

# Reply form

**For the Consultation Paper (CP) on ESMA's Opinion on the trading venue perimeter**



## Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions. Comments are most helpful if they:

1. respond to the question stated;
2. indicate the specific question to which the comment relates;
3. contain a clear rationale; and
4. describe any alternatives ESMA should consider.

ESMA will consider all comments received by **29 April 2022**.

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading 'Your input - Consultations'.

### Publication of responses

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

### Data protection

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading [Legal Notice](#).

### Who should read this paper

This document will be of interest to all stakeholders involved in the securities markets. It is primarily of interest to competent authorities, investment firms and market operators that are subject to MiFID II and MiFIR. This paper is also important for trade associations and industry bodies, institutional and retail investors, their advisers, consumer groups, as well as any market participants because the MiFID II and MiFIR requirements concern the market structure of the EU and the perimeter of trading that should be considered as multilateral and regulated as such.

## Q1 Do you agree with the interpretation of the definition of multilateral systems?

<ESMA\_QUESTION\_TVPM\_1>

**ICMA Consultation response introduction:** ICMA's response solely relates to trading of bonds in secondary markets and not primary markets. Primary markets can be distinguished from secondary markets as buying and selling interests are not “matched” in a primary market context. This is because the securities are newly created (not pre-owned), hence there is no selling interest to match. The primary market is where securities are created and sold to investors for the first time. Securities are purchased directly from the issuer, typically through an underwriting syndicate.

ICMA would also like to note, while a clear majority of ICMA members are in consensus agreement, a few trading venues disagree with ICMA's overall response to the consultation.

## Q1 Do you agree with the interpretation of the definition of multilateral systems?

Providing ESMA amends the ‘system or facility’ definition as below, ICMA will agree to the definition of multilateral system. This agreement is contingent on the following:

ICMA considers in order for an entity, whether automated or non-automated [a recognised established routine], to qualify as ‘multilateral’, requiring authorisation as a trading venue, all four of the following framework points below **must** apply:

1. System or facility – In the context of Article 4 (19) a system [or facility] must be understood as a set of rules using the following framework to govern how third-party trading interests interact:
  - a. A third-party entity (e.g., the final arbiter), which ‘governs’ the terms that results in a contract under which operates rules/terms of business (determines whether an execution has occurred or not).
  - b. A third-party entity which provides an execution timestamp. Such rules could be contractual agreements or standard procedures that shape and facilitate interaction between participating trading interests.
    - i. Regarding ‘timestamp’, if a separate entity governs

the terms that results in a contract, then that entity overrides the third-party entity provider of the timestamp, and in this instance the entity provider of the timestamp is only functioning as an expediter.

2. There are multiple third party buying and selling interests.
3. Those trading interests need to be able to interact within the system,
4. Trading interests need to be in financial instruments

Regarding system or facility, ICMA agrees with points 20 and 21, that in order to qualify as a system or facility, “the main criterion is whether there are specific rules concerning the interaction of multiple market participants to which participants shall adhere to”.

Also, ICMA agrees that “non- automated [a recognised established routine] systems or repeatable arrangements that achieve a similar outcome to a computerised system, including for instance where a firm would reach out to other clients [allowing interaction] to find a potential match when receiving an initial buying or selling interest would also be characterised as a system” and should be considered for authorisation as a trading venue.

Although, a good example of when an authorisation as a trading venue is not required, is an OMS or EMS which provides an alert to execute. The OMS or EMS is not governing the interests that would result in a contract, nor does an OMS or EMS pass the criteria described above.

<ESMA\_QUESTION\_TVPM\_1>

**Q2 Are there any other relevant characteristics to a multilateral system that should be taken into consideration when assessing the trading venue authorisation perimeter?**

<ESMA\_QUESTION\_TVPM\_2>

Yes, ICMA believes ESMA should take into consideration the existence of a ‘third party system operator’ who is the ‘controller’ of the terms that result in a contract, as a key characteristic of multilateral, when assessing trading venue authorisation. For a system to be multilateral, it must have a third-party system operator, who facilitates the matching of interests. This is particularly important when taking into account the organising of protocols. Often terms of business

are involved with protocols. An example of an 'organiser' of protocols is an MTF or OTF.

An EMS or OMS does not set the protocols or rules which governs the interaction of multiple trading interests. For example, instead, they are used to organise interests involving a single user (such as a broker or portfolio manager) and, while multiple bilateral communications can be sent, the interests involving separate users do not interact. In other words, these management systems do facilitate bilateral communications (in a more efficient way than communicating over the phone or by e-mail) but they are not 'platforms' in which multiple buyers and multiple sellers interact. Therefore, it is ICMA's considered view that an EMS or OMS does not qualify for authorisation as a trading venue.

In addition, an entity that solely aggregates or consolidates is also not sufficient to qualify for authorisation as a trading venue. As the aggregating entity does not qualify as a 'system' or 'facility' as defined below:

'System' or 'facility': In the context of Article 4 (19) a system [or facility] must be understood as using the following framework to govern how third-party trading interests interact:

- a. A third-party entity (e.g., the final arbiter), which 'governs' the terms that results in a contract under which operates rules/terms of business (determines whether an execution has occurred or not).
  
- b. A third-party entity which provides an execution timestamp. Such rules could be contractual agreements or standard procedures that shape and facilitate interaction between participating trading interests.
  
- c. Regarding 'timestamp', if a separate entity governs the terms that results in a contract, then that entity overrides the third-party entity provider of the timestamp, and in this instance the entity provider of the timestamp is only functioning as an expediter.

It is important to note that ICMA members believe a 'timestamp substitute' does not disqualify a firm from being authorised as a trading venue, just because a different method of confirmation has taken place. Any method that confirms terms resulting in a contract have taken place will meet point '1b' criteria in answer to question 1, on the previous page.

<ESMA\_QUESTION\_TVPM\_2>

**Q3 In your experience, is there any communication tool service that goes beyond providing information and allows trading to take place? If so, please describe the systems' characteristics.**

<ESMA\_QUESTION\_TVPM\_3>

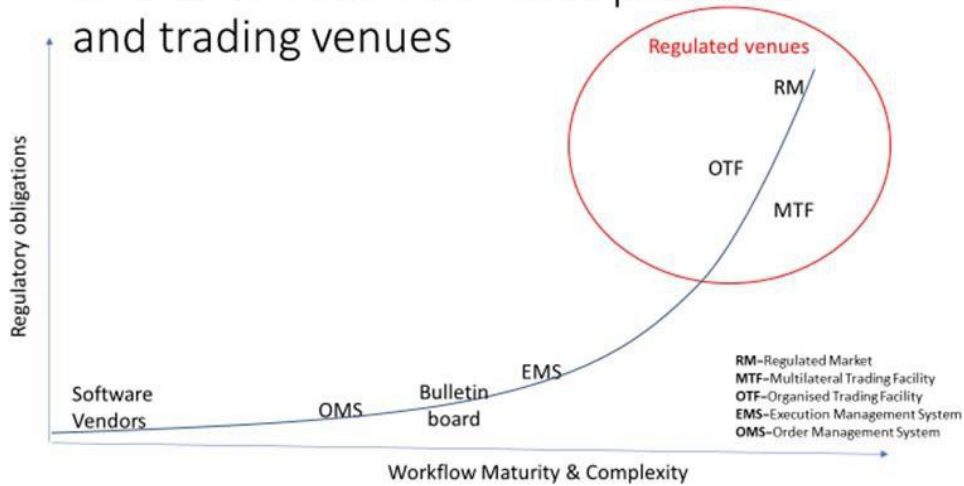
No. Regarding communication tools, ICMA believes it should be the design of the system, the role the firm assumes, their involvement and responsibilities in the day-to-day operation, and the interactions between participants within them that should be evaluated by ESMA when determining authorisation as a trading venue.

Furthermore, ICMA agrees with ESMA's statement in point 40 in the consultation paper: "40. Whilst ESMA supports and encourages new business models and innovative solutions, it is important to ensure that such models and solutions are appropriately regulated to ensure an adequate level of protection for investors and to maintain the resilience of EU markets. In order not to hamper the development of new solutions, the supervisory approach should take into account proportionality while ensuring a level playing field between all firms operating in the Union".

It is important to ensure that technologies that are not 'multilateral' do not unintentionally get caught up in a trading venue definition, thereby inhibiting fintech advancement. As a result, ICMA believes any new initiative business model should be evaluated by ESMA on a case-by-case basis.

ICMA considers ESMA should use the diagram below as a guide when considering the scale of trading venue authorisation.

## Innovation in Capital Markets – Characteristics of software providers and trading venues



<ESMA\_QUESTION\_TVPM\_3>

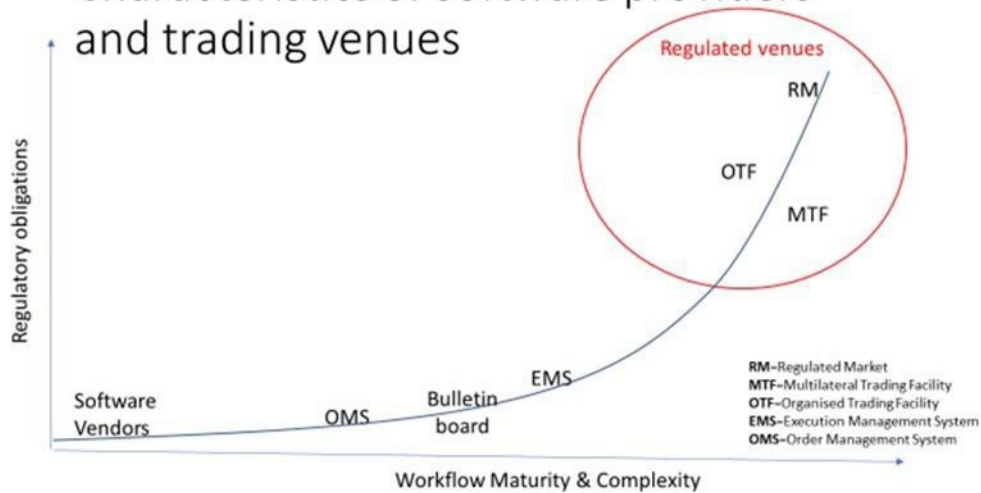
**Q4 Are you aware of any EMS or OMS that, considering their functioning, should be subject to trading venue authorisation? If yes, please provide a description.**

<ESMA\_QUESTION\_TVPM\_4>

No. As referenced in the criteria described in the answer to question 1, both an EMS and OMS cannot be authorised as trading venues, this is because neither is a third-party entity (final arbiter) 'governing' (through rules, which determine whether an execution has taken place or not) terms resulting in a contract.

ICMA considers ESMA should use the following diagram as a guide when considering the scale of trading venue authorisation, for any of the entities referred to below.

## Innovation in Capital Markets – Characteristics of software providers and trading venues



Unless an EMS or OMS are themselves somehow making trading decisions, it is normally the user (i.e., the trader who controls the execution, usually a member of a regulated firm) who is making the decision to execute. For example, an EMS can send multiple RFQs to potential counterparties. Notably, the decision to execute is the firm's decision, and not the firm's EMS. The EMS is a decision support tool.

Furthermore, while algos may trigger a decision to execute, it is based on the parameters designed by and on behalf of, the firm.

In addition, if the investment firm directly controls the rules/parameters by which their EMS or OMS selects counterparties and executes bilaterally, then that activity does not qualify for authorisation as a trading venue.

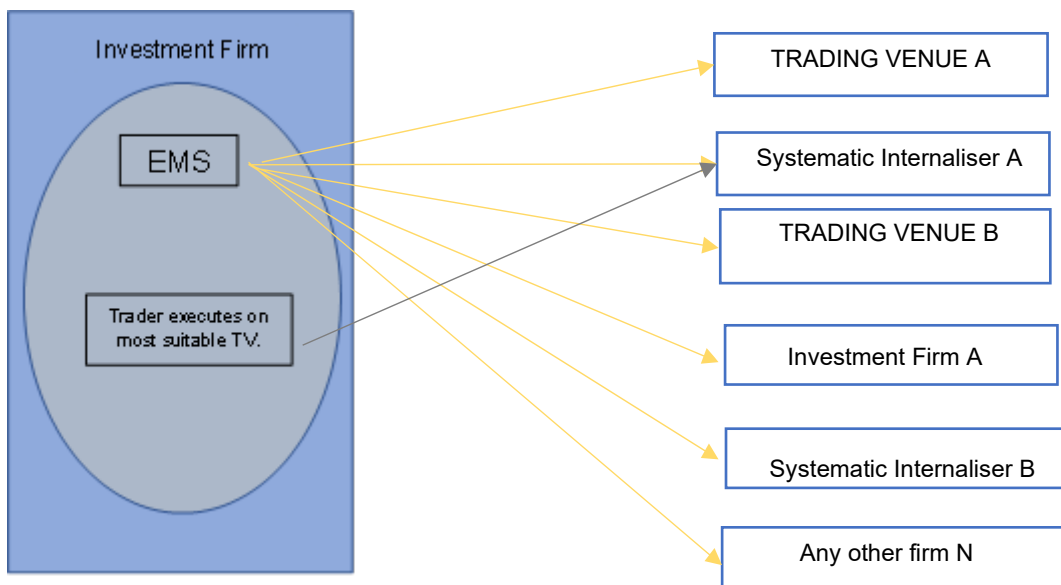
However, if a non-automated (a recognised established routine) third-party system operator passes the criteria described in the answer to question 1, then they could qualify for authorisation as a trading venue.

Moreover, if a fixed income software and/or technology provider aggregates third party bilateral indications and allows multilateral interactions with those aggregated indications, whereby trading interests interact with each other, that is a multilateral facility and should be authorised accordingly as a trading venue. For example, a system that aggregates bilateral indications from third parties and allows those third parties to interact.



Also, if an entity describing itself as an EMS or OMS meets all the criteria referenced in the answer to question 1, then said EMS or OMS could qualify for authorisation as a trading venue.

However, it is important to point out that ICMA considers an EMS and an OMS, as described in the answer to question 2, cannot qualify for authorisation as a trading venue, as evidenced in the diagram below. This is because an EMS or OMS in this example does not meet the criteria (as referenced in the answer to question 1) of a trading venue which is: (1) there is not a third-party system operator (2) who is governing the execution/protocol and (3) and multiple buyers and multiple sellers are unable to interact (4) in financial instruments.



<ESMA\_QUESTION\_TVPM\_4>

**Q5 Do you agree that Figure 4 as described illustrates the operation of a bilateral system operated by an investment firm that should not require authorisation as a trading venue?**

<ESMA\_QUESTION\_TVPM\_5>

Yes, ICMA agrees that figure 4 (page 20 of the consultation) represents a bilateral system, which should not require authorisation as a trading venue.

<ESMA\_QUESTION\_TVPM\_5>

**Q6 Do you agree that a “single-dealer” system operator by a third party, as described in Figure 5, should be considered as a multilateral system? If not, please explain.**

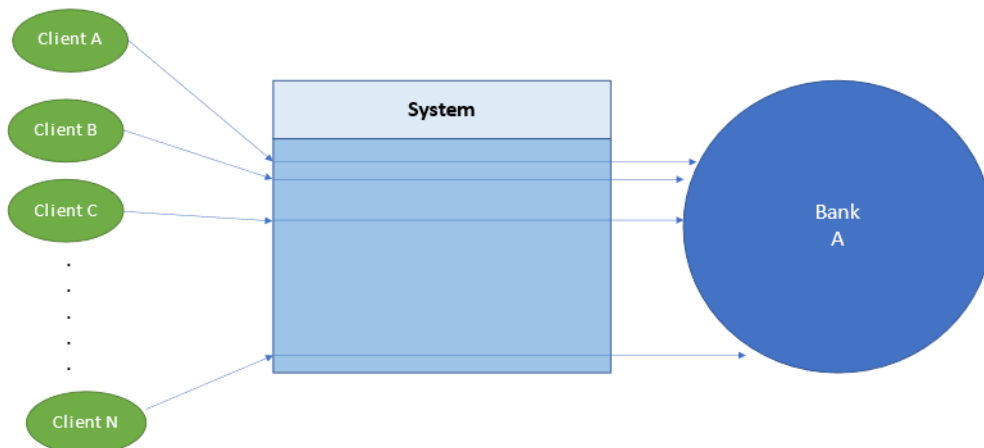
<ESMA\_QUESTION\_TVPM\_6>

No, ICMA disagrees with the diagram as presented.

**Figure 5 is a “single-dealer” multilateral or bilateral system.**

ICMA believes Figure 5 below, could be a diagram of a (multilateral) MTF or a (bilateral) SI execution, depending on where the rules governing the execution are located. For example, if ‘Bank A’ is governing the execution, and determining when the execution is done, then Figure 5 is evidencing a bilateral SI execution. However, if the ‘system’ is governing the execution, and governing when the execution is done, then Figure 5 is illustrating a multilateral MTF execution. It really depends on who is governing the execution. The term ‘system’ is relative as trading venue authorisation concerns ‘who’ governs the execution.

Figure 5: Single -dealer, multilateral system



ICMA would also like to highlight, it is important for ESMA to remember that an execution can only ever happen in one place. An execution cannot happen in both the “System” (multilateral) and “Bank A” (bilateral).

<ESMA\_QUESTION\_TVPM\_6>

**Q7 Do you agree that systems pre-arranging transactions that are formalised on a trading venue, even when arranged in a multilateral way, should not be required to be authorised as trading venues? Do you agree with the justification for such approach?**

<ESMA\_QUESTION\_TVPM\_7>

Yes, ICMA agrees with ESMA.

<ESMA\_QUESTION\_TVPM\_7>

**Q8 Are there any other conditions that should apply to these pre-arranged systems?**

<ESMA\_QUESTION\_TVPM\_8>

No. ICMA believes there are no other conditions that should apply.

<ESMA\_QUESTION\_TVPM\_8>

**Q9 Are there in your views any circumstances where it would not be possible for an executing trading venue to sign contractual arrangements with the pre-arranging platforms? If yes, please elaborate**

<ESMA\_QUESTION\_TVPM\_9>

No, ICMA members are not aware of any such scenario where a contractual agreement, practical or not, would benefit the market.

<ESMA\_QUESTION\_TVPM\_9>