

# FESE Response to the ESMA Consultation Paper on the Review of RTS 1 and RTS 2

Brussels, 1<sup>st</sup> October 2021

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## Introduction

FESE welcomes the opportunity to respond to the ESMA Consultation Paper on the Review of RTS 1 and RTS 2.

We agree with ESMA on increasing the large-in-scale (LIS) thresholds for exchange-traded funds, developing a more consistent and clearer approach on non-price forming transactions, and strengthening pre-trade transparency requirements in general. FESE also shares ESMA's general views on the fields and flags to be populated when publishing transparency information and providing reference and quantitative data for transparency calculations. However, we disagree with the proposal to prescribe the order of the population of trade flags as it is potentially very disruptive and does not have obvious value-added.

With regards to non-equity, we appreciate ESMA's announcement to conduct a targeted review of the threshold methodology for derivatives, other than commodity derivatives. In our view, the methodology seems to be especially flawed for the sub-asset classes of bond options and stock futures. Moreover, we see also room for improvement for stock index options and stock index futures. In the response, we have included several suggestions on how to fix the existing issues.

For commodity derivatives, we acknowledge ESMA's proposals and have identified those areas that are worth further consideration. As a general remark, we believe that it is crucial that the liquidity assessment and the LIS threshold calculation should be based on order book data alone.

Lastly, we underline that ESMA's recommendations are potentially very disruptive and will trigger substantial IT engineering efforts. The industry can only start the impact analysis, specifications updates, and engineering work once the final provisions get published. The suggested entry into force date by 2023 looks therefore over-ambitious. We would consider a 12 to 18 months implementation period as the minimum. Having said this, we believe that for commodity markets it would be good if the new calculations for the liquidity assessment and the pre-trade transparency LIS thresholds would already become effective sooner, e.g. from June 2022.

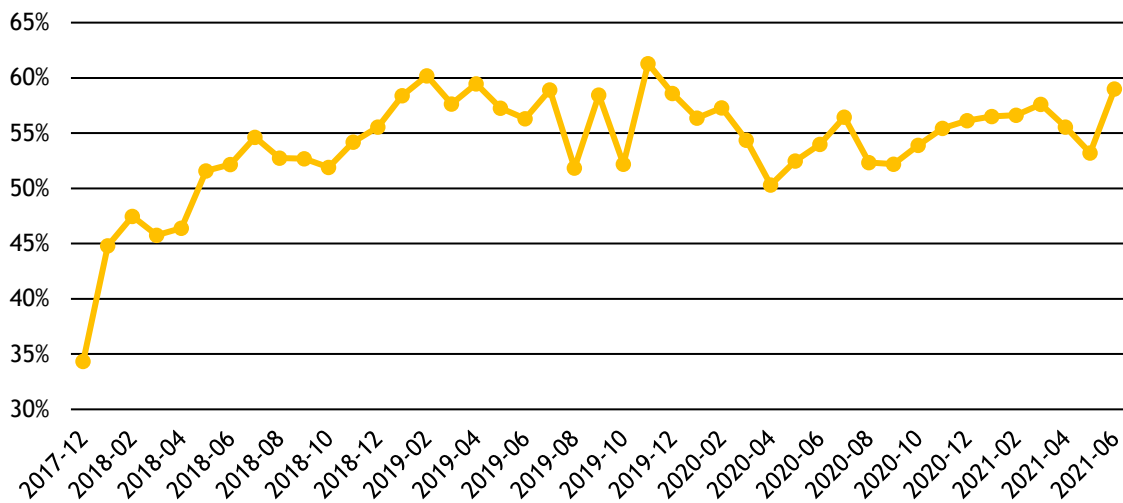
## Review of RTS 1

**Question 1: Do you agree with the proposed amendment to Article 7(2) of RTS 1? If not, please explain your concerns about the proposed increase of the threshold.**

FESE agrees with ESMA's proposal to increase the pre-trade LIS threshold for ETFs to EUR 3,000,000. We would also mention that, while this change would go in the right direction, we urge ESMA to complement this measure with additional steps to further promote transparency for on-venue trading of ETFs. Notably, we noticed that the trend towards

Request for quote (RFQ) systems has not reversed considering that, according to data published by Flow Traders, the market share of value traded on EMEA RFQ MTFs in ETPs increased from 34% in December 2017 to 59% in June 2021.

### RFQ MTF Market Share for ETPs in EMEA



Source: Flow Traders ETP Market Statistics

This development is worrisome as RFQ trading systems provide less transparency than lit order book trading systems due to their very nature of facilitating non-public requests. Since RFQ trading systems provide investors with actionable ETF price information only on request rather than on a continuous basis, their transparency level is significantly lower than that of lit order book trading systems which continuously provide investors with actionable price information. Specifically, the publication of quotes does not take place continuously whenever quote updates are received by the RFQ trading system but only for a brief instant in the form of a snapshot of the most recent quote update from each quote respondent before a transaction is concluded. As a consequence, we believe that transparency in European ETF trading has actually suffered from this shift in volumes

following the introduction of MiFID II/R. To improve transparency in European ETF trading and to level the playing field between RFQ trading systems and lit order book trading systems, ESMA may consider implementing a pre-trade transparency regime for RFQ trading systems similar to that for lit order book trading systems. This would require the publication and dissemination of each quote submitted in response to a sub-LIS RFQ immediately after the reception of the quote by the RFQ trading system.

While the decline in transparency presents an issue in itself, we also believe that this development may have a detrimental impact on the accessibility and liquidity of the overall ETF market in the long term. From our perspective, RFQ systems primarily add value when it comes to facilitating the execution of large block orders in ETFs. However, as RFQ systems become more widely adopted even for very small ETF transaction sizes, the liquidity and price quality provided on lit order book systems may decrease as a consequence of the declining demand for this type of trading system. While this would have a negative impact on all types of investors, we believe that retail investors would likely suffer the most from this development as alternative trading systems such as RFQ systems are typically not readily accessible to this investor group. Hence, robust lit order book systems are essential for retail investors to access and trade ETFs in an effective way.

We would therefore suggest that ESMA further investigates the liquidity shift from lit order book trading to RFQ trading and assesses its potential long-term impact on ETFs market structure. We would also ask ESMA to identify potential mitigating measures if this trend is perceived to be not compliant with ESMA's objective to ensure the quality and robustness of the ETF price determination mechanism for all types of investors. From our perspective, introducing a minimum transaction size for RFQ executions, in combination with an improved pre-trade transparency regime for RFQ trading systems, could serve as an effective mitigating measure to ensure that lit order book trading can continue to play its pivotal role in enabling efficient and cost-effective access to ETFs for all types of investors. Such a minimum transaction size could be based on the large-in-scale threshold for ETFs.

**Question 2: Do you agree with the proposed amendment to Table 5 of Annex II of RTS 1? If not, please explain why you are concerned about the proposed increase of the thresholds.**

FESE agrees with ESMA to increase the minimum qualifying size of transaction for permitted delay with a 60-minute delay from EUR 10,000,000 to EUR 15,000,000. The volume of transactions subject to deferred publication in relation to the total volume of ETFs executed on-venue is significantly high, which goes against the objective of achieving higher real-time post-trade transparency.

**Question 3: Do you agree with ESMA's amendments to Articles 2, 6 and 13 of RTS 1 described above? If not, please explain why.**

As a preliminary remark, FESE would stress that the notion of addressable liquidity is not about the place of execution and is not limited to multilateral venues. Such an overly simplified view risks unforeseen major consequences on equity market structure: where MiFID II/MiFIR looked at increasing market transparency, an unjustified definition of non-addressable liquidity could be at odds with this main objective and question the concept of an efficient price discovery process. Whilst in this debate it is important to recognise as well the distinction between price-forming and non-price-forming transactions, addressable liquidity refers to the interactive nature of liquidity and encompasses both categories. Likewise, mixing technical transactions, non-pre trade transparent trades, and trades without an economic trading interest is incorrect. For example, a significant number of non-price forming transactions (like those executed under the negotiated transaction waiver) are addressable, and would even be price forming if executed on a trading venue. Trades can be identified as addressable liquidity regardless of whether conducted OTC or in an SI.

The topic of non-addressable liquidity and non-price forming transactions should also be considered in the context of the STO as well as the consolidated tape, the categories of trades under its scope are a fundamental aspect and in no case the consolidated tape should be ringfenced to addressable liquidity.

These preliminary remarks having been made, FESE generally agrees with ESMA's approach to streamline regulatory requirements, while eliminating inconsistencies. The concept of non-addressable liquidity has taken a significant place in the debate on market data quality, with spillovers on the discussions on equity market structure particularly in the context of the MiFID II/MiFIR Review. Streamlining the regulatory framework where there are inconsistencies is necessary to ensure a clear and harmonised understanding across the EU (for example, in connection with Article 23 MiFIR and RTS 1 Articles 2, 6, and 13, and Article 2 RTS 22).

**Question 4: Do you agree with the proposed description of FBA trading systems and the updated description of periodic auction trading systems? If not, please explain why and which elements should be added to the description and/or removed.**

FESE would like first to note that any changes proposed in the upcoming review of MiFID II/MiFIR will have consequences on market structure and logically FBAs. We suggest that a holistic approach is taken, with the aim of creating a market structure that serves all market participants, from the smaller to the bigger. This includes supporting transparent and multilateral trading, and at the same time taking into account the dynamics of alternative venues such as SIs, dark pools and OTC, thereby ensuring a robust price formation process for the benefit of the overall market and its individual participants, not least retail investors. We encourage ESMA to prioritise a converging supervisory and enforcement approach.

Regarding the definition of FBAs proposed by ESMA, we also notice that, as mentioned by ESMA, the duration is missing. When it is understood that setting a maximum or average length for an auction is difficult and prone to easy circumvention, the description as it stands would now cover systems with auctions lasting potentially longer than the conventional periodic auctions, in complete opposition to the description provided by ESMA (“FBAs have a shorter duration than conventional periodic auctions, often only lasting for some milliseconds”, paragraph 61). This aspect is exacerbated by the deliberate choice by ESMA to remove the reference to human intervention in the document. To our knowledge for equity instruments, all FBAs function without human intervention in the price setting; removing “operated without human intervention” from the definition has two consequences. First it means that all systems with and without manual intervention are captured by the definition of FBAs. Second, it negates further the dimension of duration as the mention of “using a trading algorithm operated without human intervention” would ensure that systems running on a much slower pace than FBAs because of a human intervention are not captured in the definition.

Moreover, we would question the mention of “during continuous trading hours” since periodic auctions could potentially run outside of trading hours without any impact on the trading system per se. It is also not consistent with the definition of periodic auction trading systems which does not include nor exclude any specific session to run those auctions.

Regarding the description of periodic auction trading systems, we do not see any merit in providing a list of auctions to be included in the definition as it denies the relevance of the definition. Instead, we believe it would be preferable to maintain the current definition but to explicitly exclude FBAs from the definition. Together with the definition, a list shall only provide examples of what periodic auctions would be, which is not how ESMA did formulate its proposal (“Periodic auction trading systems include”). FESE would specifically highlight that the list provided is not exhaustive: intraday auctions which are not opening auctions, nor closing auctions nor auctions following a volatility interruption, are not mentioned. Those intraday auctions taking place usually at midday, are scheduled and do interrupt continuous trading, they shall be included in the list of periodic auctions.

**Question 5: Which of the two options for the pre-trade transparency requirements for FBA trading systems do you prefer? Please explain in case you are supportive of a different approach than the two options presented.**

Regarding the concerns raised in our response to question 4, we cannot recommend a suitable option for the pre-trade transparency requirements for FBAs. Considering that the definition as it currently stands for FBAs, and the trading systems which would fall under it, we have identified that some of them already provide a level of pre-trade transparency which is optimal and calibrated to the needs of the investors. Indeed, for

selective models in equity instruments but as well non-equity instruments, market participants have access to quotes in real-time with price and volume. In that case, Option 1 described by ESMA would bring less information, potentially irrelevant when a limited number of participants are involved in the auction compared to an order-by-order display.

While the requirements mandated in Option 1 already provide for an appropriate amount of transparency, we do not see why FBAs which also display information related to orders, as reflected in Option 2, should not be possible. We therefore are of the view that trading venues should be able to operate FBA's in line with the requirements following from both options put forward by ESMA. The varying FBA auctions have been calibrated to the needs of the market participants and we strongly advise providing venues with flexibility.

Finally, we would like to note that we have observed that the Level 3 Guidelines are applied differently across EU jurisdictions with for example some NCAs having forbidden midpoint order pegging as opposed to other jurisdictions where the Level 3 guidelines have not been applied. Although FESE understands that Level 3 regulation is not mandatory, we also notice distortion to the benefit of some players. In this instance, FESE advises moving the Level 3 measures with respect to forbidding midpoint order pegging by FBAs to Level 2 to avoid competition distortion.

**Question 6: Do you agree with ESMA's proposals for 'hybrid systems'? If not, please explain why and which elements should be added and/or removed.**

FESE agrees with ESMA's proposal to split hybrid systems and any other systems into two different categories. This is in line with our interpretation of the current regulation which is already implemented in our members' post-trade transparency implemented measures.

**Question 7: Do you agree with aligning both Table 1, Annex I of RTS 1 and Table describing the type of system and the related information to be made public in accordance with Article 2, of Annex I of RTS 2, to describe the same systems (with the exception of voice trading systems) and pre-trade transparency requirements? If not, please explain why.**

**Question 8: Do you agree with ESMA's proposals to require a specific format and standardise further the pre-trade information to be disclosed? If not, please explain why. If yes, please clarify which elements should be amended, added and/or removed, if any.**

There is some merit in attempting to harmonise the pre-trade information to be disclosed however FESE does not agree with all of ESMA's proposals in this area. ESMA should in general stick to the data content requirements and abstain from being intrusive in technical data formats.

Except for end-user terminals where human beings consume the information, the rest of the market processing value chain is invisible and designed for transparent and efficient data transmission. Feed handlers operated by vendors are efficient and can easily make the correct interpretation of incoming data from trading venues and APAs and reproduce compliant information on display services for end-users.

As stated in the ESMA Q&As on MiFID II and MiFIR transparency topics (see question 2c), it is also important to ensure efficient distribution in terms of reasonable bandwidth consumption and latency performance.

Asking for human-readable informational content across the invisible sequences of the data processing chain would trigger huge re-engineering costs, more bandwidth consumption, and slow down the overall data transmission speed. This would add no transparency improvements and make costs explode. The ISO data format for timestamps is the archetypical example of potential inadequate format requirements for efficient distribution via data feeds. We assume that this is not ESMA's intention.

In short, FESE would strongly dissuade ESMA from making changes that could affect the efficiency of pre-trade information disclosed and overload data users with unnecessary data.

**Question 9: Do you agree with the changes proposed by ESMA to amend Article 15 (3) of RTS 1? If not, please explain your rationale.**

Yes, FESE agrees with the changes proposed by ESMA. Bringing the publication of deferred trades to the opening of the next trading session for trades executed less than two hours before the end of the trading day brings more transparency and appears technically feasible. However, ESMA suggests publishing the information "no later than the opening of the trading day of the most relevant market in terms of liquidity [...]". This requirement means an adjustment on an instrument-by-instrument level which brings unnecessary complexity both for venues and market participants. We would therefore propose to publish the information earlier than noon but at the same time for all reporting entities: "no later than 09:00 local time [...]".

**Question 10: Do you agree with the proposed amendments to Article 17? If not, please explain.**

FESE agrees with the proposal to modify Article 17(2) of RTS 1 for the date of application of transparency calculations replacing the 1<sup>st</sup> April for the first Monday of April of each year. We understand this change means that the annual update on the most relevant market in terms of liquidity and the average daily turnover for the purpose of identifying large-in-scale orders and the standard market size will apply on the first Monday of April. We would like to signal to ESMA that this decision does have an impact beyond RTS 1 and requires adjustment due to the operational risk coming from discrepancies between regulations. Indeed, regarding tick sizes Article 3(4) of RTS 11 stipulates that "Trading venues shall apply the tick sizes of the liquidity band corresponding to the average daily number of transactions as published in accordance with paragraph 1 from 1 April following that publication." Leaving RTS 11 as it currently is would require two updates of our systems which entails a significant operational risk for trading venues and in general confusion for all market participants. We then very much urge ESMA to modify RTS 11 to align both regulations as follows: "Trading venues shall apply the tick sizes of the liquidity band corresponding to the average daily number of transactions as published in accordance with paragraph 1 from 4 the first Monday of April following that publication."

**Question 11: Do you agree with the proposed amendment of Article 11(3)(c) of RTS 1? Please**

FESE believes that a simple amendment to Article 11 should be made to include post-trade LIS transactions. This amendment would ensure that the SMS level is properly representative of liquidity in equity markets.

**Question 12: Do you agree with the changes proposed to Table 3 of Annex I of RTS 1 (List of details for the purpose of post-trade transparency) presented above? If not, please**



**explain and provide any alternative proposal you might have. Are there other issues to be addressed and how?**

FESE believes that from a data management perspective, it is not wise to ask for an alphanumeric entry in a numeric field (price field). This was true with the “PNDG” entry and it is true again with the proposed “NOAP” entry. Many systems operated by vendors cannot cope with this piece of information. Considering that trade flags are usually components of standard trade messages, it would be more convenient to have that “PNDG” and “NOAP” as trade flags rather than price field value. The informational content for post-trade transparency purposes would be equivalent.

**Question 13: Do you agree with ESMA’s proposal not to change Tables 1 and 2 of Annex III of RTS 1? If not, and you consider that certain modifications shall be made, please explain.**

Yes, FESE generally agrees with ESMA’s proposal not to change Tables 1 and 2 of Annex III of RTS 1.

**Question 14: Do you agree with ESMA’s proposal on the new Tables 1 and 2 of Annex IV of RTS 1? If not, please explain and provide any alternative proposal you might have.**

FESE would like to underline the significant technical impact on RTS files and subsequent systems for the transparency calculation that ESMA’s proposal on the new Tables 1 and 2 of Annex IV of RTS 1 would have (especially considering the short indicative timeline provided by ESMA in its consultation paper). FESE hopes that ESMA will take these considerations into account.

**Question 15: Please provide concrete examples or scenarios when the price cannot be determined as described or cases of the need to set a zero price for the different types of instruments: shares, ETFs, depositary receipts, certificates, other equity-like financial instruments.**

FESE considers that the most problematic case for providing a price is case 1 (price for the day corresponding to the ‘Date of admission to trading or first trading date’). As a consequence, we would propose that default values apply until trading venues are able to provide a price referring to a price forming transaction.

**Question 16: Do you agree with the deletion of the SI flags ‘SIZE’, ‘ILQD’ and ‘RPRI’? If not, please explain what you consider to be their added value.**

FESE disagrees with the deletion of the SI flags ‘SIZE’, ‘ILQD’, and ‘RPRI’. Steps should be taken to improve the consistency and completeness of SI data quality in order to increase visibility of what is happening in this space. The deletion of three SI flags may facilitate easier flagging of SI trades but it would ultimately fall short of addressing the underlying issue and constitute a concerning development from a level playing field perspective.

We understand that the unambiguous identification of a trade executed via an SI is done via the MIC (SINT) field. We appreciate the simplification attempt, but the three pre-trade transparency waiver flags applicable to SIs are not replaced by any flag and the “NTLS” flag is designed to be applied to on-venue trades only.

**Question 17: Do you agree with the deletion of the ACTX flag? If not, please explain what you consider to be its added value.**

FESE does not agree with ESMA's proposal to delete the ACTX flag. As per RTS 1, the ACTX flag applies to "transactions where an investment firm has brought together two clients' orders with the purchase and the sale conducted as one transaction and involving the same volume and price." The ACTX flag therefore does not apply to transactions executed on a trading venue. Instead, the ACTX flag reveals, if a transaction was arranged and executed OTC. As the ACTX flag is the only flag for post-trade transparency purposes that allows to identify OTC, removing this flag would deprive market participants from information of the true level of transactions in these markets. Since the OTC already is an opaque market, further reducing its level of post-trade transparency does not appear appropriate and contrary to the goal of MiFID II/MiFIR to increase the overall transparency in equity markets. Hence, FESE would welcome ESMA to reconsider its proposal and to not remove the ACTX flag from the list of flags for the purpose of post-trade transparency.

**Question 18: Do you agree with the approach suggested for non-price forming transactions? If not, please explain.**

FESE generally agrees with ESMA's approach for non-price forming transactions in RTS 1, which would improve data quality and facilitate the aggregation of information. At the same time, to preserve fair, stable, and transparent markets, loopholes in the definitions should be avoided. One example of such loopholes could be found in what exactly defines a portfolio trade "PORT". This is important in order to ensure a common understanding and avoid necessary adaptations in the future. We also notice a potential mutual exclusivity issue among "BENC", "PORT", and "CONT" flags. From our perspective, such flags can be applied simultaneously.

FESE would also like to remark that trade flags represent one part of the solution. Definitions of rules on how to properly use the flags (reporting guidelines) as well as supervisory enforcement are equally important. Communication and education of stakeholders (reporting organisations, APAs, auditors, etc) around flags and flag usage rules are very much needed as well.

**Question 19: Do you agree with ESMA's proposal to introduce a pre-trade LIS waiver flag for on-book transactions? If not, please explain. Should it be limited to completely filled LIS orders?**

FESE does not agree with ESMA's proposal. FESE believes that the proposal should not be limited to completely filled LIS orders. According to the solution outlined by ESMA, initial partial fills for LIS orders would not transport any "WAIV" flag in order to avoid information leakage on remaining hidden quantity in the book. Only the very last final partial fill would transport the "WAIV" flag. This would consequently provide a massively understated and misleading picture of the volume actually executed that is waived from pre-trade transparency. Furthermore, we believe this additional flag would only increase complexity when informing it since orders' size need to be linked to the correspondent transaction.

**Question 20: Do you agree with ESMA's proposal to introduce a pre-trade LIS waiver for offbook transactions? If not, please explain.**

Yes, FESE agrees with ESMA's proposal to introduce a pre-trade LIS waiver flag for off book transactions brought onto a venue. As specified, this flag would allow to identify LIS transactions executed off book and benefiting from the LIS waiver. We do welcome that



additional transparency is brought besides transactions executed under the negotiated trade waiver.

With respect to the proposed NTLs flag, we do not believe it is suitable since most of the block trades could end under that one which is aimed to be used for OTC transactions brought onto a venue.

**Question 21: Do you agree with the proposal not to add such additional flags? If not, please explain why those flags are needed in your view.**

FESE agrees with ESMA's proposal not to add such flags, especially looking at redundancy and complexity issues as well as misconceptions linking some new flags with addressable liquidity. For example, trades occurring outside of trading hours can be addressable, the same applies to transactions like inter-affiliate trades and internal crossing network executions. Any additional flags should be properly justified and defined, not only in order to ensure regulatory certainty (which is necessary for correct reporting of off-venue transactions), but as well to create a common understanding and reliable trade reportings resulting in reliable data for the EU. For the sake of high-quality market data in the EU, clear definitions are indispensable.

**Question 22: Do you recommend adding/deleting/amending any other flags? If yes, please explain.**

Please see our answer to question 12.

**Question 23: Do you agree with the proposal to prescribe the order of the population of flags? If not, please explain and provide an alternative proposal.**

FESE disagrees with the proposal as it is potentially very disruptive and does not have obvious value-added.

We understand that ESMA suggests a different data hierarchy that does not match the current FIX MMT data structure and also suggests additional provisions on data representation. We believe that such prescriptive measures on data structure and data format will trigger a massive re-engineering effort across the market data value chain. Trading venues, APAs, vendors, application service providers, and order management systems of buy- and sell-side stakeholders will be impacted. Such rigid provisions will have no informational value-added for the end-consumer and supposedly will create large additional costs within the industry.

FESE considers that trade flags and the related rules on how to properly apply them are of paramount importance to secure efficient post-trade transparency. This is one clear pillar of investor protection. Both compliance with RTS provisions and data standardisation are instrumental in that sense. However, explicit trade flags and the order of these flags are solely important at the end of the chain when human beings consume the data on a screen. All upstream data processing stages are invisible and should be left to the discretion of actors across the market data value chain. Otherwise, the proposed provisions will slow down the stream of data (and thus conflict with the MiFID provisions on data distribution latency), increase the bandwidth requirements to channel the data, and make the setup more expensive without any transparency benefits.

Consequently, FESE strongly recommends ESMA to abstain from issuing potentially very disruptive provisions on data structure and data format, in our view they add no value to post-trade transparency quality and will make implementation overly expensive without good reasons. Existing industry standards are fit for purpose. The FIX MMT data standard

is an efficient industry solution for compliance with regulatory trade flagging requirements, its logic has a wide acceptance across the industry. There is consequently a deep chain of dependencies on MMT data. FIX MMT will for sure deliver a new release in a timely manner when the final RTS 1 and RTS 2 provisions are known.

## Review of RTS 2

**Question 24: Do you agree with the proposed amendments above? If not, please do not reiterate the arguments made under the previous question asked for equity instruments and please rather explain why those amendments are not suitable for non-equity financial instruments.**

Yes, FESE in principle would agree with ESMA's proposed amendments. Although trading systems in equity are different from non-equity ones (i.e. voice trading systems are not relevant at all for equities), adopting a homogeneous approach looks reasonable. This should not prevent to define in the future different transparency requirements for equity and non-equity trading systems within a single table, if necessary.

Generally, it is appreciated that the description of trading systems and pre-trade transparency requirements applicable to those systems are consistent across RTS1 and RTS2. However, referring to our response to Question 4, we have reservations about the proposed definitions for FBAs and periodic auction trading systems.

As stated in the response to Q4, we believe that it is crucial that the FBA definition in RTS1 captures specifically those FBAs that could benefit from more meaningful pre-trade information, i.e. those auctions that meet the characteristics outlined in paragraph 61 of the consultation paper.

Introducing the concept into RTS2 will exacerbate the unintended consequences. It is rather recommended to develop a more precise definition of FBA. Alongside we urge ESMA to maintain the current definition for periodic auction systems as per RTS 2, i.e. a system that matches orders on the basis of a periodic auction and a trading algorithm operated without human intervention. This definition has established proven and well-working auction mechanisms.

**Question 25: Do you agree with the proposal to specify the fields to be populated for pre-trade transparency purposes? If not, please explain. In case you support the proposal, please comment on the fields proposed, in particular whether you would consider them necessary and/or whether additional information is required.**

With regards to derivatives markets, we do not believe that it is necessary for the regulations to specify in detail the information that trading venues need to disclose in the operation of their markets. Requiring venues to add data that participants do not need would slow the operation of the venue, which we do not believe is in consumers' best interests, and would hamper the formation of an orderly and efficient market.

We would therefore disagree with ESMA's proposal and would suggest keeping the current regime.

Having said this, we hold the view that all market participants in the EU should contribute to more pre-trade transparency. Excluding SIs from the mandate to publish pre-trade transparency data for non-equity instruments according to the same standards that apply to trading venues will, however, hinder the ability of data consumers to retrieve all required pre-trade information in a harmonised manner. FESE would therefore like to encourage ESMA to extend the mandate for a standardised publication of pre-trade transparency data also to SIs.

With regards to fixed income instruments, the added value of the pre-trade table is not clear. Any short-term technical changes running up to the MiFIR Review should have a

clear benefit to the market. We question the addition of the type of trading system for each individual price, at this point we do not see the need to have info on the type of trading system. In general, exchanges already make available pre-trade data which is consumed by many market participants and other data users. The costs of implementing these changes to both trading venues and data subscribers will be significant. The requirement to implement standardised fields, field formats and field values for pre-trade data will require trading venues to invest significant human and financial resources. Similarly existing data subscribers will have to invest significant human and financial resources to consume the pre-trade data according to the new formats.

We believe that the benefit that ESMA identifies is not aligned with the recent guidance published in the ESMA Guidelines on Market Data. In particular, ESMA identifies in paragraph 235 that this new requirement will “facilitate the consumption and aggregation of the pre-trade information”. The Market Data Guideline 18 however notes: “Given that the [pre-trade] data is not provided for the purpose of consolidation, it should be available until the next more recent quote is available (i.e. a snapshot view, without historical information), or in case of lack of such update, until midnight of the following business day.”

We therefore suggest that ESMA does not take forward this proposal.

Should ESMA include this proposal, we would like to make the following comments on the proposed fields:

#### **Field 1 Submission date and time**

This field is likely to be misleading to data subscribers in cases where an order, quote or AIOI is updated, which could occur frequently and a long time after the submission of the original quote, order or AIOI. It would make more sense to publish the latest update time for the order, quote or AIOI.

#### **Field 2 ISIN**

For some instruments the ISIN may not always be available at the point of order submission, for example some derivative contracts such as interest rate swaps where the ISIN may be requested from ANNA-DSB after the order submission. This should be an optional field or allow for the use of alternative identifiers, in line with the existing ESMA Q&A on transparency issues:

Question 5 [Last update: 03/04/2017]

Does an ISIN need to be included for pre-trade quote publication?

Answer 5

Pre-trade transparency information should allow identifying unequivocally the financial instrument to which the information published refers. ISINs are one of the available ways to ensure the unequivocal identification of a financial instrument. However, ESMA recognises that ISINs may not always be available when providing a quote. Trading venues and systematic internalisers are free to use other ways for identifying instruments for pre-trade transparency purposes as long as the financial instrument can be unequivocally identified.

#### **Field 3 Side**

Publicly disclosing the side of an AIOI would present an issue for RFQ trading systems, where requests are usually single-sided (i.e. a request for a buy quote or a request for a

sell quote) rather than double-side (i.e. a request for a buy quote and a sell quote). The side field would allow data subscribers to be aware of the side of the responders to the RFQ. This information could allow other market participants to move the market to the disadvantage of the RFQ responder in anticipation of the RFQ responder seeking to cover any positions arising from the RFQ. This would likely to be accounted for by RFQ responders should the proposal be implemented, resulting potentially in worse pricing for RFQ requestors or potentially a loss of RFQ responders.

Additionally, this could encourage RFQ requestors to instead ask for quotes OTC from SIs that would not have the same pre-trade transparency format requirements as trading venues under ESMA's proposals. This would result in a shift from regulated RFQ trading venues to OTC trading.

**Question 26: Please indicate, if applicable, which medium-term targeted improvements you would like to see to the threshold calibrations in RTS 2.**

FESE appreciates ESMA's announcement to conduct a targeted review of the threshold methodology for derivatives, other than commodity derivatives. FESE members are committed to transparent markets and share the goal of MiFID II/MiFIR to shift more trading activities in derivatives from opaque OTC markets to trading venues. However, after three years of experience with the current design of the transparency regime as per RTS 2, we would like to highlight several improvements that we consider necessary regarding the methodology for exchange-traded derivatives (ETDs). Even though, ETDs are already characterised by high levels of pre- and post-trade transparency, the current methodology for the threshold calculation for certain sub-asset classes of equity derivatives and interest rate derivatives leads to outcomes that either limit or reverse the transparency ambition.

In our view, the methodology for the transparency calculations as per RTS 2 seems to be especially flawed for the sub-asset classes bond options and stock futures. Moreover, we see also room for improvement for stock index options and stock index futures. A recalibration of the existing LIS calculation methodology would allow ESMA to determine LIS thresholds in order to tier them more specifically to individual market specifics of each of the aforementioned asset classes. In the following, FESE therefore proposes improvements to the methodology for the threshold calculations for equity and interest rate derivatives to achieve a better transparency situation for the above-mentioned sub-asset classes.

**(1) Methodology for Equity Derivatives**

**1.1 Stock index options and stock index futures**

The current RTS 2 methodology for setting LIS-thresholds for equity derivatives is based on the average daily notional amount (ADNA), calculated over the period of one year. RTS 2 assigns for equity derivatives certain ranges of ADNA based on which LIS-thresholds are determined. Depending on the respective equity derivatives sub-asset class, RTS 2 provides either four or five possible ADNA-ranges for LIS-threshold designation. However, RTS 2 does not explain why certain sub-asset classes are provided with either four or five ADNA-ranges. For example, stock index options are only provided with four ADNA-ranges, whereas stock index futures, for example, have five ADNA-ranges according to which LIS-thresholds are assigned.

FESE considers the current levels of granularity as insufficient. For example, stock index options which have evolved from  $\text{EUR } 200 \text{ million} \leq \text{ADNA} < \text{EUR } 600 \text{ million}$  to  $\text{ADNA} \geq \text{EUR } 600 \text{ million}$  experience a significant jump in the applicable LIS-threshold from EUR 5.5

million to EUR 20 million. Similar jumps in LIS-thresholds from EUR 5.5 million to EUR 20 million are also foreseen by RTS 2 for stock index futures.

The reason why the current levels of granularity are considered as insufficient is because the ADNA is being defined by Table 4 Annex II RTS 2 as the notional amount of traded contracts. Hence, the ADNA of a stock index option or stock index future can not only change due to more or less traded contracts over the period of one year. Changes in the ADNA can also occur, if the notional amount changes due to spot price movements of the underlying index.<sup>1</sup> For example, a stock index option has in the first year an ADNA of EUR 590 million. In the second year, the number of traded contracts in the stock index option are equal to the previous year. However, in the second year the spot price of the underlying has increased by 10%. Despite constant trading activities measured by the number of contracts, the ADNA of the stock index option is in the second year therefore 10% higher as in the first year and above the threshold of EUR 600 million. As a consequence, the stock index option is equipped with a significantly higher threshold, despite no changes in the trading activities.

These jumps in the applicable thresholds can have significant impacts on affected products. For example, the 2021 ESMA transparency calculations classified Options on the EURO STOXX® Banks Index (OESB), into the highest ADNA-range for stock index options. As a result, the applicable LIS-threshold increased from EUR 5.5 million to EUR 20 million, which translated into an increase of the minimum block trade size (MBTS) for OESB from 3000 contracts to 6000 contracts. This increase led to a situation where market participants were not able to appropriately manage their risk exposure in bank assets, as uncertainty prevailed as to whether the order-book could absorb orders above 3000 contracts, which previously had been executed off-book. If an asset manager, for example, intended to trade at the previous MBTS of 3000 but was now using the new MBTS of 6000, he would end up adding as much risk as he tried to reduce and that would likely deter him from trading and risk could stay unhedged. Following the implementation of the new thresholds, trading data and market feedback in that particular instance show that market participants avoid submitting orders between 3000 and 6000 contracts into the order book as execution cannot be guaranteed at a given price. Market participants therefore need to split their order into smaller ones, which in turn increases their trading costs and disincentivizes on-exchange trading activities.

To avoid such consequences for stock index options and stock index futures, whose ADNA fluctuates around the current ADNA-ranges and where slight increases in their underlying spot price can lead to significantly higher LIS-thresholds, FESE suggests adding more granularity to the current ADNA-ranges. We propose to extend the ADNA-ranges for stock index options and stock index futures to 6 and 7 respectively, as indicated below. We are of the opinion that more granularity for stock index options and stock index futures with respect to the ADNA-ranges will reduce the steps between the LIS-thresholds and thereby facilitate a smoother transition towards higher LIS-thresholds.

New Stock index Options	LIS Pre Trade	LIS Post Trade
	RTS 2 Threshold	RTS 2 Threshold
<100 m	25,000	1,500,000
100m<=ADNA<=200m	2,500,000	25,000,000
200m<=ADNA<=600m	5,000,000	50,000,000

<sup>1</sup> FESE is aware that ESMA proposes to amend the measure of volume. However, even under the new definition of the measure of volume the described dynamics would still apply.

600m<=ADNA<=2b	10,000,000	100,000,000
2b<=ADNA<=4b	15,000,000	120,000,000
ADNA >= 4b	20,000,000	160,000,000

New Stock index Futures/Forwards	LIS Pre Trade	LIS Post Trade
	RTS 2 Threshold	RTS 2 Threshold
<100 m	25,000	1,500,000
100m<=ADNA<=1b	550,000	5,500,000
1b<=ADNA<=2b	2,500,000	25,000,000
2b<=ADNA<=3b	5,500,000	55,000,000
3b<=ADNA<=5b	7,500,000	75,000,000
5b<=ADNA<=10b	20,000,000	160,000,000
ADNA >=10b	30,000,000	240,000,000

## 1.2 Stock Futures

Despite the introduction of the MiFID II/MiFIR transparency regime in 2018, the overwhelming majority of trades in stock futures are still concluded off-book via block trading. The reason is that trading in stock futures is characterised by irregular trading activities, even for liquid products. Stock futures are mostly traded around corporate events, e.g. M&A, additional distributions, earnings announcements etc. Around these dates, relatively high trading volumes can be attributed to only a few trades. Trading and hedging using leverage and cost efficiency are often the main reasons participants choose stock futures.

Yet, despite only a few trades are being concluded per year in individual stock futures, the methodology for setting LIS-thresholds only focuses on the ADNA as guiding number for the LIS-threshold determination. This leads to a situation, where stock futures with sometimes only a few trades per year are equipped with the highest available LIS-threshold for stock futures. FESE therefore believes that the ADNA, as measure of trade magnitude, does not appropriately reflect the liquidity situation of stock futures.

As a result, RTS 2 applies LIS-thresholds to stock futures that are explicitly high, disturbing the off-book block-trading driven market of stock futures. Due to the high LIS-thresholds, smaller market participants, intending to make precise adjustments to their small portfolios but also market makers that aim to accurately hedge their options exposure are driven out of the stock futures market, since order-book liquidity is virtually not existent for stock futures and off-book thresholds are too high for their trading needs. As these participants are still required to address their individual risk exposures, most of these smaller participants either have to leave their risks unaddressed or need to turn to OTC-markets, where they are served bespoke solutions offered by banks. Against this background, FESE members have observed declining volumes in stock futures since the introduction of the transparency regime in 2018.

We, therefore, suggest amending the liquidity measure for stock futures. We believe that a measure of trade frequency to determine the liquidity of stock futures, alongside the current measure of magnitude, i.e. the ADNA, would reflect the trading activities in stock futures more accurately. Hence, we propose to enhance the ADNA with a minimum number of trades per day across all exchanges for stock futures. Such a minimum number of trades per year across all exchanges as additional measure to determine the liquidity situation



and to ultimately set the applicable LIS-thresholds of stock futures as more in line with the actual market structure.

This would mean that only if a stock future exceeds (or falls below) the current levels of ADNA as provided by Table 6.2. Annex II RTS 2 and the to be determined minimum number of trades per day across all exchanges it can be classified into the next higher (or lower) LIS-category for stock futures. As starting point, a minimum number of trades per day across all exchanges of 5 would be appropriate, meaning only if a stock future exceeds an ADNA of 25,000 EUR and a minimum number of trades per day across all exchanges of 5, it can be categorised into the next higher LIS-threshold category.

Ultimately, FESE believes that the number of trades per year as guiding measure for the LIS-threshold determination will lead to more accurate LIS-thresholds and therefore help to shift volumes from OTC markets back to stock futures executed on transparent regulated markets.

## **(2) Methodology for Interest Rate Derivatives**

### **Bond Options**

ESMA correctly acknowledges in the consultation paper that trading in European exchange-traded fixed income options (or bond options in the RTS 2 terminology), such as, for example, Options on Euro-Schatz Futures, Options on Euro-Bund Futures or Options on Buxl-Futures, is mostly conducted in large trade sizes. There are essentially two reasons, why trading in bond options is characterised by large trade sizes:

(1) Trading in bond options is driven by institutional investors, who employ these products to hedge against or take directional positions to address yield movements of the underlying fictitious bond yield (please find more information regarding the underlying of bond options in our response to Q33). Due to the professional nature of investors who have large portfolios to hedge and trade, trade sizes are generally large in bond options.

(2) Bond futures and options on bond futures normally have varying tenors from 2 to 30 years with respect to the underlying cash bonds. Short-dated bond derivatives show the lowest sensitivities to changes in bond yields while longer-dated bond derivatives have higher sensitivities. Far greater sizes are therefore required in low duration products to achieve the same economic payoff for a given change in yield. This results in larger trade sizes for fixed income futures and options on underlying's with a lower duration. Low duration products require higher trade sizes to achieve the same economic pay-off.

Against this background, the current 70<sup>th</sup> trade percentile-oriented methodology for the LIS-threshold determination for bond options leads to a situation where especially those bond options with lower durations and thus larger trade sizes, for example options on Euro-Schatz Futures, are equipped with extraordinarily high LIS-thresholds. On the other hand, bond options in with longer durations, such as options on Euro-Bund Futures, which generally have lower trade sizes and thus also a relatively liquid order-book, are attached with relatively low LIS-thresholds.

The methodology therefore in particular negatively impacts the market structure and the trading dynamics in products with longer durations. For example, trade sizes in options on Euro-Schatz Futures further increased after ESMA mandated a LIS threshold that equates 1,250 contracts (prior to 2018 the exchange had set the block trade size at 300 contracts). Fewer market makers serviced investors at less favourable prices for greater

size creating a negative feedback loop in which investors refrain from trading and the median trade sizes further increased.

FESE therefore considers the uniform methodology of assessing the LIS-thresholds based on the trade percentile as not adequate in bond options as the sizes traded at market depend heavily on the duration and sensitivity of a given point of the yield curve. As a result, bond options with an already liquid order-book situation receive relatively low LIS-thresholds and vice versa, which is not in line with the intention of the transparency regime for derivatives to bring more trading activities to the order-book. We therefore strongly recommend scaling the 70<sup>th</sup> trade percentile down for products with lower durations to reverse the negative volume and liquidity impact on the market.

**Depending on the tenor of the underlying, FESE proposes to scale the trade-percentile for the LIS-threshold determination as follows:**

<i>Tenor of underlying</i>	<i>Percentile to apply for LIS determination</i>
<i>2 years</i>	<i>30</i>
<i>5 years</i>	<i>50</i>
<i>10 years and greater</i>	<i>70</i>

Lastly, for fixed income instruments we support deletion of the SSTI waiver and SSTI deferral and the lowering the LIS thresholds. With particular reference to bonds markets, we believe that it is necessary to consider the size of the single order, regardless of the liquidity of the instrument, to assess the liquidity status. Different sizes should be established by asset class (e.g., govies, supra, corporate ...), below which there must be full transparency. We suggest ESMA to set the levels to ensure sufficient pre-trade transparency for the various asset classes and order sizes without having a negative impact on market liquidity.

**Question 27: Do you agree with the proposed changes to Article 13? If not, please explain**

Yes, FESE agrees with the proposed changes regarding the date of application of the transparency calculations. Monday is an ideal effective date from a system perspective. Allowing trading venues to implement technical changes over the weekend helps them ensure the smooth functioning of their systems. It also leaves more time for the verification of the changed configuration.

However, FESE does not consider the first Monday of June as appropriate application date because of the following reasons:

- The first week of any month is often preceded by the weekend following the expiries of commodity derivative contracts. During the weekend the exchange and clearing house are focusing their resources ensuring that this life cycle event is completed correctly;
- In the past, new transparency calculation sometimes coincided with the use of a different data template from ESMA. If this occurs, there is simply too little time between April 30 and the first Monday of June to work through the impact of the changes to the data template and implement the updated transparency calculation at the same time. A period of 5-6 weeks seems more suitable to ensure that the deadline is met, and the changes are implemented in an orderly manner.

We, therefore, believe that a change of trading parameters before the expiry week bears the risk of creating uncertainties amongst market participants and ultimately might destabilise the functioning of financial markets. Furthermore, it is important to highlight

that different contracts have different expiry weeks and that these different timelines need to be taken into consideration so as not to create disruptions.

To prevent the potentially detrimental effects described above, we urgently request ESMA to move the effective date of the updated transparency calculations for non-equity instruments across all EU trading venues to the second Monday following the different contracts' expiry weeks in June.

**Question 28: Do you agree with the proposed changes to Article 4? If not, please explain**

FESE agrees with ESMA's proposal to transfer the Q&A provisions on minimum size of orders held in an order management facility to Art. 4 RTS 2.

**Question 29: Do you agree with the proposed changes to Article 12? If not, please explain. Please do not reiterate the general comments made in the equity section and try to focus on arguments that are specific to non-equity financial instruments.**

ESMA proposes to amend Art. 12 RTS 2 such that redundancies in the legislative text are removed. The amendments entail no practical changes for non-equities. FESE therefore agrees with the proposed changes to Art. 12 RTS 2.

**Question 30: Please provide your comments on the analysis and proposals related to the liquidity framework applicable to commodity derivatives, EA and DEA detailed in Section 4.2 and summarised in Section 4.2.5. Please list the proposals with their ID (#1 to #9) for ease of reference.**

As an introductory remark, FESE believes that it is crucial that the liquidity assessment and the LIS threshold calculation should be based on order book data alone. To determine whether a market is liquid enough to accommodate a LIS threshold it is important to assess liquidity parameters such as the ADNT on the basis of the order book data alone.

**Proposal Commodity Derivatives 1: [Metals] Determine that all metal sub-asset classes do not have a liquid market.**

Yes, we agree and support the proposal.

**Proposal Commodity Derivatives 2: [ADNT] Maintain the criterion "average daily number of trades" (do not switch to "median daily number of trades")**

We agree with ESMA's proposal to maintain the current criterion "average daily number of trades" as the current ADNT system works and reflect the proportionality principle.

We have, however, some concerns regarding the suggestion to bundle pre-arranged and screen trades. The average daily number of trades should be focused on the number of trades being executed on screen.

**Proposal Commodity Derivatives 3: [ADNT] Increase the parameter of the ADNT to 50 trades per day for all commodity, C10, EA and DEA sub-classes.**

No, we would prefer an increase up to 100 trades for the ADNT. Given that trading is rarely uniformly distributed throughout the day, a higher threshold is a better basis for determining liquidity and, thus, an indication of the ability to find a counterparty in a relatively short period of time within a given trading day. Moreover, we should take account of the fact that trades are aggregated across venues.

**Proposal Commodity Derivatives 4: [ADNA] Replace the criterion “average daily notional amount” with the criterion “standard trade size” calculated as the most frequently traded size (mode) and set the parameter of the STS\_mode at 5 lots for futures: any class for which the most frequently traded size is lower than or equal to 5 lots would be deemed liquid (provided the other quantitative liquidity criterion is also fulfilled).**

We appreciate the introduction of the new STS\_mode criterion, as it is in some cases slightly more accurate than its predecessor ADNA. The STS\_mode does not, however, solve or reflect what should determine if a contract is liquid or not.

Firstly, the STS\_mode does not take into account the number of “units” in each lot when arguing that any class for which the most frequently traded size is lower than or equal to 5 lot would be deemed liquid. As an example, an average monthly contract has 720 MWh per 1 lot. A yearly contract has an average of 8,760 MWh per 1 lot (i.e., 12 times the monthly). In theory, when trading 1 year contract, the market participant is trading 12 x monthly contracts, equalling 12 “monthly” lots. The criterion is hence dependent on the technical contract setup, and does not reflect the liquidity in the contract, especially for contract with a large number of “units”, in this case MWh embedded in 1 lot.

Secondly, the trading pattern for a monthly contract and a year contract also differs significantly, as a trader looking to hedge long term would gradually build his/her book with yearly contracts as a foundation (small percentage of his exposure), and gradually trade more coming the next quarter and months. This can easily be reflected in the open interest building up in the short end of the curve, versus the long.

Lastly, when looking at the proportion of what has historically been traded (in lots) on screen versus pre-arranged, it varies a lot - and that it is especially dependent on the number of “units” in the contract trade (e.g., month, quarter, year). The smaller the number of “units” in the contract the trades are relatively larger on screen than the contract with a large number of units, which in our opinion is only logical - especially if you compare a monthly contract to a yearly contract. The STS\_MODE fails to demonstrate liquidity in this respect.

This being said, we do believe that the STS\_mode criterion fixes a vital flaw of the current ADNA criterion as the ADNA does not allow distinguishing between (1) a market with on average few trades of large sizes (potentially illiquid); and (2) a market with on average numerous trades of small sizes (potentially liquid).

We therefore believe that the STS\_mode criterion should be used in combination with ADNA and ADNT, bearing in mind that the average daily notional amount traded should no longer be a notional value but should be expressed in lots and therefore be called ADAL, “Average Daily Amount of Lots traded”.

Adding the STS\_mode criterion is especially important to ensure that options markets and commodity options markets are classified as illiquid. Almost no screen trading takes place in the existing options contracts, for example gas, power or emissions derivatives. Under the majority of methodologies discussed by ESMA in the consultation document, an extremely inappropriately high LIS threshold (ranging from 200 lots to 1000 lots) would apply to these options markets if they were deemed liquid by virtue of the amount of block transactions. This would have serious negative consequences for the orderly functioning of these markets. We finally would like to reiterate that the liquidity assessment should of course be performed on the basis of order book data alone.

**Proposal Commodity Derivatives 5: [ADNA] Set the same parameter of the STS\_mode for all contract types, including options (5 lots)**

As noted earlier, with several modifications to, amongst others, the liquidity determination, FESE supports the percentile approach for establishing the LIS thresholds. Energy options contracts and certain spread trading strategies (intercommodity spreads), however, require special treatment under RTS 2, as they have different characteristics and would receive inappropriate LIS thresholds if a standard methodology would be applied.

Whilst FESE understands the rationale to have more granular view of the markets' liquidity, we believe that there is no "one size fits all" approach in order to assess the liquidity of a particular commodity asset class. Commodity futures markets, notably nascent and new futures contract markets, have different types of users, and applying a standardised approach (i.e. the same parameter of the STS\_mode for all contract types) would not meet all of the various different characteristics and specificities.

**Proposal Commodity Derivatives 6: [LIS/SSTI] LIS and SSTI thresholds are equal to a set percentage of the average daily volumes (in lots), rounded to the nearest 5 lots and bounded by a floor and a cap.**

The introduction of ADVL as a benchmark to set the LIS and SSTI thresholds does not make sense in many ways. Again, it fails to address the number of "units" in the contract being traded. By introducing a floor at 5 lots makes in this case little sense as well, as the former remark makes the methodology fail.

As an example, the Nordic Electricity futures would wrongfully suffer from this methodology. If we take a look at the Nordic Baseload Yearly Futures in maturity bucket 3 number, the contract, based on 2020 figures, ESMA has calculated the following:

- ADNT = 58 trades (liquid per criterion 2)
- ADVL = 119 lots
- STS\_MODE = 1 lot (liquid per criterion 1)
- % of ADVL, pre-trade LIS = 5.95 lot = 5 lots rounded down to the nearest 5 lot.

When taking a look at the actual distribution of the trade, i.e. the percentage of trades traded in the different lot sizes (1,2,3 etc.), we see the following;

- 1 lots trade = 53% off all trades (79% screen, 21% pre-arranged)
- 2 lots trade = 25% off all trades (56% screen, 44% pre-arranged)
- Accumulated 1 and 2 lots = 78% off all trades
- 3 lots trade = 9% off all trades (49% screen, 51% pre-arranged)
- Accumulated 1-3 lots = 87% off all trades
- 4 lots trade = 3% of all trades (44% screen, 56% pre-arranged)
- Accumulated 1-4 lots = 90% off all trades
- 5 lots trade = 7% off all trades (24% screen, 76% pre-arranged).
- Accumulated 1-5 lots = 97% off all trades.

By this, it becomes clear to us that the methodology of setting a pre-trade LIS based on 5% of the ADVL does not reflect a logical pre-trade LIS value. With reference to our previous comments about the flaws of the methodology, the fact that the number of "units" - in this case MWh is not taken into account, eradicates the logic behind having a fixed floor at 5 lots as pre-trade LIS, in conjunction with the STS\_mode.

Having considered several alternative methodologies, we have concluded that the current percentile approach might be the least flawed methodology. However, the percentile approach should not be increased to 95 but remain at 70.

We came to this conclusion regarding the percentile approach because we believe that many of its weaknesses are now removed or possible to remove:

1. The counterintuitive effects are reduced by adding the STS criterion to the liquidity assessment as well as by increasing the ADNT from 50 to 100.
2. The LIS thresholds can be converted into lots.
3. The minimum floor, for which we see no justification, can be removed.
4. The round rules can easily be set at a more granular level.

Hence, we believe that, when the above measures are taken, the current 70 percentile approach would be the most suitable way forward.

**Proposal Commodity Derivatives 7: [Units or Lots] Set the liquidity framework in lots (STS\_mode parameter set in lots, volumes reported to ESMA in lots, LIS and SSTI thresholds published in lots) accompanied by Level 3 measures to address the risk of downward revisions of the lot sizes.**

See response above.

**Proposal Commodity Derivatives 8: [Reporting to FITRS] number of transactions shall be reported to FITRS per trade-size bins which are defined in the new Annex V of RTS 2. Total volumes in lots and total volumes in underlying units shall also be reported to FITRS as specified in the new Annex V of RTS 2.**

Yes, FESE would agree.

**Proposal Commodity Derivatives 9: [data scope] The transparency calculations continue to be performed with all data (on-venue, SI and OTC).**

Please see the introductory remark to this question. We believe that both the liquidity assessment as well as the LIS threshold calculation should be performed on order book data alone.

## Reporting fields

**Question 31: Do you agree with the changes proposed to Table 2 of Annex II of RTS 2 (List of details for the purpose of post-trade transparency) presented above? If not, please explain and provide any alternative proposal you might have. Are there other issues to be addressed and how?**

**Question 32: Do you agree with the changes proposed to Table 4 of Annex II of RTS 2 (Measure of volume) presented above? Do you think that it now provides more clarity? If not, please explain and provide any alternative proposal you might have.**

ESMA proposes to replace the term “Notional amount of traded contracts” in Table 4 of Annex II of RTS 2 with the definitions of the notional amount provided by Article 3a(1)(a) for futures and Article 3a(1)(b) for options of Delegated Regulation (EU) No 148/2013 (3).



In Article 3a(1)(a) the notional amount of futures is defined as “(...) *the reference amount from which contractual payments are determined in derivative markets*”. According to our understanding, this definition encompasses the multiplication of the current market price with the tick value of the respective future contract as method to obtain the notional volume for futures.

Based on this understanding, we agree with ESMA’s proposal.

**Question 33: Do you agree with ESMA’s proposals on Table 1 (Symbol) and Table 2 of Annex IV of RTS 2? If not, please explain and provide any alternative proposal you might have.**

For options on bond futures, such as, for example, Options on Euro-Bobl Futures, Options on Euro-Bund Futures, Options on Euro-Buxl Futures or Options on Euro-Schatz Futures, the ISIN code of the ultimate underlying bond cannot be provided. The reason is that these options have as underlying a bond future. These bond futures however are specified as futures on a fictitious underlying government bond with a given term range and a fixed coupon. This means that upon delivery of such futures, a bond from a basket of existing government bonds, that qualify for delivery based on their issuance size and maturity, can be chosen. The individual bonds within the basket may vary significantly as to their coupons and residual time to maturity. When it comes to the physical delivery of a futures position, the seller of the futures must decide which government bond from the basket will be chosen to fulfil the delivery obligation. As the direct underlying is fictitious and bond futures are not referring to a unique underlying, a ISIN code of the ultimate underlying bond cannot be provided to field 22.

Against this background, if field 22 could only be filled with ISINs of bonds, this would therefore create uncertainties and confusion with regards to the underlying of options on bond futures. Ultimately, this would also lead to potentially false transparency calculations for options on bond futures as the underlyings for these products would not be recognised by field 22.

To improve the accuracy of the transparency calculations, FESE instead proposes to amend field 22 of Table 2 Annex IV such that this field can also be populated with the ISIN of bond futures, if they serve as underlying for options on bond futures.

We disagree with the proposed specification of field names and sequential order in Section 3.3.1.1 for RTS 1 and Section 4.3.1.1 for RTS 2 Annex II Table 2 for the post-trade transparency publication. The market data feeds developed by trading venues are designed to optimise the publication of real-time data for the benefit of data subscribers.

Instead ESMA could require trading venues and APAs to provide data subscribers with a mapping table that allows data subscribers to map the data publication to the RTS 1 and RTS 2 post-trade publication fields.

**Question 34: Do you agree with ESMA’s proposals on the segmentation criteria for bonds (Table 2.2), securitised derivatives (Table 4.1), interest rate derivatives (Table 5.1), equity derivatives (Table 6.1), credit derivatives (Table 9.2 and 9.3) and emission allowances (Table 12.1) of Annex III of RTS 2? If not, please explain and provide any alternative proposal you might have.**

FESE supports ESMA’s proposal to include a clarification of the reference data required for the segmentation.

With regard to the segmentation criteria for bond options proposed in table 5.1, FESE does not agree with removing bond futures/forwards as underlying in segmentation criterion 1. As outlined in our response to Q33, options on bond futures generally have bond futures

as underlying, which cannot be linked to a specific bond. Therefore, any segmentation of options on bond futures along underlying bonds will be not feasible.

Hence, FESE strongly recommends to not remove bond futures/forwards from the segmentation criteria 1 for bond options. Instead, in line with our response to Q34 it is suggested to recognise bond futures as underlying for options on bond futures in field 22, which would allow to keep bond futures/forwards as segmentation criteria for options on bond futures.

Furthermore, we would like to flag that, in the context of data reporting, RTS 2 - Field 9 - Bond type, table 2.2 of Annex III briefly explains the difference between the different types of bonds (i.e. Sovereign Bond type, other Public etc). However, there have been some issues with ISINS, as there is no clear mapping table with this information (for example based on CFI Code or other references). Due to this lack of harmonisation, trading venues have often different understanding and identification of bond type.

**Question 35: Please provide your comments in relation to the proposals related to the segmentation criteria applicable to commodity derivatives summarised in Table 11. Please list the proposals with their ID for ease of reference. Do you have other proposals related to the segmentation criteria applicable to commodity derivatives and C10 derivatives?**

**[SC\_Commo\_1: Settlement location should be a segmentation criterion for gas (in addition to electricity), and reported with an EIC code.**

Yes, FESE agrees.

**SC\_Commo\_2: Settlement location should not be a segmentation criterion for energy other than gas and electricity (unless a standard is provided by stakeholders).**

Yes, FESE agrees.

**SC\_Commo\_3: Add the duration of the delivery period as a new segmentation criterion for electricity and natural gas contracts:**

We strongly support adding the duration of the delivery period as a new segmentation criterion for the reasons laid down in the consultation paper.

**SC\_Commo\_4: Align wording of the list of energy types with RTS 23 (in particular add renewable energy):**

Yes, FESE agrees.

**SC\_Commo\_5: For energy sub-asset classes, delete the segmentation criterion “load type”:**

Yes, FESE agrees.

**SC\_Commo\_6: For energy sub asset-classes, the segmentation criterion “underlying energy” should not apply to natural gas:**

FESE disagrees that “underlying energy” should not apply to natural gas. It is important that a distinction can be made between for example LNG, hydrogen and natural gas.

**SC\_Commo\_7: For commodity swaps, align the segmentation criterion “settlement type” with RTS 23:**

No comments.

**SC\_Commo\_8: For agricultural sub asset- classes, split the segmentation criterion “underlying agricultural commodity” in two:**

FESE agrees with splitting segmentation criterion 1 in two.

**SC\_Commo 9: For freight derivatives, amend the values listed after segmentation criterion “contract type” and delete the contract type FFA from the reference data table:**

FESE agrees with deleting the contract type FFA as futures and FFAs are used interchangeably.

**SC\_Commo\_10: Define reporting standards for RTS2#12 “specification of the size related to the freight sub- type” and RTS2#13 “specific route or time charter average”:**

FESE agrees that containerships should be considered as a further sub product of dry freight. FESE also agrees with having fix lists for the segmentation criterion 4 (specification of the size related to the freight sub-type) and the segmentation criterion 5 (specific route or time charter average). However, both should include a field called “other” to ensure that when new sizes of ships emerge, as well as new routes, they can be categorised properly. Particularly routes are subject to a lot of change, hence it would certainly benefit from such a category. Furthermore, FESE noted there is only a list of routes or time charters for wet freight. We would recommend to ESMA to also have a list detailing the different routes and time charters for fry freight.

**Question 36: Do you agree with ESMA’s proposal on the new Table of Annex V of RTS 2 (Details of the data to be provided for the purpose of determining a liquid market, the LIS and SSTI thresholds for non-equity financial instruments)? If not, please explain and provide any alternative proposal you might have.**

ESMA proposes to add the total volume and the notation of the total volume to the quantitative data to be provided by trading venues for the transparency calculations. However, ESMA provides no reasoning as to why these numbers would be required for the transparency calculations. FESE considers the already provided quantitative data for the transparency calculations as of high quality and sufficient to conduct the transparency calculations. Against this background, extending the quantitative data for the transparency calculations appears unjustified and of no added value. FESE therefore does not agree with adding the total volume and the notation of the total volume to the quantitative data to be provided by trading venues for the transparency calculations.

**Question 37: Do you agree with ESMA’s proposal to delete the ACTX flag? Please explain.**

We do not agree with ESMA’s proposal to delete the ACTX flag. As per RTS 2, the ACTX flag applies to “transactions where an investment firm has brought together two clients’ orders with the purchase and the sale conducted as one transaction and involving the same volume and price.” The ACTX flag therefore does not apply to transactions executed on a trading venue. Instead, the ACTX flag reveals, if a transaction was arranged and executed OTC. As the ACTX flag is the only flag for post-trade transparency purposes that allows to identify OTC trading activities, removing this flag would deprive market participants from information of the true level of transactions in these markets. Since OTC markets are already opaque markets, further reducing their levels of post-trade transparency does not

appear appropriate and contrary to the goal of RTS 2 to increase the overall transparency in non-equity markets. Hence, we would welcome ESMA to reconsider its proposal and to not remove the ACTX flag from the list of flags for the purpose of post-trade transparency.

**Question 38: Do you agree with ESMA’s proposal to merge the current non-equity deferral flags into one general flag?**

ESMA proposes to merge the currently existing non-equity deferrals flags, i.e. the LIS deferral (‘LRGS’), the illiquid deferral (‘ILQD’) and the SSTI deferral (‘SIZE’), into one general deferral flag (‘DEFR’), as ESMA has observed that these flags are often used inconsistently and are also applied to flag transactions benefitting from a waiver.

We do not agree with ESMA that these inconsistencies should be addressed via a new general deferral flag. A removal of the currently existing non-equity deferral flags will deprive market participants from valuable post-trade information. As these flags indicate, which deferral applies to a respective non-equity instrument, market participants can draw conclusions on the applicable LIS-threshold and how this threshold may develop. For example, a LIS-threshold is determined differently for products benefitting from a LIS-deferral compared to an illiquid deferral. Having this information, market participants can form expectations about the future transparency threshold development more easily. Rather than removing these deferrals flags, we therefore suggest enforcing compliance with the current flag regime more strictly in order to improve post-trade transparency data while maintaining the benefits of the status quo.

**Question 39: Do you agree with ESMA’s proposal not to change the existing flags regarding non-price forming transactions in non-equity financial instruments? If not, please explain.**

FESE believes that, for the sake of overall coherence, as a “PORT” flag is introduced for equities, this should also be applicable to non-equities.

**Question 40: Do stakeholders agree with ESMA’s proposal to introduce a general waiver flag for non-equity transactions benefitting from a waiver? For LIS, should it be limited to completely filled LIS orders?**

ESMA suggests introducing a new flag ‘WAIV’ to mark non-equity transactions benefitting from LIS, SSTI or illiquid waivers to avoid cases where the ‘LRGS’ or ‘ILQD’ deferral flags are used to indicate that a transaction benefitted from a waiver.

We do not deem such a new flag as necessary. First of all, in line with our response to Q38, we hold the view that rather than introducing new flags, ESMA should focus on enforcing compliance with the currently existing flags. Second, a flag to mark non-equity transactions benefitting from LIS, SSTI or illiquid waivers does not provide any added value to market participants. Exchanges employ the LIS and the illiquid waiver to waive the pre-trade transparency requirements for their off-book trading models. When concluding transactions off-book, market participants are therefore already aware of the fact that these transactions must benefit from a waiver, otherwise an off-book transaction would not be possible. Attaching an additional ‘WAIV’ flag to off-book transactions would thus only be redundant information. Against this background, FESE does not agree with ESMA about introducing a general waiver flag for non-equity transactions benefitting from a waiver.

**Question 41: Do you agree with ESMA’s proposal to introduce a flag for pre-arranged non-equity transactions?**

ESMA proposes to introduce a flag for pre-arranged transactions formalised on trading venues to allow NCAs and market participants to identify these transactions. In the consultation paper, ESMA acknowledges that MiFIR does not provide specific provisions for pre-arranged transactions for non-equity instruments. It is therefore referred to the response to Q11 on negotiated trades in the ESMA Q&A on transparency issues, where it is clarified that for non-equity instruments that are not subject to the trading obligation for derivatives, pre-arranged transactions are only possible under the LIS-waiver, the illiquid waiver, the package order waiver or the EFP waiver.

As mentioned in our response to Q40, exchanges employ these waivers to enable their off-book trading models. Off-book trading models generally allow market participants to execute pre-arranged transaction within the environment of an exchange. Off-book transactions are therefore the equivalent of pre-arranged transactions formalised on trading venues.

The market data feeds of exchanges already allow market participants and NCAs to identify off-book transactions, i.e. pre-arranged transactions formalised on trading venues. These feeds provide valuable, often real-time information on transactions concluded at an exchange, including whether a transaction was formalised in the order-book or via off-book models. Exchanges even provide publicly accessible guidelines to help extract such information from the market data feed.

Hence, we do not agree with ESMA’s proposal to introduce a flag for pre-arranged non-equity transactions as market participants and NCAs can already identify such pre-arranged transactions formalised on trading venues, even in real-time.

**Implementation and timing issues (RTS1 & RTS2)**

**Question 42: Do you agree with the proposal on the delayed implementation of certain provisions of the amended RTS 1 & 2? Do you have proposals to minimise the delay?**

We assume the final RTS 1 and RTS 2 provisions will be available by late Q1 2022. ESMA recommendations are potentially very disruptive and will trigger substantial IT engineering efforts. The industry can only start the impact analysis, specifications updates, and engineering work once the final provisions get published. The system complexity of exchanges requires that any technical or operational changes are planned months beforehand. For this reason, exchanges have technical release cycles in place to plan, test and implement technical changes appropriately and securely, also in alignment with market participants, who often are required to also update their systems following technical changes of exchanges. Typically, exchanges have two release cycles per year within which technical changes are being rolled out. However, in order for a technical change to be included in a release cycle, these changes need to be scripted, designed and internally aligned, before they can enter the roll-out phase via release cycles. It is critical that exchanges have sufficient time to follow these steps. Otherwise, the system stability can be at risk in the worst case. The suggested entry into force date by 2023 looks therefore over-ambitious. We would consider a 12 to 18 months implementation period as the minimum.

We ask that sufficient time is provided to trading venues to update their FIRDS and FITRS submissions. Sufficient time should also be provided for any updates to the trading venue pre- and post-trade transparency publication systems, especially since existing data subscribers will also have to update their systems to consume new fields, field values, and field formats.

Having said this, we believe that for commodity markets there is the need to have in place an interim solution as soon as possible, as the current methodology is ill-fitted and is failing the market. In particular, we would suggest that the new calculations for the liquidity assessment and the pre-trade transparency LIS thresholds (based on the data that commodity exchanges provided to ESMA earlier in 2021) become effective no later than the 1<sup>st</sup> of June 2022.

## Annexes

**Question 43 (CBA): Can you identify any other costs and benefits not covered in the CBA below? Please elaborate.**

FESE believes that the high-level assessment would benefit from including the industry view and adding a quantitative costs element.