European Securities and Markets Authority

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ECON MiFID II/MiFIR Scrutiny Session – 21 June 2016

Committee on Economic and Monetary Affairs
European Parliament

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Chair
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Dear Members of the European Parliament,

Ladies and gentlemen,

Thank you for again giving me the opportunity to discuss with the Members of ECON the current state of play of MiFID II implementation. This implementation will be essential to ensure that the overall objectives of MIFID II, as envisaged by the co-legislators, are achieved in practice.

ESMA submitted 42 draft technical standards to the Commission under MiFID II and MiFIR in 2015 after having finalised its technical advice back in December 2014. For three of those draft standards, the Commission has notified ESMA of its intention to introduce changes, which means that ESMA expects the large majority of standards to be endorsed in due course by the Commission without amendments.

As far as the recently adopted delegated acts are concerned, I am pleased to note that with respect to investor protection matters, the Commission appears to have followed to a large extent ESMA's technical advice.

ESMA has also issued three Opinions on those standards which the Commission indicated it intends to endorse with amendments, while agreeing with the overall approach ESMA has taken. These concern the much debated issues of non-equity transparency, position limits and ancillary activity. It is not the first time that we have had an exchange of views on these three

standards in this forum and I am sure we are all aware how important it is that all three of them are concluded in a timely and practicable manner while fully respecting the Level 1 text of MIFID II. I want to thank ECON for their letters of 27 November 2015 and 7 April 2016 on these three standards, the contents of which we have taken into account as much as possible when issuing our opinions.

Non-equity transparency

For non-equity transparency, we agree that a cautious approach is warranted and we have always been of the view that a phase-in of mandatory transparency provisions for such a large group of asset classes is desirable. Such a phase-in allows us to see the impact of the new requirements and adjust them when necessary. We have therefore adapted the non-equity transparency standard so that bonds face a stricter liquidity test when MiFID II first applies and all non-equity asset classes benefit from a lower size-specific-to-the instrument threshold at which quotes do not have to be pre-trade transparent. In plain English this means that fewer bonds will be subject to real-time transparency in the beginning and bonds and derivatives will only have to be pre-trade transparent if they are of a significantly lower size than under the original proposal.

However, we have deviated from the suggestions by the Commission when it comes to designing the actual phase-in requirements.

The Commission proposed that the standard should set the less strict criteria for the first stage only. ESMA should then conduct an annual assessment and amend the standard for each move to the next stage of the phase-in.

Contrary to this proposal, ESMA has proposed in its Opinion that all four stages of the phase-in are included in the standard itself from the outset and the move to the next stage is already planned and included. If ESMA detects adverse circumstances, it would halt the move to the next stage by way of an amendment to the standard. We believe our approach gives maximum clarity and legal certainty to all involved. It would also cater for the European Parliament's scrutiny process.

Moreover, in ESMA's view, the Commission's proposal risks not meeting the co-legislators' wish of bringing more transparency to the bond market, or only doing so with long delays. The transparency requirements in the first phase are close to existing practices. Having three consecutive Regulatory Technical Standards endorsement processes would be costly for all

involved and risk endorsement delays. ESMA's proposal would also ensure that voice trading and request for quote systems, which are the only beneficiaries of the lower size-specific-to-the–instrument thresholds, would not profit from a substantial competitive advantage over other trading platforms for a long, and possibly indefinite, period of time. We should avoid such an un-level playing field.

Position limits

Moving on to the position limit standard, I can confirm that we have integrated the Commission's requests, which I believe to a large extent align with those of the European Parliament, into the standard. In essence, a stricter limit of 2.5% can now be imposed for the important area of agricultural derivatives while contracts with limited liquidity can now profit from a higher maximum limit. ESMA has also developed some measures to deal with the issue of potentially diverging deliverable supply and open interest, and ensuring consistency when moving from the non-spot month to the spot month.

To give you a glimpse of the implementation challenges ahead, our current estimate is that limits for around 1,500 liquid contracts will have to be established by national regulators before 2018 with ESMA having to produce an opinion for every single contract in the run-up to MiFID II coming into force.

Ancillary activity

Finally, there is the ancillary activity standard. I am aware that the ESMA opinion does not settle the difficult issue on the table as we are not proposing a concrete capital-based test.

We maintain that a capital-based test has significant drawbacks. The main ones being, first, that typically non-financials do not administer the capital allocated to derivatives trading and a capital test would therefore be costly to implement, especially for smaller non-financials. Secondly, the capital needed for a non-financial's derivatives trading will change very much over time depending on the development of trading positions. Hence, whether a non-financial would meet the capital test and be caught by the MIFD II requirements, could be very unstable over time.

We have nonetheless identified some metrics that could be used by the Commission to construct a capital-based test. We did not consider that we could go any further and propose a particular threshold as, within the timeframe available, we have no data to calibrate such a

threshold. Moreover, I think it is fair to raise the question of whether setting such a threshold is a technical issue or rather a policy choice regarding which non-financials should be under the scope of the Regulation in the first place.

ESMA IT Project

With the delivery of these three Opinions, ESMA's focus is shifting to implementation. This includes the IT project which will centralise the data collection for more than a hundred trading venues and calculate transparency parameters for several million instruments at ESMA under a delegation agreement with 27 national regulators. I am pleased to confirm that ESMA is on track to go live in January 2018. However, let me also be clear that it remains of paramount importance that all implementing measures are adopted without further delay to ensure legal certainty for all parties concerned and timely implementation.

Thank you for your attention and I would be happy to answer any questions you may have.