|  |
| --- |
| 10 November 2016 |

|  |
| --- |
| Reply form for the Consultation Paper on draft RTS on package orders for which there is a liquid market |
|  |

|  |
| --- |
| 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>

Nasdaq is concerned that the proposal presented in the Consultation Paper, will result in a much more restrictive pre-trade transparency regime for Exchange Traded Derivatives (ETDs) package orders than for individual transactions. This is because the approach proposed in the Consultation Paper would result in the vast majority of ETD packages being determined as liquid, meaning the waiver could not be applied to them. From an exchange and ETD point of view, the proposed rules would in effect negate the waiver for package orders in Level 1.

In this respect, Nasdaq has 2 principle issues that we want to raise:

1. The need to safeguard that if all components of a liquid package are above their respective pre-trade LIS thresholds, pre-trade transparency shall be implicitly waived for the package.
2. Equity derivatives packages should be considered as illiquid as in the lit strategy orderbooks they trade infrequently when compared to the turnover traded on the individual component.

It is therefore imperative to properly address the issues described above, as neglecting them would:

* harm the ability of dealers in providing liquidity in a cost effective way and would ultimately result in increased total cost of trading for the end investors.
* Result in an inappropriate transparency regime for package orders that could lead to volumes moving from on-exchange to OTC
* A move to OTC trading would greatly reduce the liquidity in the trading venues, increase liquidity fragmentation and negatively impact the overall level of transparency compared to current situation

Failing to consider the above two principles could result in no pre-trade transparency waiver for package orders irrespective of their size and/or their real level of liquidity and would have far reaching negative consequences on non-equity markets.

The impact, specifically on equity derivatives block market, could be dramatic given the current levels of well calibrated transparency regimes.

1. **Basic principle for a pre-trade transparency waiver for package orders**

In the obvious case where **all** components are above their individual Pre-trade LIS thresholds, it must be safeguarded that an implicit pre-trade transparency waiver for the whole package exists. Failing to do so would critically damage the ability of liquidity providers to hedge the risk they undertake.

Nasdaq is therefore very concerned about the text in page 11 (19) of the consultation paper:

*Following the publication of the Quick Fix Regulation ESMA received requests from stakeholders to introduce the possibility to waive pre-trade transparency obligations for a package order that is considered liquid as a whole where the package order is “as a whole” large in scale (LIS) compared with normal market size. ESMA understands the wish of stakeholders to benefit from a waiver to such orders.* ***However, after due consideration of the legal mandate, ESMA does not see any room for developing LIS-thresholds for liquid package orders****.*

Many non-equity instruments are deemed as liquid under RTS 2 and based on extensive quantitative analysis and criteria, pre-trade transparency thresholds have been defined in order to safeguard the critical role of liquidity providers when trading sizes.

The results of these analysis (i.e. the thresholds) should implicitly be extended to any ESMA recognized type of liquid package transactions based on such non-equity components. ESMA in that sense does not need to develop any specific LIS-thresholds for liquid packages.

It is hard to conceive a situation where a package order based on components that can avail of the pre-trade LIS waiver when traded individually (e.g. common equity derivatives strategies) could not be granted any pre-trade transparency waiver even when above the min block trade size.

As an example, it would be illogic to allow pre-trade transparency waiver for trading individually a call option or put option on ERIC B when the transaction is above pre-trade LIS, but not allowing any form of waiver for a package built with these same components (should the package be considered liquid) when all components are above the pre-trade LIS thresholds.

It is therefore imperative to preserve this principle, as neglecting them would harm the ability of dealers in providing liquidity in a cost effective way and would ultimately result in increased total cost of trading for the end investor.

Failing to recognise this obvious need, would have dramatic consequences for the block market. Large package orders cannot be traded in the lit orderbooks which means that in the absence of such a LIS waiver, liquidity would move OTC in order to avoid the negative impact of a transparency regime that neglects the basic principles of facilitating liquidity provision.

1. **Exceptional cases for a pre-trade transparency waiver for package orders**

In Nasdaq’s view, the key element in the pre-trade transparency regime specific for packaged transactions introduced by the ‘Quick Fix’ Regulation in the level 1 text, is to ensure that the transparency regime applied to a package order does not harm the liquidity providers (e.g. hedging purposes) in the case where **one or more** component is above the Pre-trade LIS.

This case would therefore be an exception to the general rule described above in (a). (See also FESE non-paper on EFPs/Package Transactions published in Q2 2016):

***[…]***

***at least one of its components is LIS compared with the normal market size, unless there is a liquid market for the package order as a whole;***

*all of its components are executed on a request-for-quote (RFQ) or voice trading system and are above the size specific to the instrument (SSTI).*

It responds to the basic need to continue to protect the ability of dealers to provide liquidity in the case where not all components are above the pre-trade LIS, but only a few are (i.e. **one or more**). That is, it extends the pre-trade waiver also to the specific situation of *mixed sizes* among the components that could arise.

Furthermore, the legislator states that the waiver does not apply if “*there is a liquid market for the package order as a whole”*. Clearly, this (a liquid market) is an exception to an exception and should therefore result in a very narrow application.

Nasdaq is very concerned that, with the proposed approach described in the CP, the *exception to the exception* is applied to all type of equity derivatives strategies and in conjunction with the concerns expressed in (a), effectively eliminates any possible pre-trade transparency waiver for equity derivatives packages, no matter what the size is.

1. **Overview on equity derivatives packages**

When it comes to equity derivatives strategies, there are many standardized type of strategies based on common definition from market participants (e.g. price spreads, calendar spreads, straddles, strangles, butterflies, etc). While the *strategy types* are limited in numbers and well standardized, the *actual strategies* can be a very large number due to the variety of possible combination of different strikes & maturities chosen by the investors to define the specific package they need to trade.

Usually the vast majority of the strategy orderbooks listed by the venues trade very infrequently due to the very diversified and investor specific package that needs to be traded (i.e. a specific combination of different strike/maturity and strategy types).

To put things into perspective: typically across EU trading venues, a large percentage (40-50%) of on-exchange index and equity option volumes are trades negotiated off-screen; that is, with pre-trade transparency waived and are reported to the exchange (i.e. block trades).

*(See as a benchmark Eurex Equity Derivatives statistics* [*http://www.eurexchange.com/blob/2833166/ee48495ea638f0ef225e96e7f7810d65/data/monthlystat\_201611.pdf*](http://www.eurexchange.com/blob/2833166/ee48495ea638f0ef225e96e7f7810d65/data/monthlystat_201611.pdf) *where OTC volumes has the meaning of on-exchange trades conducted off-screen (i.e. non traded electronically))*

A large part of these off-screen trades are common option strategies.

This because quite often it is institutional clients trading in large sizes and also due to the intrinsic complexity of executing a trade in a multi-leg option strategies.

For properly assessing if a package is liquid or not, it is therefore key to consider whether the strategies trade on a frequent basis **in electronic orderbooks** (i.e. with pre-trade transparency).

In the answer to question Q2 of this consultation paper Nasdaq provides clear indication and statistics supporting the conclusion that the standard types of equity derivatives strategies cannot be considered as having a liquid market for the purpose of Article 9 (1)(e)(ii).

Nasdaq would also like to draw the attention to a specific type of package transaction: **volatility trades**.

A “volatility trade” in equity derivatives markets is a type of package transaction that includes one or several interlinked transactions in listed options contracts contingent on the simultaneous execution of the equity instrument or futures contract underlying the options transaction(s). The cash equity or futures component executed as part of the package transaction hedges the net equity exposure, the delta, from the options why this transaction is also referred to as a “delta-hedged options trade”. Given its structure, a volatility trade can be used to gain or hedge exposures to the volatility of the underlying instrument.

In short, a volatility trade order is characterised by the following criteria:

         One or several options components which are large in size compared to normal market size

         One delta hedge component in the equity instrument or futures contract underlying the options transactions which is half the size of the options component or less

         In case of an underlying equity instrument, the hedge component is listed and traded on a different trading venue and under a different rulebook than the options component(s)

The transaction is crucial for derivatives markets as it lets liquidity providers transfer and manage risk efficiently by buying and selling the expected future volatility of an underlying instrument.

Due to its specific nature with the contingent and cross-product component transactions, volatility trades are arranged outside of central limit order books and facilitated by specialised brokers. In order for this package transaction to continue trading without disruption it is important that it can be executed under the pre-trade transparency waiver given to package orders where at least one component is large in scale (MiFIR Art. 9(e)(ii).

Simplified, volatility trades are typically initiated by one party as an indication of interest to a broker asking for a market in either one single options strike or a multi-strike strategy, both cases with a delta. The broker determines a reference price in the underlying instrument and then source two-way options prices from counterparties given that reference. If the initiating party is willing to execute on the best price provided, the two parties will then have to agree also on the delta, the quantity of the hedge component, before the whole package transaction can be concluded. In other cases the volatility trade is initiated by one party as a firm order with all attributes fixed including the delta and reference price.

**Example 1: Single stock options with cash equity hedge**

         Party A contacts a broker asking for a two-way market for 2,000 Jun-17 38.00 calls on the stock XYZ.

         The broker confirms with A that the trade shall be delta-hedged, sets the reference price for XYZ at 34.80 and starts sourcing prices from liquidity providers

         Following a round of price discovery the broker has a market of 0.40-0.65 where the best offer is provided by party B.

         Party A is willing to buy at 0.65 and the broker then asks party B what his delta is. Party B quotes a 27 delta which A agrees to and the package transaction is finally concluded.

         The options contract size is as in most cases 100 why a delta of 27% translates into 54,000 shares. The package transaction will consist of the following components:

o   Party A buys 2,000 XYZ Jun-17 38.00 calls at 0.65 from B (SEK 7,600,000 notional value)

o   Party A sells B 54,000 XYZ shares at 34.80 (SEK 1,879,200 notional value)

**Example 2: Index options straddle with futures hedge**

         Party X contacts a broker with an order to sell 1,250 Dec-16 1,360 straddles on the ABC index at a net price of 226.00 and simultaneously sell 175 ABC Dec-16 futures (14 delta) at price 1,285.00.

         The broker starts sourcing bids where party Y agrees to execute the order.

         The package transaction is concluded, the broker determines the individual options prices and the final transaction will consist of the following components:

o   Party X sells Y 1,250 ABC Dec-16 1360 calls at 76.00 (SEK 170Mn notional value)

o   Party X sells Y 1,250 ABC Dec-16 1360 puts at 150.00 (SEK 170Mn notional value)

o   Party X sells Y 175 ABC Dec-16 futures at 1285.00 (SEK 22,5Mn notional value)

< 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>

Nasdaq agrees with the proposed approach.

<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>

It is important that any qualitative criteria used to define a package as liquid is not at the expense of the key priority of protecting the activity of the liquidity providers and should avoid resulting in classifying as liquid, packages that indeed trade infrequently.

Unfortunately, the rules proposed in the CP do not include the ‘frequently traded’ criterion. Therefore, we would recommend that ESMA considers some quantitative criteria, some of which should assess the package order as a whole. Therefore, we propose that a package should be deemed liquid if the following criteria are fulfilled (to be applied cumulatively):

* There are three or more investment firms which hold themselves out as market-makers in relation to the specific package order in question; and
* Transactions which occur as a result of such a package order account for at least 25% of the total transactions in each component of the package (calculated on an annual basis); and
* The average daily number of total transactions in the package as a whole is 10 or more (calculated on an annual basis).

**What standardized equity derivatives strategies do trade frequently?**

While it is quite easy to identify for equity derivatives standardized *type* of strategies, it needs to be recognized that most of these do trade very infrequently.

The possible *strategies* can be a very large number due to the variety of possible combination of different strikes & maturities chosen by the investors to define the package they need to trade.

The vast majority of the strategy electronic orderbooks listed by the venues trade very infrequently due to the very diversified and investor specific package that needs to be traded (i.e. a specific set of strike/maturity vs other specific set of strike/maturity, etc).

For this reason, Nasdaq some years ago decided to stop pre-list standardized option strategy orderbooks (with the sole exception of index futures calendar rolls), to avoid listing hundreds if not thousands of different strategy orderbooks that would trade very infrequently, if anything at all.

Similar to other trading venues in Europe, Nasdaq gives instead, market participants the possibility to create in real-time the specific strategy electronic orderbooks they need to trade (a.k.a. Tailor-made combinations).

The most common scenario is that each of these strategy orderbooks is traded only once during the day and just by the initiating market participant against a market maker responding to a request for quote on the specific strategy.

Below some statistics that could help assessing the frequency of trading strategies in Nasdaq Nordic equity derivatives market for the period: 1 Aug to 31 Oct 2016

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Product** | **Total Volume (SC)** | **Volume,**  **Strategies (SC)** | **Nbr of Total Deals (SC)** | **Nbr of Deals, Strategies (SC)** | **Nbr of Strategy orderbooks** | **Nbr Deals per Strategy orderbook** |
| Equity Options | 5 231 513 | 185 077 | 76 528 | 2 188 | 1 033 | 2,1 |
| Index Futures | 9 289 394 | 1 993 571 | 1 221 469 | 98 210 | 12 | 8 184 |
| Index Options | 1 850 014 | 34 913 | 56 064 | 829 | 1 194 | 0,7 |

The table reports total traded volumes in contracts (column *Total Volume (SC)*) for different product types including also volumes traded as part of packages. The column *Volume Strategies (SC)* reports the total volumes for each product type that was traded only as part of package.

Already by comparing these numbers, it is quite obvious that volumes traded via packages in electronic orderbooks are very limited compared to the total.

The next 2 columns (*Nbr of Total Deals(SC)* and *Nbr of Deals, Strategies (SC)*) are providing a similar comparison but in terms of deals.

The column Nbr of Strategy orderbooks, reports how many electronic orderbooks for packages where available for trading during the observation period.

The ratio of deals on strategy orderbooks and number of total strategy orderbooks is extremely low with the sole exception of index futures where the calendar roll orderbook trades relatively frequently but only limited to expiration weeks.

For these reasons Nasdaq concludes that none of the standard types of equity derivatives strategies are considered as having a liquid market for the purpose of Article 9 (1)(e)(ii).

.

<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>

When it comes to the criteria of identifying standardized package types:

1. all components of the package are standardised. This includes that the components are admitted to trading or traded on a trading venue (a regulated market, an MTF or an OTF) and that there is a high level of standardisation of the contractual terms of the components of packages. This criterion ensures that only sufficiently standardised packages within the scope of MiFID II/MiFIR are eligible for being liquid as a whole.

For equity derivatives this seems a reasonable approach to identify standardized types of packages. Although the key aspect is that individual packages do trade very infrequently and as such should not be considered as liquid.

1. a package order should only be considered liquid as a whole where each derivative financial instrument component of the package can be cleared through a CCP. ESMA believes that linking the liquidity of a package to clearing is helpful since requiring pre-trade transparency for package orders composed of uncleared and cleared derivatives might give rise to technical issues

For exchange traded derivatives, CCP clearing is given and does not add any additional value in assessing standardization of packages or frequency of trading.

The focus in assessing the liquidity of a package should instead be on how frequently the packages are traded with regards to the turnover traded on the underlying components. Please refer to the conclusion and proposal in Q2.

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

.

<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>

For identifying the most standardized strategies a limit to maximum 2 components could be reasonable.

Strategies with different ratios among components should not be considered standardized.

Volatility package trades as described in the introductory comments should not be considered standardized and frequently traded.

Strategies with cross-asset equity instruments (e.g. derivatives vs the underlying shares) should not be considered standardized as the individual components are usually traded on different trading venues (i.e. not possible today to trade electronically such a strategy in a single orderbook).

<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>

.

<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>

For equity derivatives the standard type of strategies have all components based on the same underlying and therefore it seems reasonable to introduce this criteria too but keeping in mind the recommendations in Q10.

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

Nasdaq is of the opinion that there is no need to further specify underlying indices as it would only artificially limit packages that may be liquid.

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT 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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

In Nasdaq view cross-asset classes packages for equity derivatives (e.g. covered calls or futures/forwards vs shares or volatility trades) should not be eligible for being considered as liquid packages.

These type of strategies are typically traded off-screen today due to the fact that the cash-equity leg is usually traded on a different venue than the derivative leg.

For this reason there are today no venues (to our knowledge) that provide electronic strategy order books that combine cash-equity components with derivatives components.

<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>

Nasdaq disagrees with the approach of using the trading obligation as a possible criteria.

The trading obligation on the individual components is not a guarantee that any package based on such component has such a high level of liquidity to overcome the need for a pre-trade transparency waiver.

It would seem inconsistent that an order on an instrument subject to trading obligation can be granted a waiver if above pre-trade LIS but a package built on such instruments, it cannot be granted a pre-trade transparency waiver. In the first case the liquidity provider is safeguarded in executing its hedge while in the second case they are not.

<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>

Nasdaq disagrees with the approach of using the trading obligation and the clearing obligation as possible criteria without further assessing the liquidity of the whole package based on some quantitative criteria. The trading and clearing obligation on the individual components is not a guarantee that any package based on such components has such a high level of liquidity to overcome the need for a pre-trade transparency waiver.

It would seem inconsistent if an order on an instrument subject to the trading and/or clearing obligation can be granted a waiver if above the pre-trade LIS when traded individually, but a package built on such instruments cannot be granted such a pre-trade transparency waiver. In the first case the liquidity provider is safeguarded in executing its hedge while in the second case they are not.

<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>

Nasdaq agrees that the table provides a good list of type of equity derivatives strategies that are standardized but disagrees in considering these as trading frequently as there is no quantitative foundation to it.

The key question should be: is the notional traded on components as part of a standard package so high that it represents a significant portion of the total notional traded for the component (i.e. as outright) to justify negating a pre-trade transparency waiver on a package where one component is above LIS?

It is quite clear from the numbers provided by Nasdaq in Q2 that strategy orderbooks are not traded frequently compared to the individual components. The notional traded via these packages are a minimal part of the overall volumes traded on the individual instruments.

For this reason Nasdaq recommends that the equity derivatives package types listed in Table 2 are not considered as liquid.

<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>

TYPE YOUR TEXT HERE

<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>

Nasdaq disagrees with ESMA proposal in the RTS and wants to raise two critical aspects:

* There is a need to safeguard that if all components of a liquid package are above their respective pre-trade LIS thresholds, pre-trade transparency shall be implicitly waived for the package.
* Equity derivatives packages should be considered as illiquid as in the lit strategy orderbooks they trade infrequently when compared to the turnover traded on the individual component.

Nasdaq believes that the draft RTS would instead result in a much more restrictive pre-trade transparency regime for package orders than for individual transactions based on the current proposal.

Furthermore, the proposed regime for package orders is inconsistent with the regime for individual transactions regarding the methodology used: while the pre-trade transparency regime for individual transactions is based on quantitative methodology, the regime for package orders is based on qualitative criteria.

From an exchange and exchange-traded derivatives (ETDs) point of view, the proposed rules would in effect negate the waiver for package orders in Level 1, as ETDs automatically fulfil the ‘general criteria’, and the majority would also fulfil the ‘asset-specific criteria’, for being considered liquid.

Therefore, we propose that a package should be deemed liquid if the following criteria are fulfilled (to be applied cumulatively):

* There are three or more investment firms which hold themselves out as market-makers in relation to the specific package order in question; and
* Transactions which occur as a result of such a package order account for at least 25% of the total transactions in each component of the package (calculated on an annual basis); and
* The average daily number of total transactions in the package as a whole is 10 or more (calculated on an annual basis).

It is therefore imperative to properly address the issues described above, as neglecting them would:

* harm the ability of dealers in providing liquidity in a cost effective way and would ultimately result in increased total cost of trading for the end investors.
* Result in an inappropriate transparency regime for package orders that could lead to volumes moving from on-exchange to OTC
* A move to OTC trading would greatly reduce the liquidity in the trading venues, increase liquidity fragmentation and negatively impact the overall level of transparency compared to current situation

Failing to consider the above two principles could result in no pre-trade transparency waiver for package orders irrespective of their size and/or their real level of liquidity and would have far reaching negative consequences on non-equity markets.

The impact, specifically on equity derivatives block market, could be dramatic given the current levels of well calibrated transparency regimes.

<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>

With reference to the data already presented in Q2 for the Nasdaq Nordic equity derivatives market for the period: 1 Aug to 31 Oct 2016:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Product** | **Total Volume (SC)** | **Volume,**  **Strategies (SC)** | **Nbr of Total Deals (SC)** | **Nbr of Deals, Strategies (SC)** | **Nbr of Strategy orderbooks** | **Nbr Deals per Strategy orderbook** |
| Equity Options | 5 231 513 | 185 077 | 76 528 | 2 188 | 1 033 | 2,1 |
| Index Futures | 9 289 394 | 1 993 571 | 1 221 469 | 98 210 | 12 | 8 184 |
| Index Options | 1 850 014 | 34 913 | 56 064 | 829 | 1 194 | 0,7 |

It is our assessment that no equity derivative strategy in our market should be considered as having a liquid.

The average number of deals per strategy orderbook is extremely low with the sole exception of index futures where the calendar roll orderbook trades only during expiration weeks.

For these reasons Nasdaq suggest that none of the standard types of equity derivatives strategies are considered as having a liquid market the purpose of Article 9 (1)(e)(ii)TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

As the proposal stands the impact on our current business model and overall activity in the Nordic equity derivatives market could be very large.

This assessment is based on the concern that the current proposal in the CP indicates that standard equity derivatives strategies could be considered as liquid and the concerns expressed in the introductory comments about the risk of not being able to grant a pre-trade LIS waiver for a liquid package.

Typically across most EU venues a large percentage (40-50%) of on-exchange index and equity option volumes are trades negotiated off-screen and reported to the exchange (i.e. block trades).

A large part of off-screen trades are option strategies.

Should, these packages be considered liquid (which Nasdaq firmly disagrees) and with the inability of applying a pre-trade LIS waiver if all components are above their individual pre-trade LIS thresholds, would have a disruptive impact on such block market and could lead to such liquidity to move trade OTC.

<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>

TYPE YOUR TEXT HERE

<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…)** | Yes |  | An inappropriate transparency regime for package orders could lead to volumes moving from on-exchange to OTC |
| **Liquidity**  **(please explain how you measure liquidity)** | Yes |  | A move to OTC trading would greatly reduce the liquidity in the trading venues and the overall level of transparency compared to current situation |
| **End users** | Yes |  | End investors may face significantly higher cost of trading due to the risk the liquidity providers would be exposed in case of an inappropriate transparency regime for package orders |
| **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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_MIFID\_PO\_38>

**For trading venues only**

1. CBAQ11: Do you offer trading in packages?

<ESMA\_QUESTION\_MIFID\_PO\_39>

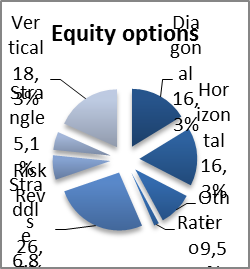
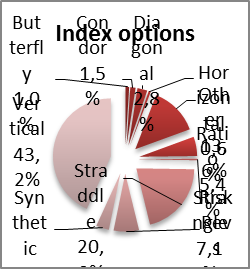
Yes Nasdaq offers trading in packages for its equity derivatives markets.

This is offered in two ways:

1. **Tailor-made combination functionality**

This functionality allows market participants willing to trade a specific package, to submit to the trading system via its API a request for the creation of the corresponding combination orderbook.

The combination orderbook is created in real-time and a notification of the new orderbook is sent to all market participants. From this point, the combination orderbook will accept orders and quotes that will be matched electronically. The initiating participant will typically place an order and the price discovery process will start, which may result in concluding a transaction.



In the above chart a distribution of the type of the option strategy orderbook created by the market participants. Majority of the strategies are 2 –legged.

Nasdaq, as well as many other trading venues, have decided not to list pre-defined combination orderbooks, since in order to meet the broad variety of potential combinations that might be needed by market participants (i.e. by taking in consideration all type of standard strategies, all possible selection of strike price, maturities and underlying), it would have to list thousands of different orderbooks where each of them would trade very infrequently, if anything at all.

1. **Automatic listing of index futures calendar rolls.**

These are the only combination orderbooks that nowadays Nasdaq lists automatically as it trades on a recurrent basis during each expiration week when investors typically move their positions from the expiring contract to the next one.

Both types 1) and 2) are offered by Nasdaq with pre- and post-trade transparency. Market participants are also allowed to report trades on strategies negotiated off-screen of any size.

Below some statistics that could help understanding the frequency of trading strategies in Nasdaq Nordic equity derivatives market for the period: 1 Aug to 31 Oct 2016

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Product** | **Volume (SC)** | **Volume,**  **Strategies (SC)** | **Nbr of Deals (SC)** | **Nbr of Deals, Strategies (SC)** | **Nbr of Strategy orderbooks** | **Nbr Deals per Strategy orderbook** |
| Equity Options | 5 231 513 | 185 077 | 76 528 | 2 188 | 1 033 | 2,1 |
| Index Futures | 9 289 394 | 1 993 571 | 1 221 469 | 98 210 | 12 | 8 184 |
| Index Options | 1 850 014 | 34 913 | 56 064 | 829 | 1 194 | 0,7 |

From these numbers it should be evident that each equity option package although belonging to a standardized type, trades very infrequently.

The average number of deals per strategy orderbook is extremely low with the sole exception of index futures where the calendar roll orderbooks trades during expiration weeks.

<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** |  |  |  |  |  |
|  |  |  |  |  |  |
|  |  |  |  |  |  |
|  |  |  |  |  |  |
|  |  |  |  |  |  |
| **Equity derivatives** |  |  |  |  |  |
| **All standardized and tailor made option strategies on index and equity options** | **SEK, NOK, DKK, EUR** |  | **OMXS30, OMXC20CAP, OMXO20 and all single stock names** | **Same UL for all components and max 4 components** | **Not liquid as each package orderbook trades very infrequently as described in Q2** |
| **Index future calendar roll** | **SEK, NOK, DKK** |  | **OMXS30, OMXC20CAP, OMXO20** | **Same UL for all components and max 2 components** | **Not liquid as these packages trades only in conjunction to the expiration of contracts as described in Q2** |
|  |  |  |  |  |  |
|  |  |  |  |  |  |
| **Credit derivatives** |  |  |  |  |  |
|  |  |  |  |  |  |
|  |  |  |  |  |  |
| **Commodity derivatives** |  |  |  |  |  |
|  |  |  |  |  |  |
|  |  |  |  |  |  |
| **Others (please specify)** |  |  |  |  |  |
|  |  |  |  |  |  |
|  |  |  |  |  |  |

<ESMA\_QUESTION\_MIFID\_PO\_40>