE considers that in this scenario the following parts of the current CT framework should be maintained:

- Art 65 1.-5
- Art 8 a), b) and e)

FESE does not consider Art 65 8. c) to be key as there is agreement that a CT should include all instruments from all sources and as such provide a 100% view of the market including off-venue information. Any CT must reflect 100% of activity per asset class. A large portion of transactions in the EU takes place outside of transparent exchanges with asset classes such as ETFs or Fixed Income predominantly traded off-venue. In order to get a full picture of the market and the liquidity of such instruments, there is a need to include all data sources. In the case of ETFs, it is possible to count approximately 46 data sources, compared to 150 data sources reported by ESMA for cash equities, and at least half of those data sources are categorized as off-venue data.

Furthermore, FESE does not consider that Art 65 8. d) of the current CT framework should be incorporated into a potential future CT framework. The reason for this is that the model of Competing Tapes for single asset classes (to be newly set-up) would increase the cost for the industry and lead to a sub-optimal outcome.

As regards Art 65 1. FESE would like to point out that use of the tape by market participants is key. An analysis should be conducted to ensure that market participants will purchase and use the tape.

FESE believes that the relevant technical standards (Regulation (EU) 2017/571) should apply with a few adjustments to the following articles:

- Art 14: Machine readability should not apply to “free of charge and publicly available”;
- Art 15: While a 6 months onboarding period for a new venue is prescribed in Art 15, no time limited for onboarding of new instruments from already contributing venues to the CT is set. FESE proposes to mandate the onboarding of new instruments from contributing venues to into a CT to take no longer than 30 days.

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1.2. Availability and price of market data

Q9: Do you agree with the above targeted amendments recommended by ESMA to address market data concerns? Please explain your answer

FESE agrees with the German Finance Ministry in their MiFID II/R position paper of August 2019, which underlines that it should be assessed whether competition authorities, rather than financial supervisory authorities, are better suited for ensuring that pricing policies are set up on a "reasonable commercial basis". Nevertheless, FESE appreciates ESMA's recommendation to pursue the transparency plus model with some clarifications and harmonisations.

Specifying the content, format and terminology of RCB information
FESE Members have taken note of the concerns expressed regarding pricing schedules and are supportive of an initiative aimed at improving them and making them more comparable for customers. FESE is currently conducting work (with the assistance of external legal counsel) to make MIFID RCB disclosures more comparable and reduce complexity for users. In parallel, a number of exchanges have proactively reached out to market participants to discuss main sources of complexity. FESE stands ready to contribute to ESMA's work in this area.

Deletion of articles allowing to charge for market data according to value
FESE does not support the suggestion to delete Art. 86(2) of CDR 2017/565 and Art. 8(2) of CDR 2017/567 allowing trading venues, APAs, CTPs and SIs to charge for market data based on the value for users. Art. 8(2) allows for differentials in prices based on different pre-defined categories (e.g. retail vs professional) of customers taking into account the value market data represents to those customers. Not allowing a differentiation between customer groups would be disproportionate and distort competition between venues/business entities.

There is concern about the impact such a measure would have on private investors, smaller market participants and (smaller) exchanges:

1) If private investors are required to pay the same fees as a Professional Investor, the price could be too high for private investors potentially undermining their activities.
2) If professional investors / legal entity - for NDIU - only pay the fee applicable to private investors, exchanges risk being severely undermined and unable to cover costs of producing and disseminating data.
3) Retail investors and smaller firms may indirectly end up financially supporting the market data needs of major international firms.

Competition law precedents recognise that product differentiation is reflective of competition on the market[1] and that even dominant undertakings (which exchanges are not)

[1] See Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31, 5.2.2004, para. 45. ("*It is also easier to coordinate on a price for a single, homogeneous product, than on hundreds of prices in a market with many differentiated products*"). See also Communication of the Commission - Guidance on the Commission's enforcement priorities in applying Art. 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, OJ C 45 of 24.2.2009, para.

can apply different commercial conditions to their customers (and are even required to do so if there are different objective circumstances)[2].

Communication of costs and margins to NCAs
Exchanges are willing to provide information on their cost bases or how prices were set to their regulators where this is warranted and appropriate, as long as information is not shared with the market at large. Level 2 measures specifying the frequency, content and format of information provided should respect the heterogeneity of exchange business models and take account of the diversity of commercial models. FESE regrets that while a majority of stakeholders agree price regulation is not the right way forward, some ESMA proposals come very close to regulating prices.

It is important that regulators and policymakers acknowledge the need to keep commercial incentives for market data to exists. A number of entities use data provided by exchanges to run commercially rewarding business models. Alternative trading venues benefit substantially from exchange data.

FESE generally considers that Capital Markets Regulation is not the right place to review the pricing of market data by Trading Venues as it would turn financial markets' supervisors into price regulators. FESE therefore agrees with the German Finance Ministry's proposal which underlines that it should be assessed whether competition authorities, rather than financial supervisory authorities, are better suited for ensuring that pricing policies are set up on a "reasonable commercial basis".

Nevertheless, FESE appreciates ESMA's recommendation to continue the transparency plus model with some clarifications and harmonisations.

ESMA mandate to specify the content, format and terminology of RCB information
FESE Members intend to optimize pricing schedules, reduce their complexity and make them more comparable for customers, where possible. In order to do so, FESE is currently conducting work to make MIFID RCB disclosures more comparable across exchanges. This work is conducted with external legal counsel. The initiative also covers terminology and categories used in market data agreements to examine whether further harmonisation could reduce complexity for users taking data from many trading venues. In parallel, a number of exchanges have also proactively reached out to market participants to discuss the main sources of complexity and where harmonisation is most needed. FESE stands ready to contribute to ESMA's work in this area. We would also stress the need to exclude price regulation, as well as measures having equivalent effect, from the scope of any mandate given to ESMA to specify the content, format and terminology of RCB information.

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13 ("*the Commission will interpret market shares in the light of the relevant market conditions, and in particular of the dynamics of the market and of the extent to which products are differentiated.*")

[2] See for example Judgment in *AKZO Chemie v Commission*, Case C-62/86, ECLI:EU:C:1991:286, paras. 119-120 ("*It should next be pointed out that there was no abusive policy of discrimination between the individual mills in the Allied group and the 'large independents', as these two categories of customers are not comparable*"). See also Judgment in *United Brands v Commission*, Case C-27/76, ECLI:EU:C:1978:22, para. 228 ("*differences in transport costs, taxation, customs duties, the wages of the labour force, the conditions of marketing, the differences in the parity of currencies, the density of competition may eventually culminate in different retail selling price levels according to the Member States*") and Judgment in *Clearstream v Commission,* Case T-301/04, ECLI:EU:T:2009:317, paras. 172 and 179.

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Deletion of articles allowing to charge for market data according to value
FESE cannot support ESMA's suggestion to delete Article 86(2) of CDR 2017/565 and Article 8(2) of CDR 2017/567 allowing trading venues, APAs, CTPs and SIs to charge for market data proportionate to the value the data represents to users.

Article 8(2) of CDR 2017/567 currently allows for differentials in prices charged to different pre-defined categories (e.g. retail vs professional) of customers taking into account the value which the market data represents to those customers. Not allowing a differentiation between customer groups would make the suggested regulatory intervention disproportionate, discriminatory and would in fact distort competition between venues / business entities.

We are concerned as well about the impact such a measure would have on private investors and smaller market participants, as well as (smaller) exchanges:

1) If private investors are required to pay the same fees as a Legal Entity / Professional Investor, the price could be too high for private investors potentially undermining their activities.
2) If professional investors / legal entity - for NDIU - only pay the fee applicable to private investors, exchanges risk being severely undermined and would not be able to cover the costs of producing and disseminating market data.
3) There is also concern that retail investors and smaller firms may, ultimately, indirectly end up financially supporting the market data needs of major international firms in such a scenario.

Furthermore, competition law precedents recognise that product differentiation is reflective of competition on the market and that even dominant undertakings (which exchanges are not) can apply different commercial conditions to their customers (and are even required to do so if there are different objective circumstances) .

Market data pricing cannot be considered or analysed in a vacuum. The production and dissemination of market data is an intrinsic part of the operation of fair and orderly markets. Given the structure of order books and order matching systems, it is not possible to provide execution services without generating market data, and it is not possible to generate pre and post trade data without also supplying a trade execution service. Market data is the outcome of a dynamic price formation process, and is a joint product with trade execution. Most activities undertaken by an Exchange deliver both trading and price formation. The economics literature confirms that, in such cases, it is efficient to generate revenues through fees from both products and find the right equilibrium based on value. Indeed, this is what exchanges do in practice.

The joint product nature of trade execution and market data services has important economic implications. With joint products, the production costs of the outputs (market data and trading) cannot be fully separated – i.e. some, if not all, costs are joint costs. Indeed, joint costs are incurred when production facilities simultaneously produce two or more products, this is clearly the case of trade execution and market data services where there are fixed costs that have to be incurred to produce either product. Secondly, this means that whether the recovery of costs by a trading venue is appropriate or not cannot be assessed effectively by the independent analysis of either trade execution services or market data services. Overall, an exchange's business is supported by a largely unified cost base underpinned by activities and technology that contribute to ensuring the operation of fair and orderly markets, including the provision of market data. Consequently, a holistic assessment of an exchange's costs is necessary in this context.

Communication of costs and margins to NCAs
Exchanges are willing to provide some information on their cost bases or how prices were set to their regulators where this is warranted and appropriate, as long as information is not shared with the market at large. Any Level 2 measures specifying the frequency, content and format of information provided should respect the heterogeneity of exchange business models and take account of the diversity of commercial models. However, FESE regrets that while a majority of stakeholders agree price regulation is not the right way forward, some of the proposals put forward by ESMA (e.g. defining a typology of eligible costs when setting market data fees) come very close to regulating prices.

When considering ESMA's recommendations, it is important that regulators and policymakers acknowledge the need to keep commercial incentives for market data to exists. Indeed, a number of entities use data provided by exchanges on a non-discriminatory basis to run commercially rewarding business models. Alternative trading venues benefit substantially from exchange data. Instead of investing in their own price formation, they use exchange data to execute order flow on basis of exchange prices (pegging) while competing with the original data source for the same order flow at much lower cost, due to the fact that they are using exchange data. In this context, regulators and policy makers should be wary of enabling free-riding which, if left unchecked, could ultimately threaten the quality of the price formation process and undermine the objective of the Capital Markets Union (CMU) to strengthen public capital markets. In FESE's view, any changes to the current pricing would also need to be in line with Competition Law.

Inaccuracies in figures provided by market participants to characterise evolutions in market data prices
Lastly, FESE would like to provide a number of observations in relation to inaccuracies in the figures provided by market participants to characterise evolutions in market data prices. Before acting on the recommendations contained in the ESMA report, FESE believes that it is important for policy makers to take a step back and assess whether figures provided by market participants are a fair and accurate representation of the situation.

Exchanges take issue with the way some variations of prices have been presented by certain stakeholders. It is not rare for a single fee type or a single trading venue to be presented as being representative of the entire industry, this is cause for concern. Furthermore, in some cases, fluctuations presented do not exclusively reflect changes in data pricing but significant changes in data usage and consumption by the stakeholder and therefore should not be taken out of context. In practice there is ample evidence that user firms are changing their data consumption driven by structural changes. We feel this has not been sufficiently acknowledged so far but consider it to be a must.

In this context, there is a need for more transparency in the methodologies used to calculate and inform regulators about evolutions in market data costs of single data users/hypothetical data users so that these accusations can be thoroughly checked, confirmed, or challenged where appropriate. FESE believes that increased transparency on methodologies would contribute to bridging the gap between user perceptions and the exchange viewpoint. In addition, more transparency on the total market data bill borne by end users – including the share of providers other than exchanges or technology fees, and the extent to which data usage has changes over the years - is sorely needed and key to making progress in this important and challenging debate.

More generally, FESE would like to take this opportunity to reiterate that in assessing the costs of market data, it is critical that the overall market data value chain is taken into account. Exchanges are frequently not "the last mile" of data distribution since most users obtain data through data redistributors and other intermediaries. Furthermore, the cost to

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end-investors are small with aggregate market data revenues representing only 0.003% of total assets under management (Source: Oxera. (2019). The Design of equity Trading Markets in Europe).

The market data offered by stock exchanges is a small element in a much longer value chain, in a broader market data industry that is large and growing. Stock exchange market data is distributed directly or indirectly via data vendors, to brokers, asset managers, and other market participants. In taking forward the current assessment of market data costs, it is crucial to consider the complete value chain as outlined above and overall evolutions in capital markets, notably the ongoing issues with market structure arising from the MiFID II framework. Not doing so would pose a real threat to the price formation function of exchanges as well as their ability to innovate and service investors. Exchange market data cannot be looked at in isolation since exchanges are part of a longer value chain and as such do not operate in isolation.

1.3. Use cases for a consolidated tape

Q10: What do you consider to be the use cases for an EU consolidated tape

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
Transaction cost analysis (TCA)	x					
Ensuring best execution	x					
Documenting best execution				x		
Better control of order & execution management	x					
Regulatory reporting requirements	x					
Market surveillance	x					
Liquidity risk management		x				
Making market data accessible at a reasonable cost						x
Identify available liquidity		x				
Portfolio valuation			x			
Other						x

Please specify what are the other use cases for an EU consolidated tape that you identified

The main use case that we see is to control execution quality obtained by investors on their orders. This is done based on transactions (post-trade data). We note as indicated above that the cost to the industry of a pre-trade tape would outweigh any advantages, due to latency it will not be possible to fairly trade on such a tape i.e. it will not be possible to route orders to a best price because due to latency the "best price" while visible on the CT will in the vast majority of cases either not be accessible (no connection to 170+ venues) or not be available anymore, as firms directly connected to venues will trade on that price before it is reflected on the tape.

Q10.1: Please explain your answers to question 10 and also indicate to what extent the use cases would benefit from a CT:

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For a fully comprehensive aggregation of data by market data vendors the quality of off-venue data needs to be improved to allow for a full and reliable consolidation of data.

FESE is sceptical regarding some of the purported use cases listed under Q10. Market participants have clearly indicated that they will continue to rely on services provided by data vendors even after the emergence of an EU CTP since an EU CTP will not be in a position to deliver on all of the CT's purported use cases. In this context, FESE's proposal of TOR would deliver clear value to the market and investors: notably, a means for them to analyse execution quality ex post or to value positions. It is important to underline that whilst a tape can help to analyse execution quality, it is misguided to believe that a real-time tape could be used as a reference for best execution given that a CT will not be in a position to provide a full representation of available liquidity in the market either. Making the CT the best execution benchmark would not work from a broker perspective and would not offer an adequate representation of liquidity available to each broker (as they will not necessarily have the connections to trade where liquidity can be). Ultimately, the view provided by the tape would be one of ghost liquidity, illusory liquidity. This has the potential to harm the market by creating a two-tier market structure between retail and professional users, potentially generating arbitrage opportunities and front running. In such a scenario, retail investors would systematically not get the best price since the best price would automatically be taken by those having latency solutions that surpass what is provided by the tape. With this in mind, it makes sense to question whether a real-time CT for best execution purposes would solve or create issues, e.g. making it more difficult for certain firms to stay active in the market to the detriment of EU investors and companies.

FESE is doubtful as to whether a real-time tape will be used to ensure and document best execution under MiFID II/MiFIR, as no need exists to verify best execution against all venues within the EU. Only those venues to which the execution broker has established trading ties form part of the best execution requirements/policy. If the CT only exists for SIs and OTC to execute within the spread of transparent trading venues in an even more systematic way, this creates market structure issues including the question of fair or unfair competition in the EU between trading venues and alternative trading mechanisms to the detriment of transparent markets.

Moreover, it is misguided to imagine that a tape could be of use to regulators for the purposes of monitoring cross-market activity. By nature, the consolidated tape will solely disseminate anonymous public data and is consequently not suitable for market surveillance or regulatory audit trail purposes. The data needed for this type of activity is much more granular in nature and must be based on transaction reporting and order record keeping data.

MiFID II/R requirements have increased operating costs for exchanges and market participants alike, including costs relating to producing and administering market data. Therefore, it remains unclear to FESE how a consolidated tape would actually be able to lower the price for market data.

- For instance, changes brought in by MiFID II/R such as the separation of pre and post trade data and the creation of a multitude of different data packages leads to increased administrative costs for the industry, including exchanges.
- Additionally, in line with RTS 14 exchanges have enhanced their market data environments in order to be able to respond to any disaggregated data request. The actual demand for disaggregated data by market participants has been very limited however.
- Exchanges also have to create public pre and post data machine-readable files. The creation and continued maintenance of these mandated offerings create additional

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costs for the exchanges. However, the demand for public pre and post data machine-readable files is almost non-existent.

CTP – Part 2 (General features of a CTP)

Q11: Which of the following features, as described above, do you consider important for the creation of an EU consolidated tape?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N. A.
High level of data quality					x	
Mandatory contributions			x			
Mandatory consumption				x		
Full coverage					x	
Very high coverage (not lower than 90% of the market)	x					
Real-time (minimum standards on latency)	x					
The existence of an order protection rule						x
Single provider per asset class					x	
Strong governance framework					x	
Other					x	

Please specify what other feature(s) you consider important for the creation of an EU consolidated tape?

The identification of an appropriate and feasible regulatory use case (and a clear definition of this in the regulation) is particularly important to ensure that the tape does not add cost (i.e. infrastructure and maintenance costs) to the industry without any clear benefits, which would make it a disproportionate and discriminatory intervention by regulators. As outlined in our response to question 10, FESE is concerned that most of the tape use cases currently envisaged have not been thoroughly checked and thought through. A consolidated tape is not a silver bullet and will not, by itself, remedy current shortcomings in the EU market

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structure which are detrimental to investors and capital raising by companies. FESE does not consider it appropriate that a CTP should be funded with taxpayer's money, as currently proposed by some stakeholders. In the same context, a CTP cannot and should not be considered a public good.

The importance of protecting the quality of the price formation process and the role that lit markets play in delivering the CMU should be at the forefront of the CTP debate. There is a risk that the creation of a CTP will have negative consequences (e.g. high cost for the industry without any clear additional benefit and affect Exchanges' ability to continue to deliver high quality price formation for all EU market participants) to the detriment of investors and robust capital markets as well as the objective of the CMU. The price formation process carried out by Exchanges is highly beneficial to the well-functioning of transparent EU capital markets. This crucial price formation process should be fully acknowledged, preserved and fostered. In short, market data and market structure questions should be looked at together. If the CTP does not take into account the investments made by exchanges in the production of high quality price data, MTFs or SI's will be able to use the data to run their own, lucrative, business models without having to make any of the investments in price formation/technology/surveillance/compliance. This goes against the overall objective of MiFID II/MiFIR to create a level playing field and could seriously harm the rationale of exchanges' business models.

The specificities and uniqueness of the EU financial markets landscape should also be a primary consideration for the creation of a consolidated tape. It is important to note that the fact that there is a consolidated tape for shares in the US that consolidates both pre- and post-trade data does not in itself validate or justify taking the same approach in Europe. Whilst existing tapes could, where warranted, offer some inspiration to policymakers, it is nonetheless important to recognise that EU markets are very different to US markets, more fragmented, and it is therefore not possible to assume that the practical experience of the tape in the US presupposes the success of a tape in the EU. Third country CT models should not simply be replicated as their specificities do not apply to European financial markets. In the US, there are less contributors of data and more consumers thus allowing for economies of scale. In Europe however, there are ten times more potential contributors to a tape as well as important geographic constraints which separate market actors and infrastructures by thousands of kilometres, adding to the latency issues of any CT. It is also worth noting that there is not a single tape in the US, that the CT situation in the US has given rise to front-running, has not reduced the overall market data bill for end users, and is currently under review.

Finally, FESE considers that acting under clear and fair contractual relations with a CTP provider is a necessary prerequisite.

Q11.1. Please explain your answers to question 11 and provide if possible detailed suggestions on how the above success factors should be implemented (e.g. how data quality should be improved; what should be the optimal latency and coverage; what should the governance framework include; the optimal number of providers.

FESE would suggest that the Commission review the large number of consolidated offerings through third party vendors, in order to identify what data is currently not available through such offerings. The creation of a CT should be guided by the level of transparency/the lack thereof in the relevant asset classes.

Given the high level of transparency in the equity market, the actual use case for an equity CT is limited. However, with the high level of fragmentation and lower transparency in the fixed income and ETFs markets, we recommend that fixed income and ETFs consolidated

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tapes be considered ahead of an equity consolidated tape with the caveat of improved data quality at the source first.

While MiFID II/R pushes for data disaggregation, it also requires consolidated data. These seem to be opposing policy objectives. FESE remains sceptical about the demand and use case for fully disaggregated data offerings.

High level of data quality is a necessary pre-requisite to the creation of a CT
First and foremost, the inconsistent trade reporting behaviour of SIs and OTC execution venues must be addressed. Guaranteeing high quality, reliable and consistent off-venue data including flagging of SI and OTC trades is key to delivering a CT that can be considered meaningful. Without firstly improving off-venue data quality and consistency at the source (i.e. investment firms), an EU CT will never be in a position to deliver data consistency and quality: the quality of output data generated by a CT can only be as good as the quality of its input data.

While market data from exchanges is usually 100% reliable, market data originating from SI and OTC trade reporting still lacks quality and consistency. This issue seems to be especially driven by inconsistent SI and OTC reporting at the source. Such shortcomings be addressed as a matter of priority. It is important to note that although APAs and ARMs contribute to efficiency (data quality checks/first point of contact for regulators and customers alike), there is still uncertainty across investment firms in the EU on how to adequately flag executed transactions before submitting them to APAs.

Trading venues produce good data, due to the fact that they have full insight over the order-transaction lifecycle. Exchanges have a well-informed view on how to deliver a meaningful and fully compliant market data output that serves transparency and investor protection purposes. Vendors, APAs and a CT operator do not have comparable insight over the order-transaction lifecycle limiting their ability to assess data quality.

Full coverage is essential
Coverage of all execution venues is paramount. Having a 100% view of the market – including SIs and OTC – is critical to ensuring that investors can assess execution quality in a comprehensive manner. It would be nonsensical to establish a CT with limited coverage where SIs and OTCs are dispensed from contributing. Such a CT would be deprived of practical significance.

It is necessary to seriously consider how a CT could go about solving data quality issues that originate from inconsistent trade reporting behaviours at the source and which APAs have been powerless to address. The extension of the MMT to all market participants can contribute to addressing these issues. An enforceable user guide on how to use these MMT tools could also be necessary.

Real-time should not be the focus
FESE would advise against the creation of a real-time tape. Real-time should not be the focus, a tape of record (TOR) would be a significantly less complex and costly technical set-up, providing a comprehensive overview of overall liquidity within the EU on an instrument level to verify execution quality.

A strong governance framework is necessary
The governance framework should ensure the neutrality of the CT and high-level data quality and transparency.

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In particular, Exchanges consider that the current DRSP regime and the minimum set of regulatory requirements should be applied, with strong focus on the avoidance of conflicts of interest, corporate transparency, and strict business continuity management requirements. A strong governance framework must ensure fair and ethical behaviour, as well as a full representation and voting power of data sources within the CTP Board. The board should include neutral representatives (e.g. ESMA) and the Board should be responsible for monitoring the impact of the CT on capital markets and report on risks and/or benefits to regulators using fact-based evidence.

FESE does not consider it appropriate to use taxpayer money to fund the CT for the benefit of large capital markets firms.

Revenue sharing model for the CT

FESE is aware that the approach that the Commission is taking may include a suggestion to define a revenue sharing model for the reporting entities based on their contribution to the price formation process. We remain sceptical regarding the CT's ability to play a role in incentivising lit trading.

Q12: If you support mandatory consumption of the tape, how would you recommend to structure such mandatory consumption? Please explain your answer and provide if possible detailed suggestions on which users should be mandated to consume the tape and how this should be organised:

The issue of mandatory consumption very much depends on the type of tape that would ultimately emerge. In any case, contributors must be sufficiently compensated for their data and users should contribute to the funding of the CT.

That being said, FESE would note that there has been some significant pushback amongst data users on the issue of mandatory consumption. This reticence seems to highlight that market participants are not convinced of the added value of a tape and that its purported use cases are not entirely compelling.

Q13: In your view, what link should there be between the CT and best execution obligations? Please explain your answer and provide if possible detailed suggestions (e.g. simplifying the best execution reporting through the use of an EBBO reference price benchmark):

Whilst a tape can help to analyse execution quality, it is misguided to affirm that a tape can be used to verify and ensure best execution since under the MiFID II best execution obligations, investment firms have to take into account a range of criteria in addition to price (e.g. costs, speed, likelihood of execution, and always external transaction cost). Furthermore, making the CT the best execution benchmark would not work from a broker perspective and would not offer an adequate representation of liquidity available to each broker, simply because each firm has access to a different set of trading venues and SIs, the latter having the capability under MiFID to interact only with certain counterparties and not others.

Furthermore, significant technological hurdles increasing with number of venues to be consolidated mean that the tape would most likely distort the reality meaning that users would not be able to determine in real-time which order transactions truly occur. The speed of light provides an upper limit on the speed with which information can flow. This has large implications for any rules that are based on prices at a given time and means that two observers in two different locations can simultaneously observe two different “best” prices.

The argument that best execution will be a benefit of a real-time pre-trade consolidated tape does not take into account the fragmented nature of the European market structure and its wide geographical footprint, as opposed to the US.

Enforcing best execution on the basis of a European Best Bid and Offer (EBBO) carried by a real-time pre-trade tape would be **an oversimplification of the market and create a flawed, easily gameable benchmark that would ultimately be harmful to investors**. When a tape is used as the reference price for best execution, it creates an environment ripe for gaming at the expense of investors.

This is because best execution is only a local reality, true at one moment, for one specific location where the Smart Order Router (SOR) of the broker is located. Geographical spread and consequently latency considerations will mean that two observers in two different locations can **simultaneously observe two different “best” prices**. This renders the use of a unique EBBO as an ex ante or ex-post benchmark to ensure best execution misleading at best.

In addition, research demonstrates that liquidity displayed by trading venues in the order book is not always accessible because of **“ghost” liquidity** provided by certain types of market participants[3]. The emergence of a real-time pre-trade tape promoting a “visible” EBBO would give market participants the **illusion of achieving best execution**, while in fact creating an environment where ghost liquidity and latency arbitrage could easily be exploited by the most technology-savvy market participants.

As previously stated, each Smart Order Router has its own EBBO subject to its geographical location. The concept of a pan-European EBBO, carried by the tape and presented as “true” for every market participant, could in that case be used as a misleading execution benchmark at the expense of less sophisticated investors. **The tape would create a false sense of comfort amongst investors that best execution was achieved, reducing vigilance on execution quality, while in fact their orders would have been arbitraged.** This would be rendered even worse were the tape’s EBBO be used as a reference price for SIs and dark pools as it would weaken the price formation process on lit markets while creating significant arbitrage opportunities.

Q14: Do you agree with the following features in relation to the provision, governance and funding of the CTP?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
The CT should be funded on the basis of user fees					x	
Fees should be differentiated according to type of use					x	
Revenue should be redistributed among contributing venues					x	
In redistributing revenue, price- forming trades should be compensated at a higher rate than other trades					x	
The position of CTP should be put up for tender every 5-7 years			x			

[3] DEGRYSE, Hans, DE WINNE, Rudy, GRESSE, Carole, *et al. High frequency trading and ghost liquidity*, 2018

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Other					x	-

Please specify what other important feature(s) for the funding and governance of the CT you did identify?

A valid commercial use case is a pre-requisite for the funding of the CT. FESE would caution against pursuing the CT project in the absence of a clear business case.

Q14.1: Please explain your answers to question 14 and provide if possible detailed suggestions on how the above features should be implemented (e.g. according to which methodology the CT revenues should be redistributed; how price forming trades should be rewarded, alternative funding models):

Exchanges believe that mandatory consumption together with mandatory payment by each market participant would be necessary for the establishment and operations of a CT so to ensure funding and revenues to the CT. While the details of mandatory consumption very much depend on the type of tape that would ultimately emerge (e.g. a tape of record would have lower cost compared to other types of latency), it is critical that mandatory consumption is enforced, regardless of doubts expressed by some market participants which question the overall use case for a CT. To ensure that the CT does not only add costs to the industry overall, the CT must deliver on a regulatory use case as well. When reflecting upon the overall funding structure, mandatory tape fees should reflect the number of data sources and the data fees of the respective data sources plus operational charges for the tape provider. It is important to underline that in the event of an EU CT, the number of data sources would be significantly higher than the number of contributors to the tapes in comparison to the US. For this reason, the tape fees that exist in the US can neither be compared nor be used as a benchmark for tape fees in the EU, since they would not reflect the make-up of capital markets in Europe and would misrepresent the number of data sources, as well as the number of data users, in the EU. Exchanges also wish to underline that the sum of the fees of an EU tape should also not be compared to the US market since markets in the EU are more fragmented than the US market, which means that the costs of producing and disseminating market data are higher as there are less economies of scale.

The Tape of Record – as a viable alternative in the current regulatory setting, provided that it offers 100% coverage of all execution venues (including SIs and OTC), would provide substantial additional transparency at EU level, at comparably low cost.

A feasible and workable CT model would have to charge for the provision of consolidated data and redistribute a meaningful part of the revenues to the contributing entities, reference price forming venues especially. Contributors cannot be asked to contribute data for no or very limited fees, as this would be a disincentive to investing and operating transparent markets.

The funding model should be aligned with the overall objective of MiFID II providing incentives to trade lit as opposed to dark and therefore reward price forming venues.

CTP – Part 3 (Scope of the consolidated tape)

3.1. <u>Pre- and post-transparency and asset class coverage</u>

Q15: For which asset classes do you consider than an EU consolidated tape should be created?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
Shares pre-trade	x					
Shares post-trade				x		
ETFs pre-trade	x					
ETFs post-trade				x		
Corporate bonds pre- trade	x					
Corporate bonds post- trade				x		
Government bonds pre- trade	x					
Government bonds post- trade				x		
Interest rate swaps pre- trade	x					
Interest rate swaps post- trade				x		
Credit default swaps pre- trade	x					
Credit default swaps post- trade				x		
Other						

Please specify for which other asset classes you consider that an EU consolidated tape should be created?

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FESE would suggest that the European Commission review the large number of consolidated offerings through third party vendors for exchange data, in order to identify what data is not available through such offerings. FESE believes that the creation of a CT should be guided by the level of transparency/the lack thereof in the relevant asset classes. Given the high level of transparency in the equity market, the actual use case for an equity consolidated tape remains unclear to FESE. However, with the high level of fragmentation and lower transparency in the fixed income and ETF markets, we recommend that fixed income and ETF consolidated tapes be considered ahead of an equity consolidated tape. This should also include work on a more meaningful level of transparency compared to the current regulatory requirements, which provide rather unusable low-quality data. We would expect the same level of transparency provided on an equity CT as on a bond or ETF CT. This also includes timing and the comprehensiveness of data being consolidated for the public.

Q15.1: Please explain your answers to question 15:

Misguidedly attempting to develop a tape for pre-trade data in Europe would raise a number of issues and is therefore not advisable nor reasonable.

Some argue that pre-trade tape would give a better view of liquidity available on trading venues and help retail brokers access an increased range of execution options, however expectations on the impact of a pre-trade tape in terms of liquidity are unrealistic.

Firstly, pre-trade transparency is only available for lit market and a very limited portion of SIs' business and will therefore not offer a complete view of liquidity in the market. The majority of SI trading will most likely not appear in a pre-trade tape, unless regulation would be changed. Secondly, the liquidity displayed on a pre-tape would not be accessible to all market participants in the same way since a broker will only be able to access liquidity on the venues or SIs to which he is technically and commercially connected for execution. The tape would therefore create a false sense of liquidity and options. Executions that smaller brokers will be able to provide will not be in line with the tape. Ultimately, the view provided by the tape would be one of ghost liquidity, or illusory liquidity. This has the potential to harm the market by creating a two-tier market structure between retail and professional users, potentially generating arbitrage opportunities and front running. Thirdly, due to latency issues, an order or quote shown on the tape will likely have disappeared or changed by the time it is displayed on the tape. This would, in many ways, be similar to situations where airline price comparison websites systematically advertise promotions or low fares, which prove to be "not available or sold out" each time a client tries to book the fare on the airline website.

While conceptually appealing, the concept of a universal truth of visible liquidity **does not take into account the geographical and technical realities of European markets**. Each trader has a specific view of the visible liquidity depending on its physical location. The liquidity displayed by a real-time pre-trade tape would only be true for a specific set of traders close to the CT provider and leveraging the same technologies.

A real-time pre-trade tape would - far from providing a consolidated view of European liquidity - **only advertise a misleading and illusory sense of liquidity**.

In addition, as mentioned under Q13, enforcing best execution on the basis of a European Best Bid and Offer (EBBO) carried by a real-time pre-trade tape would be **an oversimplification of the market and create a flawed, easily gameable benchmark that would ultimately be harmful to investors**.

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A pre-trade tape would not be useful to for the purposes of monitoring cross-market activity. By nature, the consolidated tape will only publish anonymous data (apart from MIC code for the venue which provides the data) targeted at the public and is consequently not suitable for regulatory audit trail purposes.

Significant technological hurdles mean that the tape would not be useful for trading and/or for best execution since the tape would most likely distort the reality meaning that users may not be able to determine in which order transactions truly occur. The speed of light provides an upper limit on the speed with which information can flow. This has large implications for any rules that are based on prices at a given time and means that two observers in two different locations can simultaneously observe two different “best” prices. Similarly, the inherent limits to the precision of time measurement mean that there will be an irreducible uncertainty as to when particular events occurred.[4]

The fact that there is a consolidated tape for shares in the US that consolidates both pre- and post-trade data does not in itself validate or justify taking the same approach in Europe. EU markets are very different to US markets and more fragmented. Third country CT models should not simply be replicated as their specificities do not apply to European financial markets. In the US, there are less contributors of data and more consumers thus allowing for economies of scale. In Europe however, there are more contributors to a tape (170+ in EU compared to 17 in the US) as well as important geographic constraints which separate market actors and infrastructures by thousands of kilometres.

Overall, FESE would advise against the creation of a pre-trade tape and reiterate that a “Tape of Record” would be a significantly less complex and costly technical set-up, providing a comprehensive overview of overall liquidity within the EU on an instrument level to verify execution quality. A pre-condition for a reliable CT is an improvement of off-venue data quality, covering all execution venues.

Q16: In your view, what information published under the MiFID II /MiFIR pre- and post-trade transparency should be consolidated in the tape (all information or a subset, any additional information)? Please explain your answer, distinguishing if necessary by asset class and pre- and post-trade. Please also explain, if relevant, how you would identify the relevant types of transactions or trading interests to be consolidated by a CT:

FESE considers a CTP with full coverage (100% of the market) to be the only option when providing transparency via a CTP. This refers to all data sources, be it RMs, MTFs, APAs or SIs. As regards data fields, FESE Members refer to the information as outlined under Art. 65 MiFID II. The information consolidated by the tape should be identical to the post-trade transparency publication requirements of trading venues and APAs. We do not recommend adding any additional requirements beyond what is already required by the regulation.

Non-addressable liquidity as defined under MiFIR/MiFIR II should also be displayed but should be flagged accordingly. MMT should be used by any data source to ensure harmonised flagging.

3.2. The official list of financial instruments in scope of the CT

[4] Angel, J.J, 2014. When Finance Meets Physics: The Impact of the Speed of Light on Financial Markets and their Regulation, *The Financial Review, May 2014, Volume 49, No. 2,* 1.202.687.3765

Shares

Q17: What shares should in your view be included in the Official List of shares defining the scope of the EU consolidated tape?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
Shares admitted to trading on a RM				x		
Shares admitted to trading on an MTF with a prospectus approved in an EU Member State				x		
Other				x		

Please specify what other shares should in your view be included in the Official List of shares defining the scope of the EU consolidated tape?

FESE would underline that the use case of the CT should ultimately determine what shares are within scope. Given that the focus of a CT appears to be trading data, any proposed CT should therefore include all shares admitted to trading on EU venues. This includes shares with and without a prospectus.

In terms of terminology used, FESE would caution against using the term "Official List" for the CT as this could be confused with the Official Lists of exchanges under the Listing Directive and may not cover the same securities.

Q17.1. Please explain your answers to question 17:

FESE generally stands for and promotes transparent markets. While FESE does not support a real-time CT, as outlined earlier, we would promote a Tape of Record. FESE realises that the lack of certain reference data (ISIN) for shares admitted to trading, which are not listed in the EU are difficult to obtain. Not all EU instruments, however, are listed/traded on an EU exchange, but where demand for transparency in off-venue data is high: ETFs and fixed-income. Those instruments should form part of any CT or Tape of Record.

Q18: In your view, should the Official List take into account any additional criteria (e.g. liquidity filter to capture only sufficiently liquid shares) to capture the relevant subset of shares traded in the EU for inclusion in the consolidated tape? Please explain your answer:

In FESE's view, the scope of the list should not take into account any additional criteria (e.g. liquidity filter to capture only sufficiently liquid shares) to capture the relevant subset of

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shares traded in the EU. FESE considers it important that any official CTP provides a comprehensive picture of the market, this includes liquid and illiquid instruments.

Q19. What flexibility should be provided to permit the inclusion in the EU consolidated tape of shares not (or not only) admitted to an EU regulated market of EU MTF? Please explain your answer:

FESE would agree with allowing for flexible voluntary contribution of third country shares (not admitted to trading in the EU) to the consolidated tape by EU and/or third country trading venues, as long as the data provided is fully compliant with the requirements set out at EU level.

In other words, any inclusion in the EU consolidated tape of shares not admitted to an EU trading venue (so called third country shares) should be possible on a voluntary basis but not compulsory.

Seemingly, FESE believes there should be no flexibility when it comes to EU shares (solely admitted, in the sense of listing, in the EU).

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ETFs, Bonds, Derivatives and other financial instruments

Q20: What do you consider to be the most appropriate way of determining the Official List of ETFs, bonds and derivatives defining the scope of the EU consolidated tape? Please explain your answer and provide details by asset class:

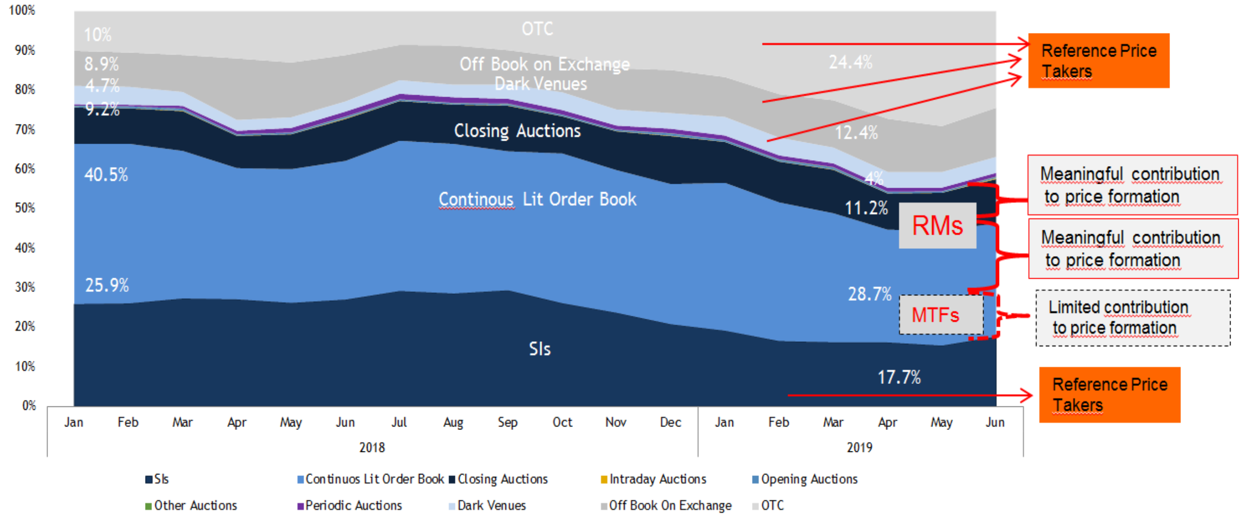
FESE would like to point out that it would not be sensible to have an aggregated tape across all asset classes. We would recommend having separate tapes, for equity and equity-like instruments, including ETFs, and separate tapes for bonds, and derivatives, where the latter would most likely be differentiated further.

CTP – Part 4 (Other MiFID II/MiFIR provisions with a link to the consolidated tape)

4.1. Equity trading and price formation

Q21: What is your appraisal of the impact of the share trading obligation on the transparency of share trading and the competitiveness of EU exchanges and market participants? Please explain your answer:

While the objective of MiFID II/MiFIR was to bring broker crossing networks (BCNs) to lit multilateral trading venues (i.e. RM and MTFs) to increase transparency and improve price formation and investor protection, the current situation is at odds with the spirit of MiFID II/MiFIR. The market share of continuous lit order books is decreasing while the combined share of OTC and SI trading keeps growing. It can be observed that the aggregated levels of OTC and SI trading in terms of turnover represent 22% and 18% respectively for 2019 based on data from Big xyt.



Source: data and from big-xyt, calculations and comments on price formation contribution from FESE

This has led to increased complexity of equity markets and further fragmentation of liquidity – in contrast with the spirit of the legislation. In this sense, the STO has not delivered on increasing transparency on European markets.

However, FESE believes that the STO can have a significant positive impact on transparency of share trading and the competitiveness of EU trading venues and market participants. The STO should be retained provided that some modifications are considered. Consistent with a definition of EU shares and a clear delimitation of the universe of shares the STO applies to (see our response to Q23.1), the notion of equivalent third country venues becomes obsolete and could be removed. Exemptions from the STO should be removed where trades are "non-systematic, ad-hoc, irregular and infrequent"; instead, exemptions should only apply for those trades that do not contribute to price formation based on a clear and consistent list of qualifying transactions not contributing to price discovery. Furthermore, the scope of the STO is currently too narrow since it only applies to shares. The STO should be extended to other asset classes, in particular to ETFs to encourage lit trading and promote investor protection in this growing asset class. FESE believes that an extension of the trading obligation to other asset classes would reinforce investors' ability to take informed investment decisions and would prevent negative effects deriving from market fragmentation. This would result in strengthened investor protection and increased efficiency.

Q22: Do you believe there is sufficient clarity on the scope of the trades included or exempted from the STO, in particular having regards to shares not (or not only) admitted to an EU regulated market or EU MTF?

☐ 1 - Not at all
☒ 2 – Not really
☐ 3 - Neutral
☐ 4 - Partially
☐ 5 - Totally
☐ Don't know / no opinion / not relevant

Q22.1: Please explain your answer to question 22

The share trading obligation (STO) remains necessary and is an important cornerstone of the overall aim of MiFID II/MiFIR to enhance the efficiency, resilience and integrity of financial markets in the EU. For the STO to be fully functional, further work on clearly determining which shares should be considered EU shares is necessary. The approach should avoid undue complexity and be based on predictable and meaningful criteria.

FESE supports limiting the trading obligation to EU shares. The current approach does not provide certainty to the industry as the regulation's requirement exempting 'non-systematic, ad hoc, irregular and infrequent' trading has not been clarified in a conclusive way.

Furthermore, according to the current STO definition, EU investment firms can only undertake trades in shares admitted to trading in the EU on EU trading venues or equivalent third country trading venues and Sis.

To date, only a handful of equivalence decisions have been adopted, while the Commission and ESMA have de facto limited application of the STO by interpreting the scope in a narrow way. Both the Commission and ESMA have indicated that equivalence decisions will only be adopted for countries where the EU trading in the shares is of a certain magnitude and that the absence of an equivalence decision therefore does not prevent EU investment firms from trading shares admitted to trading in the EU on non-EU venues.

In addition, as highlighted by ESMA, there is a further challenge with respect to securities that are dual listed on an EU and non-EU trading venue as EU brokers may need to access both pools of liquidity. The STO should not restrict such access to this liquidity as this would harm EU investors and could disincentivise dual-listed issuers to retain their listing in the EU in order to extricate themselves from the STO if their primary liquidity is outside the EU.

Determination of EU shares

Given the various challenges highlighted above in relation to the STO, a careful approach is essential. Therefore, to determine which shares should be considered as EU shares, FESE suggests the following approach:

- the STO should apply to those shares with an ISIN starting with a country code corresponding to an EU27 Member State plus those starting with a non-EU country code but where the issuer has its primary listing within the EU27
- the STO should not apply to those shares with an ISIN starting with a country code corresponding to an EU27 Member State where the issuer has its exclusive listing in a third country
- in cases where the security is dual-listed on both an EU trading venue and a non-EU trading venue at the specific request of the issuer, we propose that the STO should also still apply but that there is an exception in the provision (as suggested by ESMA in its consultation ESMA 70-156-2188 – para 278), to allow trading to take place on the non-EU trading venue where the issuer has listed the security, in addition to the EU venues.
- "Listing" in this sense is always made upon request of the issuer and involves various obligations for initial listing and for maintaining a listing.

This approach will ensure that the key objective of the STO can still be achieved i.e. more transparency with OTC trading moving to lit trading, it will also ensure in the case of dual-listed securities, that EU brokers and their investors can still access the main pools of liquidity where the issuer itself has requested its security to be traded and does not in any way disincentivise issuers from listing on EU trading venues.

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Furthermore, we would also highlight the following points relevant to the STO:

- For dual-listed securities (where the issuer has chosen to have one of the two listings in the EU), investment firms should have the possibility to trade on either listing venue. To address the consequences of this exemption, reporting arrangements for such dual listed shares ought to be devised to achieve the transparency of these shares in the EU.
- Exemptions should be removed where trades are “non-systematic, ad-hoc, irregular and infrequent”, instead exemptions should only apply for those trades that do not contribute to price formation based on a clear and consistent list of qualifying non-price forming trades
- The scope of the STO should be extended to ETFs in order to incentivise lit trading and investor protection in this growing asset class. It should follow the same methodology for STO determination by accessing where the issuer has chosen to add the same financial instrument to an EU and/or third country trading venue.

Q23: What is your evaluation of the general policy options listed below as regards the future of the STO?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
Maintain the STO (status quo)	☒	☐	☐	☐	☐	☐
Maintain the STO with adjustments (please specify)	☐	☐	☐	☐	☒	☐
Repeal the STO altogether	☒	☐	☐	☐	☐	☐

Q23.1: Please explain your answer to question 23:

FESE supports maintaining the STO with adjustments i.e. limiting the trading obligation to EU shares. The current approach does not provide certainty to the industry as the regulation’s requirement exempting ‘non-systematic, ad hoc, irregular and infrequent’ trading has not been clarified in a conclusive way.

The share trading obligation (STO) remains necessary and is an important cornerstone of the overall aim of MiFID II/MiFIR to enhance the efficiency, resilience and integrity of financial markets in the EU. For the STO to be fully functional, further work on clearly determining which shares should be considered EU shares is necessary. The approach should avoid undue complexity and be based on predictable and meaningful criteria.

Determination of EU shares

Given the various challenges highlighted above in relation to the STO, a careful approach is essential. Therefore, in order to determine which shares should be considered as EU shares, FESE suggests the following approach:

- the STO should apply to those shares with an ISIN starting with a country code corresponding to an EU27 Member State plus those starting with a non-EU country code but where the issuer has its primary listing within the EU27

- the STO should not apply to those shares with an ISIN starting with a country code corresponding to an EU27 Member State where the issuer has its exclusive listing in a third country
- in cases where the security is dual-listed on both an EU trading venue and a non-EU trading venue at the specific request of the issuer, we propose that the STO should also still apply but that there is an exception in the provision (as suggested by ESMA in the consultation ESMA 70-156-2188 – para 278), to allow trading to take place on the non-EU trading venue where the issuer has listed the security, in addition to the EU venues.
- "Listing" in this sense is always made upon request of the issuer and involves various obligations for initial listing and for maintaining a listing.

This approach will ensure that the key objective of the STO can still be achieved i.e. more transparency with OTC trading moving to lit trading, it will also ensure in the case of dual-listed securities, that EU brokers and their investors can still access the main pools of liquidity where the issuer itself has requested its security to be traded and does not in any way disincentivise issuers from listing on EU trading venues.

Furthermore, we would also highlight the following points relevant to the STO:

- For dual-listed securities (where the issuer has chosen to have one of the two listings in the EU), investment firms should have the possibility to trade on either listing venue. To address the consequences of this exemption, reporting arrangements for such dual listed shares ought to be devised to achieve the transparency of these shares in the EU.
- Exemptions should be removed where trades are "non-systematic, ad-hoc, irregular and infrequent", instead exemptions should only apply for those trades that do not contribute to price formation based on a clear and consistent list of qualifying non-price forming trades – see our response to Q.33 for further detail.
- The scope of the STO should be extended to ETFs in order to incentivise lit trading and investor protection in this growing asset class. It should follow the same methodology for STO determination by accessing where the issuer has chosen to add the same financial instrument to an EU and/or third country trading venue.

Q24: Do you consider that the status of systematic internalisers which are eligible venues for compliance with the STO, should be revisited and how?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
SIs should keep the same current status under the STO	☐	☒	☐	☐	☐	☐
SIs should no longer be eligible execution venues under the STO	☐	☐	☒	☐	☐	☐
Other	☐	☐	☐	☐	☒	☐

Please explain in what other way(s) the status of systematic internalisers, which are eligible venues for compliance with the STO, should be revisited:

For equity trading, FESE considers that SI activity should be limited to trades above LIS. Below LIS, this type of execution venue should operate as a trading venue, under non-discretionary and non-discriminatory rules, and comply with the tick size and transparency regimes. We would recommend retaining SIs as eligible execution places for the purposes of the share trading obligation but limiting the activity to trades above LIS.

In such a scenario the large in scale threshold would be used as the main tool to delineate lit and dark trading. Below LIS trading would be confined to Regulated Markets and MTFs exclusively. These trading venues would in principle always be subject to real-time pre- and post-trade transparency requirements thus creating a lit space for below LIS. The available waivers under the pre-trade transparency regime (Art. 4 MiFIR) would be limited to the LIS and OMF waivers and the double volume cap mechanism would disappear.

SI activity would be restricted to above LIS only. Above LIS trading would constitute a dark space in which trades would not be subject to pre-trade transparency and would benefit from delayed post-trade transparency. This would result in an appropriate limitation of SI activity and a welcome simplification of the fragmented execution landscape.

Q24.1: Please explain your answer to question 24:

The market share of SIs has grown from 15% to 25% in the first 9 months of application of the SI regime under the new MiFID II/MiFIR rules. A drop in lit book market share can also be observed over the same period. Against this backdrop, FESE suggests restricting trading in SIs to above LIS only for equity and equity-like instruments in order to preserve the price formation process all the while acknowledging the need for bilateral trading.

FESE believes that trading below LIS should only be allowed under the full pre-trade transparency scope. Whilst no waivers exist for SIs, and pre-trade transparency requirements are not comparable to those of trading venues, FESE would nevertheless question why trades below LIS should be taking place on SIs at all when they can be traded on a trading venue with full transparency. Such a measure will foster the robustness of lit order book systems. This is essential for investors that do not have access to SIs.

FESE believes that using the LIS threshold as the main tool to delineate lit and dark trading would be highly beneficial from an investor protection perspective. Such a simplification of the market structure would not interfere with investors' choice of where to execute transactions as different types of execution venues are still available albeit subject to transparency requirements fundamentally different to the existing set-up. Of course, it makes sense for an individual to continue executing on less transparent markets if this is possible. However, this leads to a classic economic problem: the private gain of a market participant not sticking to the agreement will always be greater than the common loss. We would note however, this occurs at the expense of liquidity on public markets and threatens the price formation process.

Our proposal implies that the pre-trade transparency requirements will no longer apply for SIs as SIs will only be allowed to trade above LIS with no restrictions apart from fulfilling post-trade transparency requirements. This would render the concept of standard market size obsolete. This proposal would also greatly reduce complexity and provide for a much simpler market structure to everyone's benefit. This approach appears as the most pragmatic and effective way to address the existing failures of the SI regime.

It is commonly understood that publicly available orderbooks of regulated exchanges maximise transparency and hence benefits financial markets overall. Therefore, orderbook trading at regulated exchanges should be encouraged by financial regulation wherever possible.

The argument that the disclosed identity of the SI provides a higher level of transparency than trading in a regulated exchange's orderbook does not hold true for centrally cleared products, as for these products the identity of each trades' counterparty, namely the CCP, is also known to all market participants before any trade is executed.

The argument that SIs have to hold their own capital against trades executed on the SI, does not benefit the SI's customers other than by implicitly decreasing their SI's counterparty credit risk towards them. However, considering the stringent prudential framework applicable to all EU CCPs, it can be assumed that a centrally cleared trade bears lower counterparty credit risk than a trade executed on an SI, all other things equal.

Q25: Do you consider that other aspects of the regulatory framework applying to systematic internalisers should be revisited and how? Please explain your answer:

When it comes to pre-trade transparency requirements, FESE would first note that the current minimum quoting size of 10% of the SMS is too low. Compared to MiFID I the current threshold only increased by 250 EUR to 1,000 EUR. This is not enough to effectively increase transparency and even provides SIs with a competitive advantage. Requiring SIs to quote 10,000 EUR on each side as suggested in the ESMA consultation on equity transparency would be more appropriate.

FESE would also agree with ESMA's proposal in its consultation on equity transparency that an extension of the transparency obligation for SIs to illiquid instruments would be an effective way to improve market transparency and level the playing field between on-venue and SIs. SIs currently benefit from a competitive advantage as trading in illiquid instruments is still not subject to any pre-trade transparency requirements. On the other hand, illiquid instruments are in scope for pre-trade transparency for all trading venues unless a waiver is used. FESE is of the view that such new requirements would not be overly burdensome for SIs and would rather foster lit trading and overall transparency.

Moreover, FESE would like to stress the importance of enforcement of existing rules. While SIs are regulated under MiFID II as execution venues providing bilateral trading, they provide less transparency than on-exchange trading. This can be problematic when the distinction between purely bilateral and hybrid multilateral trading is blurred. In theory, every trade in an SI must take place against the proprietary account of the operator. SIs are prohibited, when dealing on their own account, from entering into matching arrangements with entities outside their group with the objective of carrying out *de facto* riskless back-to-back transactions in financial instruments outside trading venues. However, some investment firms seem to have developed models by which third party trading firms are able to provide liquidity to the customers of SIs. Such activities must be monitored as there is a risk that trading takes place on a multilateral basis rather than on a bilateral basis.

Furthermore, details of the operation of the business model required seem to be lacking. This is in contrast with what MTFs and RMs need to fulfil. Hence, we would suggest levelling the playing field regarding the description of the business model and how regulatory compliance is maintained. In addition, there is no level-playing field with regard to flagging of SI trades at an EU level. Two years on from MiFID II implementation, the flagging remains unclear and inconsistent. One way to address this would be a broader implementation of the MMT which currently ensures consistency of exchange data. It is our view that the extension of the MMT would promote enhancing data consistency and contribute to an increase in regulatory oversight of SI activity.

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That being said, for equity trading FESE supports the proposal outlined above to restrict SI trading to above LIS only to incentivise lit trading and ensure the quality and robustness of the price determination mechanism in line with the initial objective of MiFID II/MiFIR.

For non-equity, the LIS threshold may be too high to require all trading below LIS to happen on a RM, MTF or OTF. Therefore, for bonds and securitised derivatives we would recommend using the 100,000 EUR denomination threshold to delineate lit (RM, MTF and OTF) trading from dark (OTC and SI trading). We would recommend allowing trading, which takes place at and below a threshold of 100,000 EUR, on transparent RMs, MTFs and OTFs only. This would significantly reduce market fragmentation, aggregate liquidity and increase pre- and post-trade transparency, in particular for retail investors. Furthermore, this threshold would also be in line with the one currently used for the calculations to determine whether a bond is liquid or not. For securitised derivatives, this delimitation would simplify the fragmented execution landscape. We expect that this change would be beneficial for investors – especially retail investors – as it would allow for a better interaction on multilateral markets.

SI quotes (and prices) in bonds and securitised derivatives are mainly available using proprietary arrangements (if any) and websites of SIs. This conflicts with the aim to increase transparency in the traditionally opaque markets in these instruments. Therefore, FESE strongly supports ESMA's proposal to define the requirements that should be met by SIs in non-equity instruments for publishing their quotes and to extend the requirements set out in art. 13 of Regulation 2017/567 on obligations for SIs to make quotes easily accessible to SIs in non-equity instruments.

Q26: What would you consider to be appropriate steps to ensure a level-playing field between trading venues and systematic internalisers? Please explain your answer:

In FESE's view there are several aspects that give SIs a competitive advantage over trading venues (please see our response to Q25). When it comes to pre-trade transparency requirements the current minimum quoting size of 10% of the SMS is too low. Compared to MiFID I the current threshold only increased by 250 EUR to 1,000 EUR. This is not enough to effectively increase transparency and even provides SIs with a competitive advantage. Requiring SIs to quote 10,000 EUR on each side as suggested in the ESMA consultation paper on equity transparency would be more appropriate.

When it comes to the instruments in scope, FESE would agree with ESMA's proposal in its consultation paper on equity transparency that an extension of the transparency obligation for SIs to illiquid instruments would be an effective way to improve market transparency and level the playing field between on-venue and SI trading. SIs currently benefit from a competitive advantage as trading on most instruments is still not subject to any pre-trade transparency requirements. On the other hand, illiquid instruments are in scope for pre-trade transparency for all trading venues unless a waiver from pre-trade transparency is used. FESE is not of the view that such new requirements would be overly burdensome for SIs rather they would effectively foster lit trading and overall transparency.

Furthermore, we believe that ESMA should review how SIs operate by looking more deeply into the transactions they conclude and report. One issue arises from riskless trading. Hubs that have the potential to link up SIs and counterparties should be monitored to guarantee that they always work on a bilateral basis, and in case they do not but operate an internal matching system they must operate an MTF. Such activities must be monitored as there is the risk that trading takes place on a multilateral basis rather than on a bilateral basis and hence would be in violation with the legislation.

Moreover, details of the operation of the business model required to run an SI seem to be lacking. This is in contrast with what MTFs and Regulated Markets need to fulfil. Hence, we would suggest levelling the playing field regarding the description of the business model and how regulatory compliance is maintained. In addition, there is no level-playing field with regard to flagging of SI trades at an EU level. Even more than two years after MiFID II got introduced the flagging is very unclear and inconsistent. One way to address this would also be a broader implementation of the Market Model Typology (MMT) which currently ensures consistency of exchange data. It is our view that the extension of the MMT would promote enhancing data consistency and contribute to increase regulatory oversight of SI activity.

That being said, we believe that the most effective way to address the shortcomings of the SI regime when it comes to inconsistent flagging of trades or the question of riskless principal trading being based on a bilateral relationship and to create a level-playing field would be to restrict SI activity to above LIS trading. FESE believes that the approach mentioned above – i.e. limiting SIs to activity above the LIS threshold – would provide an adequate way of ensuring a level playing field between trading venues and SIs. Such enhancements to the SI regime are necessary in order to increase transparency as well as price formation and promote a level playing field between trading venues and SIs. Above LIS trading would thereby constitute a legitimate dark space in which trades across bilateral execution venues and multilateral trading venues are not subject to pre-trade transparency and would benefit from delayed post-trade transparency.

Q27: In your view, what would merit attention to further promote the price discovery process in equity trading? Please explain your answer:

To further promote the price discovery process in equity trading FESE suggests working on a simplified market structure concept:

<u>1. SIs</u>

FESE believes that restricting SI equity trading to above LIS only would be an efficient way to incentivise lit trading, ensure the quality and robustness of price formation, in line with the initial objective of MiFID II.

In such a scenario, the LIS threshold would be used as the main tool to delineate lit and dark trading. Below LIS trading should be confined to RMs and MTFs exclusively. FESE underlines that rules applicable to MTFs should continue to apply, specifically operators of MTFs would still be prohibited from engaging in prop trading, running bilateral systems and applying discretionary and discriminatory rules. These TVs would in principle always be subject to real-time pre- and post- trade transparency requirements thus creating a lit space for trades below LIS. There would no longer be a need for a DVC mechanism since pre-trade transparency waivers would be limited to the LIS and OMF.

SIs activity would be restricted to above LIS only. Above LIS trading constitutes a legitimate dark space in which trades are not subject to pre-trade transparency and would benefit from delayed post-trade transparency. This proposal applies to RMs, MTFs and SIs and it would result in an appropriate limitation of dark activity and a simplification of the fragmented execution landscape. Above LIS, transactions benefit from waivers to avoid market impact. To take away from the price formation process is only warranted when the potential market impact is sizable.

<u>2. Dark/OTC trading</u>

FESE suggests limiting dark trading by reducing the number of waivers to mainly LIS - this includes the repeal of the DVC mechanism: The main purpose of the waiver regime is to protect market participants from adverse market movements following the execution of large orders.

OTC would be restricted to trades in shares not subject to the STO. FESE also suggests extending MMT to all execution venues as well as to OTC transactions under ESMA governance.

3. RFQs

MiFID II introduced increased transparency requirements applicable to ETFs however the fundamental concern is that the majority of trading – approx. 90% - still takes place on alternative trading systems, as opposed to on-exchange lit markets. FESE suggests that ESMA investigates this liquidity shift from lit order book trading to RFQ trading and assesses its potential long-term impact on ETF market structure. ESMA should propose mitigating measures if this trend is perceived to be non-compliant with ESMA's objective to ensure the quality and robustness of the ETF price determination mechanism for all investors. FESE suggests that RFQ systems should only be made available for ETF transactions above the LIS thresholds (1m EUR) so that the bulk of trading, i.e. smaller size trades, are executed on transparent trading platforms thereby contributing to the price formation process.

4. STO

FESE proposes to modify the STO regarding its third country dimension, scope, exemptions and application to asset classes:

i) To address the third country impact of the current scope, the STO should apply to those shares with an ISIN starting with a country code corresponding to an EU27 Member State plus those starting with a non-EU country code but where the issuer has its primary (fully-fledged) listing within the EU27;
ii) The STO should not apply to those shares with an ISIN starting with a country code corresponding to an EU27 Member State where the issuer has its exclusive listing in a third country;
iii) In cases where the security is dual-listed on both an EU trading venue and a non-EU trading venue at the specific request of the issuer, we propose that the STO should still apply but that there is an exception in the provision to allow for trading to take place on the non-EU trading venue where the issuer has admitted the security, in addition to the EU venues;
iv) Exemptions should be removed where trades are "non-systematic, ad-hoc, irregular and infrequent", instead exemptions should only apply for those trades that do not contribute to price formation based on a clear and consistent list of qualifying non-price forming trades.

The scope of the STO should be extended to ETFs in order to incentivise lit trading and investor protection in this asset class. "Listing" in this sense is always made upon the request of the issuer and involves various obligations for initial listing and for maintaining a listing.

5. Midpoint

Midpoint orders are executed at the expense of participants willing to set or display a price. Ultimately, the idea that a midpoint price is fairer is flawed, as pegging can in some circumstances act similarly to a reference price without being subject to a waiver. FESE considers that for below LIS orders, midpoint pegging should not be allowed in central limit order books. However, midpoint pegging should be available for orders above LIS.

4.2. Aligning the scope of the STO and of the transparency regime with the scope of the consolidated tape

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Q28: Do you believe that the scope of the STO should be aligned with the scope of the consolidated tape?

☒ 1 - Disagree
☐ 2 - Not really
☐ 3 - Neutral
☐ 4 - Partially
☐ 5 - Totally
☐ Don't know / no opinion / not relevant

Q28.1. Please explain your answer to question 28:

No, FESE believes that the scope of the STO should not be aligned with the scope of the CT. All instruments, no matter if liquid or illiquid, if admitted to an EU regulated market or EU MTF or simply being included to trading (including those without a prospectus) should be included in the consolidated tape. In addition, flexible voluntary contribution of third country shares (not admitted to trading in the EU) to the consolidated tape by EU and/or third country trading venues can be envisaged (as explained in Q19) as long as the data provided is fully compliant with the requirements set out at EU level.

Q29: Do you consider, for asset classes where a consolidated tape would be mandated, that the scope of financial instruments subject to pre- and post-trade requirements should be aligned with the list of instruments in scope of the consolidated tape?

☐ 1 - Not at all
☐ 2 – Not really
☒ 3 - Neutral
☐ 4 - Partially
☐ 5 - Totally
☐ Don't know / no opinion / not relevant

Q29.1: Please explain your answer to question 29:

FESE would underline that such an approach could introduce undue complexity and it is not clear what the rationale would be for including some instruments in the transparency regime and not others. Therefore, FESE would support retaining the current situation where all instruments trading on trading venues should be subject to pre- and post-trade transparency requirements, with appropriate calibrations, regardless of whether they are included in the consolidated tape.

Ultimately, the scope of the consolidated tape should align with the securities that are subject to pre-and post-trade transparency requirements, not the other way round.

4.3. Post-trade transparency regime for non-equities

Q30: Which of the following measures could in your view be appropriate to ensure the availability of data of sufficient value and quality to create a consolidated tape for bonds and derivatives?

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	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
Abolition of post-trade transparency deferrals			x			
Shortening of the 2-day deferral period for the price information			x			
Shortening of the 4-week deferral period for the volume information			X			
Harmonisation of national deferral regimes			X			
Keeping the current regime			x			
Other						

Please specify what other measures could in your view be appropriate to ensure the availability of data of sufficient value and quality to create a consolidated tape for bonds and derivatives?

We suggest that there should be a reduction in the number of options available in the transparency regime, in particular the deferrals that enable only partial publication or no publication of trades, as well as the 4-week deferral.

Q30.1: Please explain your answer to question 30:

The analysis of the evolution of the EU non-equity market structure suggests that policy measures, aimed at bringing trading out of the dark, have not been as successful as originally expected. Non-equity trading is still very opaque compared to equity and there was no increase in transparency triggered by MiFID II / R vis-à-vis MiFID I.

Bonds and derivatives markets with deep pools of high-quality liquidity are a crucial component of healthy ecosystems as well as an important contributor to competitive, transparent and stable EU financial markets. Ensuring transparency in these markets requires tailored and flexible rules that balance the need for enhanced transparency whilst recognising the specificities and nuanced working of such markets. Given the different characteristics between bonds and derivatives, the table above cannot be completed for both in the same way. Under the current regulation, there is hardly any sensible transparency in bonds available. For what concerns bonds, besides overly long delays, the possibility to publish selected data points of one single transaction in bonds over a certain period, is not only overly complex but it prevents usable transparency to the public rather than providing it. This is to the disadvantage of EU investors, as proper transparency data in bonds could enable passive investment as well in bonds for the benefit of investors and issuers alike.

MiFiD II contains multiple options for post-trade deferrals. As the fixed income market is fragmented and there is no “one-size-fit-all”, there should still be different options available, but we believe these could be reduced and simplified. In terms of the table above, while there should still be post-trade deferrals allowed, we propose the regime should be amended and suggest the four week deferral period should be shortened.

It should be evaluated whether reducing the number of alternatives could be beneficial. One reason for this is that the more optionality, the higher the cost of adapting IT-systems and operational procedures. This will especially apply for service providers such as APAs as these will need to be flexible on their offering in order to attract business. Similarly, the more options, the more work market participants will need to put into their internal procedures as they would need to know which deferrals are used in each market they are trading on, in order to control their own risk. Another reason is that if publication of trades may be postponed significantly (e.g. 4 weeks or partial publication), the information is outdated at time of publication, except for compliance purposes. Similarly, the indefinite deferral for government bonds means that market participants will not have insight into these transactions. Market participants should, though, still have the possibility to defer publication, and a few various options should still be possible as there may be national needs that the regulators should be able to accommodate. Therefore, we do not recommend a full harmonisation across all markets, but rather a more simplified framework.

II. Investor protection

5000 character(s) maximum
including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

Q31 - Please specify to what extent you agree with the statements below regarding the experience with the implementation of the investor protection rules?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N. A.
The EU intervention has been successful in achieving or progressing towards more investor protection.						
The MiFID II/MiFIR costs and benefits are balanced (in particular regarding the regulatory burden).						
The different components of the framework operate well together to achieve more investor protection.						
More investor protection corresponds with the needs and problems in EU financial markets.						
The investor protection rules in MiFID II/MiFIR have provided EU added value.						

Q31.1 - Please provide both quantitative and qualitative elements to explain your answer and provide to the extent possible an estimation of the benefits and costs. Where possible, please provide figures broken down by categories such as IT, organisational arrangements, HR etc.
Quantitative assessment:

	Estimate (in euro)
Benefits	

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Costs	

Qualitative elements for question 31.1:

Q32 - Which MiFID II/MiFIR requirements should be amended in order to ensure that simple investment products are more easily accessible to retail clients?

	Yes	No	N.A.
Product and governance requirements			
Costs and charges requirements			
Conduct requirements			
Other			

Please specify which other MiFID II/MiFIR requirements should be amended:

Q32.1 – Please explain your answer to question 32:

Q33 - Do you agree that the MiFID II/MiFIR requirements provide adequate protection for retail investors regarding complex products?

☐ 1 – Disagree
☒ 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q33.1 - If your answer to question 33 is on the negative side, please indicate in the text box which amendments you would like to see introduced to ensure that retail investors receive adequate protection when purchasing products considered as complex under MiFID II/MiFIR:

Securitised derivatives are not defined as an independent category in Level 1 and therefore cannot benefit from differentiated and homogenised rules. We believe that there might be merit in creating a stand-alone category for securitised derivatives in MIFID and introducing differentiated rules for these instruments.
The current definition of securitised derivatives in MiFID II is not appropriate. Some of the MiFID II requirements, that by default apply to securitised derivatives, are also inconsistent, for instance:

- Securitised derivatives are covered by the clearing obligation for trading on a regulated market.
- MiFID II rules on position limits apply to securitised derivatives.

These requirements, when applied to securitised derivatives, offer no added value for investor protection and the functioning of financial markets since they seek to reduce risks that do not exist with cash market instruments. In short, for regulatory purposes, bundling of products with a different set-up, may lead to unintended consequences when applying rules. Beyond being inefficient and costly, this also undermines confidence in the regulation. It would be helpful if the above requirements were to be reconsidered under this review.

Q33.1 – Please explain your answer to question 33:

Q34 - Should all clients, namely retail, professional clients per se and on request and ECPs be allowed to opt-out unilaterally from ex-ante cost information obligations, and if so, under which conditions?

	Yes	No	N. A.
Professional clients and ECPs should be exempted without specific conditions.			
Only ECPs should be able to opt-out unilaterally.			
Professional clients and ECPs should be able to opt-out if specific conditions are met.			
All client categories should be able to opt out if specific conditions are met.			
Other			

Please specify what is your other view on whether all clients, namely retail, professional clients per se and on request and ECPs should be allowed to opt-out unilaterally from ex-ante cost information obligations?

Q34.1 - Please explain your answer to question 34 and in particular the conditions that should apply:

Q35 - Would you generally support a phase-out of paper based information?

- ☐ 1 – Disagree
- ☐ 2 – Rather not agree
- ☐ 3 - Neutral
- ☐ 4 – Rather agree
- ☐ 5 – Fully agree
- ☐ Don't know / no opinion / not relevant

Q35.1 - Please explain your answer to question 35:

Q36 - How could a phase-out of paper-based information be implemented?

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	Yes	No	N. A.
General phase-out within the next 5 years			
General phase out within the next 10 years			
For retail clients, an explicit opt-out of the client shall be required.			
For retail clients, a general phase out shall apply only if the retail client did not expressively require paper based information			
Other			

Please specify in which other way could a phase-out of paper-based information be implemented?

Q36.1 - Please explain your answer to question 36 and indicate the timing for such phase-out, the cost savings potentially generated within your firm and whether operational conditions should be attached to it:

Q37 - Would you support the development of an EU-wide database (e.g. administered by ESMA) allowing for the comparison between different types of investment products accessible across the EU?

- ☐1 – Disagree
- ☐2 – Rather not agree
- ☐ 3 - Neutral
- ☐4 – Rather agree
- ☐5 – Fully agree
- ☐ Don't know / no opinion / not relevant

Q37.1 - Please explain your answer to question 37:

Q38 - In your view, which products should be prioritised to be included in an EU-wide database?

	1 (irrelevant)	2 (rather not relevant)	3 (neutral)	4 (rather relevant)	5 (fully relevant)	N. A.
All transferable securities						

All products that have a PRIIPs KID/ UICTS KIID						
Only PRIIPs						
Other						

Please specify what other products should be prioritised?

Q38.1 - Please explain your answer to question 38:

Q39 - Do you agree that ESMA would be well placed to develop such a tool?

☐ 1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q39.1 - Please explain your answer to question 39:

Q40 - Do you consider that MiFID II/MiFIR can be overly protective for retail clients who have sufficient experience with financial markets and who could find themselves constrained by existing client classification rules?

☐1 – Disagree
☐2 – Rather not agree
☐ 3 - Neutral
☐4 – Rather agree
☒5 – Fully agree
☐Don't know / no opinion / not relevant

Q40.1 - Please explain your answer to question 40:

A definition for 'experienced and knowledgeable High Net Worth investors', for these to have tailor-made investor protection rules, should be introduced. This would apply to a category of investors that have sufficient experience and financial means to understand the risk attached.

Q41 - With regards to professional clients on request, should the threshold for the client's instrument portfolio of EUR 500 000 (See Annex II of MiFID II) be lowered?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☐5 – Fully agree
☐Don't know / no opinion / not relevant

Q41.1 - Please explain your answer to question 41:

Q42 - Would you see benefits in the creation of a new category of semi-professionals clients that would be subject to lighter rules?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☒5 – Fully agree
☐Don't know / no opinion / not relevant

Q42.1 - Please explain your answer to question 42:

Yes, but such a definition should not be linked to profession but rather experience, knowledge and risk-profile. A definition for 'experienced and knowledgeable High Net Worth investors' should be introduced to allow those identified in this category to have tailor-made investor protection rules. This would apply to a category of investors that have sufficient experience and financial means to understand the risk attached.

Q43 - What investor protection rules should be mitigated or adjusted for semi-professionals clients?

	1 (irrelevant)	2 (rather not relevant)	3 (neutral)	4 (rather relevant)	5 (fully relevant)	N.A.
Suitability or appropriateness test						
Information provided on costs and charges						
Product governance						
Other						

Please specify what other investor protection rules should be mitigated or adjusted for semi-professionals clients?

Q43.1 - Please explain your answer to question 43:

Q44 - How would your answer to question 43 change your current operations, both in terms of time and resources allocated to the distribution process?
Please specify which changes are one-off and which changes are recurrent:

Q45 - What should be the applicable criteria to classify a client as a semi-professional client?

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	1 (irrelevant)	2 (rather not relevant)	3 (neutral)	4 (rather relevant)	5 (fully relevant)	N.A.
Semi-professional clients should possess a minimum investable portfolio of a certain amount (please specify and justify below).						
Semi-professional clients should be identified by a stricter financial knowledge test.						
Semi-professional clients should have experience working in the financial sector or in fields that involve financial expertise.						
Semi-professional clients should be subject to a one-off in-depth suitability test that would not need to be repeated at the time of the investment.						
Other						

Please specify what other criteria should be the one applicable to classify a client as a semi-professional client:

Q45.1 - Please explain your answer to question 45 and in particular the minimum amount that a retail client should hold and any other applicable criteria you would find relevant to delineate between retail and semi- professional investors:

Q46 - Do you consider that the product governance requirements prevent retail clients from accessing products that would in principle be appropriate or suitable for them?

- ☐1 – Disagree
- ☐2 – Rather not agree
- ☐ 3 - Neutral

☒4 – Rather agree
☐5 – Fully agree
☐Don't know / no opinion / not relevant

Q46.1 - Please explain your answer to question 46:

The product governance obligations under MiFID II for the product life cycle put a number of requirements on investment firms which manufactures financial instruments for sale to end clients ("manufacturer") and on investment firms offering products to end clients ("distributors"). Some requirements have introduced significant administrative burden on manufacturers and distributors alike without ensuring a higher level of investor protection. There are Level 3 measures which offers certain exemptions for the non-advised client business and these rules should be taken into account in the MiFID II /R Level 1 Review.

The concrete differentiation between a positive and a negative target market lead to practical difficulties in implementation. Since some criteria that refer to a negative target market cannot be used as a counter-argument to a positive. The requirement to define a negative target market should potentially be reconsidered.

Moreover, new provisions for product governance (Guidelines on MiFID II product governance requirements) extend the requirements for issuers and retail banks. Issuers must define a target market for every product. Retail banks must consider the target market for every buy order by comparing the target market data with the customer characteristics. These provisions may further reduce retail investors' access to classic bonds. This also applies in cases where the bond issue lacks attributes which may not be suited for retail investors.

Retail investors' access to classic corporate or bank bonds is increasingly limited due to regulation. This is due to the inclusion of classic bonds in the PRIIPS regulation and the increasing number of bond issues availing of the wholesale bond regime for qualified investors with reduced requirements under the Prospectus Regulation, as well as new provisions for product governance defined in the "Guidelines on MiFID II product governance requirements" further reduce retail investors' possibilities to invest in classic bonds.

These guidelines for product governance require issuers to define a target market for every product, including classic bonds and retail banks must consider the target market for every buy order by comparing the target market with the individual customer's characteristics.

There is an increasing trend towards issuers of classic bonds defining the target market of their bond issuances as "institutional" irrespectively of whether the bonds are suited for retail investors or not. In this case, retail investors are not able to invest in these bonds as retail banks are not allowed to provide for retail investors to buy these bonds. The reasons why issuers choose to do this may vary (e.g. to reduce the risk of being sued by retail investors). However, regulators should ensure that the target market definition is not adversely used by issuers to prohibit retail investors from investing in products like classic bonds that otherwise suit them.

Q47 - Should the product governance rules under MiFID II/MiFIR be simplified?

	Yes	No	N.A.
It should only apply to products to which retail clients can have access (i.e. not for non-equities securities that are only eligible for qualified investors or that have a minimum denomination of EUR 100.000).			

It should apply only to complex products.			
Other changes should be envisaged – please specify below.			
Simplification means that MiFID II/MiFIR product governance rules should be extended to other products.			
Overall the measures are appropriately calibrated, the main problems lie in the actual implementation.			
The regime is adequately calibrated and overall, correctly applied.			

Q47.1 - Please explain your answer to question 47:

Q48 - In your view, should an investment firm continue to be allowed to sell a product to a negative target market if the client insists?

☐Yes
☐Yes, but in that case the firm should provide a written explanation that the client was duly informed but wished to acquire the product nevertheless.
☐No
☐Don't know / no opinion / not relevant

Q48.1 - Please explain your answer to question 48:

Q49 - Do you believe that the current rules on inducements are adequately calibrated to ensure that investment firms act in the best interest of their clients?

☒ 1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐4 – Rather agree
☐5 – Fully agree
☐Don't know / no opinion / not relevant

Q49.1 - Please explain your answer to question 49:

FESE has observed that payment for order flow (PFOF) schedules have become an established feature of certain Regulated Markets. The UK FCA has described the commercial relationships between order flow providers, liquidity providers/market makers and exchanges in detail. This may serve as a common point of reference for the consideration of the potential implications of PFOF schedules, please see further details here.
These market developments are partly a result of the increase in market fragmentation and the proliferation of trade execution modes stemming from MiFID II/MiFIR. The trend was enhanced by online brokers (order flow providers) which actively route free of charge their clients' order flows for execution exclusively to venues that facilitate PFOF schedules and receive a fee or commission from liquidity providers/market makers closely connected to these venues in return.

FESE considers that PFOF schedules warrant further supervisory scrutiny and potentially regulatory action. It is important to assess PFOF not only from the perspective of their compliance with best execution provisions and inducement rules but also from a market structure perspective. These perspectives should be combined to have a comprehensive view of the economic prerequisites in the respective exchange rules that facilitate PFOF. Where they receive payments in exchange for the submission of order flow, online brokers/order flow providers are exposed to a serious conflict of interest, which undermines their incentives and ability to act in the best interests of their clients. From a retail investor's perspective, the trend towards higher PFOF from larger market makers/liquidity providers to order flow providers is worrisome as it may impair competition and/or serve as entry barriers for new market participants. As it may diminish choice for retail investors, we understand it to contradict the MiFID II policy objectives, in particular, the best execution regime. Against this background, FESE calls on the Commission to intensify their regulatory scrutiny as regards the implication of PFOF on market quality and investor protection and to establish a common supervisory and regulatory approach towards PFOF. This examination should comprise the option to ban these practices to achieve a level-playing field within the EU.

Q50 - Would you see merits in establishing an outright ban on inducements to improve access to independent investment advice?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☐5 – Fully agree
☐Don't know / no opinion / not relevant

Q50.1 - Please explain your answer to question 50:

Q51 - Would you see merit in setting-up a certification requirement for staff providing investment advice and other relevant information?

☐1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q51.1 - Please explain your answer to question 51:

Q52 - Would you see merit in setting out an EU-wide framework for such a certification based on an exam?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☐5 – Fully agree
☐Don't know / no opinion / not relevant

Q52.1 - Please explain your answer to question 52:

Q53 - To reduce execution delays, should it be stipulated that in case of distant communication (phone in particular) the cost information can also be provided after the transaction is executed?

☐ 1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q53.1 - Please explain your answer to question 53:

Q54 - Are taping and record-keeping requirements necessary tools to reduce the risk of products mis-selling over the phone?

☐ 1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q54.1 - Please explain your answer to question 54:

6. Reporting on best execution

Q55: Do you believe that the best execution reports are of sufficiently good quality to provide investors with useful information on the quality of execution of their transactions?

☐ 1 - Disagree
☐ 2 - Rather not agree
☒ 3 - Neutral
☐ 4 - Rather agree
☐ 5 - Fully agree
☐ Don't know / no opinion / not relevant

Q55.1: Please explain your answer to question 55:

Feedback from some members indicates that the current regulatory requirements for best execution reports are met by the providers of the reports as these rules have been in place for a sufficient time. This allows a satisfactory level of information.

Whilst it is understood that this question is targeted at investments firms in respect to the reports produced by those investment firms stemming from RTS 27 and RTS 28 FESE would nevertheless note that all trading venues are requested to produce Best Execution reports

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according to RTS 27. The purpose of such reports is to support the design of best execution policies established by investment firms and to allow ex post check for those investment firms.

We would underline that FESE Members have put significant efforts and resources towards the production and publication of RTS 27 reports. Exchanges, as well as all other institutions in the industry, such as execution venues or investments firms (including SIs), have made efforts to interpret associated regulatory requests. The data that requires processing and storing in the context of the RTS 27 reports is considerable. The RTS 27 reports are produced for every trading day and each traded instrument on a given trading venue and covers pre- and post-trade statistics, costs, qualitative information.

Regarding the content of the different reports, FESE Members have dedicated efforts towards understanding the relevant requirements as well as respecting the spirit of the regulation where interpretation of the texts has, on occasion, been challenging. In the absence of an industry led initiative on RTS 27 (the FIX Best Execution group being more focused on RTS 28), we are well aware that some discrepancies might arise between interpretations of statistics provided by trading venues. We understand this may cause some confusion especially since most of the time the only support investors can refer to is text itself (RTS 27 and annex of RTS 27). We would encourage regulators to proceed with caution in this area since a complete revamp of RTS 27 and RTS 27 would be counterproductive. In any case, whatever the potential extent of the review, we ask that policymakers work closely with trading venues and investment firms on envisaged changes in order to ensure that they are meaningful and, where possible, non-disruptive (see our answer to question 56).

Q56: What could be done to improve the quality of the best execution reports issued by investments firms?

	1 (irrelevant)	2 (rather not relevant)	3 (neutral)	4 (rather relevant)	5 (fully relevant)	N.A.
Comprehensiveness			X			
Format of the data			X			
Quality of data				X		
Other						

Please specify what else could be done to improve the quality of best execution reports issued by investments firms:

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The quality of the data is paramount to an insightful report. Quality should be constant across best execution report providers to also ensure homogeneity of the results and allow for proper comparison between executing brokers.

Not all brokers access the same venues under the same conditions making comparison difficult sometimes and consistency across providers is important to allow meaningful comparison.

We would also reiterate that all parties, be it investment firms or trading venues, have put enormous efforts and resources in the production and publication of RTS 27 reports. Whilst some improvement might be desirable, exchanges would ask that policy makers keep in mind that the range and amount of data to process on a daily basis and for all traded instruments is considerable as it covers pretty much all aspects of trading (pre- and post-trade costs). Moreover, the large number of calculations requested in all RTS 27 tables as well as the storage capacity requested (daily reports shall be available for free for 2 years) imply significant IT capacities.

Question 56.1 Please explain your answer to question 56:

FESE understands that this question specifically targets investments firms and reports produced by those investment firms stemming from RTS 27 and RTS 28. However, we would like to provide the European Commission the view of trading venues on this topic.

FESE Members have dedicated enormous efforts and resources to the production and publication of RTS 27 reports. More than two years after the entry into force of MiFID II, best execution reports are published according to a methodology which has been defined in the past four to five years and covers format, calculations, publication frequency, storage. If the regulators were to amend in any way the regulation, we urge them to take into account the costs associated with any type of change – small or large – to those reports and to apply a reasonable approach which would take into account the ratio of costs/benefits of those reports and we would ask that investment firms and the trading venues are thoroughly consulted and given enough time to implement those changes and not request retroactive application of the regulatory texts.

Question 57: Do you believe there is the right balance in terms of costs between generating these best execution reports and the benefits for investors?

☒ 1 - Disagree
☐ 2 - Rather not agree
☐ 3 - Neutral
☐ 4 - Rather agree
☐ 5 - Fully agree
☐ Don’t know / no opinion / not relevant

Question 57.1 Please explain your answer to question 57:

As indicated in the previous responses, one-off costs for producing and publishing the RTS 27 were significant. Running costs must also be taken into account (storage, production) and still do not include following one-off costs to modify the reports, add tables, modify calculation logics which arise from the decommission or launch of new products, new pricings, creation of new market segments etc.

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Benefits for investors are from FESE's point of view rather unclear and in any case not quantifiable regarding RTS 27.

While understanding the intention of the regulators to provide transparent and free information directly from the investment firms/execution venues to the final investor FESE does not believe best execution reports have significantly improved trading decisions.

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III. Research unbundling rules and SME research coverage

Q58 - What is your overall assessment of the effect of unbundling on the quantity, quality and pricing of research?

Since January 2018, MiFID II has accelerated the reduction in equity research focussing on smaller issuers. 334 European smaller issuers lost coverage completely in 2018, 91% of which only had 1 analyst before the implementation of MIFID II.[5] Now, most small and mid-caps are covered by 0 to 1 analyst whilst large caps benefit from much wider coverage and better visibility to investors. As an example, in the case of Spain, the reduction of the number of analysts covering small caps (<€300 M market cap) has dropped by 55% since 2015. In 2019, the average was 0.7.

For SMEs to receive research coverage, they usually have to commission and pay for research themselves. An increasing number of SMEs have found themselves in a position where they have to fund equity research, thereby justifying the increase in sponsored research. A survey leg by the CLIFF showed that 80% of issuers with a market capitalization >€500 million used sponsored research in 2019 (compared to 60% in 2018). Two thirds of these issuers only rely on this sponsored research.

The effect has also been negative in terms of the quality and regularity of reports. The deep downturn in the income of the local research providers (typically local brokers) has meant that less senior analysts produce the reports and less time is dedicated to SMEs.

Q59 - How would you value the proposals listed below in order to increase the production of SME research?

	1 (irrelevant)	2 (rather not relevant)	3 (neutral)	4 (rather relevant)	5 (fully relevant)	N.A.
Introduce a specific definition of research in MiFID II level 1	X					
Authorise bundling for SME research exclusively					X	
Exclude independent research providers' research from Article 13 of delegated Directive 2017 /593					X	
Prevent underpricing in research			X			

[5] Bingxu, Fang, Hope, Ole-Kristian, Huang, Zhongwei and Moldovan, Rucsandra, Rotman School of Management Working Paper, 'The Effects of MiFID II on Sell-Side Analysts, Buy-Side Analysts and Firms', 2019.

Amend rules on free trial periods of research			X			
Other					X	

Please specify what other proposals you would have in order to increase the production of SME research:

Pre-MiFID II, research was supplied as part of a bundled service, paid by execution fees. Research post-MiFID II is required to be unbundled and priced separately from execution of trading of financial instruments.
A growing number of SMEs are paying independent research providers to write research and take the initiative in approaching investors directly. However, this is challenging due to potential conflict of interests and a lack of recognition and coverage limitations due to budget constraints. Some exchanges have launched programs to cover the costs of SME research coverage and the first results suggest that it can create additional liquidity for listed SMEs.
A Pan-European program should be launched to cover the costs of research coverage based on the lessons learnt from these pilot programs. A possible additional way to improve liquidity of SME shares would be to establish user-friendly platforms for analysts to share their reports on. Retail investors should also have access to such a platform.
As a result of unbundling rules, fund managers are prevented from accepting research on small companies provided by brokers for free. The rules should be amended to allow brokers to send SME-research reports to fund managers without having to establish a research contract with them. In doing so, a threshold could be established for what should be considered an SME.
Access to equity research on SMEs could be improved by:

- **Launching a Pan-European program to cover the costs of research coverage.**
- **Establish user-friendly platforms for analysts to share their reports on.**
- **Amend unbundling rules to allow brokers to send SME-research reports to fund managers.**

Accelerating the development of an “access point” of entry for financial reports from listed companies supported by machine-readable information provided by issuers under the Transparency Directive, or in the case of issuers on SME GMs, the relevant disclosure documentation required, could help facilitate access and availability of data about companies (in particular SMEs) and as such serve as a basis for investors’ assessments, potentially informing their decisions. SMEs would benefit from pooling the information they disclose at a one-stop shop: SMEs’ visibility would be increased and barriers to access capital reduced, overall ensuring and increasing their competitiveness. This could also serve as a starting point for the establishment of a European database for SME-research.

Q59.1 - Please explain your answer to question 59 and in particular if you believe preventing underpricing in research and amending rules on free trial periods of research are relevant:

Q60 - Do you consider that a program set up by a market operator to finance SME research would improve research coverage?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☒5 – Fully agree

☐Don’t know / no opinion / not relevant

Q60.1 - If you do consider that a program set up by a market operator to finance SME research would improve research coverage, please specify under which conditions such a program could be implemented:

This is, to a certain extent, already being done as some exchanges have launched programs to cover the costs of SME research coverage and the first results suggest that it can create additional liquidity for listed SMEs.

FESE sees merit in creating a pan-European program to finance SME research that would improve research coverage. Whilst we agree that a program set up by market operators to finance SME research would improve research coverage, FESE does not see benefits in one market operator setting up a pan-European programme to cover the costs of SME research coverage.

A pan-European program set up by several market operators would allow and provide flexibility to trading venues to solve their respective issuers’ research coverage issues, and meet their local investors’ demands, which differ in each of their respective local financial ecosystems. Such a program could also allow for the development of pan-European user-friendly platforms for analysts to share and submit their reports for retail investors, thereby increasing the visibility and coverage of EU SMEs which would in turn further incentivise intra-EU cross-border investments.

In line with the Commission’s priority to strengthen the Capital Markets Union, this pan-European program could also be part of the means dedicated to the private-public fund for SMEs’ IPOs. Both initiatives can be complemented to cover the costs of research coverage of newly listed SMEs. In effect, this would further incentivise SMEs to raise funds via the use of public capital markets in line with their respective financing strategy.

This program should be optional for market operators operating in the EU to set up and coordinate, based on the lessons learnt from their pilot programs. There should not be a mandatory requirement for market operators to do so.

It should be noted that market operators are currently facing regulatory burdens when distributing research reports originally provided by research firms for their listed SMEs. In addition to notification obligations with the NCAs, maintenance of insider lists and/or plausibility checks regarding the research reports can be a consequence of such distribution.

Q60.1 - Please explain your answer to question 60:

Q61 - If SME research were to be subsidised through a partially public funding program, can you please specify which market players (providers, SMEs, etc.) should benefit from such funding, under which form, and which criteria and conditions should apply to this program:

Research firms providing research coverage for SMEs and mid-caps listed on all trading venues could receive support from public funding. The research reports should satisfy certain criteria pre-developed by national or European associations for financial analysis. However, if public funds were directly distributed to the companies, the perception of conflict of interest that many investors have with the issuer-sponsored research would remain. Moreover, if funds were to be distributed directly to the research providers, it may be difficult to monitor that adequate resources are dedicated to produce good quality research and its right distribution.

An optimal solution would therefore be that market operators assume the task of distributing the subsidies from a pan-European public funding program among the best providers under the criteria stated by EFFAS or other European associations for financial analysis.

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Q62 - Do you agree that the use of artificial intelligence could help to foster the production of SME research?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☒4 – Rather agree
☐5 – Fully agree
☐Don't know / no opinion / not relevant

Q62.1 - If you agree, which recommendations would you make on the form that such use of artificial intelligence could take and do you see risks associated to the development of AI-generated research?

The use of artificial intelligence should be encouraged to help foster the production of SME research. However, this should be complemented by human-made research to meet market demand for qualitative investment research. The use of AI should not restrict the research analysts' access to pre-AI analysed figures or make it more difficult for them to form an assessment based on data that can be used or delivered by the technology. The research analysts' qualitative assessment of its investment research is what investors value most.

Q62.1 - Please explain your answer to question 62:

Q63 - Do you agree that the creation of a public EU-wide SME research database would facilitate access to research material on SMEs?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☒4 – Rather agree
☐5 – Fully agree
☐Don't know / no opinion / not relevant

Q63.1 - If you do agree that the creation of a public EU-wide SME research database would **facilitate access to research material on SMEs, please specify under which conditions this database should operate:**

FESE fully agrees that the creation of a public EU-wide SME research database would facilitate access to research material on SMEs, provided that it would not introduce additional cost or administrative burdens for listed companies covered. However, a public research database may not be perceived by professional investors as the most reliable source to work with as it would be completely different from the traditional sources of information they are used to that are all offered by the private sector.

Q63.1 - Please explain your answer to question 63:

Q64 - Do you agree that ESMA would be well placed to develop such a database?

☐ 1 – Disagree
☐ 2 – Rather not agree
☒ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree

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☐ Don’t know / no opinion / not relevant

Q64.1 - Please explain your answer to question 64:

FESE believes that ESMA could be well placed to develop and implement such a database to foster cross-border investments. However, there is a need to ensure that the creation of such a database would not introduce onerous or costly requirements for issuers.

Q65 - In your opinion, does issuer-sponsored research qualify as acceptable minor non-monetary benefit as defined by Article 12 of Delegated Directive (EU) 2017/593?

☐ 1 – Disagree
☐ 2 – Rather not agree
☒ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don’t know / no opinion / not relevant

Q65.1 - Please explain your answer to question 64:

This approach may increase the production of SME research but as this would be non-independent analysis, it may not be so attractive for the investors and not so effective in improving the liquidity.

Q66 - In your opinion, does issuer-sponsored research qualify as investment research as defined in Article 36 of Delegated Regulation (EU) 2017/565?

☐ 1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don’t know / no opinion / not relevant

Q66.1 - Please explain your answer to question 66:

Q67 - Do you consider that rules applicable to issuer-sponsored research should be amended?

☐ 1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don’t know / no opinion / not relevant

Q67.1 - If you do consider that rules applicable to issuer-sponsored research should be amended, please specify how:

Q67.1 - Please explain your answer to question 67:

Q68 - Considering the various policy options tested in questions 59 to 67, which would be most effective and have most impact to foster SME research?

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	1 (least effective)	2 (rather not effective)	3 (neutral)	4 (rather effective)	5 (most effective)	N.A.
Introduce a specific definition of research in MiFID level 1	X					
Authorise bundling for SME research exclusively					X	
Amend Article 13 of delegated Directive 2017/593 to exclude independent research providers' research from Article 13 of delegated Directive 2017 /593			X			
Prevent underpricing of research			X			
Amend rules on free trial periods of research			X			
Create a program to finance SME research set up by market operators				X		
Fund SME research partially with public money					X	
Promote research on SME produced by artificial intelligence				X		
Create an EU-wide database on SME research				X		

Amend rules on issuer-sponsored research				X		
Other						

Please specify which other policy option would be most needed and have most impact to foster SME research:

Q68.1 - Please explain your answer to question 68:

Authorising the bundling of SME research would be the fastest way to increase production and distribution of independent reports and may have the biggest effect on the liquidity of SME. At the same time, creating a program to finance the initiatives of independent research set up by market operators would help to incentivise more research providers' interest in this segment of companies and improve quality of the reports.

IV. Commodity markets

Q69 - Please specify to what extent you agree with the statements below regarding the experience with the implementation of the position limit framework and pre-trade transparency?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
The EU intervention been successful in achieving or progressing towards improving the functioning and transparency of commodity markets and address excessive commodity price volatility.	X					
The MiFID II/MiFIR costs and benefits with regard to commodity markets are balanced (in particular regarding the regulatory burden).		X				
The different components of the framework operate well together to achieve the improvement of the functioning and transparency of commodity markets and address excessive commodity price volatility.	X					
The improvement of the functioning and transparency of commodity markets and address excessive commodity price volatility correspond with the needs and problems in EU financial markets.	X					
The position limit framework and pre- trade transparency regime for commodity markets has provided EU added value.		X				

Q69.1 - Please provide both quantitative and qualitative elements to explain your answer and provide to the extent possible an estimation of the benefits and costs. Where possible, please provide figures broken down by categories such as IT, organisational arrangements, HR etc.

Quantitative elements for Q69.1:

	Estimate (in euro)
Benefits	
Costs	A medium-sized physical broker, with 20 employees, has to pay an average 150 000 – 200 000 EUR annual compliance cost, with a one-off IT cost of 100 000 EUR. This cost is probably significantly higher for clearing members. There are also examples of market members interested in the trading commodity derivatives who do not participate due to these high market-entry costs.

Qualitative elements for Q69.1:

FESE identified four main areas where negative consequences have materialised in terms of costs for European businesses and reduced economic activity, which may have resulted in a loss in tax revenues in Member States. Firstly, the position limits regime has a material negative effect on less liquid and small contracts and the ability of exchanges to develop new benchmark contracts in the EU. Secondly, it is hindering further growth and competition between trading venues within the EU trading commodity derivatives classified as liquid and which have the same physical underlying. Thirdly, the position limits regime results in significant costs in terms of lost opportunity when exchanges decide to launch contracts in other jurisdictions, which may otherwise be offered for trading inside the EU. Large exchange groups are active in multiple countries and can launch new contracts in varying locations depending on, amongst others, a favourable regulatory environment for commodity trading. Lastly, to remain competitive a substantial number of commodity derivative contracts has been transferred to other jurisdictions due to the restrictive nature of the MiFID II position limits regime.

FESE agrees with the overall objective of MiFID II/MiFIR to 'improve the functioning and transparency of commodity markets and address excessive commodity price volatility', but we feel these objectives have not materialised with the implementation of the position limits and pre-trade transparency regimes. The establishment of, and compliance with, MiFID II has proven to be a burdensome and costly process for both commodity derivatives exchanges and market participants. This is particularly true for the implementation of the large number of reporting and transparency requirements.

It is important to note that the position limit regime has been introduced to meet the MiFID II / MiFIR objective of improving 'the functioning and transparency of commodity markets', and that the implementation of appropriate management controls for trading venues to 'address the excessive commodity price volatility'.

'Excessive commodity price volatility' has been addressed in Art. 58 MiFID II on the position reporting regime, in which commodity contracts are subject to exchanges' pre-existing position monitoring and market oversight practices based on REMIT and MAR principles, to which the position limits regime offers little to no added value. Market operators possess the appropriate market supervisory tools to meet the MiFID II / MiFIR objective of addressing 'excessive commodity price volatility'.

While FESE believes the MiFID II position limits regime did not contribute to the prevention of market abuse, nor to the improvement of orderly pricing and settlement, we understand the view of policymakers that there might be a value in setting position limits to avoid excessive speculation adversely affecting prices. To achieve this objective - which

is identical to the objective of the US position limits regime - it is sufficient to consider only those contracts that are relevant for the price formation in the underlying commodities markets (i.e. mature products which serve as a benchmark for the respective market). New and nascent products constitute a minor share of commodity markets and are unlikely to influence price movements in the underlying physical markets, and thus cannot negatively impact consumers in any ways. Therefore, new and illiquid products should be outside the scope of the position limits regime. They would still remain subject to the position reporting regime under Art. 58 MiFID II, the pre-existing position monitoring and position management measures by exchanges and the market oversight practices of the exchanges' market supervision and market surveillance departments that apply the principles laid down in REMIT and MAR.
With regard to transparency, the MiFID II position reporting framework has strengthened transparency by requiring OTC reporting. However, this has increased administrative burdens and costs to market members (see above). Additionally, pre-negotiated transactions that are subsequently formalised on a trading venue, often on a regulated market, are very common in commodity markets. However, as currently designed, the pre-trade transparency regime reduces the ability for such a formalisation on a trading venue and clearing to mitigate counterparty risk. Therefore, the pre-trade transparency regime should be better tailored to commodity markets and allow for a more natural move to on venue trading and central clearing.

Q70 - Can you provide examples of the materiality of the above mentioned problem?

☒Yes, I can provide 1 or more example(s)
☐No, I cannot provide any example

Please provide example(s) of (nascent) contracts where the position limit regime has constrained the growth of the contract:
Underlying cause of the constraint (A/B/C)*:
*Note: 1 The underlying cause of the constraint is due to (A) the position limit becoming too restrictive as open interest increases, (B) an incorrect categorisation under the position limits framework or (C) the underlying physical markets are not efficiently reflected.

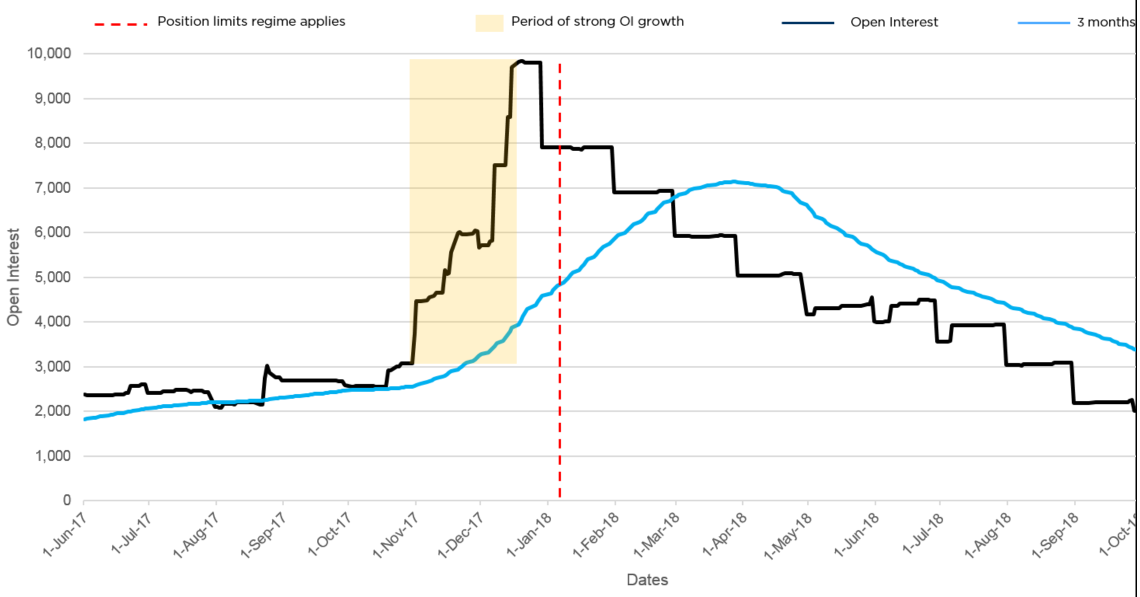
Cause A:

I) Contracts classified as 'illiquid' receive a standardised limit of 2,5k lots and get a highly restrictive limit when open interest (OI) increases close to 10k lots. Consequently, market participants are forced to decrease their positions and the OI returns to a lower level thereby sealing the illiquid status. NCAs can use different derogations for illiquid markets but are often not sufficient to mitigate the negative impact of low position limit (PL). Once the limit is reached, participants withdraw from the market, often switching to a trading outside of the MiFID II regime, thereby leaving no time to adjust the limit upwards. In new contracts, often only one participant sits on the buy or sell side. In such cases, a 50% limit is not sufficient. Therefore, the limit under the available derogation should be raised to provide sufficient relief to market participants close to the limits. It is our understanding that a market participants consider that an 'illiquid' OI contract is composed of 25k lots on average (see also cause B).

Cause B:

II) For a limit not to impede the development of fast-growing markets, the PL should be adjusted to a workable level, before it becomes unnecessarily restrictive. Therefore, the calculation of OI in a market for the purpose of setting a PL needs to adequately capture the period of growth of OI. In practice, this is not feasible.

Please see Annex I for an example of *ICE Endex Italian PSV Gas Futures* (previously fast-growing markets).



Cause C:
III) Since the application of the regime, growing liquidity in liquid competing contracts traded on different venues with the same physical underlying has proven more difficult than in trading venues on which the benchmark contracts are traded. This is due to higher position limits set in 'other months' for the benchmark contracts than for contracts listed on a second or third largest exchange. It is important to create a level playing field for competing contracts classified as liquid. When position limits are materially different, there is a risk that traders will look to trade only on the largest market, where they have a lower risk of breaching the position limit. This is the case, for instance, of the German power contract listed by Nasdaq and by EEX, where the OI is substantially larger in the latter.
IV) The current definition of 'same contract' is unfit and contributes to the problem described under III. Therefore, we agree with the proposal to delete the concept of 'same contract' and replace it with a more pragmatic approach between CAs. Please also see our response to Q71 for details.
Cause D:
V) For some 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. However, it often occurs that such a number cannot be traded without exceeding the limit. Under the current MiFID II provisions, the limit cannot be raised without sufficient increase of the OI as the regime does not allow a forward-looking approach to determine the OI on which the PL should have been set which would risk the market participants to back out entirely form the trade to avoid breaching the limits and, preventing a rise in OI and subsequent raising of the said limits.
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 6k lots. The contract is a Suezmax crude route, West Africa to UK Continent for tankers sized on average 130k MT (DWT). The biggest positions exceeding 1.9k lots are held by traders, some of which are located outside of the EU and do not hold hedging exemptions. Companies with Suezmax tankers fleets tend to hedge calendar years forward, fleet sizes up to 20 tankers and above.

To hedge a fleet of 10 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 = 15,6k lots** to hedge freight rates exposure for a single Calendar year 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 above, with potential volumes of 46,8k lots.

Size of the OTC space the contract(s) is/are trying to enter (in €):

Market share the nascent contract(s) is/are expected to gain (in %):

Contract(s) is/are euro denominated?

We welcome the recognition by the European Commission of the impact of European commodity markets in strengthening the role of the Euro and Euro-denominated instruments. For promoting new illiquid contracts and fostering liquidity in liquid contracts that are already denominated in Euro, it is key that the Eurozone as such is attractive for market participants and its regulatory framework is fit for purpose. At the moment, the framework rather weakens competitiveness of European commodity markets vis-à-vis global markets. More proportionate and efficient position limits and pre-trade transparency regimes would contribute significantly to the European Commission's objective to strengthen the competitiveness of European commodity derivatives markets in the context of the international role of the Euro.

Q71 - Please indicate the scope you consider most appropriate for the position limit regime:

	1 (most appropriate)	2 (neutral)	3 (least appropriate)	N.A.
Current scope			X	
A designated list of 'critical' contracts similar to the US regime	X			
Other				

Please specify what other scope you consider most appropriate for the position limit regime:

The MiFID II position limits regime has been able to function for a number of well-developed benchmark contracts. These highly developed benchmark contracts are characterised by a large number of different types of active trading firms and an overall substantial amount of open interest. However, for the development of new and illiquid products and further growth of the existing non-benchmark liquid commodity derivative markets, the position limits regime has proven to be a substantial barrier. Fast growing markets in particular have suffered from (1) an increasingly restrictive limit as open

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interest increases and (2) inflexible treatment in terms of their categorisation under the position limits framework. Moreover, for some commodity markets (3) the underlying physical markets is inaccurately reflected.
Furthermore, in cases of competing contracts, there is one contract listed by a given trading venue which is considered as a benchmark contract, while another contract with the same underlying listed by a competing less liquid venue suffers from the current restraining effect of the position limits regime. The benchmark contracts with the highest open interest benefits from the highest position limit and therefore an additional incentive is offered to market participants for trading on the already most liquid market to the detriment of less liquid venues.
The above-mentioned inherent flaws in the position limits framework do not occur when the regime is applied to highly liquid benchmark contracts only, as these types of contracts are characterised by high levels of open interest and normally do not require more urgent updates to their classification or position limits.
FESE therefore believes that moving to a limited scope of application to 'critical' contracts only is the most pragmatic solution to deal with this problem of fair competition.
However, as any policy process involving a fundamental Level 1 would require years to become effective, FESE welcomes ESMA's statement that some amendments to the Level 2 rules on position limits may be appropriate in the meantime. In particular, to prevent any negative consequences for new, illiquid as well as (non-benchmark) liquid markets FESE recommends that Level 2 is amended immediately while a more fundamental reform is dealt with as part of the Level 1 Review. Should limiting the scope of application to 'critical' contracts not be possible for some reason, or should there nevertheless be a situation in which two contracts with the same physical underlying are deemed critical, we believe the same position limit should be set on commodity derivatives classified as liquid market with the same physical underlying to remove barriers to competition. In line with ESMA's recommendation in its recent review report to allow for a more pragmatic approach and deleting the concept of 'same contracts', the open interest figure which serves as a basis for setting the other months limit should be provided by the trading venue with the highest average open interest over a certain period, i.e. one year. Thereby, the position limit of the most liquid commodity derivative should be applied identically to competing contracts that are deemed liquid and have the same physical underlying. Such an approach would prevent any discriminatory outcomes of the MiFID II position limits regime towards trading venues with less open interest in a contract with the same physical underlying as a contract listed by another trading venue.

Q71.1 - Please explain your answer to question 71:

To avoid hindering the development and growth of new illiquid products, as well as the on-venue trading of liquid commodity derivatives, a proportionate and efficient position limits regime should concentrate on a limited number of benchmark contracts, as per the US regime. This view is also shared by ESMA which, in its recent report, cites '*the scope of position limits should be limited to commodity derivatives where position limits can play of valuable role, i.e. to well-developed critical contracts where price formation takes place and that have a role in the pricing of the underlying commodity and other related commodity derivatives*.' This would prevent any excessive speculation which may negatively impact global retail prices, while allowing new, nascent and liquid competing products, notably Euro-denominated, to develop. Furthermore, in order to prevent market squeezes, it would be sufficient to set limits for the period right before expiry rather than covering the entire maturity curve.
By considering only those contracts that are relevant for the price formation in the underlying commodity, excessive speculation, which might adversely affect prices, will be avoided (this is also the objective of the US regime and outlined in Q69.1). In this regard, it should be noted that the MiFID II position limits regime did not contribute to the

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prevention of market abuse (as detailed in the FESE response to the ESMA Call for Evidence on this topic), nor to the improvement of orderly pricing and settlement.
When creating a designated list of 'critical' contracts, similar to the US regime, the Commission should identify these contracts based on their nature as benchmark for the underlying products' markets, rather than determining the categorisation solely on measuring their liquidity or volatility.
The EU 'critical' contracts should be similar to the 'core referenced futures contracts' that are identified in the US regime by their respective underlying commodity that are considered as important and strategic for the EU internal market. FESE believes that the Commission should propose criteria to identify these 'critical' commodities, as specified in our response in Q72 and Q72.1, and consult all relevant actors in the identified commodities' value chain.
Having said this, we believe that there is an urgent need to limit the negative impact the position limits regime in its current form has on new nascent and liquid competing contracts. For this, we recommend a two-tier approach whereby Level 2 is amended immediately by ESMA, while the more fundamental reform at Level 1 is dealt with as part of this review.
This means that non-critical contracts would be outside the scope of a position limit regime. However non-critical contracts would remain subject to the position reporting regime under Art. 58 MiFID II, the pre-existing position monitoring and position management measures by exchanges and the market oversight practices of the exchanges' market supervision and market surveillance departments that apply the principles laid down in REMIT and MAR. Thus, removing position limits for such contracts would not pose any risk to the transparency and functioning of the respective markets. On the contrary, attracting more volume to regulated venues would contribute to a more transparent trading environment.

Q72 - If you believe there is a need to change the scope along a designated list of 'critical' contracts similar to the US regime, please specify which of the following criteria could be used.
For each of these criteria, please specify the appropriate threshold and how many contracts would be designated 'critical'.

☒Open interest
☐Type and variety of participants
☒Other criterion:
☐There is no need to change the scope

Open interest:
Threshold for open interest:

We recommend a contract should have at least 300,000 lots of open interest on average over a year to qualify as 'critical'.

Number of affected contracts in the EU for open interest:

This approach would produce an outcome broadly comparable with the US regime for position limits, whereby we expect around 20 commodity derivative contracts offered for trading in Europe to be classed as critical.

Please explain why you consider that the open interest is a criterion that could be used:

Exchanges use various criteria to assess the liquidity of a market. They include, inter alia, open interest, share of open interest versus deliverable supply, number of active trading participants, churn ratio (for physically settled contracts), share of screen execution and average trading horizon. These parameters are highly correlated with the open interest.

Thus, for identifying the EU's 'core referenced futures contracts' and provide for a transparent and simple methodology that would be easy to administer, we suggest that the average yearly open interest is sufficient to determine whether a contract qualifies as a 'critical' or not, and as a second step, assess the 'critical nature' of these highly liquid contracts and set bespoke limits based on a deeper market understanding. As highlighted above, based on these criteria to determine which market should be considered mature and developed, FESE recommends that a contract should have at least 300,000 lots of open interest on average over a year to qualify as 'critical'. Should a limitation to critical contracts not be possible, as mentioned in Q71 the open interest figure should be provided by the trading venue with the highest open interest. The position limit of the most liquid commodity derivative contract should be applied identically to competing contracts that are deemed liquid and have the same physical underlying.

Type and variety of participants:

Threshold for the type and variety of participants:

FESE prefers the usage of open interest for classifying contracts as 'critical'.

Number of affected contracts in the EU for the type and variety of participants:

Please see below.

Please explain why you consider that the type and variety of participants is a criterion that could be used:

We recommend that this criterion is not considered as it is normally highly correlated with open interest. By not using this criterion, the regime would be simpler and more transparent. However, should policymakers wish to take it into account, we recommend that the definition of 'market participants' is further detailed and clarified. For simplicity, we would suggest to align the definition with the one used for the purposes of Art. 58 MiFID II.

Other criterion:

Please specify what other criterion could be used and explain your answer:

As stated in our answer to Q71.1, the Commission should propose a set of criteria to identify the 'critical' commodities that would act as an underlying to the 'critical' commodity contracts. The EU 'critical' contracts should be 'core referenced futures contracts' that are identified by their respective underlying commodity that are considered as important and strategic for the EU internal market. FESE believes that the Commission should propose criteria to identify these 'critical' commodities and consult all relevant actors in the identified commodities' value chain.

Threshold for this other criterion:

Number of affected contracts in the EU for this other criterion:

Q72.1 - Please explain your answer to question 72:

As specified above, open interest serves as most important indicator to determine whether an instrument is highly liquid and mature. When assessed in function of the market reality, it shows the potential of instruments to serve as a benchmark contract for the underlying commodity.

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ESMA rightly points out in the Review Report that, in a post-Brexit environment, a more limited amount of benchmark commodity derivatives contracts resides in the Union. However, we want to urge the Commission to refrain from artificially classifying contracts as critical. This would hinder the development of non-critical contracts in the European Union and thereby undermining the Commission's ambitions in context of the international role of the Euro to establish competitive EU commodity derivatives markets. A reduced scope to genuine 'critical' mature contracts, identified by using 300,000 lots open interest as a reference, would allow Euro-denominated commodity derivatives contracts to develop into European, and global, benchmark contracts.

In case the Commission intends to further specify and/or include additional criteria, we believe taking a two-tier approach would be most appropriate. The open interest figure on average over one year should hereby serve as a strict minimum threshold to qualify contracts to the regime. This gives NCAs and ESMA the opportunity to, as a second step, assess the 'critical nature' of these highly liquid contracts and set bespoke limits based on a deeper market understanding. This was previously impossible due to the enormous number of contracts for which limits need to be defined. Such approach ensures that only the mature products that are able to function well under the position limits regime receive an appropriate limit and 'critical' status, while nascent contracts are given the opportunity to further develop.

This determination should take into account whether the price signal of a 'critical' contract is broadly recognised in the wider market as a relevant benchmark price for its underlying commodity. Thereby, it is particularly important to consider the existence of non-EU commodity derivatives markets with the same underlying commodity. If a market has developed elsewhere on the same commodity markets, there is a risk that the non-EU market attracts the liquidity that exists in the EU markets.

We appreciate ESMA's recommendation in the Review Report that further work and consultation will need to be undertaken. This will allow for more timely adjustments as required by market developments. For this, it is of utmost importance that ESMA consults all relevant actors in the identified commodities' value chain.

Q73 - Do you agree that there is a need to foster convergence in how position management controls are implemented?

☐ 1 – Disagree
x 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q73.1 - Please explain your answer to question 73:

FESE commodity exchanges have extensive experience with operating an internal position management system and are committed to the highest standards to ensure fair and orderly trading. Exchanges' market monitoring and surveillance departments ensure compliance with all other relevant requirements under MiFID II/MiFIR, MAR and REMIT where applicable, as acknowledged by ESMA.

These regimes generally include:

1. Accountability levels above which members are required to report certain information to the exchange (e.g. their positions in a specific contract and the beneficiaries thereof);
2. Position, expiry and delivery limits indicating the maximum positions that can be held by members in a specific contract at a given time;
3. Exchange rules providing powers to the exchange to:

- Request information from members as to the purpose of the positions they hold in a specific contract;
- Order members to decrease their position;
- Discipline members that do not comply with the above.

Furthermore, these regimes would be operated by compliance teams with sufficient staff and technologically advanced tools to monitor, on a daily basis, the open interest in contracts admitted to trading, the positions held in those contracts by exchange members and the activity in physical markets underlying the commodity derivatives admitted to trading.

For example, the compliance team monitoring positions in a crude oil contract may compare these positions with the activity in the underlying physical market and the direction of travel of oil barges in the relevant geographical area. If these movements are not coherent with positions held or if the positions are considered excessive given the activity in the underlying market, the compliance team may decide to open an inquiry with regard to the entered positions and take further action if the response is not satisfactory.

These position management regimes are cautiously calibrated and tailored to the circumstances of each individual exchange such as the nature of its membership and the characteristics and underlying markets of contracts it admits to trading. There is no 'one size fits all' position management regime.

All FESE Members, except one, are convinced that it is essential to allow enough flexibility to exchanges for the design of the position management regimes.

Q74 – For which contracts would you consider a position limit exemption for a financial counterparty under mandatory liquidity provision obligations?
This exemption would mirror the exclusion of the related transactions from the ancillary activity test.

	Yes	No	N.A.
Nascent	X		
Illiquid	X		
Other	X		

Please specify for which other contracts you would consider a position limit exemption for a financial counterparty under mandatory liquidity provision obligations:

Securitised derivatives and cash-settled derivatives on broad based indices composed of commodities related items.

Q74.1 – Please explain your answer to question 74:

The exemption is needed for both liquid contracts and contracts that need financial or non-financial entities to incentivise trading in the contract, at least if the position limit regime continues to include the restrictive 2,500 lots limit on new and illiquid contracts. If no such exemption is available and the 2,500 lots limit continues to apply, exchanges have to contract a 'panel' of liquidity providers to ensure that none of these firms exceed

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this limit. In nascent markets, it is highly possible that there may not be the required number of counterparties to build such a 'panel' and even where this is the case, it adds significant costs for the exchange.
In order to avoid such a situation, FESE recommends that the position limits regime includes such an exemption based on the same conditions as the liquidity provision exemption outlined in Art. 2(4) MiFID II and the related ESMA Q&A, and implemented similarly to the hedging exemption under the position limit regime.
Furthermore, we believe that the current position limit framework fails to recognise the unique characteristics of securitised derivatives and it is not an appropriate tool for preventing market abuse and ensuring orderly pricing and settlement conditions in those instruments.

As opposed to commodity derivative contracts, securitised derivatives based on commodities are transferable securities. The commodity securitised derivatives market is characterised by a large number of different issuances, each one registered within the CSD for a specific size and any possible increase follows a specific procedure duly approved by the relevant NCA. This contrasts with standard commodity derivatives where the amount of open interest, and thereby the size of a position, is potentially unlimited. It is also worth noting that, at the time of issue, the issuer or the intermediary in charge of the distribution of the issuance holds 100% of the issue, which challenges the very application of a position limit regime. In addition, most securitised derivatives are ultimately held by a large number of retail investors, which does not raise the same risk of abusing a dominant position or to orderly pricing and settlement conditions as for ordinary commodity derivative contracts. It is also worth noting that securitised derivatives are very similar to Exchange Traded Commodities (ETCs), which are classified as debt instruments and do not fall under the position limit regime. Contracts for differences (CFDs) based on commodities are not classified either as commodity derivatives and fall outside the scope of the regime as well. Moreover, the notion of spot month and other months, for which position limits are to be set under Art. 57(3) MiFID II, is not applicable to securitised derivatives. The concept of open interest is not well suited to those instruments.
As indicated by ESMA in its recent Review Report, securitised derivatives should be excluded from the scope of the position limit and position reporting regime to ensure a more consistent approach of instruments sharing similar characteristics under MiFID II.
Further, FESE strongly recommends to exclude cash-settled derivatives on broad-based indices composed of commodities related items from the regime. As stated in our responses to ESMA's Call for Evidence and Consultation, we believe these products are wrongly captured by the regime which has been introduced with the policy objective to avoid market abuse and ensure orderly pricing and settlement in the commodities derivatives market. However, rather exchanges' market oversight systems, including compliance, supervision and surveillance activities, have proven to effectively prevent market abuse and ensure orderly pricing and delivery, while allowing new and illiquid products to develop.
Especially for cash-settled derivatives on broad-based commodities index underlyings, it does not seem reasonable to have an additional limit on the index derivatives, as the individual components are already under position limit regime on the exchanges where these are traded. Moreover, these contracts are cash-settled, and it is not possible to squeeze (corner) a market link in a physically-delivered derivatives contract. While acknowledging that regulators might be concerned that the exclusion from the scope might open opportunity for loopholes, we suggest that product design and mechanisms of derivatives on broad-based commodity indices - already fulfilling the objectives of the regime - should be taken into consideration. The position limits regime does not provide a reasonable measure for increasing market integrity but impairs the growth of and demotivates clients' flow to shift to transparent and electronically traded markets. It also limits the capability of liquidity providers to fulfil their role and comply with the

regulatory requirements, as these are stemming from a mis-categorisation into the scope of the regime.

Q75 - For which counterparty do you consider a hedging exemption appropriate in relation to positions which are objectively measurable as reducing risks?

	Yes	No	N. A.
A financial counterparty belonging to a predominantly commercial group that hedges positions held by a non-financial entity belonging to the same group	X		
A financial counterparty	X		
Other			

Please specify for other which counterparties you consider a hedging exemption appropriate:

All commodity markets participants, including financial counterparties.

Q75.1 - Please explain your answer to question 75:

Whilst the position limits regime includes exemptions for market participants pursuing hedging activity, the MiFID II definition of *hedging* as set out in RTS 20 is clear that only non-financial entities can engage in such activity, thereby rendering the exemption unviable to investment banks or commodity trading houses which both play a vital role in providing smaller commercial players with access to commodity derivatives markets.
For that reason, the hedging exemption cannot be considered a universal solution to inappropriately designed pre-trade transparency regime or disproportionate position limits.
Figure 1 illustrates the negative impact of the 2,500 lots limit in combination with the lack of hedging exemption possibilities for financial counterparties on the Gas Czech Virtual Trading Point, CZ VTP, and Zeebrugge Trading Point (ZTP) gas future markets. Both markets took off in the course of 2018, but then declined when the 2,500 lots limit became too restrictive. With only 10 to 12 market participants registered to trading and only 1 or 2 very active market participants being responsible for most of the volumes – an absolutely normal situation for a new contract - the position limit put a halt to the further development of the contract. Important participants in this example are investment firms, trading gas derivatives to hedge its retail activity. However, because of its classification as investment firm, they have no other option than to stop trading and look for other hedging alternatives.

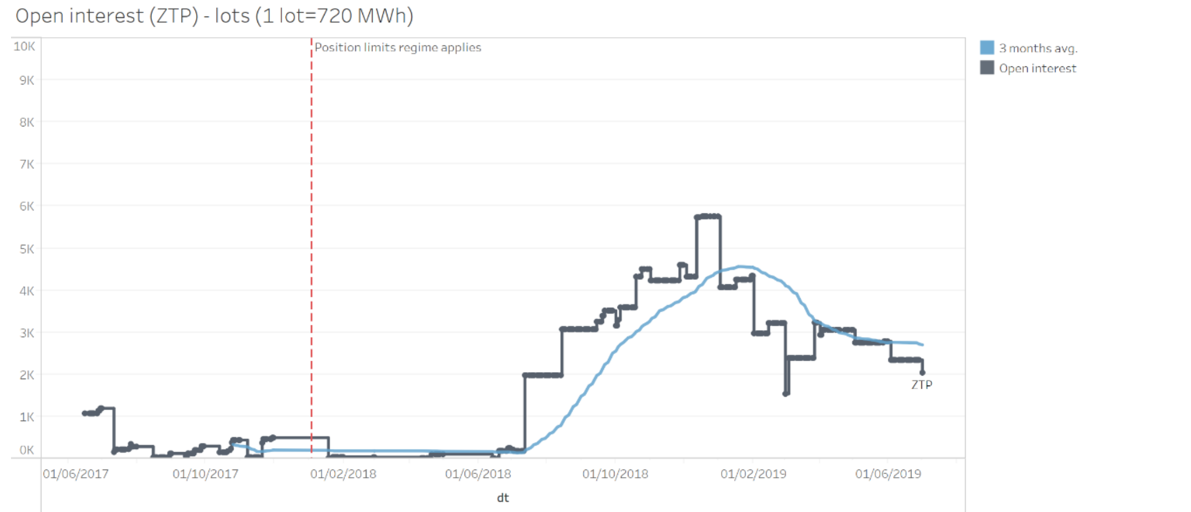

Figure 1 Impact of the position limits regime and restricted use of hedging exemption for financial counterparties on the development of PEGAS ZTP gas futures market

We believe a system, inclusive of financial counterparties, could be operated by financial regulators across the EU all the more given the amount of information they receive about the activities of such entities.

Q76 - Do you consider that pre-trade transparency for commodity derivatives functions well?

- ☐ 1 – Disagree
- X 2 – Rather not agree
- ☐ 3 - Neutral
- ☐ 4 – Rather agree
- ☐ 5 – Fully agree
- ☐ Don’t know / no opinion / not relevant

If you do not consider that pre-trade transparency for commodity derivatives functions well, please (1) provide examples of markets where the pre-trade transparency regime has constrained the offering of niche instruments or the development of new and/or fast moving markets, and (2) present possible solutions including, where possible, quantitative elements:

FESE fully agrees with the objectives of MiFID II/MiFIR to ‘*improve the functioning and transparency of financial and commodity markets and address excessive commodity price volatility*’. While we support the aim of the pre-trade transparency regime, we believe the current calibration hampers a substantial increase in commodity contracts traded on exchanges and cleared through CCPs, hence being subject to a sufficient level of security and transparency. A number of relatively illiquid products, in their development phase, have been wrongly classified as liquid and made subject to excessive LIS thresholds. Therefore, FESE recommends that both Level 1 and Level 2 provisions are revised.
The hedging exemption available in Art. 8(1) MiFIR is extended on Level 1 to cover all market participants managing risks arising from activity in the physical market, including financial counterparties. This would allow the building of liquidity in the order book to continue without jeopardising the ability of commodity derivatives markets to fulfil their function.
Such change should be combined with amendments to the methodology in RTS 2 to address the inappropriate thresholds.

1) Exclusion of price factor from the calculation of IL and LIS thresholds

The inclusion of price in the calculation of LIS and IL threshold values can lead to misinterpretations and confusion when measuring liquidity in instruments that are not natively defined in notional value. This can result in situations where price movements may:

- Occur in the same direction as changes in liquidity and exaggerate the liquidity changes;
- Occur in the opposite direction and mute the change in liquidity; and
- Without a change in liquidity make liquidity appear more volatile than it actually is. Liquidity should therefore not be measured by using the notional value of transactions.

Applying notional value as per, for example, the ADNA across all asset classes is likely to introduce a significant amount of 'noise' to an analysis of market liquidity. Moreover, market players typically hedge their production and consumption in trading in lots and not in notional value. Thus, we recommend that any liquidity analysis is normalised to a base quantity unit that is native to the asset class. For commodities, this will typically be a specific unit of measure (e.g. barrels, tons, MW).

2) Sufficiently high daily number of trades for a market to be liquid

In order for a market to be considered liquid, a sufficiently high number of trades should be executed on each trading day. We recommend that the threshold should be set at the median of 100 transactions per day instead of the current average of 10. Considering the fact that liquidity is the ability to find a counterparty in a relatively short period of time within a given trading day, a threshold of 100 trades per day has the practical implication that it represents an average of approximately 1 trade every 5 minutes on an 8-hour trading day. In contrast, a threshold of 10 trades represents just 1.25 trades per hour. For the same reason, a median is proposed as the minimum instead of a mean which can be an alternate view of the sum count of trades per year.

3) Trade frequency and standard size as liquidity indicators

Consider two instruments: Instrument 1 is traded on average once per day for 100k units and Instrument 2 is traded on average 10k times per day for 10 units. In both cases, the average volume will be 100k units per day. However, it would be very difficult to categorise Instrument 1 as liquid, whereas Instrument 2 can be considered very liquid for trade volumes of approx. 10 units. We therefore recommend that trade frequency and standard size, excluding unrelated vectors such as price and currency, are both measured to determine liquidity.

4) Counterintuitive effects of a percentile-based approach

A percentile-based approach can lead to significant counterintuitive effects, which is important to keep in mind when setting LIS thresholds. Any approach similar to the existing one using a central or percentile-based measure will result in:

- A low standard size (SS) for the high liquidity instrument;
- A high SS for the low liquidity instrument;
- A low LIS for the high liquidity instrument;
- A high LIS for the low liquidity instrument.

These results are counterintuitive and imply that the instrument with lower liquidity can support higher LIS levels than the high-liquidity instrument – when the opposite is true. While the low liquidity instruments typically trade in a higher size, the overall size of this market and trade frequency is dwarfed by the higher liquidity of the market. Setting a low LIS for high liquidity markets and a high LIS for low liquidity markets based on the standard trade size in either mean, median or mode terms is detrimental for the development of low liquidity markets. There is a clear need for a more tailored approach based on variations in distribution.

Q76.1 - Please explain your answer to question 76:

In sum, the pre-trade transparency regime could better take into account the fact that non-equity markets are fundamentally different from equity markets, and that there are significant differences across the underlying non-equity markets themselves. It is, for example, important to understand that commodity markets have specific characteristics

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and hence often suffer from a "one-size-fits-all" regulatory approach. Therefore, against the background of this targeted MiFID II/MiFIR review, we believe that transparency requirements need to be balanced and could benefit from a more tailored approach to commodity markets.

MiFIR rightly recognises that certain exemptions can be granted to trading venues from the general requirement to publish pre-trade transparency data to preserve orderly price discovery processes and allow in particular illiquid and nascent markets to develop. Though the current shortcomings of the regime have sometimes prevented market participants from moving to transparent and regulated venues and central clearing. The new methodology has led to 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 calculation methods of the LIS and IL markets waiver are based on insufficiently granular sub-asset classes as well as arbitrarily selected parameters, which resulted in disproportionately low LIS thresholds for highly liquid products and overly high thresholds for illiquid ones. The regime has proven to be ill-calibrated, for example options are often less liquid than futures, yet equity options are generally classified as liquid, which does not reflect market reality. Counterintuitively, the LIS for benchmark products is now lower under MiFID II /R than what it was under pre-MiFID regimes imposed by trading venues themselves.

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.

For commodity derivatives, trading venues and market participants are also challenged by the fact that the LIS thresholds are set in Euros instead of lots. Pre-MiFIR, lots were the standard in the market for similar threshold calculations. Using historical Euro trade values to determine the LIS thresholds - and not the number of traded lots in a particular sub-asset class - can create unintended and disproportionate LIS thresholds that ignore the actual underlying trading behaviour.

It should be noted that, compared to other financial instruments, commodity derivatives instruments are generally less liquid. In order to achieve execution, market participants often trade via brokers organising transaction through a pre-executed agreement, subject to and executed under the rules of a specific exchange with immediate clearing at the exchanges' respective central counterparty (CCP), rather than in a central order book where a satisfactory execution would be less likely. Trades are concluded outside the regulated venues, according to exchange rules of the trading venue, subject to being registered and cleared in a dedicated venue/clearing house, to ensure maximum transparency for these nascent markets. These pre-arranged transactions are often catalysts for volume in the lit order book, especially the case for energy markets. For instance, calculations done in the electricity derivatives space clearly show that the size of the pre-arranged trades are on average slightly above the average of the order book and that the majority of both pre-arranged and order book transactions in nominal value are often below the predetermined LIS minimum floor.

Lastly, another issue concerns trade registration which has been and still is essential to bring more volumes to the cleared market under the exchange rules. FESE considers that the current pre-trade transparency regime is not fit for purpose and cannot be applied to trade registration facilities in energy derivatives markets without compromising their vital role in supporting the hedging activity of commercial market participants and in mitigating wider systemic risks.

We believe that a better tailored transparency regime based on specific changes on Level 1 and Level 2 as outlined in our response to Q76 would help promote and foster EU commodity markets, notably regarding energy markets denominated in Euro, and contribute to the international role of the Euro.

PART TWO: AREAS IDENTIFIED AS NON-PRIORITY FOR THE REVIEW

V. Derivatives Trading Obligation

Q77 - To what extent do you agree with the statements below regarding the experience with the implementation of the derivatives trading obligation?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N.A.
The EU intervention been successful in achieving or progressing towards more transparency and competition in trading of instruments subject to the DTO.						
The MiFID II/MiFIR costs and benefits with regard to the DTO are balanced (in particular regarding the regulatory burden).						
The different components of the framework operate well together to achieve more transparency and competition in trading of instruments subject to the DTO.						
More transparency and competition in trading of instruments subject to the DTO corresponds with the needs and problems in EU financial markets.						
The DTO has provided EU added value.						

Q77.1 - Please provide both quantitative and qualitative elements to explain your answer and provide to the extent possible an estimation of the benefits and costs. Where possible, please provide figures broken down by categories such as IT, organisational arrangements, HR etc.

Quantitative elements for Q77.1:

	Estimate (in euro)
Benefits	
Costs	

Qualitative elements for Q77.1:

Q78 - Do you believe that some adjustments to the DTO regime should be introduced, in particular having regards to EU and non-EU market making activities of investment firms?

☐ 1 - Disagree
☐ 2 - Rather not agree
☐ 3 - Neutral
☐ 4 - Rather agree
☐ 5 - Fully agree
☐ Don't know / no opinion / not relevant

If you do believe that some adjustments to the DTO regime should be introduced, please explain which adjustments would be needed and with which degree of urgency:

Q78.1 - Please explain your answer to question 78:

Q79 - Do you agree that the current scope of the DTO is appropriate?

☐ 1 - Disagree
☐ 2 - Rather not agree
☐ 3 - Neutral
☐ 4 - Rather agree
☐ 5 - Fully agree
☐ Don't know / no opinion / not relevant

Q79.1 - Please explain your answer to question 79:

Q80 - Do you agree that there is a need to adjust the DTO regime to align it with the EMIR Refit changes with regard to the clearing obligation for small financial counterparties and non-financial counterparties?

☐ 1 - Disagree
☐ 2 - Rather not agree
☐ 3 - Neutral
☐ 4 - Rather agree

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☐ 5 – Fully agree
☐ Don’t know / no opinion / not relevant

Q80.1 - Please explain your answer to question 80:

VI. Multilateral systems

Q81: Do you consider that the concept of multilateral system under MiFID II/MiFIR is uniformly understood (at EU or at national level) and ensures a level playing field between the different categories of market players?

☐ 1 - Disagree
☒ 2 - Rather not agree
☐ 3 - Neutral
☐ 4 - Rather agree
☐ 5 - Fully agree
☐ Don't know / no opinion / not relevant

Q81.1: If your response to question 81 is rather positive, please also indicate if, in your opinion, the current definition of multilateral system is adequately reflecting the actual functioning of the market:
N.A.

Question 81.1 If your response to question 81 is rather negative, please indicate which amendments you would suggest and why:

FESE does not agree that the concept of multilateral system under MiFID II/MiFIR is uniformly understood and does not believe there is a level playing field between the different categories of market players.

This question should be placed in the context of the objective of MiFID II/MiFIR and the problems that arise when the distinction between purely bilateral and hybrid multilateral trading is blurred. Indeed, the objective of MiFID II/MiFIR was to bring OTC multilateral trading (i.e. broker crossing networks or BCNs) to lit multilateral trading venues (i.e. RM and MTFs) in an attempt to increase transparency and improve price formation and investor protection. However, the market share of continuous lit order books is decreasing while the combined share of OTC and SI trading keeps growing. The aggregated levels of OTC and SI trading in terms of turnover represent 22% and 18% respectively for 2019 based on STOXX 600 data from Big xyt. This has led to increased complexity and opacity of equity markets with further fragmentation of liquidity – in stark contrast with the spirit of MiFID II/MiFIR.

While SIs are regulated under MiFID II as execution venues providing bilateral trading, they provide less transparency than on-exchange trading. This can be problematic when the distinction between purely bilateral and hybrid multilateral trading is blurred. In theory, every trade in an SI must take place against the proprietary account of the operator. SIs are prohibited, when dealing on their own account, from entering into matching arrangements with entities outside their group with the objective of carrying out *de facto* riskless back-to-back transactions in financial instruments outside trading venues. However, some investment firms seem to have developed models by which third party trading firms are able to provide liquidity to the customers of SIs.

VII. Double Volume Cap

Q82: Please specify to what extent you agree with the statements below regarding the experience with the implementation of the Double Volume Cap?

	1 (disagree)	2 (rather not agree)	3 (neutral)	4 (rather agree)	5 (fully agree)	N. A.
The EU intervention been successful in achieving or progressing towards the objective of more transparency in share trading.		x				
The MiFID II/MiFIR costs and benefits are balanced (in particular regarding the regulatory burden).	x					
The different components of the framework operate well together to achieve more transparency in share trading.		x				
More transparency in share trading correspond with the needs and problems in EU financial markets.				x		
The DVC has provided EU added value		x				

Q82.1: Please provide both quantitative and qualitative elements to explain your answer and provide to the extent possible an estimation of the benefits and costs. Where possible, please provide figures broken down by categories such as IT, organisational arrangements, HR etc.

The double volume cap (DVC) was designed to limit the trading taking place under the RP waiver, provided in Art. 4(1)(a) of MiFIR, and the NT waiver for liquid instruments, set out in Art. 4(1)(b)(i)) of MiFIR. Whilst it is possible to see some positive effects of the DVC, market liquidity has only benefited from the DVC to a limited extent. When assessing the DVC's capacity to limit dark trading, it is important that the benefits of such a mechanism are balanced against the high complexity of the DVC system.

For this reason, FESE is calling to limit the available waivers under the transparency regime to the LIS and OMF waivers. In this case, the DVC mechanism would be rendered obsolete at the NT and the RP waivers would not exist anymore. The repeal of those waivers to mainly keep the LIS waiver is part of a broader simplified market structure where the LIS threshold

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is used as the main tool to delineate lit and dark trading. Because the main purpose of the waiver regime is to protect market participants from adverse market movements following the execution of large orders, there seems to be little justification for trading small orders via the RP or NT waivers, which is largely the case currently. Using the LIS threshold to delineate dark trading would be an efficient way to incentivise lit trading and address concerns about the impact of dark trading on financial markets and the price formation process all the while contributing to a much-needed simplification of the current framework. In addition, it makes sense to maintain the OMF waiver as an order in an OMF facility ultimately becomes pre-trade transparent and therefore contributes to the price formation process.

However, it would still be important to allow for non-price forming technical trades to be reported off-book on exchange. FESE therefore calls for such a reporting tool to be defined at Level 1.

Overall, quality and consistency of reporting and flagging are necessary in order to improve transparency available to market participants. Against this background, FESE calls for an extension of the Market Model Typology (MMT) to a full range of market participants and sees merit in looking at how the technical implementation of MMT could be done under the governance of ESMA.

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VIII. Non-discriminatory access

Q83 - Do you see any particular operational or technical issues in applying open access requirements which should be addressed?

☒Yes
☐No
☐Don't know / no opinion / not relevant

Q83.1 - If you do see any particular operational or technical issues in applying open access requirements which should be addressed, please specify for which financial instrument(s) this would apply and explain your reasoning:

The 'Non-discriminatory' access (NDA) provisions for ETDs would potentially constitute a serious risk to the EU27 financial stability and competitiveness as they would:

1. Break liquidity – A CCP NDA to trading venues (TVs) would inevitably fragment liquidity and weaken the resilience of ETD markets as a result of multiple CCPs clearing a single TV's ETDs. If a TV has access arrangements with three CCPs, it would be forced to create three separate order books for any given product (as counterparties can only trade with those who wish to clear at the same CCP). This would result in an inefficient and costly system which would provide a misleading impression of choice while, in reality, fragment liquidity. The alternative, i.e. retaining a single order book to which all orders would be submitted irrespective of CCP, would be impracticable as users that intend to hold positions at different CCPs could not be matched in a single order book, and the trade would subsequently need to be reversed to prevent the long and the short being cleared by different CCPs.
2. Undermine price-discovery – Breaking the link between TVs and CCPs and the liquidity of ETD markets would disrupt the price discovery process across different exchanges. This would have an impact on the broader economy as ETD markets serve as a benchmark for a broad range of underlying and related assets (e.g. bonds, shares and commodities), as they reflect the market's expectations of future fluctuations of these underlying markets. For example, ETD markets in Europe are used by market participants as benchmarks to manage exposures to Euro Area sovereign debts, as the underlying bonds market is too opaque and fragmented to carry out this function. The erosion of the price discovery process and the resultant weakening of an accurate reference price can ultimately lead to serious financial stability risks, such as the creation of asset bubbles or the inability of financial supervisors to set accurate capital requirements for market participants.
3. Harm competition and innovation – Concentrating all clearing activities into one CCP would effectively diminish competition in the EU (the very thing NDA provisions are supposed to bring) and bring down innovation due to increased latency in approving new products and services (which would need to be approved by one CCP). For example, both LIFFE (former ICE Futures Europe) and LME opted to split from LCH. Clearnet their common clearing house due to inhibitions to competition and innovation. The current linkage between the TV and the CCP is overwhelmingly the most efficient model for ETD markets in most developed jurisdictions, because the integrated service is more efficient for product development, leading to a highly responsive industry with faster introduction of new products.
4. Increase concentration - Breaking the link between the TV and its CCPs could lead to a situation where the most attractive CCP for one specific ETD or asset class, becomes the single place for central clearing across all asset classes. Such a high level of concentration would expose the financial system to a single point of failure with potential systemic consequences and the impossibility for market participants to efficiently move their positions to another CCP in case of failure. Beyond the

concentration risk at the CCP level, the impact of NDA requests should be also considered at the clearing member (CM) level. The more links across TVs and CCPs will multiply, the more only a minority of structurally large banks will be able to afford the costs linked to maintaining the connectivity links and checks. This risk may increase the concentration of CM and create barriers to grow the next generation EU credit institutions that can handle the complexity of interlinkages between TVs/CCPs.

5. Endanger the CCP – A TV NDA to CCPs would introduce risks to financial stability (not to mention the risk of legal challenge) arising from pooling of open interest of economically equivalent – but not identical – ETD contracts in the same CCP as a result of multiple TVs gaining access to it. It would require such contracts to be treated as fungible, despite the fact that the contracts' legal basis (in terms of governing law and jurisdiction), governing authorities (in terms of the trading venue creating the contract and its regulator) and the arrangements for taking emergency action, e.g. in relation to force majeure and other market events) would differ. This would force CCPs to match positions that are not identical but 'economically equivalent' which means the CCP itself would be liable for any difference, thereby destabilizing the CCP and the ETD market it clears. Further, we are particularly concerned by the potential impact of NDA access requests on the default management process and possible recovery of CCPs when market participants are spread across different TVs.

Q83.1 - Please explain your answer to question 83:

The EU has come a long way in increasing competition and transparency across market infrastructures, notably via MiFID I and MiFID II/R. As of today, with 137 RMs, 223 MTFs and 73 OTFs (for equity and non-equity instruments), and 16 CCPs (compared to 5 in the US), the EU is the most competitive market in the world. It is critical to realise that the 'Non-discriminatory' access provisions would result in unfairly forced and artificial competition via regulatory intervention.

Since June 2019, the only example of a voluntary interoperable link for ETDs in the EEA has ceased to exists as Oslo Børs and the London Stock Exchange Derivatives Markets announced they were ending the interoperability arrangement between Six x-clear (Norwegian branch) and LCH Ltd. Oslo Børs stated in its press release that the model of two interoperable clearing houses required such an increase in margin to balance the risk between the two clearing houses that the link was no longer viable.

We believe that including ETDs in the scope of the 'Non-discriminatory' access provisions under MiFID II/R will undermine the EU27 financial stability agenda and will damage its competitiveness at global level. As a quantitative financial stability impact assessment has never been carried out (and the basis for the qualitative impact assessment has ceased to exist) we urge the European Commission to run an impact assessment to gather further evidence on the negative impact of the provisions on the EU27 ETDs markets.

Furthermore, the scenarios described above could be further aggravated post Brexit as it is unclear how a competitive level playing field would be ensured in the event that a third country infrastructure gains access to EU CCPs and TVs. In our view, it would be inappropriate to impose wide scale market structure changes in the Exchange-Traded Derivatives markets - which may have significant financial stability consequences - while the EU/UK future relationship remains unclear. In addition, the third country safeguards around the NDA provisions appear particularly weak. Under an equivalence determination limited to Art. 38(3) MiFIR, the third country CCP is merely required to be 'subject to authorisation and to effective supervision and enforcement on an ongoing basis' and to have similar access provisions. There are no provisions in Art. 38(3) MiFIR to ensure a comparable trading environment in the third country, meaning the application of the same transparency and market structure requirements.

Finally, the current economic and financial crisis has demonstrated again the resilience of ETD markets under extreme stress scenarios. With the ongoing uncertainty around the current crisis expected to last, we do not believe it would be wise to risk destabilising key Euro-ETD markets at such a critical time. Therefore, the existing exemptions should be extended for at least another 30 months, as the implementation currently foreseen for 3rd of July will divert precious resources and strain operational capacities given the impact of the COVID 19 situation.

Q84 - Do you think that the open access regime will effectively introduce cost efficiencies or other benefits in the trading and clearing areas?

X 1 – Disagree
☐ 2 – Rather not agree
☐ 3 - Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q84.1 - If you do think that the open access regime will effectively introduce cost efficiencies or other benefits in the trading and clearing areas, please indicate the specific areas (such as type of specific financial instruments) where, in your opinion, open access could afford most cost efficiencies or other benefits when compared to the current situation:

Q84.1 - Please explain your answer to question 84:

We do not think it serves any public policy objectives to impose a fragmentary model on what are currently well functioning, inclusive ETD markets which generate prices that are viewed worldwide as representative. The provisions will not introduce cost efficiencies or other benefits but would rather make ETD markets less efficient.
While applying 'Non-discriminatory' access under MiFIR to transferable securities and money market instruments poses little systemic risk, applying 'non-discriminatory' access to ETDs would undermine the stability and liquidity of the European derivative markets. Please see our answer to Q83.
Derivative contracts can have a long duration (sometimes decades), are far more complex, and require much more stringent requirements and controls from CCPs as neutral and independent risk managers.
By design the contract specifications of ETDs are unique to the regulated market on which they are admitted to trading. This is primarily because RMs decide and determine the specifications of their derivative products in order to provide products most likely to be successful with customers, therefore building liquidity and offering an effective way to hedge risk. Their specifications relate not just to technical conditions but also to their legal status and the jurisdiction of any disputes arising and/or insolvency law that would apply.
By contrast, OTC derivatives are run by industry convention subject to ISDA specifications and are by nature much less liquid: trades are negotiated first bilaterally (incl. the choice of the CCP) before they are executed bilaterally or on an electronic venue and then cleared in the pre-agreed CCP without the use of the centre limit order book.

Q85 - Are you aware of any market trends or developments (at EU level or at national level) which are a good or bad example of open access among financial market infrastructures?
Please explain your reasoning and specify which countries:

Currently, all relevant European NCAs have decided to follow the principle of precaution due to Brexit and have granted temporary transitional provisions to all CCPs and TVs that requested it. In addition, thorough consideration should be given on how the EU27 market will look like following the departure of the UK.

It appears counterintuitive and illogical to risk breaking Europe's most liquid and successful markets at the very moment when the EU ambitions to develop a thriving Capital Markets Union (CMU) and increase the international use of the euro, in order to increase its economic and financial independence. Importantly, with the ongoing uncertainty around the current crisis, we do not believe it would be wise to risk destabilising key Euro-ETD markets at such a critical time. Europe needs deep and liquid Euro-denominated ETD markets, ensuring the proper functioning of resilient private risk transfer mechanisms and limiting costs for investors and end-users in the Union.

Furthermore, no other major open-market economy outside Europe have pursued a policy of 'non-discriminatory' access for ETDs. Historically, when ETD markets are set up, the broad majority have preferred to create a link between the TV and the CCP for efficiency and safety purposes.

By contrast, competition across ETDs has and continues to thrive – in the past DTB (former Eurex) successfully competed with LIFFE on the Bund-Future thanks to innovation (electronic execution), while new products are regularly developed to cater for new market needs, to support futurisation or pick up in Environmental Social Governance (ESG) standards.

The alleged gains of 'non-discriminatory' access for ETDs are highly questionable in a global context where other jurisdictions do not pursue the same objectives but rather focus on size and scalability. ETD open offer systems are extremely robust and efficient systems which have been preferred models in jurisdictions with developed and liquid markets.

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IX. Digitalisation and new technologies

5000 character(s) maximum
including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

Q86 - Where do you see the main developments in your sector: use of new technologies to provide or deliver services, emergence of new business models, more decentralised value chain services delivery involving more cooperation between traditional regulated entities and new entrants or other?
Please explain your answer:

FinTech can help to expand access to financial services for consumers, investors and companies, bringing greater choice and more user-friendly services, often at lower prices. New financial technologies can help individuals as well as SMEs, including start-up and scale-up companies, to access alternative funding sources to support their cash flow and risk capital needs. Automation and standardisation have changed the way customers interact with market infrastructure providers, leading to an explosion in data volumes. Technological developments in relation to data analytics, Field Programmable Gate Array (FPGA), mobile technology, cloud computing, machine learning, artificial intelligence (AI) and blockchain are opening up new possibilities in relation to the services Exchanges use and provide to customers. Individually, these technologies have enormous potential and combined, they can offer an impressive array of new solutions for clients. However, it should be noted that for FPGA the related costs and complexity of implementation may for the moment prevent these technologies from playing a leading role in innovation.
An EU general regulatory framework needs to be geared towards fostering technological development and innovation. Technological developments are moving faster than the underlying legal and regulatory frameworks and in order not to impede innovation and investment, a rigid application of existing rules must be avoided. A predictable, consistent and straightforward legal environment should instead be promoted. Areas which would benefit from review include licensing requirement for FinTech companies, data protection, conflict of laws, outsourcing, cyber security, settlement finality and proper legal recognition of holding and transferring securities and other types of assets.
It is important to establish key principles upon which the EU can build a role in facilitating the development and implementation of FinTech.
These principles include the need for:

- The application of the same rules for the same services and risks (including across different pieces of legislation) based on the principle of technology neutrality;
- A risk-based approach built on proportionality and materiality which allows for flexibility, particularly in respect of innovation with small groups of customers (i.e. sandboxes), while ensuring a level playing field across the EU;
- A balancing of the local (country) risks alongside the benefits of cross-border markets (i.e. scalability, interoperability and passporting of services).

Financial Market Infrastructures (FMIs) use modern IT and technological solutions to operate, and service the financial sector worldwide. Technologies are at the core of their operations and an integral part of the regulated services they operate. FMIs ensure the efficient functioning of these markets; including but not limited to: market data, indices, clearing, securities custody, etc.
We observe that the digital economy through the use of DLT is on the road to decentralisation which is particularly true for the financial industry. In this regard, we would like to especially stress the importance of maintaining principles such as technology neutrality and “same business, same risks, same rules” to uphold transparency, fairness, stability, investor protection and market integrity. In particular, as some forms of DLT, such as public blockchains have no legally accountable entity to be held liable for failings to implement risk management procedures to address risks in financial markets.

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In this regard a Trusted Third Party (TTP) is required in the financial industry to create trust in the market; and ensure investor protection. In a DLT environment, TTPs are building a bridge for the exiting financial instruments in the "traditional world" via DLT solutions, increasing market integrity by e.g. "OFF-Chain to ON-Chain bridging" and guaranteeing the substance of a token, which is backed by financial instruments that is kept off ledger/chain. TTPs will play the role of a gatekeeper for future native digital assets, which will be issued directly on the chain. In this regard, a TTP will be responsible for addressing functions such as:

1) Control access/admission
2) Set rules for the participating nodes
3) Address potential conflicts of interest and KYC and AML requirements
4) Apply risk management measurers
5) Be reliable for market integrity, security and other regulatory requirements

The TTP will check standards for admission and the eligibility of an asset on chain. For instance, it will check if the asset is a security and transform it to a security token. Another role that the TTP will play would be to check smart contract codes to assess adherence with international standards. A TTP should operate within a regulatory compliant framework and adhere to the relevant existing rules and regulation.

Q87 - Do you think there are particular elements in the existing framework which are not in accordance with the principle of technology neutrality and which should be addressed?

New technologies are used in different areas of application, with different goals in mind and within different regulatory frameworks. Amendments may therefore be needed in order to provide legal clarity and allow benefits of the technologies in the EU. As an overarching principle, a technology-neutral approach is very important, as regulation should be independent from the used technology.

However, for some areas, policymakers should consider the following technology specific challenges and how to address these:

1. Cloud: outsourcing of material functions, proper risk management, clarity of the liabilities on both sides and currently missing standard contract clauses to facilitate negotiations of compliant contracts with providers, especially for small/mid-sized institutions. As the importance of these services increase an overarching appropriate oversight paradigm is missing.
2. Big data / AI: quality, and source and ownership of data, data protection and data sovereignty as well as ethical questions (e.g. reconciliation of decisions, biases)
3. DLT/blockchain: liability and accountability in public permissionless chains, and smart contracts, material outsourcing considerations data protection and new IT-risks.

With regard to the existing framework, we find one example in the realm of DLT/Blockchain very important, where the principle of technology-neutrality should be upheld. Regulators should treat the technology itself as any other IT system, based on the principle "same business, same risk, same rules" regarding its use and connected risks. Further, regulators should focus especially on the "records" maintained in this environment, as they could be digital representations of different forms of assets, used in the financial industry. From our point of view, these digital or crypto-assets should be treated in a "substance-over-form" approach, meaning that if they, for example, fulfill the criteria of a financial instrument in accordance with the current regulatory framework, they should be treated as such. FESE favours a regulatory categorisation of "crypto-assets" at EU level. This would allow regulators and financial market participants to have a common definition of "digital asset" and allow distinguishing between different types to bring significant benefits to market participants and consumers.

FESE supports the introduction and application of a harmonised regime. On a general line, FESE would not favour the use of "soft law" (e.g. guiding principles), as this might be

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interpreted differently by Member States. FESE, therefore, welcomes that the Commission is considering potential regulatory requirements to address "crypto-assets" currently not covered by EU legislation. Moreover, we believe that 'investment/security tokens' should be considered as financial instruments under MiFID II (Art. 4, paragraph 15). Alternatively, such clarification could potentially be given through Level 2 amendments. However, any legislative measures should avoid undermining other potentially applicable regulations (such as EMD for certain payment tokens). In line with the Better Regulation principles, we consider it important that any changes to the definitions of financial instruments be subject to an impact assessment to avoid any unintended consequences.
If digital or crypto-assets represent a currently existing financial instruments (e.g. shares, commodities etc.), then they should adhere to the existing regulatory framework following the "same business, same risk, same rules" approach.
However, the MiFID II legal framework must bring legal clarity as to which digital assets fall under the scope of MiFID II financial instruments (as stipulated in Annex I of MiFID II Section C. To ensure technology-neutrality, a number of other, existing regulation should also be applicable (e.g. EMD, MAR, SSR, Prospectus, CSDR, SFD, FCD, EMIR, UCITS, AIFMD). Further, as new technologies carry technology-specific risks, regulators should consider how to ensure a high level of IT security. Lastly, it should be clarified that existing actors, e.g. financial market infrastructures like CCPs and CSDs, are already allowed to handle these new assets, as they do with other assets classes (e.g. CCPs can accept crypto-assets as margins or CSDs can offer services on "crypto-assets").
To ensure the integrity of the financial markets and mitigate risks, new emerging actors, like custodial wallet providers, should comply with existing financial rules and regulations and ideally be licensed accordingly.
In general, to uphold the principle of technology-neutrality and to benefit from new technology, it is important to strike the right balance between safety and the availability/usage of innovative technology.

Q88 - Where do you think digitalisation and new technologies would bring most benefits in the trading lifecycle (ranging from the issuance to secondary trading)?

In general, we think of new technologies as enabling new opportunities to the financial industry as a whole, including the trading lifecycle. At the same time, we expect an evolutionary process, rather than a revolution, due to the high level of financial stability standards and the importance of market integrity. Currently, depending on the technology, the financial industry is adapting and is still in an early stage. The benefits of the technologies differ, but are for example: increased transparency, cost reduction, speed of software development and quality by more extensive testing, increased geographical coverage, resilience etc. We are certain that new asset classes, procedures, services and actors are emerging.
Combining innovative technologies, for instance blockchain based technologies, with established, highly regulated market infrastructures would be the natural choice in order to ensure market stability while making use of the innovative potential brought about through FinTech.
DLT has the potential to accelerate, decentralise, automate and standardise data-driven processes and therefore to alter the way in which assets are transferred and records are kept. In particular, DLT allows cross-verification of information in a transparent and dependable way and can simplify complex verification and validation processes. Hurdles to wide scale adoption of DLT in securities markets are technical limitations, contextual aspects such as business model/market model design, technical integration/transition, legal/ regulatory complexity. For solutions based on DLT to reach actual implementation in securities market, visions for the future need to be broken down into defined descriptions of services and solutions that are accepted and desired by its intended consumers and meet legal, regulatory and technical requirements. DLT should not be considered a panacea that will replace all existing infrastructure in securities markets but

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rather DLT solutions need to be integrated into the existing ecosystem of infrastructure in securities market, which will require some efforts and time. Transition planning and execution is also important in DLT business cases when the intention is for DLT to replace legacy technology.

Q89 - Do you consider that digitalisation and new technologies will significantly impact the role of EU trading venues in the future (5/10 years time)?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☒5 – Fully agree
☐Don't know / no opinion / not relevant

Q89.1 - Please explain your answer to question 89:

New technologies and digitalisation seem to affect Europe's businesses in various ways. Not only has the European financial system been transformed significantly due to the introduction of digitalisation and new technologies but these initiatives have also made their first impacts on financial services throughout Europe. Despite the lack of specific laws and regulations in relation to all innovative technology related matters, the market is implementing new forms of digital products and services without a framework that provides legal certainty and trust. By examining the current trends in the financial markets, it is expected that digitalisation, new technologies and artificial intelligence (AI) will continue to impact global capital markets while affecting at the same time all financial participants, including trading venues. Based on the current trends in the financial markets, we could assume that machine learning and AI could be fully integrated into the trading space within five years and, as such, affect both services and financial instruments of exchanges throughout Europe. Trade performance analytics, real time management as well as cyber security are and will continue to be considered important to both financial markets and most of the financial market participants especially in terms of their long-term defensive solutions. Traders will focus and will continue to dedicate more time on strategies which allow them to create opportunities, in areas related to performance analytics and execution management systems (EMS). Traders believe that EMS will impact financial markets and as such the functions of the exchanges in Europe (and not only) within the next five years[6]. In addition, buy-side participants are expected to continue to use cloud adoption tactics. As such, the cost of ownership will decrease and more agile development methodologies will be adopted, increasing at the same time the innovation pace within trading venues as well. A deeper understanding of the above-mentioned services is needed, along with clear legal definitions in order to provide trust and certainty to market participants. The scope of any future initiatives from the European Commission should take into consideration the tendencies described above and the dialogue with the market on specific proposals should be further enhanced.

Q90 - Do you believe that certain product governance and distribution provisions of the MiFID II/MiFIR framework should be adapted to better suit digital and online offers of investment services and products?

1 – Disagree

[6] The Trade News, EMS Survey, 2017, available here.

☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☐5 – Fully agree
☒Don't know / no opinion / not relevant

Q90.1 - Please explain your answer to question 90:

The EU regulatory framework needs to be geared towards fostering technological development as the financial industry and its users are benefitting significantly from such developments. Data analytics, machine intelligence and robot advice is already significantly aiding the decision process and quality of information being shared. FPGA also supports distribution of massive amounts of data with high throughput for market transparency and equality. Cloud techniques to efficiently distributed data, easily scale storage needs and secure data for resiliency purposes will also help to improve the access to finance. Another area which improves access to finance is mobile banking.
However, it is crucial to adequately manage potential risks in order to ensure that markets can remain fair, orderly and trusted venues to carry out business.
Product governance means the controls and the systems that a firm must put in place for the ongoing management, the marketing, the design and the approval of all products throughout their lifecycle to verify that they comply with the relevant regulatory and legal requirements.
The product governance requirements have impacted and will continue to impact both distributors, sub-distributors as well as manufacturers in various ways. In particular, all their relevant obligations can be categorised based on the four distinctive phases of the product governance cycle: i) design and approval, ii) development and implementation, iii) launch and promotion and iv) monitoring and review.
The new regime constitutes a significant change to European financial product distribution and is challenging for firms to implement. Distributors and manufacturers, of financial services and products need to set standards in order to supervise their ongoing monitoring of distribution activities, while encouraging the development of efficient procedures for the design of financial services and products and for the proper identification of the target market.
The MiFID II/MiFIR review is an opportunity for a simplification of these standards in line with the principle of technology neutrality. The current framework could be further adapted to better suit both traditional and digital offers of investments services and products. By applying the technology-neutral approach in reviewing the existing regime, the distribution of a product (be it a traditional asset or a crypto-asset for example) should not be differentiated by the means of its distribution (be it human or via technological means). This would guarantee an even level of investor protection and allow for the technology and market infrastructure to develop.

Q91 - Do you believe that certain provisions on investment services (such as investment advice) should be adapted to better suit delivering of services through robo-advice or other digital technologies?

☐1 – Disagree
☐2 – Rather not agree
☐3 - Neutral
☐4 – Rather agree
☐5 – Fully agree
☒ Don't know / no opinion / not relevant

Q91.1 - Please explain your answer to question 91:

As passive management of assets is gaining importance and considering the already large (and growing) universe of financial products, this could lead to a proliferation of robo-advising platforms. In this sense, any adaptation of provisions or inclusions into already existing frameworks should be aimed at fostering the entrance of new competitors in order to improve services.

X. Foreign exchange (FX)

Q92. Do you believe that the current regulatory framework is adequately calibrated to prevent misbehaviours in the area of spot foreign exchange (FX) transactions?

☐ 1 – Disagree
☐ 2 – Rather not agree
X 3 **-** Neutral
☐ 4 – Rather agree
☐ 5 – Fully agree
☐ Don't know / no opinion / not relevant

Q92.1 - If you do not believe that the current regulatory framework is adequately calibrated to prevent misbehaviours in the area of spot foreign exchange (FX) transactions, which recommendations would you make to improve the robustness of the regulatory framework?

Q92.1 - Please explain your answer to question 92:

Q93 - Which supervisory powers do you think national competent authorities should be granted in the area of spot FX trading to address improper business and trading conduct on that market?

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Section 3. Additional comments

You are kindly invited to make additional comments on this consultation if you consider that some areas have not been covered above.
Please, where possible, include examples and evidence.

5000 character(s) maximum
including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

In addition to the points raised in this CP, we would like to make the following observations:

1. Reference data and reporting: From our experience, operationally speaking, the main concerns raised by MiFID II/R are related to reference data and reporting, in particular RTS 23, among others. Actually, we revisited the inputs prepared for ESMA FIRDS/FITRS Workshop in 2018 (attached for convenience) and we realized that it still valid and updated. The problems raised by that paper, unfortunately, remain.

2. Interpretation: (i) Interpretation of certain terms: Exchanges have different interpretation of key concepts as, for instance, "maturity date". For instance, some Exchanges use the settlement date while others use the valuation date if the Final Terms do not mention explicitly maturity date. This can pose some problems. Guidance on these specific questions would be useful. (ii) Level 3 Q&As: Also, not always the questions submitted to the Authorities are replied in a satisfactory way.

3. CFI Code: In an ideal world, when the financial instrument is listed, the CFI Code should not change. However, that is not always the case. CFI Code can be modified and this can change everything on data validation (modification of MiFID II mandatory fields). The MiFID II data sent to ESMA changes according to the CFI code (CFI validation matrix). As CFI changes often on ANNA (e.g. from bond to warrant) it would have an impact on the information sent to ESMA and different fields should be completed. In an ideal case the original CFI code in ANNA should not be modified during the listing period to mitigate reporting issues and inconsistencies.

Question 94. Have you detected any issues beyond those raised in previous sections that would merit further consideration in the context of the review of MiFID II/MiFIR framework, in particular as regards to the objective of investor protection, financial stability and market integrity? Please explain your answer:

5000 character(s) maximum
including spaces and line breaks, i.e. stricter than the MS Word characters counting method.

Should you wish to provide additional information (e.g. a position paper, report) or raise specific points not covered by the questionnaire, you can upload your additional document(s) here:

- **Annex I: FESE Non-paper on the EU Consolidated Tape Study**

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