To
ESMA

NORDIC SECURITIES ASSOCIATION

NSAs response to ESMA's consultation re. MiFIR report on systematic internalisers in non-equity instruments

Memo

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NSA[1] welcomes the opportunity to respond to ESMAs consultation re. MiFIR report re. systematic internalisers in non-equity instruments. However, as the deadline for this consultation falls within the period of the COVID-19 situation, which puts significant restraints on the functioning of all stakeholders, we reserve the right to come back with further comments at a later stage.

1. General comments

As a general comment, NSA members see little value of the pre- trade transparency rules for SI in article 18 MiFIR and would support if the rules were abolished. However, noting that ESMA has not made such proposal, our comments and responses below are based on the assumption that article 18 MiFIR is kept but amended.

The NSA supports a review of article 18 MiFIR which aims at ensuring that the pre-trade transparency requirements for non-equity instruments provide meaningful information to clients whilst limiting the risks that SIs take when executing client orders against own account. A cost/benefit analysis of the rules is very important.

The NSA agrees with ESMAs analysis that the pre-trade transparency rules for SIs in MiFIR are more stringent than those applicable for trading venues and that this creates an unlevel playing field. Moreover, we want to underline that some of the SI obligations could have a very negative impact on the ability of SIs to provide liquidity to the market, in particular if the SSTI thresholds increase above retail size and/or more instruments are classified as liquid. The NSA therefore fully support ESMAs proposals to abolish the obligation to execute transactions with other clients in article 18 (6) and 18 (7). As a consequence, it could also be considered to delete 18(5) and to allow SIs to trade on an anonymous basis.

In the context of a cost/benefit analysis of article 18 MiFIR it is important to consider the characteristics of the type of non-equity instrument in question. In our experience, the application of pre-trade transparency information to bespoke OTC derivatives do

[1] The Nordic Securities Association (NSA) is a Nordic cooperation that works to promote a sound securities market primarily in the Nordic region. The NSA is formed by the Danish Securities Dealers Association (Børsmæglerforeningen), Finance Finland (Finanssiala), the Norwegian Securities Dealers Association (Verdipapirforetakenes Forbund) and the Swedish Securities Dealers Association (Svenska Fondhandlare-föreningen).
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not make sense to clients and create a lot of administrative burdens, costs and compliance risks to investment firms. A simple but efficient solution would in our view be to limit the scope of the transparency rules, SI determination and best execution reporting requirements to "ToTV" instruments.

An additional way of making the pre-trade transparency requirements more meaningful to clients would be to take measures to improve the data quality. Here we think that a higher degree of standardization of the CFI codes would be helpful.

Finally, the NSA is very concerned with the fact that trading venues require SIs to pay for the data which they need to comply with their legal requirements as SIs under MiFID/MiFIR. In practice this has forced SIs e.g. to restrict access to the information on its webpage and to keep track of which information that use the data. We strongly suggest that this matter is addressed by the Commission in the MiFID review.

2. Specific questions

Q 1: Do you consider that there is a need to clarify what a "firm quote" is? If so, in your view, what are the characteristics to be met by such quote?

No, there is no need to introduce a new definition of "firm quote". We are not aware of any problems in this area and fear that a new definition could further complicate the rules.

Q2: (For SI clients) As a SI client, do you have easy access to the quotes published, i.e. can you potentially trade against those quotes when you are not the requestor? Do you happen to trade against SIs quotes when you are not the initial requestor? How often? If it varies across asset classes, please explain.

The NSA does not represent the views of SI clients.

Q 3: What is your overall assessment of the pre-trade transparency provided by SIs in liquid non-equity instruments? Do you have any suggestion to amend the existing pre-trade transparency obligations? If so, please explain which ones and why

As mentioned under General Comments, NSA members generally see little value of the pre- trade transparency rules for SI in article 18 MiFIR and would support if the rules were abolished.

As regards the experience of the rules it is important to look at different asset classes.

The Nordic bond markets are structured a bit differently and for detailed comments we therefore refer to national responses (See separate responses from Finance Denmark and Swedish Securities Dealers Association). However, a common message from all Nordic bond markets to the Commission and ESMA is however that SIs are necessary in order to uphold the liquidity and that any amendments to the transparency regime must ensure that SIs ability to execute client orders against own account is not compromised. In this analysis it is important to consider that the effect which we have seen so far of the pre trade transparency is closely linked to current SSTI levels and liquidity thresholds. If the SSTI levels were to dramatically increase and article 18 is not changed, we see a significant risk that SIs ability to trade against own account will be negatively affected.

As regards the OTC derivatives the input received from members is the same across the Nordic countries. For OTC derivatives, the pre trade transparency requirements do not make sense to clients and the rules create a lot of administrative burdens, costs and compliance risks to investment firms. A simple solution would in our view be to limit the scope of the transparency rules, SI determination and best execution reporting requirements to "ToTV" instruments.

The NSA is very concerned with the fact that trading venues require SIs to pay for the data which they need to comply with their legal requirements as SIs under MiFID/MiFIR. In practice this has forced SIs e.g. to restrict access to the information on its webpage and to keep track of which information that use the data. We strongly suggest that this matter is addressed by the Commission in the MiFID review.

Finally, in order to make the information more valuable to clients, additional work needs to be carried out in order to improve the data quality and ensure the comparability of the information. One measure that could help would be to increase the level of standardization of the CFI codes so that a specific ISIN would be classified as the same asset by all types of venues. Moreover, the "ToTV" concept should be made subject to a review as it is not reasonable that a new ISIN is created each day for some derivatives.

Q 4: (For SI clients) do you have access to quotes in illiquid instruments? If so, how often do you request access to those quotes? What is your assessment of the pre-trade transparency provided by SIs in illiquid instruments?

The NSA does not represent the views of SI clients.

Q 5: (For SIs) Do you disclose quotes in illiquid instruments to clients upon request or do you operate under a pre-trade transparency waiver? In the former case, how often are you requested to disclose quotes (rarely, often, very often)? Does it vary across instruments / asset classes?

The NSA considers that art. 18.2 covers two issues: First the possibility to provide a quote to a client if the SI agrees to provide a quote in an illiquid instrument. Second. The requirement to disclose such quote to other clients if they may ask for such.

SIs also provide quotes in illiquid bonds if requested (In DK it is often) provided that no waiver applies (not available in all Nordic countries)

However, SIs do only rarely, if ever, receive request from clients on access to historical quotes.

Q6: Do you consider that there is an unlevel playing field between SIs and multilateral trading venues active in non-equity instruments, in particular with respect to pre-trade transparency? If so, please explain why and suggest potential remedies

Yes, the NSA considers that the current pre trade transparency rules create an unlevel playing field. Unlike trading venues, SIs trade against their own capital which make them exposed to risk. That makes SIs more vulnerable to pre- trade transparency than trading venues, as SIs have to disclose their identity when making the quotes public.

In particular, NSA members are concerned with the requirement in article 18(6) that SIs shall allow other clients to execute transactions on the same terms. An SI should not be forced by regulation to provide quotes which are not considered acceptable from a commercial or risk perspective. Therefore, we support ESMAs proposals to delete this requirement and in connection hereto, to also delete article 18(7) and 18(5). In case article 18(6) and article 18 (7) are deleted, the present requirements for SIs to publish quotes with name/MIC can also be abolished.

In NSAs experience SIs active on the non-equity market trade bilaterally with clients. The discussion on SI networks relate to the equity market.

Q 7 (for SIs who are also providing liquidity on trading venues): What are the key factors that determine whether quote requesters (your clients) want to receive the quote through the facilities of a trading venue or through your own bilateral trading facilities?
According to NSA the key factor that determine where clients want to receive the quote is where the liquidity is. Many bond markets are illiquid, only a limited number of professional investors are active and trade in very large sizes. For such trading it is difficult to organise order driven trade on a venue. Instead clients' orders are executed bilaterally with an SI. Bilateral trading reduces the risk of market impact when trading in large sizes.

As a result of MiFID II there has been a development of new ways of trading though the facilities of venues. To our understanding the technical developments and the complex regulatory rules are the main factors behind this development.

Q 8: What is your view on the proposal to simplify the requirements in relation to SI quotes in liquid non-equity instruments under Article 18(6) and 18(7)?

The NSA is strongly in favour of the proposals to delete article 18(6) and 18 (7). In addition to simplifying the rules, this measure would also increase the level playing field with venues and avoid that the MiFIR rules have a negative impact on the liquidity of EU bond and derivatives markets. (See also response to Q 6.)

Q 9: Do you consider that the requirements in relation to SI quotes in illiquid non-equity instruments (Article 18(2)) are appropriate? What is your preference between the options presented in paragraph 52 (please justify)?

The NSA agrees that the circular construction between article 18 and 9 MiFIR is not optimal and would support a full harmonisation of the waiver regime for illiquid instruments.

Moreover, the obligation to "disclose information to other clients" in article 18.2 should be abolished. In our experience clients do not ask for this information. We do however not support the proposed "supervisory convergency tool" in option 3. This seems like a very complex rule which can lead to a lot of unnecessary legal uncertainty.

Thus, we support option 1 (status quo).

Q 10: What is your view on the recommendation to specify the arrangements for publishing quotes?

We see no need to specify the publication arrangements.

If such measures are taken we would however like to underline the need to adapt the rules to that they are relevant for non-equity trading. For instance, the rules on "exceptional circumstances" need to take into account that SIs trade on own account and therefore face other risks than trading venues.

The NSA is very concerned with the fact that trading venues require SIs to pay for the data which they need to comply with their legal requirements as SIs under MiFID/MiFIR. In practice this has forced SIs e.g. to restrict access to the information on its webpage and to keep track of which information that use the data. We strongly suggest that this matter is addressed by the Commission in the MiFID review.

Q 11: Do you have any comment on the analysis of Bond data and the relation with the SSTI thresholds as presented above?

The analysis that there is little trade around the SSTI thresholds is in line with our expectations.

Q 12: Do you have any comment on the analysis of derivatives data and the relation with the SSTI threshold as presented above?

The analysis that there is little trade around the SSTI thresholds is in line with our expectations.

Q 13: What is your view on the influence of the SSTI thresholds on the pre-trade transparency framework for SI active in non-equity instruments? Are there any changes to the legal framework that you would consider necessary in this respect?

As mentioned above, the SSTI threshold as well as liquidity thresholds are very important in order to determine the risks that pre-trade (and post trade) transparency requirements have on an SIs ability to provide liquidity to the market.

We support the phase-in approach taken by the Commission

As regards possible changes to the framework, the NSA would support the introduction if fixed SSTI thresholds, provided that they are set at an appropriate level which protects SIs from undue risk.

Q 14: What is your view on the best way for ESMA to fulfil the mandate related to whether quoted and traded prices reflect prevailing market conditions and in particular: (1) the source of data for the SI quotes/trades (RTS 27, APA); (2) the source of market data prices; and (3) the methodology to compare the two and formulate an assessment?

Provided that the data quality is improved, the NSA supports that APA data is used. The requirements of RTS 27 are not well suited for SI trading, the scope is not the same as for the transparency rules, the format of the RTS 27 reports vary and the reports are only provided on a quarterly basis.

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