

Briefing note

ESMA Q&A updates on MiFID II / MiFIR market structure and data reporting

published on 7 July 2017 &

ESMA Q&A update on MiFID II investor protection topics (SFTs and RTS 27)

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The European Securities and Markets Authority (ESMA) has published on 7 July Q&A updates providing further guidance on [market structure](#) topics and [data reporting](#) requirements under MiFID II and MiFIR. As part of another Q&A update on investor protection on 10 July, ESMA further clarified that the best execution [reporting](#) requirements set out in RTS 27 should not apply to SFTs.

Below is a summary of key issues preceded by an executive summary. The technical requirements on MiFIR data reporting can be found in the Q&A updates.

Market structure topics:

- (i) **Non-discriminatory access to trading venues:** ESMA clarified that trading venues shall not impose “restrictive criteria governing their access” eg:
 - a) **Members or participants should not be required to be direct clearing members of a CCP.**
 - b) For centrally cleared financial instruments, **trading venues should not allow participants to require other participants to be enabled before they are allowed to trade with each other.**
 - c) **Trading venues should not require minimum trading activity.**
 - d) **In a request for quote (RFQ) protocol, a trading venue should not impose limits on the number of participants that a firm can request a quote from.**
- (ii) **Participation in a regulated market (RM) or an MTF:** An entity that is not an investment firm or a credit institution can be a member under certain conditions. However, this only applies to entities that are exempted such as insurance companies or collective investment undertakings.
- (iii) **A system that provides quote streaming and order execution services for multiple SIs should be considered a multilateral system** and would be required to seek authorisation as a RM, MTF or OTF.
- (iv) Access to CCPs and trading venues: **ESMA recommends that CCPs should notify their intention to make use of the temporary opt-out under Article 35(5) of MiFIR no later than 30 September 2017.**
- (v) **A CCP using an open offer trade acceptance model that receives a request for access from a trading venue using a novation trade acceptance model should grant access unless it entails undue risks.**

MiFIR data reporting:

- (i) **Actionable indications of interest are subject to pre-trade transparency requirements, and investment firms and trading venues are required to maintain records.**

Investor protection topics (best execution under RTS 27):

- (i) **ESMA considers that the best execution reporting requirements set out in RTS 27 should not apply to SFTs.**

1) Non-discriminatory access to trading venues [Section 5, Question 3]

Article 18(3) of MiFID II requires that investment firms and market operators operating an MTF or OTF establish, publish and maintain and implement transparent and non-discriminatory rules, based on objective criteria, governing access to its facility. A similar requirement is applied to regulated markets through Article 53(1) of MiFID II.

What sort of behaviour or restrictions should be considered as non-objective, or discriminatory?

- (i) One of the benefits of more on-venue, pre-trade transparent trading is to broaden access to liquidity for market participants. In order for these benefits to be fully realised, **it is important that trading venues do not have restrictive criteria governing their access**, which place unreasonable restraints on certain market participants' access to particular liquidity pools.
- (ii) In particular, **ESMA does not consider the following arrangements to be in compliance with Articles 18(3) and 53(1) of MiFID II**. This is not, however, an exhaustive list of arrangements which are non-objective and discriminatory.
 - a) **Trading venues should not require members or participants to be direct clearing members of a CCP.** [...] Trading venues may however require members or participants to enter into, and maintain, an agreement with a clearing member as a condition for access when trading is centrally cleared.
 - b) For financial instruments that are centrally cleared, **trading venues should not allow members or participants to require other members or participants to be enabled before they are allowed to trade** with each other.
 - In **centrally cleared** markets, **enablement mechanisms** whereby existing members or participants of a trading venue can decide whether their trading interests may interact with a new participant's trading interest **are considered discriminatory and an attempt to limit competition**.
 - In **non-centrally cleared** markets, trading venues may wish to carry out **credit checks**, or ensure that a member or participant has **appropriate capital to support the positions** it intends to take. Also, there may be a need for **bilateral master netting agreements** to be in place between participants before the trading venue can allow their trading interests to interact in derivatives markets.
 - c) **Trading venues should not require minimum trading activity.**
 - d) Trading venues should not impose restrictions on the number of participants that a participant can interact with.
 - **In a request for quote (RFQ) protocol, a trading venue should not impose limits on the number of participants that a firm can request a quote from.**
 - Limiting the number of participants a firm can request quotes from risks restricting the ability of market participants to access liquidity pools, and only sending requests to traditionally larger dealers who they assume might have larger inventories.
 - This simultaneously restricts the ability of the requestor to access the best pool of liquidity and reduces the likelihood of a smaller dealer receiving requests, despite it having a strong trading interest.

2) Can a person that is not authorised as an investment firm but meets the requirements of Article 53(3) of MiFID II be a member or participant of a regulated market or an MTF? [Section 5, Question 4]

- (i) Yes. Article 53(3) of MiFID II provides that **an entity that is not an investment firm or a credit institution can be a member of a regulated market under certain conditions**, this rule being **extended to MTFs** by Article 19(2) of MiFID II.
- (ii) ESMA considers that **this provision should be read in conjunction with the requirements of [Article 2\(1\) \[Exemptions\]](#)**. Under this provision, a person falling under any of the categories listed in Article 2(1) would not have to be authorised as an investment firm.
- (iii) However, pursuant to Article 2(1)(d) (ii) of MiFID II, **when a person dealing on own account in financial instruments [...] is also a member of or a participant in a regulated market or an MTF, it falls under the scope of MiFID II** and should accordingly be authorised as an investment firm.
- (iv) The exception being insurance undertakings (1)(a), collective investment undertakings and pension funds (1)(i) and market makers or providers of investment services in commodity derivatives or emission allowances (1)(j).
- (v) As a consequence, **the reference in Article 53(3) to persons other than investment firms and credit institutions only relates to entities that are exempted from authorisation under Article 2(1), such as insurance companies or collective investment undertakings**, as long as their own regulatory framework permits them to do so.

MiFID II Article 53 – Access to a regulated market

(3) Regulated markets may admit as members or participants investment firms, credit institutions authorised under the Capital Requirements Directive (2013/36/EU) and other persons who:

- (a) are of sufficient good repute;
- (b) have a sufficient level of trading ability, competence and experience;
- (c) have, where applicable, adequate organisational arrangements;
- (d) have sufficient resources for the role they are to perform, taking into account the different financial arrangements that the regulated market may have established [...].

Article 19 – Specific requirements for MTFs

(2) Member States shall require that the rules referred to in Article 18(3) governing access to an MTF comply with the conditions established in Article 53(3).

Article 18 – Trading process and finalisation of transactions in an MTF and an OTF

(3) Member States shall require that investment firms and market operators operating an MTF or an OTF establish, publish and maintain and **implement transparent and non-discriminatory rules, based on objective criteria, governing access to its facility.**

3) Should a system providing quote streaming and order execution services to multiple SIs be authorised as a multilateral system? [Section 5, Question 19]

- (i) Articles 14(1) and 18(1) of MIFIR require SIs to make public firm quotes, which may be published through an APA. Some prospective APAs propose setting up arrangements which, on top of their APA services, provide a suite of quote streaming and order execution services to SIs and their clients. Clients cannot interact with more than one SI via a single message but can send multiple messages to multiple SIs participating in the service provided.
- (ii) **Article 4(19) of MiFID II defines a multilateral system as "[...] any system or facility in which multiple third-party buying and selling trading interests in financial instruments are able to interact in the system"**. Article 1(7) of MiFID II requires all multilateral systems to operate as either a RM, an MTF or an OTF.
- (iii) **In line with the criteria set out in Q&A 3 on OTFs published on 3 April 2017** for identifying multilateral trading systems, ESMA notes that:
 - a) **If a system allows multiple SIs to send quotes to multiple clients and allows clients to request execution against multiple SIs, then this meets the interaction test** foreseen in Article 4(1)(19) even if there is no aggregation across individual SI quote streams;

- b) The arrangements described above have the **characteristics of a system** as they are **embedded in an automated facility**; and,
 - c) Those arrangements are **not limited to pooling potential buying and selling interests from SIs** but **also cater for the direct execution of the selected SI quotes**. Genuine trade execution would be taking place on the system provided.
- (iv) **Accordingly, a system that provides quote streaming and order execution services for multiple SIs should be considered a multilateral system and would be required to seek authorisation as a regulated market, MTF or OTF** in accordance with Article 1(7) of MiFID II.
- (v) ESMA reminds that if a firm were to arrange transactions on one system and provide for the execution of the transactions on another system, **the disconnection between arranging and executing would not waive the obligation for the firm operating those systems to seek authorisation as a trading venue**.

**4) Access to CCPs and trading venues [Section 6, Question 1]
When should CCPs notify the transitional arrangements foreseen in Article 35(5) of MiFIR?**

- (i) Article 35(5) of MiFIR does not establish any timing other than indicating that CCPs must submit their notification before the application of MiFIR.
- (ii) However, [...] ESMA encourages CCPs that [...] are considering applying for the transitional arrangements to do so as early as possible during the course of 2017.
- (iii) In any case, **ESMA recommends that CCPs should notify their intention to make use of the temporary opt-out under Article 35(5) of MiFIR no later than 30 September 2017**.

MiFIR Article 35 – Non-discriminatory access to a CCP

(5) As regards transferable securities and money market instruments, a CCP that has been newly established and authorised as a CCP [...] may, before 3 January 2018 apply to its competent authority for permission to avail itself of transitional arrangements. The competent authority may decide that this Article does not apply to the CCP [...] for a transitional period until 3 July 2020. [...]

5) Is a CCP using an open offer trade acceptance model obliged to accept a request for access from a trading venue using a novation trade acceptance model? [Section 6, Question 2]

- (i) **Yes, a CCP using an open offer trade acceptance model that receives a request for access from a trading venue using a novation trade acceptance model should grant that access unless it can identify how precisely the simultaneous use of an open offer and a novation trade acceptance model would give rise to significant undue risks that cannot be managed.**

[ESMA Q&A updates on MiFIR data reporting:](#)

ESMA has furthermore provided a number of [clarifications](#) on technical reporting requirements related to reference data for financial instruments [RTS 23], transaction reporting [RTS 22], and on order record keeping [RTS 24]. Below is the clarification on pre-trade transparency and record keeping requirements.

1) Are actionable indications of interest subject to the order record keeping requirements for Investment Firms and trading venues under Article 25(1) and (2) of MiFIR? [Question 15]

- (ii) Yes. An “*actionable indication of interest*” is defined in Article 2(1)(33) of MiFIR as “*a message from one member or participant to another within a trading system in relation to available trading interest that contains all necessary information to agree on a trade*”.
- (iii) Actionable indications of interest are **subject to pre-trade transparency requirements** under Articles 3(1) and 8(1) of MiFIR, along with current bid and offer prices and the depth of trading interests at those prices.

- (iv) **To ensure that relevant and sufficient data is kept at the disposal of competent authorities, paragraphs 1 and 2 of Article 25 of MiFIR set out the obligation on investment firms and trading venues to maintain records** of, amongst others, the relevant data relating to these orders, **including actionable indications of interest.**

[ESMA Q&A update on investor protection topics \(best execution under RTS 27\):](#)

1) Do the RTS 27 reporting requirements apply to Securities Financing Transactions (SFTs)? [Question 15]

- (i) Article 1(5)(a) of MiFIR, subsequent to amending Regulation (EU) 2016/1033 of 23 June 2016, states that SFTs are not subject to the pre and post trade transparency obligations set out in Title II and III of MiFIR.
- (ii) While no specific exemption was included with respect to the RTS 27 best execution reporting obligations, Recital 10 of RTS 27 refers to the need for regulatory consistency between its requirements and those on post trade transparency. **In this context, ESMA considers that the best execution reporting requirements set out in RTS 27 should not apply to SFTs.**
- (iii) ESMA wishes to make clear that, irrespective of the above clarification concerning the application of RTS 27 to SFTs, **the MiFID II best execution requirements otherwise apply to investment firms when carrying out SFTs.**
- (iv) ESMA also wishes to clarify that while RTS 27 would not apply to SFTs, this would not lead to a complete absence of execution quality reports for SFTs, as RTS 28 explicitly requires investment firms to report, inter alia, on order routing behaviours specifically with respect to SFTs and to provide a summary on the quality of execution obtained. Investment firms should also note that RTS 28 already makes specific reference to how data concerning SFTs should be published.

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