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| 10 November 2016 |

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| Reply form for the Consultation Paper on draft RTS on package orders for which there is a liquid market |
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| Date: 10 November 2016 |

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the ESMA Discussion Paper on the trading obligation for derivatives under MiFIR, published on the ESMA website.

*Instructions*

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

* use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
* do not remove the tags of type <ESMA\_ QUESTION\_MIFID\_PO\_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
* if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

* if they respond to the question stated;
* contain a clear rationale, including on any related costs and benefits; and
* describe any alternatives that ESMA should consider.

**Naming protocol**

In order to facilitate the handling of stakeholders responses please save your document using the following format:

ESMA\_MiFID\_PO\_NAMEOFCOMPANY\_NAMEOFDOCUMENT.

e.g. if the respondent were ESMA, the name of the reply form would be:

ESMA\_MiFID\_PO\_ESMA\_REPLYFORM or

ESMA\_MiFID\_PO\_ESMA\_ANNEX1

***Deadline***

Responses must reach us by **3 January 2017.**

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input/Consultations’.

***Publication of responses***

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

***Data protection***

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the headings ‘Legal notice’ and ‘Data protection’.

# Introduction

Please make your introductory comments below, if any:

< ESMA\_COMMENT\_MIFID\_PO\_0>

London Stock Exchange Group (**LSEG**) is a financial market infrastructure provider, headquartered in London, with significant operations in Europe, North America and Asia. Its diversified global business focuses on capital formation, intellectual property and risk and balance sheet management. LSEG operates an open access model, offering choice and partnership to customers across all of its businesses.

LSEG operates a broad range of international equity, ETF, bond and derivatives markets, including London Stock Exchange; Borsa Italiana; MTS (Europe's leading fixed income market); and Turquoise (a pan-European equities MTF). Through its platforms, LSEG offers market participants, including retail investors, institutions and SMEs unrivalled access to Europe’s capital markets. The Group also plays a vital economic and social role, enabling companies to access funds for growth and development.

Through FTSE Russell, the Group is a global leader in financial indexing, benchmarking and analytic services with approximately $10 trillion benchmarked to its indexes. LSEG also provides customers with an extensive range of real time and reference data products, including SEDOL, UnaVista, XTF and RNS.

Post trade and risk management services are a significant part of the Group’s business operations. In addition to majority ownership of LCH, a multi-asset global CCP operator, LSEG owns CC&G, the Italian clearing house; and Monte Titoli, a leading European custody and settlement business.

LSEG is a leading developer and operator of high performance technology solutions, including trading, market surveillance and post trade systems for over 40 organisations and exchanges, including the Group’s own markets. Additional services include network connectivity, hosting and quality assurance testing. MillenniumIT, GATElab and Exactpro are among the Group’s technology companies.

###### Executive Summary

LSEG welcomes the opportunity to comment on ESMA’s consultation on the “Draft RTS on package orders for which there is a liquid market”. We understand that the draft RTS reflects ESMA’s preliminary views on this topic and ESMA said that it might significantly amend the draft RTS in view of feedback that it receives. We have considered ESMA’s draft RTS very carefully and hope that LSEG’s comments may assist ESMA in preparing the final RTS for submission in this very complex area for submission to the Commission by the end of February.

We agree with ESMA that the methodology for determining whether a specific package order has a liquid market as a whole should be based on a holistic approach taking into account both quantitative and qualitative criteria. There are some areas where we have certain concerns (explained in more detail in our responses to the questions) which we would like to share with you.

In terms of general clarification, it would appear to us that package orders do not have a liquid market as a whole where all components are financial instruments for which there is no liquid market or where all components are large in scale or where the package order consists of a combination thereof, i.e. where one or more of its components are financial instruments for which there is no liquid market whilst all other components are large in scale. We think that in these circumstances the simultaneous and contingent execution of all components each one of which is either not liquid or large in scale means that, in practice, the package order as a whole would also be illiquid. A clarification to this effect would be welcome and, as we believe, appropriately reflect the legislator’s intention to make waivers from pre-trade transparency requirements available for package orders that meet the above descriptions.

With regards to the **proposed general criteria** we believe that market participants may find it challenging from an operational point of view to determine with the necessary degree of certainty which components/contracts are “available for clearing” and we can see how similar difficulties may arise for purposes of establishing if a component is trading/admitted to trading on a MiFID II trading venue, in particular with regards to OTFs. Engaging in on-going and real-time monitoring is likely to strain the resources of most market participants and it is unclear to what extent consistent results can be achieved across the industry. Against this background and in order to avoid any unintended consequences by excluding those package orders from pre-trade transparency waivers which do not actually have a liquid market as a whole, we believe it would be prudent to act with a degree of caution when developing a methodology for assessing the liquidity of a package order.

In this spirit we have picked up and developed our thinking around the criteria used by ESMA under Article 1(a) of the draft RTS. We think that it is possible to strike the right balance between liquid and illiquid package orders by looking at possible combinations of package components and assessing the potential liquidity of the package order as a whole at the level of the **general criteria** on the basis of their classification as

* OTC derivatives within the meaning of EMIR that are, or are not, subject to the clearing obligation and/or the trading obligation;
* derivatives that are not OTC derivatives under EMIR, i.e. derivatives traded on a regulated market; and
* cash instruments.

In addition we believe it would be helpful if the general criteria were supplemented by certain restrictions relating to

* the number of possible components (we think there should be no more than 3 components generally whilst further restrictions might apply at the level of the asset-class specific criteria);
* the number of possible instrument classifications comprised in a package order (limiting the number to no more than 2 different instrument classifications per package order would appear to us to be appropriate);

and by requiring that all components are denominated in the same notional currency of EUR, USD or GBP. Please refer to our detailed response under question 2 for a description of how we think this can work.

As regards the **specific criteria** in the context of the wider approach summarised above, we consider that an asset-class specific liquidity assessment would only be needed in respect of any components traded on a regulated market (the “exchange leg”). The specific criteria would also assist assessing the actual “standardisation” of a package order as they would ensure that only those package orders are classed as having a liquid market as a whole which are automatically pre-packaged/defined by the regulated market’s trading system to the exclusion of those package orders that are, by nature, bespoke due to being negotiated by the counterparties to the transaction and configured by the trading system upon request. Again, please refer to our more detailed description in relation to package orders including interest rate derivatives, equity derivatives and commodity derivatives as set out in our responses to questions 5, 10 and 16 respectively.

Finally, LSEG has undertaken some internal analysis to get a better understanding of the possible number of combinations across package orders that include basic **option strategies**, taking into account different maturities but a maximum of two components only. On the basis of these statistics it is very difficult to see how any one option strategy can in practice be classed as having a liquid market. We have provided the relevant data for illustration in our response to question 2.

**Contacts:**

* Jonathan Farrimond, LSE Senior Rules and Compliance Officer, [JFarrimond@lseg.com](mailto:JFarrimond@lseg.com);
* Corentine Poilvet-Clediere, LSEG Head of Regulatory Strategy and Post Trade Policy, Europe

[CPoilvetClediere@lseg.com](mailto:CPoilvetClediere@lseg.com);

* Lucia Bordigato, Secondary Markets and Infrastructure Regulation, [Lucia.Bordigato@borsaitaliana.it](mailto:Lucia.Bordigato@borsaitaliana.it);
* Fabrizio Plateroti, Head of Capital Markets and Post-trade Regulation,

[Fabrizio.Plateroti@borsaitaliana.it](mailto:Fabrizio.Plateroti@borsaitaliana.it).

< ESMA\_COMMENT\_MIFID\_PO\_0>

1. Do you agree with ESMA’s proposal to apply the SI obligations at the package order level where the investment firm is an SI in at least one component instrument of the package order? If not, please explain why and propose an alternative.

<ESMA\_QUESTION\_MIFID\_PO\_1>

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<ESMA\_QUESTION\_MIFID\_PO\_1>

1. Do you agree with the proposed methodology based on qualitative criteria? Do you consider an alternative methodology as better suited for identifying liquid package orders as a whole?

<ESMA\_QUESTION\_MIFID\_PO\_2>

We agree with ESMA that the methodology for determining whether a specific package order has a liquid market as a whole should be based on a holistic approach taking into account both quantitative and qualitative criteria. We also agree with the split between “general” and “specific” criteria. However on the basis of the general and asset-class specific criteria as currently proposed, we would like to share the following concerns and suggestions regarding the current proposal:

1. We fear that there might be a risk that certain package orders would be deemed to have a liquid market and therefore subject to the pre-trade transparency regime, whilst they were not actually intended to be captured. Indeed, we believe that in circumstances where all components of the package are illiquid or all components are large in scale (LIS), then the package as a whole should be considered illiquid. Similarly, where the package order consists of a combination of the above, i.e. where one or more of its components are financial instruments for which there is no liquid market whilst all other components are large in scale, then again the package as a whole should be treated as not having a liquid market. We would recommend that ESMA include in the proposed RTS a clarification that in the cases above, the package order as a whole would be considered illiquid. This would provide consistency and would be in line with a purposive interpretation of Article 9(e)(i) and (ii) of the “Quick Fix Regulation” (as this has been defined in ESMA’s consultation paper).
2. So far as the “general criteria” are concerned we fully agree with ESMA that the assessment of whether a package order is potentially eligible to be classed as having a liquid market should conceptually be linked to “on venue trading”, “standardisation” and “clearability”. On the other hand it would appear that the application of these criteria is likely to be challenging for market participants in practice. We believe that there are operational issues associated with monitoring whether the individual components of a package order are traded on certain trading venues and cleared/eligible for clearing as, strictly speaking, such monitoring would have to occur on an ongoing basis and in real time. We can also see how the assessment could be particularly difficult where the component is traded on a regulated market but the regulated market itself is not connected to the particular CCP(s) on which the component is eligible for clearing.

Against this background we gave careful consideration as to which general criteria could be used that are similar but likely to raise less complexities in this regard. We consider that the well-established distinction between those derivatives that are traded on a regulated market and those traded OTC might be a helpful base for the criteria and we set out our thoughts in further detail below.

***General criteria***

We have tried to define an approach that would allow ESMA to “assess whether packages are standardised and frequently traded” as required by MiFID Article 9(6)(c). To do so, we have used and built on ESMA’s proposal set out in Article 1(a) of the draft RTS which applies the clearing obligation and the trading obligation in combination. This principle underpins the below matrix in so far as it suggests that a package order to be considered liquid as a whole, the *individual legs* must first have a proven degree of standardisation and liquidity. A package order consisting of a number of individual legs would generally be more specialised and bespoke by virtue of being traded simultaneously and contingently (either as a basis trade or as a hedge trade), meaning that the package order as a whole is probably unlikely to be liquid without proven standardisation and liquidity first in the individual legs. Whilst we acknowledge that the individual legs/contracts might well be liquid in the absence of being subject to the clearing obligation, we think that, for reasons of simplicity and legal certainty, there is merit in using the clearing obligation as a means to determine the liquidity potential of the package order as a whole at general criteria level. The main benefit associated with this approach is that it would enable market participants to rely on publicly available information (i.e. the public register for the clearing obligation under EMIR) in assessing the potential liquidity of a package order, and it is likely to be welcome by both the market and regulators for the level of legal certainty it delivers. Based on ESMA’s comments at paragraphs 60-64 of the consultation paper and the overriding criterion set out in Article 1 of the draft RTS, we believe that this is something that ESMA continues to look at as a viable approach.

In this spirit we would propose that a package order may be considered as potentially liquid only when there is a nexus between:

* OTC legs subject to the clearing and/or trading obligation;
* exchange legs that pass certain asset-class specific criteria;
* and liquid sovereign bonds.

We, therefore, think it is possible to distinguish between the following categories:

* OTC derivatives defined under Regulation (EU) No 648/2012 (EMIR) not subject to the clearing obligation / trading obligation;
* OTC derivatives defined under Regulation (EU) No 648/2012 (EMIR) subject to the clearing obligation but not the trading obligation;
* OTC derivatives defined under Regulation (EU) No 648/2012 (EMIR) subject to the trading obligation;
* Derivatives that are not OTC derivatives defined under Regulation (EU) No 648/2012 (EMIR) (i.e. derivatives on regulated markets);
* Cash instruments (such as cash bonds).

As pointed out by ESMA in the consultation paper, because a precondition under EMIR is that derivatives are sufficiently standardised and liquid, the clearing obligation lends itself to be used as one of the parameters at general criteria level. Following on from this, and as also flagged by ESMA itself, because the clearing obligation is a precondition to the trading obligation it makes sense to deploy the trading obligation as a further parameter in the assessment.

With these thoughts in mind and taking the above mentioned broad categories, we think that it is possible to create a two-way matrix showing all the possible combinations across the two types of instruments listed above:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Derivatives on a regulated market** | **OTC derivatives not subject to CO/TO** | **OTC derivatives subject to CO** | **OTC derivatives subject to TO** | **Cash instruments** |
| **Derivatives on a regulated market** | Standardised and potentially liquid but further asset class specific liquidity assessment needed **for exchange leg(s).** | Not liquid on the basis the OTC leg is less likely to be liquid. | Not liquid on the basis the OTC leg is standardised but likely to not be liquid enough to be traded on a venue. | Standardised and potentially liquid on the basis the OTC leg is liquid enough to be traded on a venue, but further asset class specific liquidity assessment needed **for exchange leg(s).** | For the most part not liquid, except: (i) where this includes a liquid sovereign bond (per RTS 2); and (ii) **the exchange leg(s)** meet(s) further asset class specific liquidity test. |
| **OTC derivatives not subject to CO/TO** |  | Not liquid on the basis the OTC legs are less likely to be liquid. | Not liquid on the basis the OTC legs are less likely to be liquid. | Not liquid on the basis the OTC legs are less likely to be liquid. | Not liquid on the basis the OTC legs are less likely to be liquid. |
| **OTC derivatives subject to CO** |  |  | Not liquid on the basis the OTC leg is standardised but likely to not be liquid enough to be traded on a venue. | Liquid | Liquid only where this includes a liquid sovereign bond (per RTS 2) |
| **OTC derivatives subject to TO** |  |  |  | Liquid | Liquid only where this includes a liquid sovereign bond (per RTS 2) |
| **Cash instruments** |  |  |  |  | More analysis needed |

We think that the parameters set out in the matrix table could be used as **general criteria** to assess whether a package is considered liquid as a whole. In addition, we would propose that the general criteria are further supplemented in the following way:

* For a package order to be considered liquid as a whole we believe that it should contain **no more than 2 of the 5 instrument classifications** in the matrix table. A package order containing 3 or more types of instrument classifications is likely to be bespoke and customised, and therefore not liquid.
* For a package order to be considered liquid as a whole we consider that it would be reasonable to say that it should contain **no more than 3 legs in total**. The greater the number of legs, the greater the possible combinations across maturities and contracts. It is difficult to see how package orders with 4 or more legs would in practice have a liquid market as a whole.
* Only packages where all the legs are traded in a **single currency** should be deemed liquid and standardised. Although the existing wording in Article 3(1)(b) of the draft RTS is slightly ambiguous we believe that ESMA intended to require all components of the package order to have a single notional currency denominated in either EUR, USD or GBP.
* In terms of **cross-asset class package orders** we consider that these should be largely excluded on the basis that these are more specialised, complex trades and unlikely to be liquid to any large degree, with one exception: sovereign cash bonds vs. certain derivatives (as set out in the matrix above) which can trade frequently. Certain other cross-asset class package orders could be brought into scope at a later stage in the light of further assessment and practical experience of applying the waiver regime.

As explained by ESMA, we agree that the general criteria should be a first step in scoping whether a package order could be deemed standardised or liquid. Failure to pass the general criteria stage means the package should not be considered liquid as a whole.

***Specific criteria***

As reflected in the matrix above, for certain package orders that include one or more exchange legs we propose a further **asset-class specific liquidity assessment** **in respect of the exchange leg(s) only**. Although the exchange leg(s) can be considered standardised, by virtue of being listed according to a standard contract specification, we agree with ESMA that the final determination of liquidity depends on various other factors relevant to the specific contract. Our thoughts on this are set out in more detail in our responses to questions 5, 10 and 16.

***Options excluded***

In relation to package orders that include option strategies, LSEG has looked at a range of data to establish if/under what circumstances these could be classed liquid. Following our analysis, we would propose completely to exclude options from the liquidity assessment because there does not seem to be a single strike price that can be considered liquid. By way of illustration, we have provided some statistics on the FTSE MIB options market (all data correct at the time of writing):

* Across various maturities there are **419** puts and **419** calls listed in the on IDEM, LSEG’s Italian derivative markets. That is a total of **838** possible strike prices in just one contract.
* Even taking the simplest 2-legged strategy, a straddle (+1 call +1 put, same expiry and same strike), this would result in **100** different straddles on the December 2016 expiry alone, and **419** straddles overall across all the available expiries.
* Another 2-leg strategy, a strangle, would result in **4,950** strangles on the December 2016 expiry alone, and **9,223** strangles overall across all the available expiries.

These figures demonstrate how large the number of possible combinations across basic options strategies is. The number of possible combinations increases exponentially as the number of legs increases, such as for 3-legged strategies (e.g. butterflies, collars, spreads) and 4-legged strategies (e.g. condors). So whilst “standard strategies” in options do exist, the number of possible permutations across different maturities, puts and calls, means that liquidity is dispersed at multiple points (including for a single maturity). Additionally, the likelihood of an option being traded at its strike price heavily depends on the movement in its underlying; what may have once been a liquid strike price because it was at‑the‑money, may not longer be if the underlying has moved away from that strike. This would suggest to us that **realistically no single options strategy can be considered liquid**. We hope that ESMA will find the data useful and that it will assist ESMA in forming a view on whether or not option strategies should be excluded from the liquidity assessment.

***Impact of a package order being classed as liquid***

We have come across one point of ambiguity which we would like to share with ESMA arising from the particular nature of package orders that include multiple legs traded across **different venues**. Given the example of a package order containing an exchange traded future vs. a related OTC swap, the exchange traded future is listed on a regulated market, but the OTC swap is unlisted and traded “OTC” (although under MiFID II, it could be possible for the swap to be “traded on a trading venue” if typically executed on an OTF, for example).

If this package order was to be considered liquid as a whole, we recognise that the waivers listed under MiFIR Articles 9(e)(i) and 9(e)(ii) would not be available. Therefore, unless the package order could be executed in accordance with the waiver under MiFIR Article 9(e)(iii), then pre-trade transparency must be applied to the package order in accordance with MiFIR Article 8.

In the example stated above where the package order **was not** considered liquid as a whole, the waivers under MiFIR Article 9(e)(i) and 9(e)(ii) **would** be available. However, which venue would be required to apply for the waiver? The regulated market or the OTF? We would suggest that where there is an exchange leg to a package order, **the responsibility should rest with the regulated market.**

<ESMA\_QUESTION\_MIFID\_PO\_2>

1. Do you agree with the general criteria for identifying package orders that may be eligible for being liquid as a whole? Do you consider necessary to add further criteria or to remove any of the criteria proposed? Please explain.

<ESMA\_QUESTION\_MIFID\_PO\_3>

Please refer to our response to question 2.

<ESMA\_QUESTION\_MIFID\_PO\_3>

1. Do you consider it necessary to further specify the first criterion on the standardisation of components? If yes, which characteristics should be considered to specify the standardised components of packages?

<ESMA\_QUESTION\_MIFID\_PO\_4>

Please refer to our response to question 2.

<ESMA\_QUESTION\_MIFID\_PO\_4>

1. Do you agree with the proposed interest rate derivatives specific criteria? If not, please explain why and present your preferred approach. Do you consider it necessary to add further criteria? If yes, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_5>

We agree with all the factors identified by ESMA as being relevant but would like to seek some clarification on certain aspects:

* We think that the language related to maturity “tenors” is more specific to the OTC market and there is a level of uncertainty as to how this applies in an exchange-traded derivative context. We think it would be preferable to apply the asset-class specific liquidity assessment only to exchange-traded derivatives where these are eligible for assessment under the matrix approach (i.e. either where all legs were ETDs, or where the package contained ETD leg(s) vs. an OTC derivative subject to the trading obligation or liquid sovereign cash bond). In that context, we also think the maturities stated are too broad and there might be a risk that package orders are brought within scope where they are likely to be illiquid in practice.
* Assuming that the asset-class specific criteria would only apply to the exchange leg(s) of a package order, we believe that the proposed number of components (up to 3) is too broad and would capture strategies that were not liquid. As set out in our response to question 2, whilst there are “standard strategies” of 3 legs, it does not necessarily mean that these strategies are liquid; the number of combinations across 3 different contracts / maturities is high and a 3-legged strategy would appear to be bespoke in its particular terms.
* As mentioned under the general criteria in question 2, it would be helpful if ESMA could clarify that all the legs of the package order should be denominated in the same currency.

In light of these comments ESMA may want to consider the following changes to the asset-class specific criteria relating to package orders in interest rate derivatives:

* + The asset-class specific criteria for the liquidity assessment should apply to packages containing exchange traded derivatives **only**, where dictated by the general criteria matrix;
  + The **exchange legs** should have **no more than two components**;
  + **All** components of the package order have the **same** notional currency of EUR, USD or GBP;
  + Each of the exchange legs should fall within one of the following maturities:

1. For derivatives based on 3 month rates, contracts with a 6 month maturity or less;
2. For derivatives based on 2 year rates, front month listed contract only;
3. For derivatives based on 5 year rates, front month listed contract only;
4. For derivatives based on 10 year rates, front month listed contract only.

<ESMA\_QUESTION\_MIFID\_PO\_5>

1. Do you consider that derivative components in other currencies (e.g. other EEA currencies, JPY) should be included? If yes, which ones?

<ESMA\_QUESTION\_MIFID\_PO\_6>

No. Extending the currencies risks illiquid package orders being classified as liquid.

<ESMA\_QUESTION\_MIFID\_PO\_6>

1. Do you agree that only packages with derivative components with the above mentioned benchmark dates should be considered liquid? If not, please explain. Which other or additional benchmark dates do you suggest?

<ESMA\_QUESTION\_MIFID\_PO\_7>

We think that the tenors should be limited to key reference rates (6 month maturities for 3 month rates, and front month maturities for 2 year, 5 year and 10 year rates). Please see our answer to question 5.

<ESMA\_QUESTION\_MIFID\_PO\_7>

1. Do you consider that for certain types of packages derivative components that have broken dates (e.g. invoice spreads) or which are traded on IMM and MAC dates (e.g. rolls) have a liquid market?

<ESMA\_QUESTION\_MIFID\_PO\_8>

###### We consider the only maturity assessment should be in relation to the exchange leg and limited to key reference rates (6 month maturities for 3 month rates, and front month maturities for 2 year, 5 year and 10 year rates). Please see our answer to question 5.

The liquidity assessment of the OTC leg should be entirely dependent on the trading obligation and clearing obligation – please see our matrix approach set out under question 2.

<ESMA\_QUESTION\_MIFID\_PO\_8>

1. Do you consider it necessary to specify criteria for non-derivative components of packages? If yes, which criteria would you suggest and why?

<ESMA\_QUESTION\_MIFID\_PO\_9>

Yes, we think it would be useful to specify criteria in this regard. We have included non-derivative components in our matrix and suggest that where a liquid sovereign bond under RTS 2 is traded as a package order against:

* a derivative subject to the trading or clearing obligation, then this should be classed as a package order that is liquid as a whole; or
* an exchange traded derivative, then this should only be classed as liquid **where the exchange leg(s) is/are deemed liquid** in accordance with the asset-class specific criteria set out under question 5.

However further work would be required to assess whether a package order made up exclusively of cash instruments (such as two cash bonds traded simultaneously) would be liquid as a whole, but we would suggest some reference to the individual liquidity assessment of the bonds per RTS 2 could work. We would be happy to look into this in more detail if requested by ESMA.

<ESMA\_QUESTION\_MIFID\_PO\_9>

1. Do you agree with the proposed equity derivatives specific criteria? If not, please explain why and present your preferred approach. Do you consider it necessary to add further criteria? If yes, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_10>

Again, we agree with all the factors identified by ESMA as being relevant but would like to seek some clarification on certain aspects:

* We note that there is no reference to maturities. We think this is an oversight and the maturities should be restricted to the front end of the futures curve. We believe that such statement would be compatible with the fact that the liquidity assessment under RTS 2 has deemed all equity derivatives liquid; this is because the exchange traded legs that make up a package order, when traded as a package, are not liquid all the way along the futures curve.
* Assuming that the asset-class specific criteria would only apply to the exchange legs of a package order, we believe that the proposed number of components (up to 4) is too broad and would capture strategies that were not liquid. As set out in our response to question 2, whilst there are “standard strategies” of 4 legs, it does not necessarily mean that these strategies are liquid; the number of combinations across 4 different contracts / maturities is high and a 4-legged strategy would appear to be bespoke in its particular terms. We consider that package orders with more than 2 components are bespoke and typically negotiated away from the order book because of the number of variables that need to be agreed bilaterally.
* As mentioned under the general criteria in question 2, it would be helpful if ESMA could clarify that all the legs of the package order should be denominated in the same currency.

We consider that changes to the asset-class specific criteria for package orders in equity derivatives along the following lines would be useful:

* + The asset-class specific criteria for the liquidity assessment should apply to packages containing exchange traded derivatives **only**, where dictated by the general criteria matrix;
  + The **exchange legs** should have **no more than two components**;
  + **All** components of the package order have the **same** notional currency of EUR, USD or GBP;
  + Each of the exchange legs must be in contracts with the **same underlying** and have 6 month maturity or less.

<ESMA\_QUESTION\_MIFID\_PO\_10>

1. Do you consider that derivative components in other currencies (e.g. other EEA currencies, JPY) should be included? If yes, which ones?

<ESMA\_QUESTION\_MIFID\_PO\_11>

No. Extending the currencies risks illiquid package orders being classified as liquid.

<ESMA\_QUESTION\_MIFID\_PO\_11>

1. Do you consider it necessary to specify that all components of the package order should have the same underlying? If yes, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_12>

Yes, we consider that this should be the case. We do not think that package orders traded across different **on-exchange** equity derivative products can be considered liquid. As explained under question 10 this would however only be relevant for the exchange legs as the OTC legs are subject to their own liquidity assessment.

We would also like to flag that the restriction for exchange legs to be traded in the same product would not be needed for interest rate derivatives because the liquidity assessment for package orders in interest rate derivatives takes account of the key tenors (effectively the key contracts) and maturities that should be considered liquid. This would not be possible in relation to equity derivatives (because the types of contracts are more diverse), so a proportionate limitation to a single product is needed here.

<ESMA\_QUESTION\_MIFID\_PO\_12>

1. Do you agree with the proposed credit derivatives specific criteria? If not, please explain why and present your preferred approach. Do you consider it necessary to add further criteria? If yes, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_13>

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<ESMA\_QUESTION\_MIFID\_PO\_13>

1. Do you agree that derivative components in USD, EUR or GBP should be considered sufficiently liquid for the purpose of this RTS? Do you consider that derivative components in other currencies (e.g. other EEA currencies, JPY) should be included? If yes, which ones?

<ESMA\_QUESTION\_MIFID\_PO\_14>

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<ESMA\_QUESTION\_MIFID\_PO\_14>

1. Do you consider it necessary to further specify the indices that are eligible? If yes, please specify which specific indices should be included. Do you consider it necessary to specify the maturity dates of the underlying indices?

<ESMA\_QUESTION\_MIFID\_PO\_15>

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<ESMA\_QUESTION\_MIFID\_PO\_15>

1. Do you agree with the proposed commodity derivatives specific criteria? If not, please explain why and present your preferred approach. Do you consider it necessary to add further criteria? If yes, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_16>

We agree with all the factors identified by ESMA as being relevant but would like to seek some clarification on certain aspects:

* The reference to maturities seems to be focusing on “rolls”. Whilst we agree that certain rolls are liquid, in practice they are not liquid all the way along the futures curve; this would suggest that there is a need to limit maturity to the front end of the curve. It might also be the case that a package order does not have a roll component and therefore it would probably be better if the maturity aspect did not specify “rolls” and simply focus on the front end of the futures curve (i.e. liquid end) for the exchange legs only; any OTC leg would be subject to its own inherent liquidity assessment as set out in the matrix at the general criteria level.
* As mentioned under the general criteria in Q2, it would be helpful if ESMA could clarify that all the legs of the package order should be denominated in the same currency.
* For completeness we agree that the package order should have no more than two components provided this is **in relation to the exchange legs**; it should be possible to have up to 3 legs in total (where the package contained other OTC or cash legs for example – see our response to question 2).

Against this background our thoughts are that the asset-class specific criteria for commodity derivatives could be amended along the following lines:

* + The asset-class specific criteria for the liquidity assessment should apply to packages containing exchange traded derivatives **only**, where dictated by the general criteria matrix;
  + The **exchange legs** should have **no more than two components**;
  + **All** components of the package order have the **same** notional currency of EUR, USD or GBP;
  + Each of the exchange legs must be in contracts with the **same underlying** and have 6 month maturity or less.

<ESMA\_QUESTION\_MIFID\_PO\_16>

1. Do you consider that derivative components in other currencies (e.g. other EEA currencies, JPY) should be included? If yes, which ones.

<ESMA\_QUESTION\_MIFID\_PO\_17>

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<ESMA\_QUESTION\_MIFID\_PO\_17>

1. In which types of contracts do package orders in commodity derivatives mostly occur? Do you consider it necessary to provide for asset class specific criteria that take option and future/forward contracts into account? If yes, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_18>

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<ESMA\_QUESTION\_MIFID\_PO\_18>

1. Do you consider it necessary to develop criteria at a more granular level (e.g. energy derivatives, agricultural derivatives) to better reflect the particularities of package orders in the different sub-asset classes? If yes, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_19>

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<ESMA\_QUESTION\_MIFID\_PO\_19>

1. Do you consider it necessary to specify that all components of the package order should have the same underlying? If yes, please explain at which level this concept of “same underlying” should apply (e.g. same asset class, same sub-asset class, same sub-class – as per Annex III of RTS 2 – or at or more granular level).

<ESMA\_QUESTION\_MIFID\_PO\_20>

Yes, we consider that this should be the case. We do not think that package orders traded across different **on-exchange** commodity derivative products can be considered liquid. As explained under question 16 this would however only be relevant for the exchange legs as the OTC legs are subject to their own liquidity assessment.

We would also like to flag that the restriction for exchange legs to be traded in the same product would not be needed for interest rate derivatives because the liquidity assessment for package orders in interest rate derivatives takes account of the key tenors (effectively the key contracts) and maturities that should be considered liquid. This would not be possible in relation to equity derivatives (because the types of contracts are more diverse), so a proportionate limitation to a single product is needed here.

<ESMA\_QUESTION\_MIFID\_PO\_20>

1. Are there package orders in other derivative asset classes that are in your view standardised and frequently traded and which should be eligible for having a liquid market as a whole? If yes, what asset class specific criteria do you suggest for those?

<ESMA\_QUESTION\_MIFID\_PO\_21>

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<ESMA\_QUESTION\_MIFID\_PO\_21>

1. Do you agree with the approach proposed for FX derivatives or do you consider it necessary to include an asset-class specific approach for FX derivatives?

<ESMA\_QUESTION\_MIFID\_PO\_22>

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<ESMA\_QUESTION\_MIFID\_PO\_22>

1. How should ESMA deal with cross-asset class package orders? Should ESMA develop cross-asset class specific criteria? If yes, please specify those. Alternatively, should cross-asset class package orders be allocated to only one asset class? If yes, how?

<ESMA\_QUESTION\_MIFID\_PO\_23>

As ESMA will appreciate, the regime for package order waivers is a complex area which requires careful consideration, and ideally criteria would be developed once market impact analysis data has become available. We think that there is a risk that the development of cross asset-class criteria at this stage could lead to package orders that do not have a liquid market as a whole being classed as liquid. Therefore we consider that ESMA should not at this time develop cross-asset class specific criteria.

Our current thinking is that cross-asset class package orders should largely be excluded on the basis that these are more specialised, complex trades and therefore not liquid to any significant degree, with one exception: liquid sovereign cash bonds vs. certain derivatives (as set out in the matrix under question 2). This approach would be consistent with the regime for EFPs, which have a separate waiver under MiFIR Article 9(d), with no conditions attached. EFPs do in many ways have very similar features to package orders that contain a derivative component vs. a cash (spot) financial instrument. Both types of trades effectively represent a time spread between the spot and the derivative. On the basis that EFP transactions may benefit from a waiver from pre-trade transparency without any conditions, we believe a broadly similar approach should apply to package orders containing derivatives and a cash (spot) financial instrument component (barring the one exception set out in the matrix under question 2).

We would note that certain other cross-asset class package orders could in the course of time be brought into scope and qualified as having a liquid market if practical experience of applying the waiver regime was to demonstrate a need for this, but from the outset a cautious approach is most prudent.

<ESMA\_QUESTION\_MIFID\_PO\_23>

1. Do you agree that package orders where all components are subject to the trading obligation for derivatives should be considered to have a liquid market as a whole? If not, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_24>

Yes, we agree. The matrix approach as described in our response to question 2 (and taking into account a maximum of 3 legs overall) would deliver the same result.

<ESMA\_QUESTION\_MIFID\_PO\_24>

1. Do you consider that package orders where at least one component is subject to the trading obligation and all other components are subject to the clearing obligation should be considered to have a liquid market as a whole? If not, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_25>

Yes, we agree. The matrix approach as described in our response to question 2 (and taking into account a maximum of 3 legs overall) would deliver the same result.

<ESMA\_QUESTION\_MIFID\_PO\_25>

1. Do you agree that the categories of packages above should be considered as standardised and frequently traded for the purpose of this RTS empowerment? If not, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_26>

###### We have applied the matrix/general criteria and the asset-class specific criteria which we have described in our responses to this consultation and illustrate below what this means in terms of liquidity for the specific package type in question:

| Package type | LSEG Comment | Liquidity assessment per LSEG revised approach |
| --- | --- | --- |
| Interest rate derivatives | | |
| Interest rate swap (IRS) curves | All legs are “OTC” per the general criteria matrix under question 2. | Liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| IRS butterflies | All legs are “OTC” per the general criteria matrix under question 2. | Liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Invoice spreads | n/a | Liquid only where: (i) this includes a liquid sovereign bond (per RTS 2); and (ii) the exchange leg(s) meet(s) further asset-class specific liquidity test. |
| CCP basis swaps | All legs are “OTC” per the general criteria matrix under question 2. | Liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Rolls | This could apply to either OTC contracts or contracts listed on an exchange, as defined per the general criteria matrix under question 2. | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, such as IRS, this would be liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Equity derivatives | | |
| Time spread | We are assuming these spreads exclude options | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, such as IRS, this would be liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Straddle | We are assuming these spreads exclude options | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, this would be liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Butterfly | We are assuming these spreads exclude options | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, this would be liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Bear Spread | We are assuming these spreads exclude options | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, this would be liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Bull spread | We are assuming these spreads exclude options | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, this would be liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Credit derivatives | | |
| Commodity derivative rolls | This could apply to either OTC contracts or contracts listed on an exchange, as defined per the general criteria matrix under question 2. | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, this would be liquid, assuming all legs are either subject to the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |
| Calendar spreads | In reality, the calendar spread is a general type of strategy of which “rolls” are a part.Where are assuming this could apply to either OTC contracts or contracts listed on an exchange, as defined per the general criteria matrix under question 2 (although for OTC spreads, they typically wouldn’t be referred to as “calendar spreads”). | Where this applies to exchange traded futures, this would be liquid only where the exchange leg(s) meet(s) further asset-class specific liquidity test.Where this applies to OTC instruments, this would be liquid, assuming all legs are either subject the trading obligation or clearing obligation; however where one of the legs does not meet this criteria, the package is illiquid as a whole. |

<ESMA\_QUESTION\_MIFID\_PO\_26>

1. Are there any categories of packages missing in the above asset classes that should be considered for the purpose of this RTS empowerment? Are there in your view categories of packages in other asset classes that ESMA should consider?

<ESMA\_QUESTION\_MIFID\_PO\_27>

No, we do not think so. We believe that our approach put forward under question 2, together with the asset-class specific criteria described under questions 5, 10 and 16, is fully scalable and applicable to any package order.

<ESMA\_QUESTION\_MIFID\_PO\_27>

1. Do you agree with the draft RTS in annex IV? If not, please explain.

<ESMA\_QUESTION\_MIFID\_PO\_28>

If it would be helpful for ESMA to see the proposed matrix/general criteria and asset-class specific criteria “translated” into RTS text, we would be happy to provide you with a draft. Please do let us know if this would be of interest.

<ESMA\_QUESTION\_MIFID\_PO\_28>

1. CBAQ1: Please identify, per asset class and per currency, the total nominal amount traded (including packages). Please also identify what % of this total trading is executed i) through packages (incl. EFPs) and ii) through packages (with only financial instruments as components), on trading venues and OTC. Reference period: September 2015–September 2016. If you are a trading venue, please fill in the trading venue columns only. If you are an investment firm, please fill in the trading venue and OTC columns as appropriate.

<ESMA\_QUESTION\_MIFID\_PO\_29>

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **Total Nominal amount traded, including packages (in euros)**  Sept 2015-Sept 2016 | | **% of packages (including EFPs)** | | **% of packages (with only financial instruments as components)** | |
| Trading venues | OTC | Trading venues | OTC | Trading venues | OTC |
| **Interest rate derivatives** |  |  |  |  |  |  |
| Euro |  |  |  |  |  |  |
| USD |  |  |  |  |  |  |
| GBP |  |  |  |  |  |  |
| Other currencies (please specify) |  |  |  |  |  |  |
| **Equity derivatives** |  |  |  |  |  |  |
| Euro |  |  |  |  |  |  |
| USD |  |  |  |  |  |  |
| GBP |  |  |  |  |  |  |
| Other currencies (please specify) |  |  |  |  |  |  |
| **Credit derivatives** |  |  |  |  |  |  |
| Euro |  |  |  |  |  |  |
| USD |  |  |  |  |  |  |
| GBP |  |  |  |  |  |  |
| Other currencies (please specify) |  |  |  |  |  |  |
| **Commodity derivatives** |  |  |  |  |  |  |
| Euro |  |  |  |  |  |  |
| USD |  |  |  |  |  |  |
| GBP |  |  |  |  |  |  |
| Other currencies (please specify) |  |  |  |  |  |  |

<ESMA\_QUESTION\_MIFID\_PO\_29>

1. CBAQ2: Based on ESMA draft RTS, out of the package orders (comprised only of financial instruments) that you trade, which percentage of the volume traded do you expect to be considered as having a liquid market as a whole? Please confirm which category the package orders you trade fall under:

1= less than 10% of the volume of package orders traded;

2= from 10% to 25% of the volume of package orders traded;

3= from 25% to 50% of the volume of package orders traded;

4= from 50% to 75% of the volume of package orders traded; or,

5= more than 75% of the of the volume of package orders traded.

<ESMA\_QUESTION\_MIFID\_PO\_30>

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<ESMA\_QUESTION\_MIFID\_PO\_30>

1. CBAQ3: In which area do you anticipate the costs of complying with ESMA’ draft RTS to stem from (e.g. IT, training)?

<ESMA\_QUESTION\_MIFID\_PO\_31>

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<ESMA\_QUESTION\_MIFID\_PO\_31>

1. CBAQ4: Could you provide an indication of the expected implementation costs of ESMA’ draft RTS (in euros) differentiating between (i) one-off costs and (ii) recurring costs (on an annual basis)?

<ESMA\_QUESTION\_MIFID\_PO\_32>

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<ESMA\_QUESTION\_MIFID\_PO\_32>

1. CBAQ5: In relation to the size of your business, do you expect those costs to be:

very low;

low;

medium; or,

high.

<ESMA\_QUESTION\_MIFID\_PO\_33>

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<ESMA\_QUESTION\_MIFID\_PO\_33>

1. CBAQ6: Do you expect any impact from ESMA’s draft RTS on your business model/activity? If so, please explain the drivers and the expected changes to your business model/activity.

<ESMA\_QUESTION\_MIFID\_PO

<ESMA\_QUESTION\_MIFID\_PO\_34>

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<ESMA\_QUESTION\_MIFID\_PO\_34>

1. CBAQ7: Do you expect you expect broader market changes from the draft RTS in the short or medium term TO?

<ESMA\_QUESTION\_MIFID\_PO\_35>

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<ESMA\_QUESTION\_MIFID\_PO\_35>

1. CBAQ8: If so, please explain

<ESMA\_QUESTION\_MIFID\_PO\_36>

|  |  |  |  |
| --- | --- | --- | --- |
| **Expected Impact on** | **Yes/No/NA** | **Positive Impact** | **Negative impact** |
| **Market structure (changes in trading models, in trading strategies…)** |  |  |  |
| **Liquidity**  **(please explain how you measure liquidity)** |  |  |  |
| **End users** |  |  |  |
| **Other (specify)** |  |  |  |

<ESMA\_QUESTION\_MIFID\_PO\_36>

1. CBAQ9: Are their specific concerns regarding ESMA’s draft RTS you would wish to highlight? Please be as specific as possible in your answer.

<ESMA\_QUESTION\_MIFID\_PO\_37>

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<ESMA\_QUESTION\_MIFID\_PO\_37>

1. CBAQ10; Are there specific benefits arising from ESMA’s draft RTS you would wish to mention?

<ESMA\_QUESTION\_MIFID\_PO\_38>

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<ESMA\_QUESTION\_MIFID\_PO\_38>

**For trading venues only**

1. CBAQ11: Do you offer trading in packages?

<ESMA\_QUESTION\_MIFID\_PO\_39>

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<ESMA\_QUESTION\_MIFID\_PO\_39>

1. CBAQ12: If so, please describe, per asset class, the categories of packages for which pre-trade transparency is currently provided. Please also state whether you consider those packages as liquid and the criteria taken into consideration (e.g. spreads, volume traded, number of transactions, number of market participants). If no sufficient space is available to respond, please provide the information in an annex.

<ESMA\_QUESTION\_MIFID\_PO\_40>

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Package Categories with pre-trade transparency** | **Currency** | **Tenor** | **Reference index** | **Other characteristics (please identify)** | **Liquidity assessment (Y/N) and underlying criteria** |
| **Interest rate derivatives** |  |  |  |  |  |
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| **Equity derivatives** |  |  |  |  |  |
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| **Credit derivatives** |  |  |  |  |  |
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|  |  |  |  |  |  |
| **Commodity derivatives** |  |  |  |  |  |
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| **Others (please specify)** |  |  |  |  |  |
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<ESMA\_QUESTION\_MIFID\_PO\_40>