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Additional Information

Level 1 Regulation
Markets in Financial Instruments Directive II (MiFID II) Directive 2014/65/EU- Secondary Markets

Topic
Multilateral and bilateral systems

Subject Matter
Transparent and non-discriminatory rules

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

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

ESMA Answer

07-07-2017

Original language

[ESMA 70-872942901-38 MiFID II MiFIR market structures Q&A, Q&A 5.3]

One of the benefits of more on-venue, pre-trade transparent trading is to broaden access to liquidity for market participants. In order for these benefits to be fully realised, it is important that trading venues do not have restrictive criteria governing their access, which place unreasonable restraints on certain market participants' access to particular liquidity pools.

In particular, ESMA does not consider the following arrangements to be in compliance with Articles 18(3) and 53(1) of MiFID II. This is not, however, an exhaustive list of arrangements which are non-objective and discriminatory.

1. Trading venues should not require members or participants to be direct clearing members of a CCP.

Given the protections afforded to non-clearing members under MiFIR and EMIR, as well as the rules on straight through processing (STP), a trading venue should not require all its members or participants to be direct clearing members of a CCP. Trading venues may however require members or participants to enter into, and maintain, an agreement with a clearing member as a condition for access when trading is centrally cleared.

2. For financial instruments that are centrally cleared, trading venues should not allow members or participants to require other members or participants to be enabled before they are allowed to trade with each other.

There are legitimate checks that a trading venue might carry out before allowing a member or participant on to their venue. For example, in markets for non-centrally cleared financial instruments trading venues may wish to carry out credit checks, or ensure that a member or participant has appropriate capital to support the positions it intends to take on the trading venue. In a non-centrally cleared derivatives market, there may be a need for bilateral master netting agreements to be in place between participants before the trading venue can allow their trading interests to interact. Trading venues will also need to be comfortable that potential participants are meeting the regulatory requirements to be a member of a trading venue such as having appropriate systems and controls to ensure fair and orderly trading.

However, in centrally cleared markets, enablement mechanisms whereby existing members or participants of a trading venue can decide whether their trading interests may interact with a new participant's trading interest are considered discriminatory and an attempt to limit competition. Enablement mechanisms also reduce the transparency around the liquidity available on different trading venues.

3. Trading venues should not require minimum trading activity.

Trading venues should not require minimum trading activity to become a member or participant of a trading venue, as this could restrict the access to the trading venue to large members or participants.

4. Trading venues should not impose restrictions on the number of participants that a participant can interact with.

In a request for quote (RFQ) protocol, a trading venue should not impose limits on the number of participants that a firm can request a quote from. Whilst a firm requesting a quote may, in compliance with Article 28 of MiFID II, want to limit the number of participants it requests quotes from in order to minimise the risk of unduly exposing its trading interest, which could result in it obtaining a worse price, this should not be mandated by the trading venue. For instance, where a smaller firm is requesting a quote to execute a low volume trade, it might be less concerned about the risks of exposing its trading interest, and so happier to request quotes from a larger number of market makers or liquidity providers.

Limiting the number of participants a firm can request quotes from risks restricting the ability of market participants to access liquidity pools, and only sending requests to traditionally larger dealers who they assume might have larger inventories. This simultaneously restricts the ability of the requestor to access the best pool of liquidity and reduces the likelihood of a smaller dealer receiving requests, despite it having a strong trading interest.