29 January 2016

FESE Response to the European Commission consultation:
"Call for evidence: EU regulatory framework for financial services"

Introduction
The Federation of European Securities Exchanges (FESE) represents 36 exchanges in equities, bonds, derivatives and commodities through 19 Full Members from 30 countries, as well as 1 Affiliate Member and 1 Observer Member.

FESE is a keen defender of the Internal Market and many of its members have become multi-jurisdictional exchanges, providing market access across multiple investor communities. FESE represents public Regulated Markets. Regulated Markets provide both institutional and retail investors with transparent and neutral price-formation. Securities admitted to trading on our markets have to comply with stringent initial and ongoing disclosure requirements and accounting and auditing standards imposed by EU laws.

At the end of 2014, FESE members had up to 9,051 companies listed on their markets, of which 7% are foreign companies contributing towards the European integration and providing broad and liquid access to Europe's capital markets. Many of our members also organise specialised markets that allow small and medium sized companies across Europe to access the capital markets; 1,442 companies were listed in these specialised markets/segments in equity, increasing choice for investors and issuers. Through their RM and MTF operations, FESE members are keen to support the European Commission's objective of creating a single market in capital markets.

FESE is registered in the European Union Transparency Register with number 71488206456-23.

In all of its activities, FESE is guided by the following overarching objectives:
- Fostering the global competitiveness of European exchanges
- Promoting public recognition of the exchanges and their contribution to the European and global economy;
- Providing a forum for open and forward-looking debate on capital markets.

Vision for European Capital Markets
As the operators of Europe's Regulated Markets, FESE members have come together to elucidate a **common vision**[1] on how European capital markets can finance Europe's future growth and development and what policymakers and industry can do to accelerate this growth. As we shall explain in greater detail in this document, we believe that **a fundamental re-orientation of Europe's policies is needed** to serve the original goals of the Single Market better at this current point in time. A re-orientation is critical to achieving the objectives of "Europe 2020", the EU's growth strategy for the current decade. As outlined above, more financing through capital markets helps achieve not just greater amounts of financing but also higher levels of innovation, risk management, savings

[1] http://www.fese.eu/images/documents/speeches-reports/2014/150522_FESE-Blue-Print.pdf
http://www.fese.eu/images/documents/speeches-reports/2015/Final_report_IPO_Task_Force_20150323.pdf

mobilisation, wealth distribution and job creation – which would serve the Union's 2020 objectives on employment, innovation, education, social inclusion and climate/ energy.

In the initial 10-15 years of building the Single Market, the EU concentrated on policies that would foster the **integration** of its national financial sectors in order to create **one united European market** that would be efficient, deep, and competitive. In doing this, a major focus was on reducing the transaction costs of trading of the largest stocks ("blue chips") which, it was assumed, would lower the cost of accessing capital markets (but there was no systematic measurement of the net effects on end-users in the real economy). **Cross-border competition** was the main tool to increase efficiency as experienced by the financial services industry. There was also limited discussion on what impact trading would have on the conditions for **listing** faced by companies, especially smaller ones.

FESE members – which traditionally operated nationally-based exchanges - endorsed the EU's objective of creating a Single Market, and rose to the challenge through greater competitiveness and, in some cases, mergers or partnerships on a regional or transatlantic basis, while also continuing to fulfil their capital raising role in the national economies. Other important changes occurring in the same timeframe – in technology and market structure – also led to more pan-European trading, a greater concentration of broker and other services around blue chips, and a shift of trading and investment away from smaller companies.

The resulting policies have helped increase the efficiency of trading, in particular in the largest companies, and as such have been effective. However, we believe that policies of the future should be underpinned by a new direction, which we summarise around three **high-level principles:**

(i) A greater focus on the end-users of capital markets, i.e. **COMPANIES** and **INVESTORS**, and in particular on the core function of capital markets to finance growth.
(ii) The EU Single Market must be **ACCESSIBLE** to companies at **ALL LEVELS**: national, regional and pan-European.
(iii) A greater awareness of the importance of the **DIVERSITY OF ECOSYSTEMS**, and the way they are impacted by the inter-action between listing and trading.

In other words, our vision is that of a capital market which exists for issuers and investors above all. It is a capital market in which European issuers of different instruments and investors can meet one another be it at a local, regional, pan-European or global level. In this vision, all policies are designed to help the capital raising function of markets above all other priorities. In this market, any policy on trading is judged on how it affects the diversity of the financial services that exist to serve companies, other issuers and investors. In our vision, competition and efficiency are put to the service of the end-users of markets - the issuers and investors - while the EU creates the right conditions for national and regional ecosystems to serve their stakeholders and economies.

These three principles will ensure that European capital markets are better adapted to the economic and political needs of Europe and better positioned to propel Europe into global economic leadership. This reorientation will not only finance economic growth, but also enhance the credibility of the EU vis-à-vis its citizens and distribute the benefits of integration among all citizenry.

Summary of response to Commission Call for Evidence

Theme A. Rules affecting the ability of the economy to finance itself and grow	
Issue 1 – Unnecessary regulatory constraints on financing	
(i) Financial Transaction tax	Introduction of an FTT will dis-incentivise equity financing in Europe.
(ii) MiFID II	Excessive fragmentation negatively impacting real economy.
Issue 2 – Market Liquidity	
(i) MiFID II & CRR	Reduction in market making activity and impact on liquidity.
(ii) EMIR & MiFIR	Dangerous shift of trading of warrants/certificates to unregulated platforms.
Issue 3 – Investor and consumer protection	
(i) MiFID I, MiFID II, MiFIR	Negative impact of hybrid systems on investor protection and best execution rules.
(ii) PRIIPs	Risk of misrepresentation of certain products to retail investors.
(iii) MiFID II	Risk of banks abandoning provision of investment advice to retail investors.
(iv) Financial Transaction Tax	Negative impact on private households and real economy.
(v) Investor Compensation Schemes & MiFID II	Need to address the inadvertent application of rules to MTFs & OTFs.
Issue 4 – Proportionality / preserving diversity in the EU financial sector	
(i) Statutory Audit Directive	Unintended inclusion of specialist issuers under the definition of "Public Interest Entity".
(ii) Prospectus Directive	Exemption limit too low for secondary issuance.
Theme B. Unnecessary regulatory burdens	
Issue 5 – Excessive compliance costs and complexity	
(i) MiFID II	Overly complex publication regimes for trading venues and SIs.
(ii) Prospectus Directive	Process for approval and publication too long and expensive.
(iii) MiFID II	Need to continue use of both ISINs and AIIs for derivatives.
(iv) MiFIR	Burdensome requirement to publish overly extensive reference data.
(v) MiFIR	Overly complex and burdensome requirements for data disaggregation.
Issue 6 – Reporting and disclosure obligations	
(i) Transparency Directive	Unnecessary requirement to republish suspension notices.
(ii) MAR	Implications of extension of MAR to MTFs for SMEs.
Issue 7 – Contractual documentation	
(i) MiFID II & MiFIR	Impact of increased costs of providing investment advice to retail investors.

(ii) PRIIPs	Need for reassessment of practical implications of scope of KID for PRIIPs.
Issue 8 – Rules outdated due to technological change	
(i) Shareholder Rights Directive	Need to update format of written communications.
Theme C. Interactions of individual rules, inconsistencies and gaps	
Issue 11 – Definitions	
(i) MiFID II & Prospectus Directive	There is a need for further consideration of the existing SME Definitions.
(ii) MiFID II	Further clarification on the definition of Systematic Internaliser needed.
(iii) General definitions across all Directives and Regulations.	There is a need for harmonised approach to definitions of key terminology across financial services legislation.
Issue 12 – Overlaps, duplications and inconsistencies	
(i) Financial Transaction Tax	Impact on risk management activity.
Issue 13 – Gaps	
(i) Stand-alone national laws and EU regulation.	Impact of national gold plating on EU single market.
(ii) MiFID II	Need to bring SIs under the tick size regime.
Theme D. Rules giving rise to possible other unintended consequences	
Issue 14 – Risk	
(i) EMIR & MiFIR	Impact of EMIR clearing obligation on MiFIR trading obligation.
(ii) MiFID II	Risks of introducing RFQ systems for equities trading.

Response to Commission Call for Evidence

Theme A. Rules affecting the ability of the economy to finance itself and grow

Issue 1 – Unnecessary regulatory constraints on financing

Example 1: Unnecessary regulatory constraints on financing

To which Directive(s) and/or Regulation(s) do you refer in your example?

- FTT: Proposal for a Council Directive implementing enhanced cooperation in the area of financial transaction tax (COM/2013/71)

Please provide us with an executive/succinct summary of your example:
The design of the Financial Transaction Tax (FTT) as currently proposed contradicts the policy objectives derived from the financial crises, as the FTT will stimulate the migration of financial transactions to less regulated and non-transparent markets outside the participating Member States. We consider that FTT will hinder the stability of the financial sector.

We continue to oppose the introduction of an FTT. Such an initiative will simply increase transaction costs and lead to SMEs, in particular, facing higher capital-raising costs as a result of rising costs. Retail investors would also suffer greater financial losses as the tax directly hits retirement provision products. In short, we see this initiative as fundamentally incompatible with the stated goals of the Capital Markets Union. We strongly believe that we have to get to grips with the fiscal disincentives to equities financing in Europe. We consider that an FTT will further increase the bias towards debt financing. Therefore, we would urge the European Commission to conduct an impact assessment on the impact on the cost of capital arising from the current tax bias against equity investments.

Furthermore, the FTT as currently discussed would not be in line with the addressing the principle causes of the financial crises as the costs of this tax would be borne by small and medium enterprises via growing capital-raising costs. Savers and private households would also suffer financial losses as the tax would directly hit their retirement provision products. Policy objectives and regulatory aims aligned to the FTT cannot be achieved considering the institutional design as well as the legal scope of the current proposal.

With regard to MiFID II's Best Execution Rules, these foresee the necessity to outline all costs that an investor faces at a trading venue and to reflect them in their Best Execution Policies. The costs outlined in these policies would most likely also have to include the FTT. However, If all EU member states are not involved in such a tax regime, then clearly trading venues located in these countries would be at an advantage, as Best Execution requirement would mandate brokers to route the orders to venues in countries without FTT.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
A central obstacle to the development of public capital markets in Europe are some of the current fiscal arrangements in place. Today, it is clear that the equity part of the market is suppressed artificially by fiscal advantages given to debt instruments, especially in the aftermath of the sovereign crisis. As the City of London's IRSG highlighted in a recent report (Long-Term Finance for Infrastructure and Growth Companies in Europe, IRSG – March 2015)[2], debt has been favoured over equity for long-term financing by a large majority of corporate tax and legal environments in Europe and

[2] http://www.irsg.co.uk/assets/Uploads/Long-term-Finance-for-Infrastructure-and-Growth-Companies-in-Europe.pdf

internationally, a situation which has developed over time. For example, allowing the deduction of debt interest costs has incentivised debt financing, while there is no similar treatment for the costs incurred in raising equity. This tax bias towards debt financing may incentivise companies to take on more debt and discourage innovative investment strategies. This fiscal bias against equity needs to be recalibrated to reduce incentives for companies to use leverage and debt and encourage the entrepreneurial culture for which equity can be the most suitable form of finance. We therefore strongly share the City of London's recommendation on the need for an impact assessment study in this area.

Similarly, the tax treatment of the income received from IPOs/equity for investors is also a factor in determining the return for the investor. Favourable treatment of assets other than public equity (e.g. sovereign debt may be treated more favourably than corporate debt) which enjoy more favourable treatment under prudential capital regimes, may reduce the appetite for other asset classes. We note that this bias against equity, in particular in respect of corporate taxation, has been recognised in the recent Commission Communication on Long-Term Financing of the European Economy, which states that the Commission will monitor the issue "through country specific recommendations in the European semester process, to incentivise equity investment in particular for Member States with high debt bias in corporate taxation" (Page 15 of the Communication on Long-term financing of the European economy).

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
We call on the Member States to review fiscal incentives against equity financing in Europe given the high potential positive impact such changes could deliver for the overall attractiveness of European public capital markets. Tax incentives could be introduced to encourage retail investors, for example, to invest in long-term instruments of listed equity of smaller companies. Initiatives such as the French saving plan for shares investment should be assessed with a view to sharing information of differing approaches which can be used to develop appropriate measures in each Member State.

Example 2: Unnecessary regulatory constraints on financing

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65 on Markets in Financial Instruments.

Please provide us with an executive/succinct summary of your example:
Excessive fragmentation in European markets following MiFID I has negatively impacted the ability of local exchanges and ecosystems to perform to finance the real economy. While rule harmonisation has facilitated cross-border business since the introduction of MiFID I, it has also had the unintended consequence of concentrating activity in larger financial centres with a disproportionate impact on local ecosystems and financing activities in smaller Member States. We explain this below in respect of what we have witnessed on our markets.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
Following MiFID I, the emergence of multilateral trading facilities (MTFs) and broker crossing networks (BCNs) competing with national stock exchanges has introduced a high degree of fragmentation in European equities markets. While there are a range of factors which have impacted these markets – not least the financial crisis – we believe MIFID I did play a part in the weakening of the local market ecosystems.

As an example, under MIFID I local brokers have been faced with the obligation to connect to an increasing number of trading platforms to ensure that their clients obtain the best execution for their orders, as required by the legislation. Given that securing access to all these platforms was associated with mounting IT and membership costs, it became uneconomical for local brokers to continue catering directly to the local markets. A majority of them decided, therefore, to outsource their order flows to larger investment banks – often in London - including the best execution requirements. As a result, the majority of trading in local shares is now done out of a small number of financial centres, impacting liquidity at the local level.

The impact of this shift has been particularly detrimental to the ability of smaller local companies to access finance, the reasons being two-fold: firstly, trading on the new platforms – ostensibly located in London – has focused on the most liquid and profitable business, i.e. trading in blue chips, with very little attention given to more local mid-caps and SMEs. In addition to that, the ability of local brokers to animate the local market and dedicate research and resources to smaller companies has been greatly hindered. This is because those less profitable activities were previously supported by activity in more profitable blue chips, which has now been 'lost' to bigger players as we explain above. In addition, one of the consequences of MIFID I was the emergence of dark pools and OTC share trading which played a role in amplifying this trend.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
Many of the measures introduced as part of the MiFID II reforms such as the introduction of the share trading mandate and caps on trading on dark venues should prove positive for public market ecosystems as they aim to restore the price discovery process on transparent and regulated markets. However, we would take this opportunity to repeat the call we have made to ESMA and the EU institutions consistently over the last year to ensure that the technical rules implementing MIFID II are consistent with the intent of the Level 1 text in this objective.

We outline our main concerns under Issue 14, Example 2 in respect of the Systematic Internaliser and proposed Request-for-Quote (RFQ) systems for equities.

Issue 2 – Market liquidity

Example 1: Market liquidity

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65 on Markets in Financial Instruments [Definition of investment firm (Article 4.1 (1)), and authorisation of investment firms (Article 5)].
- CRR: Regulation 575/2013 on prudential requirements for credit institutions and investment firms [Chapter 2 on own fund requirements for position risk, Articles 328.1 and 329].

Please provide us with an executive/succinct summary of your example:
FESE believes that investment firms that engage solely in proprietary trading are appropriately and sufficiently regulated by the organisational and risk management requirements of MiFID II. This regulatory framework exists in combination with the robust operational risk frameworks such firms have in place to manage operational risk and the margining and risk management requirements of such firms' general clearing firms. We believe that any additional capital requirements add material cost that preclude market making and liquidity provision, in contravention to the legislative intent of MiFID II, and harm liquidity across European trading venues. FESE supports the MiFID II obligation for proprietary traders to request an investment firm authorisation, however, the Commission must tackle the unintended consequences within the Capital Requirements Regulation (CRR).

Proprietary traders are within the scope of the definition of investment firm (MiFID II) and subjected to the same capital requirements, since CRR does not distinguish between proprietary traders dealing on own account and other investment firms. FESE agrees that authorisation for proprietary traders is necessary but questions the proportionality of the capital requirements for proprietary traders. FESE believes that the capital requirements should be better calibrated by distinguishing between investment firms with respect to activity. Moreover, this would also provide recognition of how these firms positively contribute to market liquidity and transparency.

We are deeply concerned that vital market makers will withdraw from the market if their business model becomes economically unviable (as cautioned by FIA EPTA). This would result in decreased liquidity on regulated markets, which would in turn favour OTC trading; effectively impeding the legislator's objective of increasing transparency in non-equity markets. As the majority of derivatives markets (approx. 80%) is already today OTC, the need for regulated markets to keep market makers that create liquidity for electronic and transparent trading is all the more pressing.

CRR needs to be reviewed to recognise that firms that will be authorised as investment firms under MiFID II have different business models and operate different levels of market risk. Their respective capital requirements should therefore be adjusted to better reflect the level of risk involved.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
<u>Example</u>: Directional exposure
Derivative market makers provide liquidity by continuously quoting groups of related financial instruments. Option market makers specialise in quoting the volatility surface as a whole. They will transact with investors at a competitive price, take on the risk of the resulting position, manage it and mitigate it by transacting against other investors who have interest in trading contracts in the same volatility surface. After inheriting a position in a certain option contract, the market maker is unlikely to be able to dispose of it by finding an investor with exactly the opposite interest in the same contract. More likely, the market maker will aim to mitigate risks when a natural buyer or seller wants to trade an option with a similar strike or expiry. The book of an options market maker is thus unlikely to be completely flat. Rather than eliminating every single position, the market maker will ensure that

position risks net-off, and that the value-at-risk of the portfolio is commensurate with the risk appetite of the trading firm and its GCM.

Derivative portfolios are heavily influenced by the behaviour of the underlying contracts. It is therefore reasonable to assess the effect of a large underlying move on the portfolio value. Paragraph 1 of Article 329 CRR states that "options and warrants on interest rates, debt instruments, equity indices, financial futures, swaps and foreign currencies shall be treated as if they were positions equal in value to the amount of the underlying instrument to which the option refers, multiplied by its delta". The delta of a portfolio reflects its sensitivity to small fluctuations in the underlying. Entities are required to treat this delta weighed position as an equivalent in the underlying instrument and subject it to the standard calculations outlined in articles of the General Risk (Sub-Section 2).

However, this directional exposure calculation gives rise to a charge that does not adequately reflect the risks – simply because delta is not a constant over the range of the underlying price. For option positions, the delta weighed directional exposure only has meaning over tiny intervals of the underlying price. The derivative of the delta of the option – its gamma – is never zero or less and is often significantly positive. Therefore, the delta of an options position will change significantly as the underlying is stressed.

Please note that as MiFID II has not yet been finalised and transposed the effects can only be envisaged.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
The European Banking Authority recommends introducing a re-categorisation for distinguishing between systemic 'bank-like' investment firms and non-systemic investment firms, where the latter should be subject to "a more limited set of prudential requirements", and calls for "a fundamental change in the criteria that determine investment firms' categorisation". Moreover, it is recognised that the current categorisation "does not contain an (inherent) analysis of the risks posed by investment firms". The EBA further states that investment firms that deal on own accounts with no external clients should be assessed differently compared to banking groups.[3]

In line with the EBA recommendations, FESE suggests that legislators and regulators respect their legal obligation to conduct a detailed impact assessment. This should focus on the effects of MiFID II authorisation requirements and CRR interaction on vital market liquidity. In order to promote the objectives announced for a Capital Markets Union, all efforts should be made to preserve and enhance market liquidity in secondary markets.

[3] European Banking Authority, "Report on Investment Firms Response to the Commission's Call for Advice of December 2014 EBA/Op/2015/20",p. 7, 19 & pp. 22-23, Available at: http://www.eba.europa.eu/documents/10180/983359/EBA-Op-2015 20+Report+on+investment+firms.pdf

Example 2: Investor and consumer protection

To which Directive(s) and/or Regulation(s) do you refer in your example?

- EMIR: Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories.
- MiFIR: Regulation (EU) No 600/2014 on markets in financial instruments.

Please provide us with an executive/succinct summary of your example:
A number of FESE members provide trading in warrants and certificates on their regulated markets with a multilateral market model and full pre-trade and post-trade transparency. We are increasingly witnessing a shift of trading in these products from the regulated environment to OTC platforms. While the intent of EMIR and MiFIR was to incentivise trading and clearing on transparent and regulated venues, our warrants and certificates products were not included in the scope of the trading and clearing mandates. This raises important investor protection issues both because investors may miss out on price improvement opportunities on regulated venues and trading on OTC platforms is mostly not going through a CCP. We believe this to be all the more problematic that warrants and certificates have an overwhelmingly retail audience.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
As we outline under Issue 14 (Risk), any instrument which does not fall under the scope of the clearing obligation (EMIR) will not be eligible for the trading obligation (MiFIR). Warrants and certificates (categorised as 'securitised derivatives' under MiFIR) do not fall within the scope of these regulations.

As a result, the way EMIR and MiFIR interlink with one another has created an incentive for investors to trade on an OTC basis, where explicit transaction costs are lower due to the absence of transparency, market surveillance, and clearing. This situations raises three major issues.

1. Retail investors miss out on price improvement opportunities
Trading in a multilateral and transparent market structure provides benefits with regard to the creation of price improvement opportunities for both buyers and sellers. Leveraging the benefits of the open order book, investors are able to trade within or at the spread of the market-maker with other market participants, thereby getting a better price than in a bilateral system where they are only able to trade with a market-maker.

Because this opportunity does not exist in a bilateral OTC system, investors shifting to unregulated trading are likely to miss out on better trading conditions. In addition, the fact that an increasing number of brokers are routing their order flow exclusively to OTC venues reduces the number of orders resting in the transparent order book and diminishes opportunities for price improvement for all investors.

2. This in turn raises questions around best execution
Because transactions on an OTC basis are free (no transparency, no market surveillance, no clearing), investors stand to make small gains in terms of explicit transaction costs (the amount charges by regulated venues for trading and clearing) by opting for OTC execution – provided the broker pass these savings onto them.

This needs to be contrasted with the price improvement opportunities we outline above. If both implicit and explicit transaction costs are taken into account, it does not seem a given that brokers are fulfilling their best execution obligations by systematically routing their retail flow to OTC platforms.

3. **Without a change in the framework, the shift to OTC creates incentives for multilateral venues to opt for less transparent market models**

In the warrants and certificates market, FESE members are competing with OTC venues on the basis of a total lack of level playing field as these venues do not clear transactions, do not provide market surveillance, and operate a bilateral and more opaque trading system.

At the moment, we face substantial competitive pressures from OTC venues and witness a considerable shift from our multilateral, cleared, and transparent model to OTC. In the absence of regulation or other incentives to counter this shift, transparent and multilateral venues will need to draw the conclusions from the competitive environment. Ultimately, we will have no choice but to pivot towards a less transparent market model in order to be able to compete on fairer grounds with OTC venues.

Therefore, the gap in EMIR and MiFIR in respect of securitised derivatives creates incentives for investors and trading venues alike to shift to less transparent trading patterns. We believe this is strikingly at odds with the overall objectives of EMIR and MiFIR to bring more trading onto regulated and transparent venues.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:

In light of the above considerations, we recommend including securitised derivatives within the scope of EMIR's clearing mandate and MiFIR's trading mandate in order to ensure that these products can continue to be traded in a transparent and multilateral environment.

Issue 3 – Investor and consumer protection

Example 1: Investor and consumer protection

To which Directive(s) and/or Regulation(s) do you refer in your example? *
(If applicable, mention also the articles referred to in your example.)

- MiFID I: Directive 2004/39/EC on Markets in Financial Instruments Directive.
- MiFID II: Directive 2014/65/EC on Markets in Financial Instruments.
- MiFIR: Regulation (EU) No 600/2014 on markets in financial instruments.

Please provide us with an executive/succinct summary of your example:
Both MiFID I and MiFID II/ MiFIR offer the possibility to operate a 'hybrid system' on Regulated Markets and MTFs (also OTFs in the case of MiFID II). While these systems are deemed to be pre-trade transparent, transparency is essentially optional as it is only required "if the characteristics of the price discovery process so permit".

This raises important investor protection and best execution issues as the definition of hybrid systems provide an opt-out from any transparency while allowing platforms to claim they are pre-trade transparent and fulfil best execution requirements.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
As things currently stand, pre-trade transparency is essentially optional on hybrid systems. We are concerned that such an open-ended provision will be used by venues operating such systems to systematically request suspension of the transparency provisions. In fact, there have been examples under MiFID I of venues making use of this mechanism to import a reference price from the reference market, offer trading at mid-point in a similar way as a dark pool operating under the reference price waiver, and market itself to investors as a pre-trade transparent venue guaranteeing best execution.

This raises questions as to how best execution is monitored, as systematic execution at the midpoint of the best bid and offer on the reference market certainly may deliver a certain degree of price improvement but reduces the notion of best execution to best price, without taking into account other factors such as overall market quality, volumes available on the platform, time of execution, etc.

In addition, following the introduction of restrictions on dark trading and the use of the reference price waiver in MiFID II, we are concerned that hybrid systems will provide a convenient loophole to bypass the double volume cap. This is because, in the absence of any guidelines on how to use the 'hybrid system' regime, the requirements are so flexible that they could accommodate systems which simply import a price from another venue instead of participating to price formation through the interaction of buying and selling interests on the platform. This is typically the kind of parasitic behaviour which endangers price discovery on the overall market and that MiFID II sought to curb under the double volume cap.

However, there are also legitimate uses of the hybrid system category that should enable idiosyncratic trading mechanisms which would otherwise remain OTC to find a home on regulated trading venues. An example of that could be the exchange-for-physical (EFPs) trading mechanism which essentially allows a transaction in a derivative contract, say a commodities future, and a transaction in its physical underlying to take place simultaneously on pre-agreed terms. While EFPs do not have an obvious regulatory home under MiFID II, they are hybrid in nature and should be able to be accommodated under the hybrid system category.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
In light of the above considerations, we urge the Commission and ESMA to clarify in Level 3 guidelines what the depth and breadth of the hybrid system category is as well as what type of activities could legitimately find a regulatory home under its umbrella. This would ensure that potential MiFID II loopholes are closed and that the provisions are applied in a uniform and consistent way across jurisdictions.

Example 2: Investor and consumer protection

To which Directive(s) and/or Regulation(s) do you refer in your example?

- PRIIPs: Regulation 1286/2014 on key information documents for packaged retail and insurance-based investment products.

Please provide us with an executive/succinct summary of your example:
With the introduction of the PRIIPS Regulation, legislators sought to ensure a coordinated set of transparency rules for these products when offered to retail investors. This is to ensure that investors are able to understand and compare the products they are being offered. While we fully support this approach, we fear that the framework currently suggested by regulators is proving too strict and too uniform. Without change, this will lead to rules that would have to be applied to products, such as exchange-traded derivatives, that do not fit properly into the framework, leading to these products potentially being misrepresented to the retail investor audience.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
The key difference between listed derivatives and 'packaged products' in the traditional sense of the word is that listed derivatives are not issued by the exchange. Moreover, the exchange does not become a counterparty to the retail investor (or anyone for that matter) committing to any pay-outs. In reality, the exchange has no relation at all with the end investor as trading in the products is undertaken by Members, themselves MiFID licensed investment firms. Those firms entertain the relationship with the end investor. This difference leads to the inability of the exchange to complete a Key Information Document (KID) according to the proposed set of rules – an exercise we have simulated and will share with regulators. In short, we encounter a number of practical problems preventing us, as exchanges, from fully complying with the set of demands.

In addition, the KID does not allow for an informed decision regarding standard derivatives. Our products (individual equity options, index options, equity futures, index futures) are traded on regulated markets and are fully pre- and post-trade transparent. The rules around the KID are very much designed to clarify the working, risks, issue price, disinvestment procedure, performance scenarios and costs of packaged products; given the complexity of packaged products this has added value. Applying these rules to options & futures might give the impression to add clarity and help to compare options & futures with packaged products, but it does not. Options & futures are fully transparent in design, in costs and in pricing. The exchange (manufacturer) is not counterparty to a trade, so the exchange does not profit from the trading price of options & futures. No counterparty to a trade can benefit at the cost of another because of an unbalanced relation between buyer and seller; every investor can create a long or a short position and therefore every counterparty is equal.

In addition, we have concerns about the positioning of these products in comparison to other products, particularly in respect of risk indicators. The risk indicator as suggested by ESMA focuses on the individual product. As options and futures are often part of a hedging strategy, the risk is low. However ESMA suggests that listed derivatives should be based in the highest risk category. This would not do justice to the nature of the product or to the trading environment. Also, during the financial crisis, no issues have arisen in and around the trading of listed derivatives that have continuously been traded and have not been under regulatory scrutiny.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
Our preferred option would be to exclude exchange-traded derivatives from the scope of the PRIIPs Regulation. Should that not be possible, we would support introducing an alternative to the KID for exchange-traded derivatives that would better fit the characteristics of these products while providing sufficient information for investors.

Example 3: Investor and consumer protection

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65/EU on markets in financial instruments [Article 25 (6)].

Please provide us with an executive/succinct summary of your example:
Tightened investor protection rules were introduced under the revised MiFID II / MiFIR framework, for example the rules for investment advice of banks and other financial institutions has the objective of improving the information retail investors receive from banks. Banks across Europe will have to document their investment advice in future, although experience shows that overwhelming documentation duties already have negative side effects.

As a consequence, many banks abandoned their investment advice services for shares significantly or completely and retreated from investment advice in other securities like bonds and investment funds. This development will further harm the equity culture among retail investors, which is already underdeveloped in the EU compared to other jurisdictions like the US. Additionally, the documentation requirement appears to be too time-consuming. These are the reasons why the EU Commission should provide experienced retail clients (e.g. those customers receiving an investment advice five times in the last two years) the option to waive the obligation that the suitability of the investment advice has to be recorded ("suitability report" Art.25 (6) MiFID II).

Transparency and a sufficient level of information are crucial for investor protection. However, they should take into account potential negative side effects. Future efforts to reform the European framework for investor protection should focus on a widespread economic literacy as a core element to enable investors to make sound and responsible investment decisions.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
A study of Deutsche Aktieninstitut provided evidence that a significant number of banks have already withdrawn from investment advisory services. Due to strict regulatory requirements 22 % of credit institutions ceased to provide any advice in shares; 65% reduced its dealings – by and large significantly – with customers regarding shares (DAI, "As a result of regulation banks refrain more and more from providing investment advice in shares - a survey", July 2014[4]). Investors do not get adequate advice from their banks, simply because advisory services have become too costly and complicated.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
Promote education in order to achieve an economy based on knowledge and innovation, including measures to improve financial and economic literacy as a core element. There is a need for well-defined investor protection rules and provide experienced clients the option to waive documentation requirements about investment advice.

[4]https://www.dai.de/files/dai_usercontent/dokumente/studien/2014-7-10%20DAI-Studie%20Regulierung%20der%20Aktienberatung.pdf

Example 4: Investor and consumer protection

To which Directive(s) and/or Regulation(s) do you refer in your example?

- FTT: Proposal for a Council Directive implementing enhanced cooperation in the area of financial transaction tax (COM/2013/71).

Please provide us with an executive/succinct summary of your example:
The introduction of an FTT would significantly and negatively affect private households and the real economy alike. It will not stabilise capital markets and will not generate the expected revenue but will rather hinder growth and increase risks for investors.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
The tax burden will be shifted to the end users of capital markets and non-financial companies. For private households almost all forms of private old-age provision and wealth accumulation are negatively affected by the FTT. This applies to direct investment in equities and bonds as well as to direct investment funds and capital funded life insurances. In Germany alone, this results in a total annual burden for private households of €2.6 to €3.6 billion based on the original proposal of the EU Commission. Adding the tax burden for the corporate finance and risk management activities of the real economy, end users in Germany would be exposed to FTT-related costs of approximately €5.0 to €7.3 billion annually (DAI/Oliver Wyman, "Die Finanztransaktionssteuer – ein politischer Irrweg?", 2013[5]).

There are empiric studies that show that such a tax will reduce market liquidity and thereby increase the volatility of prices of financial instruments. Experiences gained in Italy and France show a relative decline of trading volumes by 34.2% resp. 6.4% after the FTT was introduced (Buchanan/Baudewyn/Ling, "Financial Transaction Taxes Loom Large", Credit Suisse Market Commentary from 16 April 2014). Consequently, risks will rather be increased than reduced.

Mobile and flexible market participants will most likely relocate their issuance of financial instruments to countries not taking part in the enhanced cooperation, so that private households and non-financial companies which are rather immobile will bear the majority of costs. Additionally, the costs of implementation and enforcement will be far greater than realised, as well as the fact revenues will be far less than expected (as demonstrated by national FTTs in France and Italy).

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
We consider that policy makers should rethink the proposal of introducing a financial transaction tax.

[5]https://www.dai.de/files/dai_usercontent/dokumente/studien/2013-07-18%20Deutsches%20Aktieninstitut%20Oliver%20Wyman%20FTS-Studie.pdf

Example 5: Investor and consumer protection

To which Directive(s) and/or Regulation(s) do you refer in your example?

- IGS: Directive 97/9/EC on investor-compensation schemes.
- MiFID II: Directive 2014/65/EU on markets in financial instruments.

Please provide us with an executive/succinct summary of your example:
Directive 97/9/EC introduced rules for investor-compensation schemes to cover losses investors may face when using investment firms under Directive 93/22/EEC. The rules were also made in order to protect investors in case an investment firm was passporting its services under Directive 93/22/EEC. MiFID I included the operating of a Multilateral Trading Facility (MTF) as an additional investment services and therefore define MTF operators on investment firms. However, MTFs rules on "passporting" have been introduced in MiFID Article 31 (5) and (6) I which clearly show that "passporting" for the operation of an MTF is different than when operating an investment firm. Furthermore, MiFID I did not reflect the introduction of the new service in respect to the investor-protection scheme.

With MiFID II, the category of OTFs have been added to the investment firms and again, no change on the investor-protection scheme has been envisaged (i.e. no explicit consideration on OTF and / or MTF has been made in this regards) and for "passporting" the same rules as for MTFs apply.

Operators of regulated markets are not regarded as investment firms and this in our view holds true in case they operate a MTF or an OTF. As such, they have been prior to MiFID II not in scope of the investor-protection scheme. MiFID I clearly stated this also in Article 5 (2). (With the non-application of the relevant Article 11 [in general Articles 11 – 15 were not applicable in case an operator of a regulated market was operating in addition a MTF).

MiFID II has withdrawn the non-applicability of former Article 11 (now Article 14, in fact the whole exclusion sequence has been taken out) in Article 5 (2) – to our best knowledge without the intention to apply those articles but only to simplify the legal text. We would welcome clarification that the operation of an MTF only by a RM should not lead to the RM being required to comply with a broad set of provisions explicitly designed for investment firms – particularly where this leads to the application of high capital requirements.

We believe thatthe inclusion ofMTFs or OTFs, operated either by market operators or in investment firms, does not fulfil the aim of Directive 97/9/EC, when the only service offered is an MTF or OTF.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
We recommend that the Commission takes the following steps:

- Amend Directive 97/9/EC in order to exclude operators that only operate an MTF and / or OTF from the scope of the investment protection scheme (I any case it would be prudent to amend the Directive to reflect changes in EU law during the previous 20 years);
- Amend Article 14 MiFID II in order to reflect the above proposed exclusion;
- Re-introduce the previous exclusion in Article 5 (2) MiFID II with the revised content, as currently in MiFID I, at least excluding the applicability of Articles 14 (investor protection scheme) and 15 (minimum capital requirements as defined in CRR) MiFID II which would cover the whole company and not only the provision of investment services. However, we understand that a reopening of the Level 1 text might not be suited in the short term and note that this issue could be clarified by the Commission in the form of a Q&A document.

Issue 4 – Proportionality / preserving diversity in the EU financial sector

Example 1: Proportionality / preserving diversity in the EU financial sector

To which Directive(s) and/or Regulation(s) do you refer in your example?

- Statutory Audit Directive: Directive 2014/56/EU amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts [Article 1(2)(f) Definition of Public-Interest Entities].
- Statutory Audit Regulation: Regulation 537/2014 on specific requirements regarding statutory audit of public-interest entities [Article 5, Prohibition of the provision of non-audit services and Article 17, Duration of the Audit Engagement].

Please provide us with an executive/succinct summary of your example:
The definition of "Public-Interest Entity" includes entities governed by the law of a Member State whose transferable securities are admitted to trading on a regulated market of any Member State within the meaning of point 14 of Article 4(1) of Directive 2004/39/EC. This broad definition means that listed specialist issuers, such as investment funds and certain types of issuers of debt securities, e.g. special purpose vehicles, are captured and therefore fall within the scope of the Statutory Audit Directive and the related Regulation on Statutory Audit of PIEs.

The implications of this is that specialist issuers will be required to comply with provisions such as mandatory auditor rotation, and limitations on audit services provisions as referenced above, which in our view are more appropriate to larger commercial companies, rather than specialist issuers. We believe the approach adopted does not take into consideration the diversity of entities; and the rules have not been adapted appropriately. The imposition of these requirements and the inevitable increase in costs that they give rise to is diminishing the attractiveness of 'regulated markets' in the EU and, for already listed specialist issuers, is acting as a significant deterrent to retaining their listing. This could therefore lead to the perverse outcome of decreased disclosure and transparency of these investments which would be a very negative and backward step for EU markets and investors, which we consider would be a serious unintended consequence of these proposals.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
As these provisions have not yet been implemented, we do not have empirical evidence of the impact but we are aware that certain specialist issuers that might otherwise have listed on regulated markets in the EU are re-assessing whether this remains a viable funding option and, in addition, already listed specialist issuers are re-evaluating their status as a listed entity on a regulated market as a consequence of these provisions.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
There are a number of proposals that could be considered and we set these out below in order in of preference:

1. The definition of PIE could be amended so that specialist issuers are not included, and only entities that truly are of "public interest" would be captured in the definition.
2. The definition of PIE should not determine the entities that are within scope of the legislation, as this is too broad and it does not adequately address the diversity of entities that are captured. The trigger for certain legislation to apply should be determined by the size of the company i.e. market cap, balance sheet etc. so that only large trading companies are subjected to these provisions.
3. If the definition of PIE remains unchanged and continues to be used as the trigger for certain legislation, we believe the provisions need to be more flexible so that they are more appropriately calibrated for the entities that are included. For example, there should be

additional exemptions from certain provisions for specialist issuers were they are deemed inappropriate or not relevant to that type of entity, and these should exist within the EU legislation rather than be set out as a Member State option as this only results in an un-level playing field where different jurisdictions take different approaches.

Example 2: Proportionality / preserving diversity in the EU financial sector

To which Directive(s) and/or Regulation(s) do you refer in your example?

- Prospectus Directive: Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC [Article 4(2)(a), Exemptions from the obligation to publish a prospectus]

Please provide us with an executive/succinct summary of your example:

- **Secondary issuance exemptions**

The publication of a prospectus is an extremely costly exercise and we have received feedback from issuers that the existing exemptions from the obligation to prepare a prospectus for secondary issuances are too limited, thereby imposing unnecessarily high costs on issuers.

In particular, the 10% limit in relation to secondary issuances has proven to be very restrictive for listed issuers. It is too low and once crossed, the prospectus requirements are so detailed that they act as a disincentive to secondary issuances. The Commission has proposed to increase this threshold to 20%, which we would very much welcome. It is essential that secondary issuances are not considered too cumbersome and costly as a fund raising option for issuers.

Please provide us with supporting relevant and verifiable empirical evidence for your example:

The current threshold of 10% places a serious constraint on a company's equity capital raising, and means that 10% is an effective ceiling for share offerings within a 12 month period.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:

We welcome the proposed new threshold of 20% and stress that this must remain in the final text of the new regulation. Once this threshold is reached and the requirement for a prospectus is triggered, a much more proportionate prospectus disclosure regime should apply which excludes repetition in a prospectus of information that has already been disclosed by an issuer to the market under the Transparency Directive and MAD, and focuses on information specific to the share issuance/transaction being undertaken. Therefore it should exclude the requirement for financial information (including the Operating and Financial Review and the corporate governance disclosures) in its entirety if it is already published and available under the TD or MAD.

Theme B. Unnecessary regulatory burdens

Issue 5 – Excessive compliance costs and complexity

Example 1: Excessive compliance costs and complexity

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65/EU on markets in financial instruments [Art 27 (3) Trading Venue requirements to publish data on quality of execution and related draft RTS 27].

Please provide us with an executive/succinct summary of your example:
The proposed publication of execution information by trading venues and SIs required by MiFID II is far too complex to provide added value for investors while placing additional costs and burdens on venues to provide information for which there will be no benefit. We therefore do not believe that it meets the objectives of MiFID II to make public information that will support demonstration of best execution. The information will be too technical and stale to be supportive to retail investors, and due to its complexity there is a strong risk of it being misinterpreted resulting in a lack of confidence in markets. We believe it also won't benefit investment firms in demonstrating best execution as they will need to source information tailored to their best execution policy on a timelier basis.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
As MiFID II has not yet been implemented, we do not have empirical evidence for this example.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
FESE suggests that it would be far more appropriate for ESMA to introduce a considerably more scaled down version of the data required. There needs to be a full impact assessment undertaken of the benefits of and the demand for additional data and following that, the requirements could be expanded if proven to be of benefit.

Example 2: Excessive compliance costs and complexity

To which Directive(s) and/or Regulation(s) do you refer in your example?

- Prospectus Directive: Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading [Chapter 2 Drawing up of the Prospectus and Chapter 3 Arrangements for Approval and Publication of the Prospectus].

Please provide us with an executive/succinct summary of your example:

- **Content and process**

The feedback we have received from certain issuers of equity securities in relation to their experience of the Prospectus Directive is that the prospectus process from initial draft to approval is too long and expensive. We acknowledge some of these points are being currently addressed in the new Prospectus Regulation, but given the importance of these concerns, we believe it appropriate to include them in this Call for Evidence.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
The prescribed content under the prospectus checklists make a prospectus a very long document that is costly to prepare and that is not user-friendly for investors. We would argue it should be possible to incorporate by reference a broader range of documents and information. In addition, the risk factors section is far too detailed, does not prioritise the material risks and acts as more of a liability shield than a useful information section for investors. Furthermore, the current timeframe for the

consideration of draft equity prospectuses is too long, and does not adequately reflect commercial fundraising needs and needs to be shortened.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
It should be possible to incorporate by reference a broader range of documents and information. The risk factors disclosure requirements should be revised to only require disclosure of material risks that are relevant to the company and its securities. The current timeframe for the review of draft equity prospectuses by national competent authorities needs to be shortened.

Example 3: Excessive compliance costs and complexity

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65/EU on markets in financial instruments.

Please provide us with an executive/succinct summary of your example:
FESE is concerned with the current status of the discussions on the use of ISINs and AIIs. Therefore, we wish to reiterate our position that FESE fully supports the proposed RTS that trading venues may use at least either the Instrument Securities Identifier Number (ISIN) or Alternative Instrument Identifier (AII), while we would prefer a clear mandate to continue to use the AII.

FESE was involved in the previous work of CESR on instrument codes, and fully supported the introduction of an AII as an alternative to an ISIN. As part of our involvement we highlighted the serious issues that would arise from not allowing both standards:

- The cost of not allowing both standards would amount to double digit millions EUR over five years for the largest FESE members.
- The costs for the banking sector as a whole was considerably higher (2,566 million EUR), but diffused among a larger number of institutions (6,000 banks).
- There are unquantifiable additional problems that would be created if there was no introduction of an AII, in particular in the form of a loss of independence in the creation of new derivative instruments, since the exchanges concerned would depend on the National Numbering Agency for all new instruments.

The outcomes of this work was that CESR ultimately agreed to accept the industry's proposal to establish an alternative method (the 'Alternative Instrument Identifier') alongside the ISIN code in an effort to reduce the costs and avoid operational problems for the derivatives markets concerned.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
In particular for derivatives markets there would be huge operational difficulties involved in requiring ISINs for derivative:

- Necessity to develop and adjust all trading and back office systems for a new field to accommodate an ISIN;
- Require an unprecedented pan-European IT project to develop interfaces from exchange systems to the NNA for the exchange in question;
- The negative effect of the additional field & the additional data populating this field on the end of day (EOD) processing times. This in turn would significantly slow down the provision of close of business (COB) data to customers, which must be available prior to market open.
- Increase in the size of the static reference database, which also must be maintained.
- Necessary development time to accommodate this field only adds to timing issues that already exist for meeting the final MIFID II/MiFIR implementation deadline.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
This issue is crucial for exchanges, as we were involved in developing the AII as part of our cooperation with the previous CESR work on this. FESE understands that the initial proposal by ESMA for the RTS related to transaction reporting, states that trading venues may use either the Instrument Securities Identifier Number (ISIN) or Alternative Instrument Identifier (AII). The previously proposed RTS states:

[Previous] Draft RTS 33 - Article 5 Use of Instrument Identifiers
1. For instrument reference data purposes, trading venues and systematic internalisers shall use one of the following instrument code types to identify financial instruments:
- *(a) Instrument Securities Identifier Number (ISIN);*
- *(b) Alternative Instrument Identifier (AII)*

Therefore, FESE fully supports this proposed RTS and urges national supervisors to maintain the purpose of the original in the final RTS as outlined below.

Example 4: Excessive compliance costs and complexity

To which Directive(s) and/or Regulation(s) do you refer in your example?
- MiFIR: Regulation (EU) No 600/2014 on markets in financial instruments [Draft regulatory technical standards].

Please provide us with an executive/succinct summary of your example:
FESE is deeply concerned about the current ESMA draft regulatory technical standard (RTS 23) on the obligation to supply financial instrument reference data (Article 27 MiFIR). The ESMA proposal requires that overly extensive reference data is published on an open web-page which infringes Third Party IP rights.

MiFIR Article 27.1 refers to the publication of "identifying reference data for the purpose of transaction reporting" and thereby gives ESMA a mandate to publish the reference data that is necessary for the purpose of identifying which instruments are subject to transaction reporting requirements.

Following from that, any information that is not relevant for reporting purposes should not be published by ESMA on its website. While we agree that trading venues should report all fields to national competent authorities, we recommend that ESMA for the purpose of its FIRDS project makes public only fields 1 to 12 of Table 3 in RTS 23.

Conversely, fields 13 to 48 are not necessary for market participants to comply with their MiFIR obligations and therefore do not qualify as "identifying reference data for the purpose of transaction reporting". They should therefore not be published by ESMA in the context of the FIRDS project. We note that there are alternative sources already available in the market place that make that data widely and easily available to any interested party.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
In order to avoid detrimental consequences, ESMA must consider the following:
- The world of reference data is not harmonized, neither on a global scale nor on EU level. While reference data information is usually very costly to produce and maintain, different IP holders exist in this field, and in many cases trading venues are in fact not the ones holding the IP rights. While

this fact has been generally neglected at Level 1 discussions already, it seems to be neglected at Level 2 again.

- This is creating difficult legal situations especially for trading venues as well as Systematic Internalisers (SIs), since in most cases they do not hold the IP rights on the requested instrument data.
- Unless ESMA reduces the scope of data to be submitted to NCAs for publication on ESMAs web-site to a necessary and proportionate set of data – which can be made available free of charge on a web-site as well – market operators and firms will face a legal dilemma situation either infringing EU law or IP rights of Third Parties.
- This scenario strictly needs to be avoided. We strongly urge ESMA and the Commission to strictly respect the mandate in MiFIR Article 27.1 and only publish “identifying reference data for the purpose of transaction reporting” in the context of the FIRDS project. As explained above, we recommend publishing only fields 1 to 12 of the reference data table in RTS 23.

Example 5: Excessive compliance costs and complexity

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFIR: Regulation (EU) No 600/2014 on markets in financial instruments [Draft regulatory technical standards].

Please provide us with an executive/succinct summary of your example:

FESE is deeply concerned about the current ESMA draft regulatory technical standard (RTS 14) on data disaggregation and that this would be too granular to achieve data cost reduction for users:

- While FESE broadly supports the ESMA draft RTS as submitted to the Commission on 28th September, 2015, we still are extremely concerned about the proposed levels of data disaggregation proposed by ESMA.
- ESMA’s proposal suggests cumulative disaggregation across defined criteria which would result in higher costs instead of cost reductions for the industry once they would have to be applied. The reason for this detrimental effect is the extreme level of granularity introduced by RTS 14 as explained below.
- Following detailed discussions with other market participants, we understand that these concerns are also shared more broadly across the industry.

Data disaggregation must be manageable across the industry

- ESMA’s draft RTS 14 proposes to impose on trading venues cumulative pre- and post-trade disaggregation for: (1) 10 asset classes, (2) per country of issue, (3) per currencies and (4) per scheduled daily auctions. While the criteria as defined by ESMA seem to represent a manageable amount at a first glance, the fact that these criteria are cumulative exponentially increases the number of data packages the industry would need to manage.
- There are already 10 asset classes (characters) subsumed under one criteria. As regards currencies, there are more than 60 characters up to an open end. Taking into account the country of issuance, these characters are further multiplied.
- The theoretical universe of disaggregated data packages derived on the basis of the criteria with respective characteristics – all in a “cumulative” way - would be defined by multiplying each character to the most granular level with each character to the most granular level of another defined criteria. This would result in far too many data packages to allow for proper administration.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
Our preliminary calculations show that for 9 trading venues and on the basis of 10 asset classes, 10 currencies, 16 countries of issuance and the split for auction data, the 323 data license packages of these 9 venues currently available, would end up generating 471,036 data license packages. This is a very conservative indication since they are in fact 248 additional venues to be computed and only 10 currencies and 16 countries have been taken into consideration.

In practice, the proposed disaggregation is in fact likely to create millions of data license packages across the EU, leading to the following consequences:

- Excessive complexity prone to errors along the user chain, from data production to data vendors and onwards to users;
- Significantly increased cost base, on the data producer side for new packaging of data (license fees to be paid for classification data, additional cost for programming, hardware, etc.) and most importantly administration (considerably increased human resources, programming, etc.) resulting in significantly higher prices already on production level even if users do not buy the data packages;
- Technology service providers or market data vendors most likely will not implement this license avalanche, thus making them in effect unavailable for many customers, while significant costs on the trading venue side will nonetheless be rolled over to end-users;
- In the event of technology service providers or market data vendors offering those licenses significant investments in entitlement systems and staff would become necessary and would be passed on to end users;
- Pre- and post-trade data licensing would become impractical for end users to understand and to manage, adding costs for necessary adaptions for customers and compliance issues;
- A big bang effect would have to be planned for January 2017 which is unlikely to be achieved taking into account the already challenging MiFID II requirements for systems and compliance in the industry;
- The overall cost for such an implementation is unknown since it has not been counted for in ESMAs cost/benefit analysis as of now.
- Under these circumstances, we consider that the proposed implementing measures are disproportionate and would create an inefficient market place where the cost of data would be increased for all users instead of being reduced.
- Furthermore, it is unlikely that technology providers and market data vendors will be able or willing to apply those changes. Therefore, and in order to avoid harming the smooth running of the markets by rendering proper administration of data packages impractical and introducing an unprecedented administrative burden as well as costs to the EU industry, we urge the European Commission:
  a) not to impose “cumulative” data disaggregation (i.e. applying all/several criteria to data disaggregation at the same time) which will result in far too granular data packages for approximatively 33 million instruments within the EU, and;
  b) not to require disaggregation on the basis of country of issue and currencies. Alternatively, we would recommend reducing at least the characteristics of both criteria, to e.g. “EUR”, “GBP” and “others” for the criteria of currencies and to “EU” and “Non-EU” instruments for the country of issuance

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
In order to provide a workable solution for data disaggregation and to reduce overall market complexity, we propose that the draft RTS are amended to reflect the following:

- To ensure that pre- and post-trade data offered appropriately matches the demand from market participants, market operators and investment firms operating a trading venue should only disaggregate by the criteria set out in this Regulation on a reasonable commercial basis, and not offer any combination of these criteria.

- This data should only be disaggregated by a request to do so by a market participant.
- There should be no requirement to disaggregate by country of issue for shares and sovereign debt or by currency in which instrument is traded.

Issue 6 – Reporting and disclosure obligations

Example 1: Reporting and disclosure obligations

To which Directive(s) and/or Regulation(s) do you refer in your example?

- Transparency Directive: Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market [Article 24(4)(d)].

Please provide us with an executive/succinct summary of your example:
This relates to the requirement for operators of regulated markets to suspend securities from trading for a maximum of 10 days at a time on the basis that the competent authority has reasonable grounds for suspecting that the issuer has infringed the provisions of the TD.

In our experience, this provision is availed of most often in relation to infringements of Art 4(1) Annual Financial Reports and Art 6(1) Half Yearly Financial Reports, i.e. non-publication of financial information within the required timeframes. Given the suspension can only last for 10 days at a time, for on-going infringements, this means the security has to be re-suspended every 10 days. The requirement to re-publish the suspension notices every 10 days is onerous and provides a misleading representation of suspension activity on the market as it implies suspensions are re-occurring on a regular basis when in reality it is the same suspension that is being continued.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
The Transparency Directive should be amended to remove the requirement for suspensions to last 'a maximum of ten days at a time'. Suspensions should remain in place until the issue giving rise to the suspension has been resolved.

Example 2: Reporting and disclosure obligations

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MAR: Regulation (EU) No 596/2014 on market abuse.

Please provide us with an executive/succinct summary of your example:
FESE strongly supports the extension of MAR to MTFs. At the same time, it will be a significant transition for SMEs on smaller growth markets, especially the inside information disclosure obligations which are detailed and complex. Issues around the disclosure/non-disclosure of inside information can be compounded by volatility in the share price, e.g. an issuer may not deem certain information to be price sensitive and therefore it does not create an insider list, but if the market is volatile it could coincide with a significant price change and the NCA could take a different approach and with the benefit of hindsight deem the information to constitute 'inside information'. Larger price changes are more likely in smaller SME companies, many of which are "penny stocks". Therefore SMEs are likely to require greater levels of legal advice concerning their announcements of inside information, thereby increasing their costs.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
ESMA should closely monitor the impact of MAR on SMEs with a view to recommending changes to MAR or developing relevant guidance where necessary.

Issue 7 – Contractual documentation

Example 1: Contractual documentation

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65/EU on markets in financial instruments [Article 25(6), Investment advice].

Please provide us with an executive/succinct summary of your example:
Under the revised MiFID II/MiFIR framework tightened investor protection rules were introduced, regarding for example the investment advice of banks and other financial institutions: With the objective of improving the information for retail investors as part of the duties of banks have been increased. Banks across Europe will have to document their investment advice in future, although experience shows that overwhelming documentation duties already have negative side effects. Banks are struggling with the costs of compliance. As a consequence, banks frequently retreat from providing investment advice especially on shares. This results in a severe damage for the private wealth building with shares. Additionally, financing SMEs by issuance of shares purchased by retail investors will become more difficult as banks are increasingly reluctant to provide information regarding share investments.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
A study of Deutsche Aktieninstitut has provided evidence that a significant number of banks have already withdrawn their investment advisory services. As a result of strict regulatory requirements, 22%of credit institutions ceased to provide advice in shares; 65 % significantly reduced its interaction with customers regarding shares (DAI, "As a result of regulation banks refrain more and more from providing investment advice in shares - a survey", July 2014). Therefore, it is clear that investors do not get adequate advice from their banks, simply because advisory services have become too costly and complicated for banks to provide.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
Therefore, we believe that the rules governing investment advice of investment firms should be adjusted, such as the ability for experienced retail investors to have the option to waive the obligation that the suitability of the investment advice has to be recorded ("suitability report" Art.25(6) MiFID II). For the benefit of effective investor protection, we believe that an environment providing further financial and economic literacy should be promoted instead implementing more regulatory requirements for issuers.

Example 2: Excessive compliance costs and complexity

To which Directive(s) and/or Regulation(s) do you refer in your example?

- PRIPs: Regulation (EU) No 1286/2014 on key information documents for packaged retail and insurance-based investment products.

Please provide us with an executive/succinct summary of your example:
We consider that exchanges and exchange traded derivatives should be out of scope of the PRIIPs Regulation, and hereby confirm the understanding based on the Level 1 text and the reasoning in this consultation that regulated markets and ETD contracts are not in scope of this Regulation.

From our assessment of EU legislative texts, explanatory memorandum, impact assessments as well as Commission Communications, we find no explicit reference to the fact that listed derivatives are automatically and necessarily captured within the scope of the PRIIPs Regulation.

An important initial reference can be found in Section 3.4.1 of the Commission Proposal's Explanatory Memorandum which states that:

"Such investment products expose the investor to fluctuations in the market value of assets or in the payouts to be achieved from assets. But this exposure is not of the direct kind, as for instance when an investor buys specific assets themselves. Instead these products and those that manufacture them intercede between the investor and the markets, through a combination of wrapping of those assets, or other mechanisms that differ from a direct holding ("packaging").

Listed derivatives such as options and futures do not match this description and therefore do not fulfill the criteria established in the PRIIPs Regulation. They are contracts, the conditions of which are designed by Regulated Markets. In no way does a Regulated Market intercede between the market and the investors, as we are the market. Regulated Markets publish the conditions for their contracts on their website (which lists all of the information on the products and is available for everyone to read) and the traders (be it professional or brokers acting on behalf of their clients) buy and sell these products.

A 'Packaged Retail Investment Product' ('PRIP') is defined in Article 4(1) of the PRIIPs Regulation (Regulation (EU) No 1286/2014):

For the purposes of this Regulation, the following definitions apply:

(1) 'packaged retail investment product' or 'PRIP' means an investment, including instruments issued by special purpose vehicles as defined in point (26) of Article 13 of Directive 2009/138/EC or securitisation special purpose entities as defined in point (an) of Article 4(1) of the Directive 2011/61/EU of the European Parliament and of the Council (2), where, regardless of the legal form of the investment, the amount repayable to the retail investor is subject to fluctuations because of exposure to reference values or to the performance of one or more assets which are not directly purchased by the retail investor;

As such, it is clearly laid down in the Regulation that when referring to a 'PRIIP', what is meant is an investment including instruments issued by a special purpose vehicle or securitized instruments by special purpose entities.

In addition, the definition of a 'PRIIP manufacturer' (Article 4(4) of the PRIIPs Regulation) refers back to the PRIP/PRIIP definition:

(4) 'packaged retail and insurance-based investment product manufacturer' or 'PRIIP manufacturer' means:
   (a) any entity that manufactures PRIIPs;
   (b) any entity that makes changes to an existing PRIIP including, but not limited to, altering its risk and reward profile or the costs associated with an investment in a PRIIP;

Please provide us with supporting relevant and verifiable empirical evidence for your example:
Clearly, regulated markets/exchanges are not issuers, and are not a special purpose vehicle offering an investment, and are also not securitizing instruments. As a consequence, a regulated market is not captured in this definition in Article 4(1). Stemming from this understanding, it is further concluded that a regulated market is also not a manufacturer, since the definition in Article 4(4) describes a

manufacturer as an entity that is manufacturing such PRIPs/PRIIPs and thus refers back to Article 4(1). Moreover, Recital 12 of the PRIIPs Regulation gives further guidance on the understanding of who actually would qualify as a PRIIP manufacturer, namely, a fund manager, insurance undertaking, credit institution or investment firm.

It is also important to recognise that listed derivatives are financial instruments and not investments. They are designed for risk management purposes and speculation but not 'investment' in the generally understood meaning of the word.

Furthermore, options and futures are not packaged, and do not modify the nature of the exposure of the purchaser to the underlying. In listed derivatives such as Options and Futures, there are no additional layers of complexity, or packaging which would make the investment less transparent. There is no creation or packaging of specifically tailored products that promise or indicate a return on investment. The opposite is the case: options and futures do not promise any return on investment but simply reflect the direction of the underlying and traders can use that (for instance) as a hedge to their equity investments. In this respect we cannot see how this proposal was ever intended to - and could - legally capture these products.

The description of listed derivatives we provide clearly demonstrates that the criteria of the definition of a packaged retail investment product are not fulfilled.

The derivative instruments that satisfy the definition of a PRIIP could be for example securitized derivatives, such as certificates and warrants, potentially also mortgage backed securities (MBS) or asset backed securities (ABS) and alike. In contrast to listed derivatives we fully support the fact that covered warrants & certificates do fall within the scope of the PRIIPs Regulation as a result of the fact that they are offered as a packaged investment product. Covered warrants & certificates provide a useful counter-example of derivatives which constitute a truly packaged retail investment product, i.e. one where the purchaser is offered exposure to underlying financial assets, but in packaged forms which modify that exposure compared with direct holdings. Such financial products have been explicitly identified by the Commission when explaining what constitutes a packaged retail investment product. A clear distinction can be made between options and futures on the one hand and covered warrants & certificates on the other.

In the context of derivatives, the ESAs clarify in Annex II, Part 1, point 9 of the draft RTS (attached to the consultation paper) which instruments are included. It is specified in sub-point c that derivatives that qualify as PRIIPs within part C of Annex I of Directive 2014/65/EU are included. That means that not all derivatives are within the scope of the Regulation; only those derivatives that qualify as PRIIPs are in the scope.

A further argument why exchange traded derivatives available for trading on exchanges/regulated markets are not in scope of PRIIPs, is the concept of the KID as proposed by the ESAs and presented in this consultation. The way the KID is designed and the questions and input parameters formulated clearly indicate that the KID is customized towards the entities that offer investments as a special purpose vehicle, issuer or entity that securitizes instruments.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
The KID ultimately cannot be appropriately completed by a neutral regulated market, focused on instruments that do not actually qualify as PRIIPs.

Issue 8 – Rules outdated due to technological change

Example 1: Rules outdated due to technological change

To which Directive(s) and/or Regulation(s) do you refer in your example?

- Shareholder Rights Directive: Directive 2007/36/EC on the exercise of certain rights of shareholders in listed companies.

Please provide us with an executive/succinct summary of your example:
For listed companies with a large number of retail shareholders, paper correspondence with shareholders can be very costly e.g. AGM documents, publication of annual reports and prospectuses in paper form etc. The costs can be significant in terms of printing and postage costs.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
Consideration should be given to allowing communications by listed companies with investors to only be in electronic form, i.e. email or available on a company's website. In addition, the use of electronic payments should also be encouraged in order to phase out dividend cheques. These proposed amendments would ensure the rules are appropriate to the more modern, technologically advanced environment that now exists. This should also be considered for other legislation such as the Prospectus Directive and Transparency Directive.

Issue 11 – Definitions

Example 1: Definitions

To which Directive(s) and/or Regulation(s) do you refer in your example?
Definitions of 'SMEs':

- MiFID II: Directive 2014/65/EU on markets in financial instruments [Article 4(1)(13)].
- Prospectus Directive: Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading [Article 2(1)(f)].

Please provide us with an executive/succinct summary of your example:
Despite the Commission's "Recommendation concerning the definition of micro, small and medium-sized enterprises" issued in 2003, there are currently different definitions for SMEs across EU legislation:

- In MiFID II, SMEs are defined as "companies that had an average market capitalisation of less than EUR 200 000 000 on the basis of end-year quotes for the previous three calendar year."
- The Prospectus Directive review also includes an additional definition, derived from the 2003 Recommendation: "companies, which, according to their last annual or consolidated accounts, meet at least two of the following three criteria: an average number of employees during the financial year of less than 250, a total balance sheet not exceeding EUR 43 000 000 and an annual net turnover not exceeding EUR 50 000 000."
- The ECSIP report commissioned for DG Enterprise took the following definitions:
  - Small-caps as companies with market capitalisation from €336 million to €1.3 billion.
  - Mid-caps as companies with market capitalisation from €1.3 billion to €6.7 billion.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
In our experience, companies with up 1 billion EUR capitalization can suffer from lower liquidity and therefore merit being helped by policies targeting listed SMEs[6]. Often the costs of listing that may be fully appropriate for larger companies are disproportionate for smaller companies. In Europe, the regulatory focus is on the 5-10% biggest companies, which renders it inappropriate for the majority of companies seeking a listing.

We believe the upcoming Prospectus Regulation provides an ideal vehicle to review the current framework that distinguishes between a listing on a Regulated Market and a listing on an MTF or SME Growth Market. Specifically, we support introducing a €10 million threshold for public offers throughout Europe, which would ensure that all small and mid-sized enterprises can benefit from a lighter Prospectus regime irrespective of their size or the market they choose to go public. Companies would then be able to choose between a RM or an MTF based on their profile and the type of investors they seek to attract.

In order to ensure consistency and coherence across its financial markets, one of the core prerequisites would be to have a single uniform EU definition for SMEs. This would then be serve as the standard for all the upcoming and existing financial policies of the Union.

[6] A BLUEPRINT FOR EUROPEAN CAPITAL MARKETS

Example 2: Definitions

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65/EU on markets in financial instruments.

Please provide us with an executive/succinct summary of your example:
MiFID II extends trade transparency requirements from shares to equity-like and a number of non-equity instruments. This is a welcome development which could however be put at risk by the lack of clarity around the definition of the systematic internaliser.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
As previously discussed with the European Commission, we believe the lack of clarity around what type of activity is allowed on a systematic internaliser – bilateral or multilateral, on a principal or riskless principal basis – risks introducing a major loophole in the MiFID II transparency framework. This is because an SI operating on a riskless principal basis would essentially replicate the functioning of a multilateral venue, where the operator does not incur trading risk, but with a fraction of the transparency requirements.

Consequently, we support clarifying in the Delegated Acts being prepared for MiFID II that systematic internalisers are not allowed to run internal matching systems to execute trades on a bilateral basis. We note that this prohibition should be strictly applied in all cases and should not leave the door open to activity taking place on an occasional basis. This is because the notion of "occasional" is extremely vague and would be virtually impossible to monitor consistently across jurisdictions.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
We support limiting the use of SIs to strict bilateral trading only. Matched principal or riskless principal trading should not be allowed, even when they take place on an occasional basis.

Example 3: Definitions

To which Directive(s) and/or Regulation(s) do you refer in your example?
Definitions of all Financial Market Directives or Regulations, including Level 2 texts.

Please provide us with an executive/succinct summary of your example:
The various legislative texts do not have harmonised terminology, the definitions of terminology is spread all over various legislative texts and includes reference chains as well as contradicting terminology. This is true for very basic definitions:

- Some terms are used with the intention of same content but with differing definitions, sometimes with only slightly different wording (mainly due to history and not reflecting actual developments) and consequently potential differing outcome, e.g. "financial sector entity" in CRR (article 4 (1) No. 27 and "financial undertaking" in Solvency II (article 13 (25)) or "close link" in Solvency II (article 13 (17)) and in MiFID II (article 4 (35)). Another example is "subsidiary" defined in MiFID II (article 4 (33)), AIFMD (article 4 (1) lit ak) and CRD IV (article 4 (13))).
- Sometimes cross links do not match (e.g. Solvency II refers in article 13 (25) lit. c) for the definition of investment firm AND financial institution to MiFID II Article 4(1)(1) which only defines investment firms).
- Sometimes terms are defined in a similar manner but with slight variations on purpose (e.g. "parent undertaking" which is defined i.a. in Solvency II (article 13 (15)), MiFID II (article 4 (32))

and CRD IV (article 4 (14)); “branch” which is defined i.a. in Solvency II (article 13 (11)) and CRD IV (article 4 (16))).

- Sometimes different wording is used but same content is meant (e.g. “supervisory authority” in Solvency II (article 13 (10)) but “competent authority” in CRD IV (article 4 (36)), EMIR (article 2 (13)) as well as MiFID II (article 4 (26)) or “qualifying holding” defined in Solvency II (article 13 (21)), AIFMD (article 4 (1) lit. ah), MiFID II (article 4 (31)) and CRD IV (article 4 (33)) or “Asset Management Company” in FiCoD Article 2 (5) and “UCITS management company” in MiFID II Article 4 (28)).
- Sometimes same terms are used but with completely different meaning (e.g. “leverage” which is defined i.a. in CRR (article 4 (93)) and AIFMD (article 4 (1) v) or “operational risk” defined in CRR (article 4 (52)) as well as in Solvency II (article 13 (33))).
- Multiple definitions are made by cross-referencing to other dossiers.
- Sometimes terms are used with unclear and no explicit reference to other dossiers where it is nevertheless targeted to (e.g. EMIR article 16 in combination with the related technical standard requires to cover credit as well as counterparty credit risk. However, in CRD IV, where the capital requirements are taken from, the risk that a counterparty to a transaction defaults before the final settlement of the transaction’s cash flows for positions outside the trading book is already included in the credit risk.).
- Sometimes translations of same terms in various dossiers are not the same (e.g. German terminology for “Central Counterparty”: SFD article 2 lit a) “Zentrale Verrechnungsstelle”, EMIR Article 1 (1) “zentrale Gegenpartei”, CRD Article 78 (4) “zentrale Gegenpartei”).
- Sometimes definitions are duplicated within the same set of regulations (e.g.: CRD IV defines “ancillary services undertaking” in article 3 (1) No 17 while in General refering to the definitions of Article 4 CRR which already defines the “ancillary service undertaking” in its article 4 (18)).

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
We recommend combining all necessary definitions in a single rule book on definitions as an EU regulation which is then referred to by the various dossiers. This keeps maintenance of definitions across dossiers more simple and avoids usage of undefined terms, with varying content etc. In case on purpose a deviation is intended, this needs to be clearly stated in the legislative text targeting to do so.

Issue 12 – Overlaps, duplications and inconsistencies

Example 1: Overlaps, duplications and inconsistencies

To which Directive(s) and/or Regulation(s) do you refer in your example?

- FTT: Proposal for a Council Directive implementing enhanced cooperation in the area of financial transaction tax (COM/2013/71)

Please provide us with an executive/succinct summary of your example:
The original FTT proposal of the Commission makes derivatives transactions subject to taxation, even if used for risk management purposes. Both a significant rise in hedging costs and a decline in the provision of hedging services will most likely be the consequence. This obviously stands in sharp contrast to the EMIR which recognises the beneficial role of derivatives in the corporate risk management.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
We believe that the Commission should rethink the proposal of the financial transaction tax.

Issue 13 – Gaps

Example 1: Gaps

To which Directive(s) and/or Regulation(s) do you refer in your example?

- Stand-alone national laws that contradict European regulation.

Please provide us with an executive/succinct summary of your example:
Some countries have introduced go-alone approaches in the regulation of financial services (e.g., short-selling, financial transaction taxes, algorithmic trading). Behind the background of an integrated EU financial market, these approaches are introducing frictions and create opportunities for regulatory arbitrage for investment firms and trading venues.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
German HFT Law (2013) and German Short Selling Law (2010): Trading firms avoiding German trading venues; doing the same business at non-German trading venues to avoid the new requirements; whereas the latter being left at a competitive disadvantage.
French and Italian FTTs.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
Member states to refrain from go-alone approaches in the future.

Example 2: Gaps

To which Directive(s) and/or Regulation(s) do you refer in your example?

- MiFID II: Directive 2014/65/EU on markets in financial instruments [Article 49].

Please provide us with an executive/succinct summary of your example:
MiFID II puts in place a harmonised tick size regime for shares and certain ETFs traded on trading venues (MiFID II Article 49) with the objective of ensuring a level playing field between venues. Another objective of the tick size regime is to improve the quality of price formation in equity trading to the benefit of investors.

However, FESE regrets that the opportunity has been missed at Level 1 to extend the tick size regime to systematic internalisers. As a result, SIs will be able to offer price improvement at a very low cost and attract liquidity to their platforms by using tick size arbitrage. FESE believes this creates a regulatory gap running counter to the overall MiFID objectives of ensuring that as much trading as possible takes place on multilateral and transparent venues.

Tick size arbitrage risk further increasing fragmentation in equities' trading. As we outline under Issue 1, excessive fragmentation has contributed to eroding the ability of local Exchanges and ecosystems to fulfil their financing role. As such, we believe that any regulatory element that incentivises trading away from multilateral and transparent venues is going against the objectives of the CMU to strengthen European capital markets.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
FESE suggests bringing systematic internalisers within the scope of MiFID II Article 49.

Theme D. Rules giving rise to possible other unintended consequences

Issue 14 – Risk

Example 1: Risk

To which Directive(s) and/or Regulation(s) do you refer in your example?

- EMIR: Regulation 648/2012 on OTC derivatives, central counterparties and trade repositories [Article 4 clearing obligation & Article 5 clearing procedure for both direct and indirect clearing].
- MiFIR: Regulation (EU) No 600/2014 on markets in financial instruments [Article 28(1) and 32 outlines the provisions of the trading obligation].
- Delegated Regulation 149/2013 covers the detailed provisions for indirect clearing and the criteria to determine the asset classes that should be subjected to the clearing obligation.
- On 6th August 2015, Commission adopted Delegated Regulation 2015/2205 that determines the scope of the clearing obligation with regard to classes of derivatives subjected to it. It was published in the Official Journal on 1 December 2015 and will enter into force 20 days later. Its annex outlines the interest rate derivatives classes that are subject to the clearing obligation.

Please provide us with an executive/succinct summary of your example:
The total impact of the EMIR Clearing Obligation on the MiFIR Trading Obligation should be carefully considered, as any instrument which does not fall under the scope of the clearing obligation (EMIR) will not be eligible for the trading obligation (MiFID). FESE disagrees with the exclusion of OTC equity derivatives from the clearing obligation and considers that exchange traded derivatives are likely to, as a direct result, shift to the OTC environment. In accordance with the requirements set out in EMIR, look-alike contracts traded OTC will only be subject to a clearing obligation if ESMA decides to explicitly mandate the products for clearing. This contradicts the objectives set out by G20 and implemented by EMIR and the MiFID Review, and leaves open for short-term loopholes in the legislation.

Leaving exchange-traded derivatives outside of EMIR and MiFIR's clearing, trading, and transparency obligations would also encourage trading on venues which are not subject to any clearing requirements. For investors, this would translate into a perverse incentive to shift trading from transparent and cleared venues to the OTC space.

FESE would strongly suggest to automatically require clearing for look-a-like products where clearing is already required for that class of products on regulated markets. Since these products currently fall outside the clearing obligation (EMIR) it also makes them not fall within the trading obligation (MiFID) and would therefore exacerbate fragmentation of these markets.

In addition to harming overall transparency levels, this raises important investor protection issues, both because OTC trading in these instruments is not subject to central counterparty clearing and due to the predominantly retail nature of these markets. Investor warnings have already been issued by a number of securities regulators in Europe for forex derivatives and CFDs.

Furthermore, looking at the common criteria for the definition of a liquid market and the introduction of a trading obligation, FESE is concerned that the exclusion of any derivatives product classes from the clearing obligation, could affect the evaluation of the liquidity criteria. For criteria such as frequency of trades, number of participants, average size of transaction, etc. for product classes traded on-exchange, the lack of an EMIR clearing obligation will result in underestimating the real liquidity of the products as the considerable OTC volumes would never be taken into consideration. There is therefore a risk that some products might be deemed as illiquid with the negative result of actually preventing the development of a transparent market and efficient price formation and keeping a status quo also in terms of regional systemic risk.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
FESE members offering trading in securitised derivatives, foreign exchange derivatives, and contracts for difference (CFDs) (classified as derivatives under Annex I Section C of MiFID II) on their regulated markets are currently observing a significant shift of trading in these products to OTC platforms as defined under EMIR. This shift to OTC means that clearing which was hitherto applied to these products on regulated markets will not be required automatically in an OTC environment. Similar dynamics could easily be replicated across other products such as equity derivatives.

FESE is of the opinion that the EU equity derivatives markets is still underperforming regarding trading on listed equity derivatives products vs. OTC compared to more efficient and liquid market such as the US. We believe that such a process should be encouraged and accelerated by the introduction of a clearing obligation for standardized and flexible contracts rather than now halted. This is particularly important in some markets such as the Nordic where significant portions of standardized equity derivatives contracts are still traded OTC and are not subject to central clearing.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
FESE considers that a regional market view should be adopted to assess the characteristics of each financial market and the implications a clearing obligation would have from a regional risk reduction point of view, with the objective to promote transparency.

FESE believes that there should be an automatic clearing obligation for lookalike OTC equity derivatives. Failing that, the integrity of some exchange-traded equity derivatives markets may be threatened, especially at regional level, as these markets would be presented with a non-cleared alternative. These products falling outside the clearing obligation would also cause them not to fall within the trading obligation under MiFID and would therefore exacerbate fragmentation of these markets.

A clearing obligation for any OTC equity derivative contract should be introduced for those currencies outside the G4 currencies, that are currently not included but that mirror the listed exchange trade derivatives available for clearing.

Example 2: Risk

To which Directive(s) and/or Regulation(s) do you refer in your example?
- MiFID II: Directive 2014/65/EU on markets in financial instruments Directive 2014/65/EU.

Please provide us with an executive/succinct summary of your example:
MiFID II extends trade transparency requirements from shares to equity-like and a number of non-equity instruments. This is a welcome development which could however be put at risk by two risks of loopholes in the framework, namely regarding the introduction of RFQ systems for equities and the definition of the systematic internaliser.

Please provide us with supporting relevant and verifiable empirical evidence for your example:
- **Definition of Systematic Internalisers**

As previously discussed with the European Commission, we believe the lack of clarity around what type of activity is allowed on a systematic internaliser – bilateral or multilateral, on a principal or riskless principal basis – risks introducing a major loophole in the MiFID II transparency framework. This is because an SI operating on a riskless principal basis would essentially replicate the functioning of a multilateral venue, where the operator does not incur trading risk, but with a fraction of the transparency requirements.

Consequently, we support clarifying in the Delegated Acts being prepared for MiFID II that systematic internalisers are not allowed to run internal matching systems to execute trades on a bilateral basis. We note that this prohibition should be strictly applied in all cases and should not leave the door open to activity taking place on an occasional basis. This is because the notion of "occasional" is extremely vague and would be virtually impossible to monitor consistently across jurisdictions.

- **RFQ Systems for Equities**

In a significant departure from current practice under MiFID I, ***RTS 1*** (MiFID II Level 2 measures) introduces the possibility to operate a Request-for-Quote (RFQ) market model for equities and equity-like products[7]. ***In respect of ETFs***, we agree that this is aligned with current market trends and reflects the quote driven nature of those markets. In contrast, ***we believe the extension to equities opens up the possibility for a circumvention of the double volume cap and is not in line with the Level 1 framework.***

MIFID I provides for a **calibration of pre-trade transparency requirements for the following market systems**: order driven, quote driven, auction and hybrid. MiFIR Level 1 Article 3, covering equity & equity like instruments, maintains the market system scope of MIFID I calibration – quote, order, auction and hybrid – but extends the pre-trade transparency scope to all equity-like instruments as well as shares. In contrast, the corresponding provision in **MIFIR Article 8 on the non-equities side adds voice trading systems** to the original MiFID I trading systems.

As a result, it seems clear to us that the Level 1 text does not explicitly foresee calibration for voice trading systems in respect of equities and equity like. At the same time, **Recital 14** of MiFIR does provide clarification ***that voice trading*** should be added to the list of market systems in respect of "*specific types of financial instruments* ***other than shares***"[8].

We therefore believe a combination of MIFIR Article 3 and Recital 14 provides the legal basis for an RFQ extension to equity-like instruments (which we support), but not to shares.

Alongside question marks concerning alignment with the Level 1 text, we see no evidence of any rationale for the extension of RFQ to equities provided by ESMA. Specifically this concerns the omission in Section 3.1 of the December 2014 ESMA Consultation Paper of any rationale explaining the extension of RFQ to equities, based either on ESMA's assessment or feedback from the industry.

In our view, this type of market structure is fundamentally unnecessary for equity markets – given their order driven nature and - ***more importantly*** - would create a major loophole allowing market participants to circumvent the double volume cap on dark pools. This is because there is scope for participants on the venue to be allowed to answer a request for quote based on the price on the reference market – the same mechanism used by dark pools today. ***As the platform operating under an RFQ model would be deemed to be pre-trade transparent, it would not need to apply for the reference price waiver and would not be subject to the double volume cap.***

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[7] Table 1, Annex 1 of RTS 1

[8] MiFIR Recital 14 : *"Timely pre-trade and post-trade transparency requirements taking account of the different characteristics and market structures of specific types of financial instruments other than shares should thus be introduced and calibrated for different types of trading systems, including order-book, quote-driven, hybrid, periodic auction trading and voice trading systems."*

Above all, we strongly urge the European co-legislators to remove the provision for equities RFQ in order prevent the potential for the following situations:

- ***Superficially pre-trade transparent systems***, but with a complete absence of price discovery based on the interaction of the trading members & with execution limited to the requesting party, combined with;
- ***Freeriding of participants on such systems*** on the reference price generated from the full disclosure & interaction of trading interests on truly transparent & multilateral trading venues.

If you have suggestions to remedy the issue(s) raised in your example, please make them here:
Regarding SIs, we support limiting their use to strict bilateral trading only. Matched principal or riskless principal trading should not be allowed, even when they take place on an occasional basis.

Regarding equities' transparency, we support restricting the use of RFQ systems to equity-like and non-equity instruments.