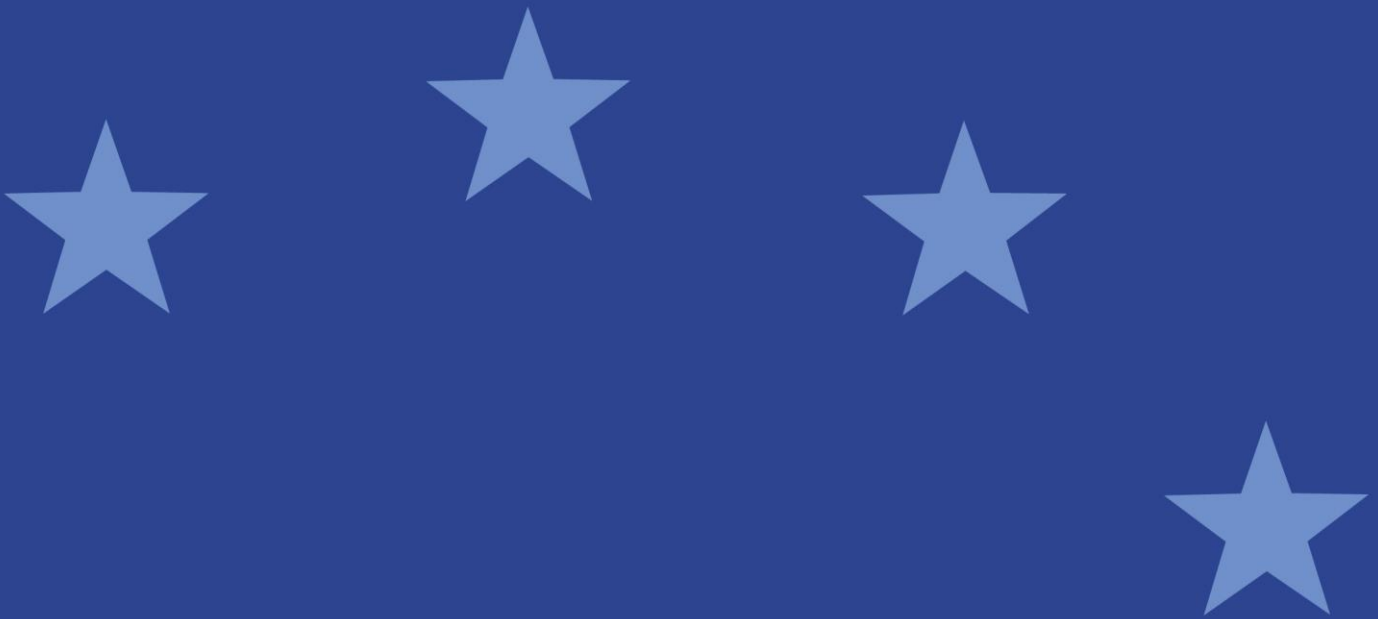




European Securities and  
Markets Authority

# MiFIR report on systematic internalisers in non-equity instruments





European Securities and  
Markets Authority

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## Acronyms and definitions used

APA	Approved Publication Arrangement
CP	Consultation Paper
EC	European Commission
EU	European Union
ESMA	European Securities and Markets Authority
FIRDS	Financial Instruments Reference Data System
FITRS	Financial Instruments Transparency System
MiFID II	Markets in Financial Instruments Directive (recast) - Directive 2014/65 of the European Parliament and of the Council
MiFIR	Markets in Financial Instruments Regulation – Regulation 600/2014 of the European Parliament and of the Council
NCA	National Competent Authority
Q&A	Question and answer
RTS	Regulatory Technical Standard
RTS 1	Commission Delegated Regulation (EU) 2017/587 of 14 July on transparency requirements for trading venues and investment firms in respect of shares, depositary receipts, exchange-traded funds, certificates and other similar financial instruments and on transaction execution obligations in respect of certain shares on a trading venue or by a systematic internaliser
RTS 2	Commission Delegated Regulation (EU) 2017/583 of 14 July on transparency requirements for trading venues and investment firms in respect of bonds, structured finance products, emission allowances and derivatives
RTS 8	Commission Delegated Regulation (EU) 2017/578 of 13 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards specifying the requirements on market making agreements and schemes
RTS 27	Commission Delegated Regulation (EU) 2017/575 of 8 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards concerning the data to be published by execution venues on the quality of execution of transactions
SI	Systematic Internaliser
SSTI	Size Specific to the Instrument
ToTV	Traded on a trading venue

# 1 Executive Summary

## Reasons for publication

Under MiFIR, competent authorities and ESMA shall monitor the application of the pre-trade transparency obligations applicable to systematic internalisers (SIs) in respect of bonds, structured finance products, emission allowances and derivatives (non-equity instruments). This monitoring shall focus on the sizes at which quotes are made available to clients of the investment firm and to other market participants relative to other trading activity of the firm, and the degree to which the quotes reflect prevailing market conditions. Based on this monitoring, ESMA shall submit a report to the European Commission by 3 July 2020. Based on the feedback received during the public consultation which ran from 3 February to 15 April 2020, this document now constitutes the final report being submitted to the European Commission.

## Contents

Section 3 explains the legal framework and presents an overview of European SIs. It also provides an assessment of the effectiveness of the regime for SIs in liquid and illiquid instruments and formulates recommendations to address possible inefficiencies. Section 4 provides the outcome of the monitoring of (1) sizes at which quotes are made available to clients and other market participants; and (2) whether quoted prices reflect prevailing market conditions. Section 5 summarizes the various proposals made in the report. The Annexes include a detailed summary of the feedback to the consultation paper, the legal mandate and further information regarding the data used to perform the monitoring.

## Next Steps

This report is submitted to the European Commission and is expected to be taken into consideration by the European Commission for further legislative proposals. ESMA stands ready to provide any additional technical advice on the legislative amendments suggested in the report.

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## 2 Introduction

1. Systematic Internalisers (SIs) are subject to the obligation to make public firm quotes, subject to certain conditions, both in respect of equity instruments and non-equity instruments. While for equity instruments, the MiFIR provisions are further specified via a Commission Delegated Regulation<sup>1</sup>, there are no equivalent Level 2 measures for non-equity instruments.
2. However, the application of the transparency provisions, which apply to SIs dealing in non-equity instruments, are to be monitored by competent authorities (CAs) and ESMA as specified in Article 19(1) of MiFIR. Based on this monitoring, ESMA is submitting this report to the European Commission in accordance with the agreed timetable<sup>2</sup>.
3. ESMA's preliminary findings and proposals have been published in a [consultation paper](#) (CP)<sup>3</sup> which was open for comments from 3 February to 15 April 2020, and to which 35 responses were submitted. The final proposals included in this document consider the feedback received in the course of this public consultation.

## 3 Pre-trade transparency obligations for SIs in respect of non-equity

### 3.1 Legal framework

4. As part of the MiFIR objective of achieving greater transparency through the introduction of a pre- and post-trade transparency regime for non-equities, Article 18 of MiFIR sets out specific pre-trade transparency requirements for SIs. Those requirements, which differ substantially from the requirements to be met by SIs in respect of equity instruments, strike a delicate balance between the objective of ensuring meaningful pre-trade transparency in non-equity instruments whilst limiting the risks SIs may be faced with when trading against their proprietary capital for the execution of client orders.
5. Under Article 18(1) of MiFIR, investment firms have to make public firm quotes in respect of bonds, structured finance products, emission allowances and derivatives (“non-equity instruments”) traded on a trading venue for which they are SIs and for which there is a liquid market when
  - they are prompted for a quote by the client of the systematic internaliser; and

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<sup>1</sup> Commission Delegated Regulation (EU) 2017/587 of 14 July on transparency requirements for trading venues and investment firms in respect of shares, depositary receipts, exchange-traded funds, certificates and other similar financial instruments and on transaction execution obligations in respect of certain shares on a trading venue or by a systematic internaliser (OJ L 87, 31.3.2017, p. 387.) (“RTS 1”)

<sup>2</sup> The deadline set in the regulation (3 January 2020) has been modified to 3 July 2020 following an agreement between the European Commission and ESMA on the overall planning for the MiFID II/MiFIR review reports (see [letter](#) ESMA70-156-907 dated 16 January 2019)

<sup>3</sup> Consultation Paper on MiFIR report on Systematic Internalisers in non-equity instruments (ESMA70-156-1757)

— they agree to provide a quote.

6. When the non-equity instrument does not have a liquid market, SIs are required to disclose quotes to their clients on request if they agree to provide a quote. This is without prejudice to the possibility for SIs to benefit from a waiver for this obligation where, as set out in the last sentence of Article 18(2) of MiFIR, the conditions in Article 9(1) of MiFIR are met.
7. In order to limit the market risk they may be faced with, SIs may update their quotes at any time. They may also withdraw their quotes under exceptional market conditions. Furthermore, the quoting obligations in relation to non-equity instruments with a liquid market are suspended where the liquidity of a class of instruments falls below a certain threshold and the CA of the trading venue where that class of instruments is traded temporarily suspends pre-trade transparency obligations on that venue in accordance with Article 9(4) of MiFIR.
8. To ensure that the pre-trade transparency provided relates to available liquidity, Article 18(5) of MiFIR sets out that the firm quotes published by SIs in relation to liquid instruments must be made available to the other clients of the concerned SI. However, to limit the risks they may face, including credit, counterparty or settlement risks, SIs may decide, based on their commercial policy and in an objective and non-discriminatory way, the clients to whom they give access to those quotes. Likewise, SIs are required to enter into transactions under the published conditions with the other clients to whom the quote is made available.
9. The requirements for SIs in relation to liquid instruments are illustrated in a diagram available in Question 9 of Section 7 of the ESMA Q&A on MiFID II / MiFIR transparency topics<sup>4</sup> and reproduced below (Diagram 1).

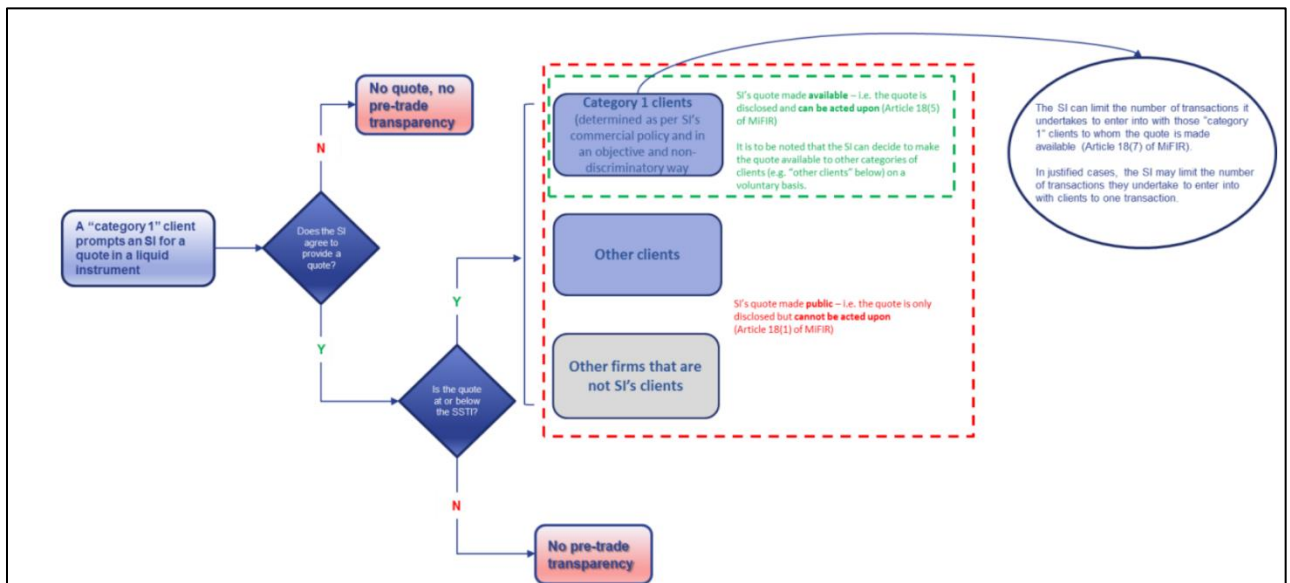


Diagram 1: SIs obligation in relation to liquid non-equity instruments

<sup>4</sup> Questions and Answers on MiFID II and MiFIR transparency topics (ESMA70-872942901-35)

10. In addition, and to put a cap on the amount of capital an SI may have to put at risk for the execution of client orders when publishing a quote, Article 18(7) of MiFIR sets out that SIs may establish non-discriminatory and transparent limits on the number of transactions they undertake to enter into with clients pursuant to any given quote.
11. The quotes published by an SI in relation to liquid instruments must be published in a manner that is accessible to other market participants on a reasonable commercial basis. Articles 6 to 11 of Commission Delegated Regulation (EU) 2017/567<sup>5</sup> further specify the obligations to be met by SIs to comply with the “reasonable commercial basis” requirements. The “reasonable commercial basis” obligations for SIs are the same as the ones applying to market operators and investment firms operating a trading venue.
12. The prices quoted must allow the SI to comply with its best execution obligations, where applicable. They also have to reflect prevailing market conditions, i.e. the prices at which transactions are concluded for the same or similar financial instruments on a trading venue. However, in justified cases, SIs may execute orders at a better price provided that the price falls within a public range close to market conditions
13. SIs have no pre-trade transparency obligations when they deal in sizes above the SSTI.
14. Possibly due to the conflicting objectives of increasing pre-trade transparency whilst limiting the risks that SIs may incur when putting their capital at risk to execute client orders, the Level 1 provisions governing pre-trade transparency obligations for SIs appear somewhat complex and sometimes difficult to understand. In the absence of Level 2 measures and in response to the many interpretation questions received from CAs and market participants, ESMA issued various Q&As aiming at enhancing supervisory convergence in the implementation of those pre-trade obligations.
15. The first set of clarifications provided by ESMA deals with publication arrangements and the information to be disclosed. Article 18(8) of MiFIR requires the SI quotes to be “made public in a manner which is easily accessible to other market participants”. However, in contrast with Article 13 of the Commission Delegated Regulation (EU) No 2017/567 that specifies how SIs should make their quotes public and easily accessible for equity instruments, there are no corresponding provisions on the publication arrangements for non-equity SIs.
16. ESMA therefore clarified that SIs should use the same means and arrangements when publishing firm quotes in non-equity instruments as for equity instruments. This includes requiring SIs to disclose their identity in the quotes when the quotes are made public through the arrangements of a trading venue or an Approved Publication Arrangement (APA). Furthermore, the quotes should be made public in a machine-readable format as specified in Commission Delegated Regulation (EU) No 2017/567 and the quotes should be time-stamped as specified in Article 9(d) of RTS 1.

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<sup>5</sup> Commission Delegated Regulation (EU) 2017/567 of 18 May 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regards to definitions, transparency, portfolio compression and supervisory measures on product intervention and positions (OJ L 87, 31.3.2017, p. 90–116).





17. The other set of clarifications provided relates to the circumstances when a quote published by an SI can be acted upon. ESMA clarified that although an SI may update its quotes at any time, the quote should remain valid for a reasonable time period to allow clients to trade against that quote. Further guidance has been provided on the potential limitation of clients that may have access to, i.e. that can trade against, the SI quote under the SI's commercial policy. ESMA also noted that, whilst SIs may limit the number of transactions they undertake to enter into with clients under Article 18(7) of MiFIR to one transaction, any such limits should be made public and be justified.

## 3.2 Overview of European non-equity SIs

### 3.2.1 European non-equity SIs based on ESMA's register

18. In accordance with Article 18(4) of MiFIR, firms that meet the definition of an SI shall notify their NCAs, and such notification shall be transmitted to ESMA. On that basis, ESMA shall establish a list of all systematic internalisers in the Union. ESMA is fulfilling this obligation via the [ESMA register](#), under the section MiFID/UCITS/AIFMD entities.

19. The list of SIs is available for download in csv format with a set of reference data associated with each SI. Additional information on the types of instruments for which each entity is an SI is also available, at the granularity of the MiFIR identifier<sup>6</sup>.

20. Based on this register, the number of SIs active in non-equity instruments (NEQ) is significantly larger than the number of SIs active in equity instruments (EQU) (see Table 1). One additional observation is that SIs tend to specialise in either equity (EQU) or non-equity (NEQ), with only about 25% of SIs being active in both EQU and NEQ.

	Number of SI (MIC code)
Active in both	60
Active in NEQ only	137
Active in EQU only	25
<b>Grand Total</b>	<b>222</b>

**Table 1: Overview of European SIs in equity and non-equity (source: ESMA register as of 11 June 2020)**

21. Zooming in on the SIs active in NEQ, there were around 200 SIs registered with ESMA, with the vast majority active in bonds (Table 2). In general, SIs tend to be active in a small

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<sup>6</sup> i.e., for non-equity instruments: Securitised derivatives, Structured Finance Products, Bonds, ETCs, ETNs, Emission Allowances and Derivatives

number of different asset classes, with more than half of them active in only one asset class, and more than 80% active in one, two or three asset-classes (Table 3).

	Unique SI (non- equity)	Bonds	Derivatives	Emission Allowances	ETCs	ETNs	Securitised Derivatives	SFPS
AUSTRIA	6	5					1	
BELGIUM	4	3	2				1	
CYPRUS	4	4						1
CZECH REPUBLIC	3	3						
DENMARK	8	8	2					
FINLAND	2	2	1					
FRANCE	15	11	10	1	5	5	6	6
GERMANY	37	31	20	7	15	15	17	17
GREECE	3	3						
HUNGARY	7	7	1					
IRELAND	7	7	2		2	2	2	2
ITALY	11	9	2					
LATVIA	1	1						
LIECHTENSTEIN	3		3					
LUXEMBOURG	2		2					
NETHERLANDS	6	5	4		1		2	1
NORWAY	2	2	1					
POLAND	7	7						
ROMANIA	1	1						
SLOVAKIA	1	1						
SPAIN	5	5	2				1	1
SWEDEN	3	3	3	1	1	1	2	1
UNITED KINGDOM	59	47	42	4	9	8	13	18
<b>Grand Total</b>	<b>197</b>	<b>165</b>	<b>97</b>	<b>13</b>	<b>33</b>	<b>31</b>	<b>45</b>	<b>47</b>

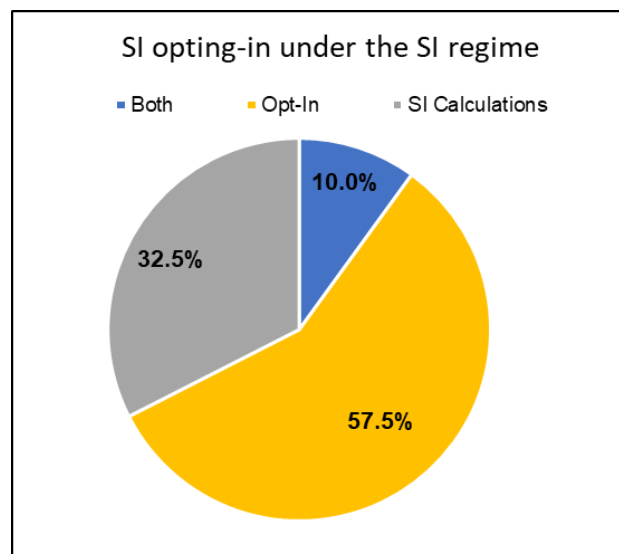
**Table 2: Overview of European SIs in non-equity instruments, per country and asset class (source: ESMA register as of 4 June 2020)**

	Number of SI (MIC Code)	As % of total
Active in 1 asset-class(es)	<b>114</b>	<b>58%</b>
Active in 2 asset-class(es)	<b>29</b>	<b>15%</b>
Active in 3 asset-class(es)	<b>19</b>	<b>10%</b>
Active in 4 asset-class(es)	<b>10</b>	<b>5%</b>
Active in 5 asset-class(es)	<b>1</b>	<b>1%</b>
Active in 6 asset-class(es)	<b>11</b>	<b>6%</b>
Active in 7 asset-class(es)	<b>13</b>	<b>7%</b>
<b>Grand Total</b>	<b>197</b>	<b>100%</b>

**Table 3: European SIs in non-equity instruments, per number of available asset class (source: ESMA register as of 4 June 2020)**

### 3.2.2 SI opting-in under the SI regime

22. An SI is defined as an investment firm (1) which is not a multilateral trading system; and (2) which on an organised, frequent, systematic and substantial basis, deals on own account when executing client orders outside a regulated market, MTF or OTF. Commission Delegated Regulation (EU) No 2017/565<sup>7</sup> further defines the meaning of “organised, frequent, systematic and substantial basis” by specifying the thresholds in terms of e.g. trading frequency and trading sizes, for each type of instruments (bonds, structured finance products, derivatives and emission allowances in Article 13 to 16). Notwithstanding those quantitative thresholds, SIs also have the possibility to voluntarily “opt-in” under the SI regime, as contemplated in Article 4(1)(20) of MiFID II.
23. Many stakeholders have reported that a significant number of investment firms have decided to voluntarily opt-in under the SI regime, rather than becoming SIs as a result of exceeding the above-mentioned thresholds defined in Commission Delegated Regulation (EU) No 2017/565.
24. This assertion is confirmed by a number of SIs having made that information public on their website, as well as a survey performed by ESMA in November 2019 (covering 40 SIs). Two thirds of the investment firms responding to the survey have opted-in under the SI regime either exclusively (57.5%) or in combination with performing the SI calculation for specific asset-classes (10%) (Figure 1).



**Figure 1: SI opting-in under the SI regime (source: SIs survey November 2019)**

25. The reason underlying the decision to opt-in appears to be linked to the post-trade obligations for OTC transactions under Article 7 of RTS 2. In general, where a transaction between two investment firms is concluded OTC, only the seller shall make the transaction

<sup>7</sup> Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive (*OJ L 87, 31.3.2017, p. 1–83*)



public through an APA. However, where one of the parties to the transaction is an SI, this reporting obligation to the APA is to be fulfilled by the SI only. This appears to have prompted numerous investment firms to opt-in under the SI regime as a response to clients requests eager to delegate their APA post-trade reporting to such investment firms.

### 3.3 ESMA’s assessment of pre-trade transparency obligations for SIs

26. Given that the pre-trade transparency requirements in respect of liquid and illiquid instruments are different, the assessment of the regimes are presented in two distinct sections below. The ad-hoc data collection exercise performed by ESMA (“ad-hoc SI data” thereafter) includes a segmentation of quoted and traded volumes depending on the liquidity status of the instrument and provides an estimation of the SI volumes that would be covered by the obligations for liquid and illiquid instruments respectively. Those figures help to form an idea of the relevance of each provision (for liquid and illiquid instruments) depending on the asset class.
27. For bonds, quoting activity is balanced between liquid and illiquid instruments while trading activity mainly takes place on liquid instruments (see Table 4 to Table 7<sup>8</sup>). This tends to indicate that despite the low number of liquid bonds in absolute terms, the volumes that they represent is significant, pointing to a reasonable discrimination between liquid and illiquid bonds as per the RTS 2 determination.
28. In relation to derivatives, most sub-classes of equity derivatives, and all securitised derivatives, are deemed to have a liquid market as per a static determination, while all FX derivatives are deemed not to have a liquid market as per a static determination (Article 13(1)(a) of RTS 2), which explains the dichotomic breakdown between liquid and illiquid instruments in those classes.
29. Finally, for the remaining classes of derivatives with coexistent liquid and illiquid instruments (credit and interest rate derivatives), most of the quoted and traded volume reported in the ad-hoc SI data was on illiquid instruments. This could be explained by (1) the small number of instruments that would classify as liquid at the moment; and/or (2) the activity on liquid instruments being mainly done on multilateral trading venues in application of the derivatives trading obligation.

	Bonds excl. ETC and ETN	ETC/ETN	Credit derivatives	Equity derivatives	FX derivatives	Interest rate derivatives	Securitised derivatives	Structured finance products
LIQUID	48.7%	18.5%	13.1%	95.6%	0.0%	2.9%	100.0%	0.0%
ILLIQUID	51.3%	81.5%	86.9%	4.4%	100.0%	97.1%	0.0%	100.0%
<b>Grand Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

<sup>8</sup> Those figures on quoted volumes do not distinguish between quotes which are published, and quotes which are not.

**Table 4: Quoted volumes based on liquidity - per asset class (source: ESMA based on ad-hoc SI data June 2019)**

	Bonds excl. ETC and ETN	ETC/ETN	Credit derivatives	Equity derivatives	FX derivatives	Interest rate derivatives	Securitised derivatives	Structured finance products
LIQUID	81.7%	0.6%	10.3%	95.0%	0.0%	4.7%	100.0%	0.0%
ILLIQUID	18.3%	99.4%	89.7%	5.0%	100.0%	95.3%	0.0%	100.0%
<b>Grand Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

**Table 5: Traded volumes based on liquidity - per asset class (source: ESMA based on ad-hoc SI data June 2019)**

	Bonds excl. ETC and ETN	ETC/ETN	Credit derivatives	Equity derivatives	FX derivatives	Interest rate derivatives	Securitised derivatives	Structured finance products
LIQUID	25.3%	63.0%	12.2%	94.7%	0.0%	3.4%	100.0%	0.0%
ILLIQUID	74.7%	37.0%	87.8%	5.3%	100.0%	96.6%	0.0%	100.0%
<b>Grand Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

**Table 6: Number of quotes based on liquidity - per asset class (source: ESMA based on ad-hoc SI data June 2019)**

	Bonds excl. ETC and ETN	ETC/ETN	Credit derivatives	Equity derivatives	FX derivatives	Interest rate derivatives	Securitised derivatives	Structured finance products
LIQUID	55.2%	10.5%	16.7%	99.1%	0.0%	22.2%	100.0%	0.0%
ILLIQUID	44.8%	89.5%	83.3%	0.9%	100.0%	77.8%	0.0%	100.0%
<b>Grand Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

**Table 7: Number of trades based on liquidity - per asset class (source: ESMA based on ad-hoc SI data June 2019)**

### 3.3.1 Effectiveness of the regime for liquid instruments

30. Notwithstanding ESMA's Q&As, the pre-trade transparency regime for liquid instruments appears to leave quite some room for discretion to SIs in the way they implement their pre-trade transparency obligations, hence potentially challenging the effectiveness of the requirements set out in MiFIR. ESMA conducted a random check of publicly available non-equity SIs' commercial policies that showed the variety of arrangements put in place and raised the question of a potential need for further harmonisation or simplification.

#### 3.3.1.1 Firm quotes

##### Analysis

31. Whilst the commercial policies checked typically refer to the publication of "firm quotes" as stated in Article 18(1) of MiFIR without further elaboration, one commercial policy provides a definition of a firm quote, stating that "*Firms quotes are executable prices provided by a SI on a given financial instrument that guarantees a bid or ask price up to the amount quoted, without negotiation. Indicative quotes that are not actionable are not firm quotes*



*and therefore are not published or otherwise communicated to clients other than the client for which it is intended”.*

32. This interpretation entails that when an SI is prompted for a quote by a client, and when there are multiple interactions between the client and the SI before the SI comes up with a price that both parties understand to be the final one, only that final price will be made public. It is also worth noting that the SI may not know whether the quote provided is the final one until the client agrees to trade on that quote, which means that pre-trade transparency will be made available almost at the same time as post-trade transparency. ESMA however notes that pre-trade transparency is also made available almost at the same time as post-trade transparency on other trading facilities such as on-venue request for quotes (RFQ) systems.
33. Based on the potential uneven understanding across SIs and market participants of the pre-trade transparency obligation related to the publication of a “firm quote”, ESMA requested feedback in the CP on the need to clarify what a “firm quote” is.

#### Feedback to the CP

34. Most respondents considered that it was unnecessary to further clarify what a firm quote is. According to those respondents, there is a clear understanding among market participants, SIs and clients of what a firm quote is. Concerns were also expressed that introducing a new definition that would not be aligned with market practices would be a source of additional costs and complexity in the SI pre-trade transparency rules. Some respondents understand a firm quote to be an executable quote. A dissenting opinion was expressed by a trading venue that suggested aligning the definition of a “firm quote” with that of an actionable indication of interest under Article 2(33) of MiFIR.

#### Conclusions and proposals

35. ESMA notes that in the feedback received to the CP, no market participants identified any drawback to the pre-trade transparency framework for non-equity SIs due to a lack of clarity as to what a firm quote is. No potential SI client expressed concerns either on the quotes published by non-equity SIs for liquid instruments. ESMA will therefore not take forward the suggestion made in the CP that the definition of a “firm quote” in Article 18(1) of MiFIR may need to be further clarified.
36. The decision reached by ESMA not to go forward with further clarifying what a firm quote is also based on the feedback received from stakeholders to some other questions raised in the CP, including on the purposes served by the quotes published by non-equity SIs, as discussed in section 3.3.1.3.

#### 3.3.1.2 Exceptional market circumstances

##### Analysis

37. ESMA notes that SIs commercial policies also differ in respect of the details provided on the exceptional market conditions under which SIs may withdraw quotes. Some SIs provide



a long list setting out those exceptional market conditions while others do not elaborate on those market conditions.

38. To foster a more convergent application of SIs' pre-trade transparency obligations, ESMA considers that there would be merit in developing a shared understanding of the exceptional market conditions under which SIs may withdraw quotes in Level 2. ESMA considers that such exceptional market conditions should be consistent with the ones set out in Article 3 of Commission Delegated Regulation (EU) 2017/578 (RTS 8) for suspending investment firms' market making obligations on trading venues.
39. Exceptional market circumstances under which an SI may withdraw quotes in liquid instruments would thus include circumstances where the SI's ability to maintain prudent risk management practices is prevented by (i) technological issues, including problems with a data feed or other system that is essential to carry out its SI activity, (ii) risk management issues in relation to regulatory capital, margining and access to clearing, and (iii) the inability to hedge a position due to a short selling ban.
40. Although ESMA unintentionally omitted to include a question related to this proposal in the CP, a few stakeholders commented on this issue.

#### Feedback to the CP

41. One respondent agreed with the proposal. Another one considered that the clarification was not necessary as pre-trade transparency only applies anyhow when the SI agrees to provide a quote. A last respondent stressed that it was important not to copy paste the rules for equities but to ensure that those circumstances are relevant for the different parts of the non-equity market.

#### Conclusions and proposals

42. Considering the limited feedback received, and in line with the overall objective of streamlining a rather complex pre-trade transparency regime for non-equity SIs, ESMA is not taking forward the proposal set out in the CP to amend Level 1 to mandate ESMA to further define the exceptional market conditions under which non-equity SIs can withdraw quotes.
43. Furthermore, considering the proposal made below in section 3.3.1.3 (i.e. SIs are no longer required to give access to quotes to other clients), ESMA sees little value in a provision setting out the conditions under which an SI may withdraw its quotes. Whereas such provision makes sense for equity SIs that are required to quote on a continuous basis or for market makers on trading venues, this provision on conditions for quote withdrawal does not appear to serve a clear purpose for non-equity SIs under the proposed framework.
44. As a result, rather than clarifying the exceptional market circumstances under which SI may withdraw their quotes, ESMA proposes to simply allow SIs to withdraw their quotes at any time, by amending Article 18(3) of MiFIR.

### 3.3.1.3 Access to quotes in liquid instruments

#### Analysis

45. As explained in the description of the legal framework, Article 18(5) to (7) of MiFIR sets out a rather complex framework for providing access to the quotes of an SI to the other SI clients and to allow them to trade on that quote subject to certain conditions.
46. Despite the quote access limitation set out in Article 18(7), the wording of the first paragraph of Article 18(6) tends to suggest that the intention of the co-legislators was that a firm quote published by an SI was to reflect somewhat broadly available liquidity.
47. However, common practice across SIs appears to restrict the commitment to trade on the quote published to one client except where the initial quote would be partially executed with the initial requesting client and the remaining volume with another client.
48. With regards to access to quotes, and beyond the criteria related to credit status, counterparty risk and final settlement set out in Article 18(5) of MiFIR, SIs' commercial policies include various other factors or criteria to deny access to their quotes. Those other factors may, for instance, include the regulatory status of the client (e.g. an SI in the relevant non-equity instrument to which the published quote relates will be denied access to the quote) or the trading type (e.g. whether the counterparties are trading via algorithm). One SI states that it may refuse access to its quotes to clients when "such execution would have a material adverse impact on market prices". Client tiering for access to quotes may include factors such as volume of trades or client profitability for the SI.
49. With regards to the number of transactions that SIs undertake to execute at the published quote, most of the commercial policies reviewed restrict execution to one transaction or to quoted size in case of partial first execution making de facto the liquidity not addressable to any other client. Some commercial policies refer to the SI's discretion to decide whether to agree to execute more than one transaction at the quoted price.
50. As all-in prices are published, commercial policies provide warning on potential price adjustments when the counterparty to the transaction would not be the client that requested the quote. Alternatively, access may be denied for instance for non-cleared derivatives in case a "material" X-Value Adjustment<sup>9</sup> would be required.
51. Taking into consideration the fact that dealers on trading venues do not have to commit to trade multiple times on a displayed quote, there seems to be little ground to require SIs to be subject to more stringent requirements and be required to enter into transactions with multiple clients under each quote published. It was therefore suggested in the CP to simplify the SI pre-trade transparency obligations for liquid instruments by deleting:

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<sup>9</sup> XVA, or X-Value Adjustment, is a collective term that covers the different types of valuation adjustments relating to derivative contracts.



- the first paragraph of Article 18(6) i.e. “Systematic internalisers shall undertake to enter into transactions under the published conditions with any other client to whom the quote is made available in accordance with paragraph 5 when the quoted size is at or below the size specific to the financial instrument determined in accordance with Article 9(5)(d)”;
- and
- Article 18(7) i.e. “Systematic internalisers shall be allowed to establish non-discriminatory and transparent limits on the number of transactions they undertake to enter into with clients pursuant to any given quote.”

52. As a result, SIs would only be required to trade on the published quote with the requesting client and would have discretion to trade with other clients on a case-by-case basis

53. To better assess how SI quotes are being used, ESMA asked SI clients in the CP whether they have easy access to the quotes published, i.e. whether they can potentially trade against those quotes when they were not the requestor and how frequently this happens (Question 2). ESMA also requested feedback on the overall assessment of the pre-trade transparency provided by SIs in liquid non-equity instruments (Question 3) and as to whether there was support for the amendments to Article 18 of MiFIR suggested above.

#### Feedback to the CP

54. Although a limited number of SI clients responded to Question 2, the overall feedback was that quotes published by SIs in non-equity instruments are of limited interest and value. Buy-side firms and other SI clients typically have a business relationship with a limited number of SIs and would not be willing to bear the costs of entering into a new relationship just to benefit from a “better quote”. As regards the quotes published by SIs they already have a relationship with, clients typically ask directly for a quote, as the quote is priced considering the characteristics of each client.

55. As regards the availability of SI quotes, some stakeholders noted that pre-trade quotes are indeed difficult to access due to the variety of channels that can be used but that even easier access would not help much considering the limited benefits of such quotes. In contrast, two respondents noted that quotes are indeed available but confirmed that clients would rather trade on published axes<sup>10</sup> and inventory rather than on MiFIR based SI quotes.

56. The overall assessment of the non-equity SI pre-trade transparency framework for liquid instruments attracted negative feedback from most stakeholders based on multiple grounds. A large majority of respondents stressed that there is no demand for SI quotes due to the bespoke nature of each request. Therefore, there is no point in having as a regulatory objective that the quotes are accessed by other clients. Respondents noted that buy-side firms (market participants/institutional investors) continue to use consistently updated market data streams for the purposes of price discovery, together with axes and

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<sup>10</sup> An axe is the interest that a trader shows in buying or selling a security that is typically already on his books



runs published by dealers as a source of information for price discovery rather than SI quotes.

57. A couple of respondents noted that the CP did not evaluate the level of pre-trade transparency being provided by SIs for package transactions. They called for an amendment to an ESMA Q&A<sup>11</sup> in relation to when SI pre-trade transparency obligations apply on a package order level. In their view, the current Q&A leaves too much room for circumvention by SIs.
58. A large majority of respondents, who were sell-side firms or their trade associations, supported the deletion of Article 18(6) and 18(7) of MiFIR. Some respondents suggested to also delete Article 18(5) of MiFIR, noting that if the SI is no longer required to trade with other clients at the displayed quote, there is no need for the SI to “give access” to its quotes.
59. The trading venues that provided feedback opposed the deletion of Article 18(6) and 18(7) of MiFIR. In their view, although trading on the quote displayed with only one client may indeed be the actual SI behaviour, this is not in line with the MiFID objectives.
60. Finally, many respondents stressed that pre-trade transparency is anyhow limited to a very small number/percentage of instruments qualifying as “traded on a trading venue” (ToTV) and considered to be liquid.
61. Based on the above, a few respondents suggested deleting Article 18 altogether to focus on post-trade transparency.

### Conclusions and proposals

62. In addition to the comparison with dealers on trading venues, the feedback received to the CP further demonstrates that the complex provisions of Article 18 of MiFIR on access to SI quotes in liquid instruments deliver little benefit to market participants. Most stakeholders confirmed that an SI client expects that the quote provided in response to a request reflects the specific characteristics of the transaction contemplated, including in illiquid instruments and complex transactions, and of the requesting client. SI clients would therefore typically not seek to trade on a displayed quote derived from the request of a different SI client.
63. Taking into account the feedback received, ESMA agrees that, should the requirement to trade with other clients on the published quote, subject to certain conditions, be deleted, it would make sense to also delete Article 18(5) of MiFIR on availability and access to quotes by other clients and to the commercial policy setting the conditions for access
64. Overall, ESMA considers that the non-equity SI pre-trade transparency obligations for liquid instruments should be simplified by amending Level 1 as follows:
  - Delete Article 18(5) i.e. “Systematic internalisers shall make the firm quotes published in accordance with paragraph 1 available to their other clients. Notwithstanding, they shall be allowed to decide, based on their commercial policy and in an objective non-

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<sup>11</sup> Section 4, Question 4(c) of ESMA’s Q&A on MiFID II and MiFIR transparency topics

discriminatory way, the clients to whom they give access to their quotes. To that end, systematic internalisers shall have in place clear standards for governing access to their quotes. Systematic internalisers may refuse to enter into or discontinue business relationships with clients based on commercial considerations such as the client credit status, the counterparty risk and the final settlement of the transaction.”

- Delete the first paragraph of Article 18(6) i.e. “Systematic internalisers shall undertake to enter into transactions under the published conditions with any other client to whom the quote is made available in accordance with paragraph 5 when the quoted size is at or below the size specific to the financial instrument determined in accordance with Article 9(5)(d)”; and
- Delete Article 18(7) i.e. “Systematic internalisers shall be allowed to establish non-discriminatory and transparent limits on the number of transactions they undertake to enter into with clients pursuant to any given quote.”

65. The only obligation left for SIs in liquid instruments would be to publish the quote provided to a client. ESMA does see value in maintaining this pre-trade transparency obligation as part of the role played by SIs in the price formation process in non-equity instruments.

66. As regards SIs’ pre-trade transparency obligations in relation to package orders, the Level 2 does not set out the test to be performed by an investment firm to qualify as an SI for package orders. The SI test is always performed at the level of the components of the package.

67. As reflected in the above-mentioned Q&A<sup>12</sup>, ESMA therefore considers that the quoting provision of Article 18(11) for packages apply to package orders only when the investment firm is an SI in all components of the package and sees currently no legal basis for extending the quoting obligation beyond those circumstances.

68. Given the overall feedback received on SI pre-trade transparency obligations, ESMA is not minded proposing an amendment to Level 1 to mandate further clarification in SI quoting obligations for package orders. No data was provided in the CP on SIs’ quoting activity for package orders due to the limited amount of data collected from market participants in this area.

69. ESMA took note of the comments received on the assessment of non-equity instrument liquidity or on the concept of ToTV. Those issues will be dealt with in ESMA’s Final Report on the transparency regime for non-equity instruments and the trading obligation for derivatives.

#### 3.3.1.4 Arrangements for the publication of quotes

##### Analysis

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<sup>12</sup> Section 4, Question 4(c) of ESMA’s Q&A on MiFID II and MiFIR transparency topics

70. ESMA suggested in the CP to set out the requirements for SIs in non-equity instruments for publishing their quotes at Level 2. This could be done via an amendment to Commission Delegated Regulation (EU) No 2017/567. More specifically, ESMA proposed that the requirements set out in Article 13 of that Regulation, on obligations for SIs to make quotes in equity instruments easily accessible, are extended to non-equity instruments. This would result in transposing the existing Q&A<sup>13</sup> into Level 2, to increase legal certainty.
71. ESMA requested general feedback on this proposal to specify the arrangements for publishing quotes (Question 10).

### Feedback to the CP

72. Stakeholders had split views on the proposal put forward by ESMA. About half of them did not support the proposal to specify in Level 2 the arrangements to be met by SIs for publishing quotes. They stressed the lack of convincing regulatory arguments to do so and the additional costs and administrative burden entailed.
73. The other half of the respondents supported ESMA's proposal to provide more clarity and legal certainty. A couple of them noted that there are elements of Article 13 of Commission Delegated Regulation (EU) No 2017/567 which relate to equities and are not readily applicable to the bond market. They recommended that ESMA reviews Article 13 to ensure that its provisions are practicable to the bond market.
74. Separately, a couple of respondents expressed concerns that prices published by SIs are considered by trading venues to be "unlawful" derived data, from the trading venues own published prices. As such, they would infringe on trading venues' intellectual property rights to those prices. It appears that many venues charge SIs to publish this information on the SIs' websites or through an APA.

### Conclusions and proposals

75. As explained above, the arrangements to be met by non-equity SIs for publishing the quotes and making those quotes easily accessible are already set out in ESMA's Q&A on MiFIDII/MiFIR transparency topics. ESMA expects Q&As to be already complied with by market participants. Therefore, setting out those arrangements in Level 2 through an amendment to Commission Delegated Regulation (EU) No 2017/567 should not create additional costs and administrative burden. In ESMA's view, the fact that half of the stakeholders did not seem to be aware of ESMA's Q&A further demonstrates the need to provide more clarity and legal certainty on the publication arrangements to be met by non-equity SIs in a Level 2 text.
76. ESMA did not identify any provision in Article 13 of Commission Delegated Regulation (EU) No 2017/567 on publication arrangements for equity instruments that would not be relevant for non-equity instruments (and those have not been clearly identified by respondents to the CP).

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<sup>13</sup> Section 7, Question 5(e) of ESMA's Q&A on MiFID II and MiFIR transparency topics



77. Finally, ESMA will consider the issue raised about SI access to trading venue data as part of its workstream on the costs of market data.

### 3.3.2 Effectiveness of the regime for illiquid instruments

#### Analysis

78. Assessing the effectiveness of the pre-trade transparency regime for SIs in illiquid instruments is a difficult exercise as the quotes are not subject to publication or reporting requirements. Likewise, there is no public information on the number of clients that have requested to have access to the SI quotes, either on a systematic or on an on-request basis.

79. In addition, whilst the requirement to disclose the quote to other clients upon request may be waived when the conditions for granting a pre-trade transparency waiver to the trading venue where the illiquid instrument is traded are met, the procedure for waiving the SIs' obligations varies across Member States.

80. In some jurisdictions, the SI must formally apply for a waiver with its CA. In some others, once the waiver for illiquid instruments has been granted to a trading venue, the waiver is automatically extended to SIs in those instruments. There is therefore no clear picture of SIs that avail themselves of the pre-trade transparency waiver for illiquid instruments. A sample check of some SIs' commercial policies publicly available does however tend to suggest that most of them are operating under the pre-trade transparency waiver for illiquid instruments.

81. This assumption is further confirmed by the ad-hoc SI data. The dataset provided by SIs includes a segmentation of quoted and traded volumes depending on whether a waiver has been granted, which provides an estimation of the SI volumes that would be covered by the obligations under Article 18(2) and those for which those obligations are waived.

82. Those figures are provided in Table 8 and Table 9 below, only for the asset classes where all or some instruments do not have a liquid market as explained in paragraph 27. This data suggests that, in all asset classes, the very large majority of trading and quoting activity in illiquid instruments (if not all of it) is performed under the waiver provided in Article 18(2).

	Bonds excl. ETC and ETN	ETC/ETN	Credit derivatives	FX derivatives	Interest rate derivatives	Structured finance products
NO WAIVER	16.2%	0.0%	7.2%	0.0%	0.4%	0.0%
WAIVER	83.8%	100.0%	92.8%	100.0%	99.6%	100.0%
<b>Grand Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

**Table 8: Breakdown of quoted volumes based on waiver - per asset class (source: ESMA based on ad-hoc SI data June 2019)**

	Bonds excl. ETC and ETN	ETC/ETN	Credit derivatives	FX derivatives	Interest rate derivatives	Structured finance products
NO WAIVER	27.5%	0.0%	12.5%	0.0%	1.2%	0.0%
WAIVER	72.5%	100.0%	87.5%	100.0%	98.8%	100.0%
<b>Grand Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

**Table 9: Breakdown of traded volumes based on waiver - per asset class (source: ESMA based on ad-hoc SI data June 2019)**

83. The pre-trade transparency regime applicable to SIs in relation to non-equity instruments for which there is not a liquid market appears to be overly complex in comparison to the delivered outcome. In practice, as evidenced by the ad-hoc SI data and the magnitude of quoted volumes provided under a pre-trade transparency waiver, it would appear that the obligation to “disclose quotes to clients on request” is hardly ever applied.
84. One option to address this situation would be to re-enforce the requirements in respect of illiquid non-equity instruments to make sure that there is genuine pre-trade transparency and apply Article 18(1) (obligation to make public firm quotes) to both liquid and illiquid instruments. To level the playing field with trading venues where a waiver is available for illiquid instruments, it would be necessary to introduce a waiver for illiquid instruments, if the conditions of Article 9(1)(c) (i.e. the illiquid waiver) are met.
85. But like the present situation, this construction appears circular, complex and suboptimal, with also possible inconsistent application across the EU: the only cases where Article 18(1) would apply to illiquid instruments would be when a CA decides not to grant the illiquid waiver.
86. An alternative option would be to remove the obligation to “disclose quotes to clients on request” for illiquid non-equity instruments (i.e. to delete Article 18(2)). Arguably, with possibly the exception of bonds, there would be little difference in outcome to the current situation as this would merely remove an obligation that is almost always waived. SIs would continue to have the possibility to publish quotes on a voluntary basis. Indeed, according to a survey performed by ESMA in November 2019 (covering 40 SIs), 30% of the firms responded that they regularly or occasionally publish quotes on a voluntary basis.

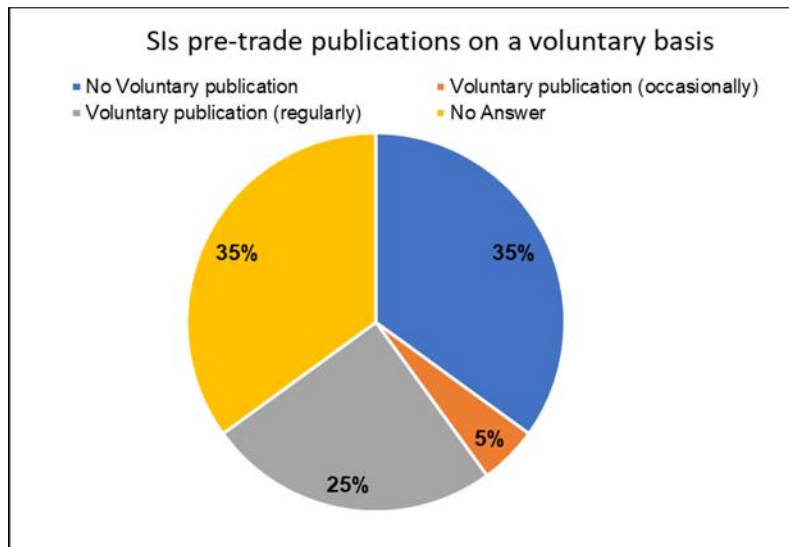


Figure 2: SIs pre-trade publications on a voluntary basis

87. In addition, to ensure a consistent application of Article 18(1) without creating a fully-fledged “waiver” process for SIs (i.e. similar to the one for trading venues), ESMA could foster supervisory convergence via e.g. drafting a template questionnaire in relation to SIs’ procedures to determine which quotes are subject to Article 18(1) (i.e. liquid above SSTI) and which are not, on the basis of which NCAs could undertake the necessary follow-up actions with SIs under their supervision, as appropriate. The objective of such workstream would be to maintain a level of monitoring on the way in which SIs are classifying instruments as liquid, but in a simpler form compared to the one envisaged for trading venues under Article 9(2) of MiFIR.
88. On that basis, ESMA proposed in the CP the following options in relation to the non-equity SI regime for illiquid instruments, with a preference for Option 3:
- Option 1: status quo (do nothing);
  - Option 2: Article 18(1) applies to both liquid and illiquid instruments and includes a waiver;
  - Option 3: Article 18(2) is deleted and ESMA develops ad-hoc supervisory convergence tools for SIs as described above.
89. To better assess how SI quotes in illiquid instruments are used, ESMA asked SI clients in the CP whether they had access to quotes in illiquid instruments and what was their overall assessment of the pre-trade transparency provided by SIs in illiquid instruments (Question 4). ESMA also asked SIs whether they disclosed quotes in illiquid instruments to clients upon request or whether they operated under a pre-trade transparency waiver (Question 5). Finally, ESMA asked for feedback on the three options considered above (Question 9).

#### Feedback to the CP

90. The few SI clients who provided feedback on access to quotes in illiquid instruments noted that most non-equity instruments are illiquid and that most SIs benefit from a waiver. Therefore, clients do not have access to quotes upon request. A couple of stakeholders stressed that they have no interest in the bespoke quotes in illiquid instruments provided to another client and that the focus should be on post-trade transparency, also referring to their responses to Question 2 and 3 (i.e. on liquid instruments).
91. About half of the SIs responding to Question 5 benefitted from a pre-trade transparency waiver. SIs that did not benefit from a pre-trade transparency waiver all stressed that the cases where they have been asked by another client to disclose a quote in illiquid instruments were rare or negligible. Clients do not have an interest in a quote that would have been tailor made to another client request, and even more so in illiquid instruments. One respondent mentioned the risks associated with “quote fishing” practices by those with no intention to trade that could compromise the trading strategies and hedging abilities of the parties involved in a bilateral transaction.
92. As regards the three options considered in relation to SI quotes in illiquid non-equity instruments, most respondents supported the deletion of Article 18(2), which is considered overly complex and providing little benefit. However, most of those respondents could not support Option 3 as they did not understand what the supervisory convergence tool mentioned in this option was referring to or were concerned by the additional burden thus created for NCAs and SIs. Option 1 (“do nothing”) therefore appeared as their fall-back solution.
93. Some respondents supported Option 3 provided that the supervisory convergence tool mentioned does not prove more burdensome for SIs than the existing Article 18(2) requirements. One banking association agreed with Option 3 provided that those tools are limited to the monitoring of the instruments’ classification by SIs (liquid versus illiquid instruments) based on the list of liquid instruments created and periodically updated by ESMA. In contrast, one respondent understood that under Option 3, SIs would oversee determining the liquidity status of non-equity instruments (and not ESMA) and disagreed with this approach.
94. Two trading venues were the only stakeholders supporting Option 2 (align the regime for liquid and illiquid instruments, with a waiver for illiquid instruments) in support of more transparency.

### Conclusions and proposals

95. The feedback to the CP confirmed that SI quotes for illiquid instruments are hardly ever provided to clients, either because the SI benefits from a pre-trade transparency waiver or because clients are not interested in the bespoke quotes provided to another client, notably in illiquid quotes. Considering the limited interest demonstrated by stakeholders in SI quotes provided to other clients, be they in liquid or illiquid instruments, ESMA considers that there would be no merit in aligning the pre-trade transparency regime for liquid and illiquid instruments.





96. ESMA acknowledges that the “supervisory convergence tools” referred to in Option 3 were not sufficiently explained. Assuming that Article 18(2) would be deleted, and in the absence of a waiver process, there would be no verification that SIs are correctly classifying their instruments as liquid / not liquid based on ESMA’s general transparency calculations, and not on the basis of SI’s own determination of whether an instrument is liquid or not. The “supervisory convergence tools” referred to in Option 3 aimed at fulfilling this objective. This task could simply be integrated into ESMA’s ongoing supervisory convergence mandate, and it does not appear necessary to develop those tools further at this stage.
97. ESMA is therefore proposing to simplify the SI pre-trade transparency regime for illiquid instruments via the deletion of Article 18(2), and to integrate a monitoring of SI classification of liquid/illiquid instruments to its ongoing supervisory convergence work.

### 3.3.3 Level playing field with trading venues

#### Analysis

98. Since the MiFID II/MiFIR application start date, the potential unlevel playing field between SIs and multilateral trading venues has been a recurrent theme. Concerns have been expressed by some stakeholders that the build-up of some SIs’ activity, including via a network of SIs, results in some SIs operating de facto as multilateral systems without being subject to similar authorisation and operating requirements.
99. On the one hand, concerns have also been expressed that the SIs’ quoting obligations and related transparency requirements are less demanding than those applicable to trading venues, thereby creating an incentive for market participants to move trading to such bilateral systems.
100. On the other hand, one can note that pre-trade transparency is provided by trading venues on an anonymous basis, i.e. without disclosing the identity of members or participants. SIs on the contrary must disclose their identity when the quotes are made public through the arrangements of a trading venue or an APA and SIs are putting their own capital at risk.
101. In the CP, ESMA asked market participants their view on a potential unlevel playing field between SIs and multilateral trading venues active in non-equity instruments, in particular with respect to pre-trade transparency (Question 6). ESMA also asked SIs providing liquidity on trading venues what were the key factors that determine whether quote requesters want to receive the quote through the facilities of a trading venue or through SIs (Question 7).

#### Feedback to the CP

102. In relation to Question 6, sell-side firms and their trade associations recalled that MiFIR recognises the need for transparency requirements to be calibrated for different types of financial instruments. This calibration should consider the interest of issuers and market liquidity, hence the different rules for trading venues and SIs.

103. According to those respondents, SIs are at a disadvantage compared to trading venues because they must give access to their quotes to other clients and 'enter into transactions under the published conditions', although acknowledging that they have managed risks through their commercial policies.
104. Furthermore, their quotes are not anonymous in contrast to on-venue quotes. Those respondents suggested deleting Article 18(6) and (7) of MiFIR as well as Article 18(5) of MiFIR to level the playing field between SIs and trading venues. A couple of respondents also quoted the burden arising from the uncertain application of the SI regime to non-ToTV instruments as another source of unlevel playing field with trading venues.
105. Trading venues considered that they were at a disadvantage compared to SIs. First, they noted that the distinction between bilateral trading and multilateral trading is being blurred due the setting up of network of SIs, and invited ESMA to further look into this issue. Second, they stressed that some SIs do not comply with the prohibition, when dealing on their own account, from entering into matching arrangements with entities outside their group to carry out de facto riskless back-to-back transactions through arrangements with third party liquidity providers. Third, trading venues claimed that Broker Crossing Network (BCN) trading volumes under MiFID I have shifted to SIs instead of moving to multilateral trading venues. In their view, this demonstrates the failure of MiFID II to move more trading to lit venues.
106. In relation to Question 7, most respondents quoted the size of the trade and the liquidity of the instrument as key differentiating factors for trading on an SI or a trading venue. Large size trade in low liquidity instruments would be executed with SIs, while trading venues would attract trades in more liquid instruments such as equity derivatives or retail bond trading. Trading with SIs in large sizes would also minimise the risk of information leakage. Clients would also turn to SIs for illiquid instruments where no pricing is available, when the trade is part of a complex trading strategy or in times of market volatility/uncertainty. Trading venues are quoted as offering the benefit of a fast transaction process and straight through processing, which is valuable for smaller trades.

### Conclusions and proposals

107. ESMA took note of the issues raised by SIs in relation to providing access to the published quotes to other clients and undertaking to enter into transactions under the published conditions. As generally acknowledged, Article 18 of MiFIR also provides SIs with risk management tools to mitigate the potential risks arising from this obligation. As noted above, the obligation for SIs to potentially enter into transactions with multiple clients under each quote does not have an equivalent for dealers trading on trading venues. Hence ESMA considers that removing that obligation for SIs should not create issues in terms of level-playing field between SIs and trading venues. However, ESMA considers it important to analyse and address level playing issues between SIs and trading venue on transparency. This will effectively be tackled in MiFIR review report on transparency for non-equity instruments.
108. ESMA's proposals regarding access to SI quotes in liquid instruments are discussed in section 3.3.1.3. As regards the uncertain application of the SI regime to non-ToTV



instruments, ESMA wishes to clarify that SI transparency obligations, including Article 18 of MiFIR, only apply to instruments that are ToTV. This is without prejudice to the assessment of the concept of ToTV discussed in ESMA's CP on MiFID II/ MiFIR review report on the transparency regime for non-equity instruments and the trading obligations for derivatives<sup>14</sup>.

109. ESMA has already been made aware of rising concerns about the blurring distinction between multilateral and bilateral trading and the development of other types of arrangements that facilitate the execution of transactions between multiple buyers and sellers without being authorised as a regulated market, an MTF or an OTF. ESMA intends to further discuss this issue in its upcoming CP on the MiFID II Review report on the functioning of OTFs.

## **4 Monitoring the application of the pre-trade transparency regime for SIs in non-equity instruments**

110. Article 19(1) of MiFIR states that "Competent authorities and ESMA shall monitor the application of Article 18 regarding the sizes at which quotes are made available to clients of the investment firm and to other market participants relative to other trading activity of the firm, and the degree to which the quotes reflect prevailing market conditions in relation to transactions in the same or similar financial instruments on a trading venue". The result of this monitoring is expected to be presented in a report to be submitted to the Commission by 3 July 2020.

111. Furthermore, Article 19(1) specifies that in case of significant quoting and trading activity just beyond the SSTI thresholds, or outside prevailing market conditions, the report to the Commission shall be submitted in advance of the foreseen date.

112. MiFIDII/MiFIR does not include a reporting obligation on SIs with respect to their quotes. To fulfil the mandate described above, ESMA has therefore decided to set-up an ad-hoc data request to collect the necessary information.

113. After consulting a subset of SIs and their NCAs over the summer of 2019 on a possible template for the data collection, the data request has been simplified to the extent possible and the look back period has been reduced to one month.

114. In relation to the first part of the mandate (i.e. the sizes of the quotes, and the potential quoting and trading activity just beyond the SSTI threshold), SIs have been asked to provide quoting and trading data for the month of June 2019 according to specific data segmentations (e.g. liquid versus illiquid instruments, ToTV versus non-ToTV instruments) and to group the quoting and trading data according to specific deviations from the SSTI threshold. The underlying intention was then to analyse whether the quoting and trading

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<sup>14</sup> <https://www.esma.europa.eu/press-news/consultations/consultation-paper-mifir-review-report-transparency-non-equity-tod> (page 65).

activity was mainly below the SSTI thresholds, close to them or well above. The outcome of this exercise is developed in Section 4.1.

115. In relation to the second part of the mandate (i.e. whether quotes reflect prevailing market conditions), SIs consulted during the summer indicated that the data request was overly complex. They also considered that the analysis expected from ESMA could be performed using the data that SIs have to produce under Commission Delegated Regulation (EU) 2017/575<sup>15</sup> (RTS 27 on Best Execution). The status of this workstream is expanded in Section 4.2

## 4.1 Monitoring the sizes at which quotes are made available

### 4.1.1 Overview of the data and quality issues

116. In October 2019 ESMA via NCAs collected data from 60 SIs located in 20 different jurisdictions, i.e. from roughly 30% of the total number of non-equity SIs that are listed on ESMA's register (Table 10). Most of those SIs are active in bonds (54 out of 60), which is consistent with the data included in the ESMA SI register. In terms of coverage, there are a few asset classes on which SIs did not report any activity (C10 derivatives, CfDs, emission allowances and derivatives thereof). Information on the data quality is provided in Annex 6.3.

	Bonds excl. ETC and ETN	ETC/ETN	Commodity derivatives	Credit derivatives	Equity derivatives	FX derivatives	Interest rate derivatives	Securitised derivatives	Structured finance products	Unique SI
CYPRUS	4									4
CZECH REPUBLIC	3									3
DENMARK	1					1	1	1	1	1
FINLAND	1									1
FRANCE	6	1		2	2	2	4	3	2	6
GERMANY	2	1	1	1		1	1	3	1	4
GREECE	1									1
HUNGARY	5									5
IRELAND						1	1			1
ITALY	3				1					5
LATVIA	1									1
LITHUANIA	3									3
NORWAY	2					1	1			2
POLAND	8									8
ROMANIA	1									1
SLOVAKIA	1									1
SPAIN	2					1	1			2
SWEDEN	4	1			3	2	3	1		4
THE NETHERLANDS	2					2	2	1		2
UNITED KINGDOM	4	2	1	4	2	4	4	3	2	5
<b>Grand Total</b>	<b>54</b>	<b>5</b>	<b>2</b>	<b>7</b>	<b>8</b>	<b>15</b>	<b>18</b>	<b>12</b>	<b>6</b>	<b>60</b>

<sup>15</sup> Commission Delegated Regulation (EU) 2017/575 of 8 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards concerning the data to be published by execution venues on the quality of execution of transactions (OJ L 87, 31.3.2017, p. 152.)

**Table 10: SIs who responded to the ad-hoc data request, per country and asset-class**

117. The tables below show, for each SI, the percentage of quoting and trading activity (both in terms of volumes and number of quotes/trades) according to four different buckets:

- Below SSTI;
- Between 100% and 101% of SSTI;
- Between 101% and 105% of SSTI;
- Greater than 105% of SSTI

118. The analysis is performed per asset class and includes only instruments which have a liquid market in the MiFIR sense (as the obligation to publish firm quotes only exists for liquid instruments). Some SIs reported only trading activity while others reported only quoting activity. Hence the population of SIs in the tables related to quoting and trading behaviours may differ.

119. Finally, due to the data quality issues described in Annex 6.3 and in particular the possible inconsistent methodologies for reporting quoting activity, ESMA has voluntarily refrained from aggregating data across SIs. It is however assumed that the data is consistent at the level of each SI.

#### 4.1.2 Bonds - quoting and trading activity in relation to the SSTI

##### Analysis

120. The analysis in relation to bonds (excluding ETCs and ETNs) is provided in the four tables below: quoted volumes in Table 11, traded volumes in Table 12, number of quotes in Table 13 and number of trades Table 14.

121. Regarding ETCs and ETNs, only 5 SIs provided data and out of those, only 2 reported volumes on liquid instruments. This coverage was considered insufficient to allow for a meaningful presentation. Therefore, in the rest of the analysis “bonds” should be read as “bonds excluding ETCs and ETNs”

122. Filtering the SIs that provided figures on *liquid* instruments reduced the population of SIs from 54 (as shown in Table 10) to 27. This means that several SIs only reported volumes on *illiquid* bonds.

123. Both for traded volumes and quoted volumes (Table 11 and Table 12), the most striking feature is the very low volume of activity close to the SSTI thresholds, i.e. between 100% and 105% of those thresholds. Instead, the activity as measured by volumes is in most cases concentrated above 105% of the SSTI thresholds. For a few SIs, it is concentrated below the SSTI thresholds.

124. In addition, the analysis based on the number of quotes and number of trades (Table 13 and Table 14), which provides a representation that is not tilted by the actual size of the transaction, leads to a similar result as the analysis based on volumes: there is little (if any) quotes and trades close to the SSTI thresholds.
125. As a result, based on the data collected for bonds, there is no evidence of significant quoting and trading activity just beyond the SSTI thresholds. It follows that the data does not suggest any intention to circumvent the pre-trade transparency obligation via the SSTI thresholds (i.e. by quoting “just beyond” the threshold).
126. In addition, the percentage of quotes and trades below SSTI (Table 13 and Table 14) varies from 0% from some SIs to 100% for other SIs, with a smooth distribution of SIs in the middle. This means that, as measured by number of quotes/trades, the SI bond activity subject to pre-trade transparency (below SSTI) and the SI activity not subject to pre-trade transparency (above SSTI) follows a relatively smooth distribution: some SIs are subject to pre-trade transparency for all their activity, others are not subject to it at all, and for others there is a mix of both under different proportions.
127. The same conclusion cannot be made based on volume data, which is expected since volumes above SSTI are by definition higher than volumes below.

#### Feedback to the CP

128. ESMA requested feedback on the analysis of bond data and the relation with the SSTI thresholds as presented above (Question 11). Most stakeholders commented that ESMA’s findings were in line with industry expectations, that there was no evidence of circumvention of the pre-trade transparency regime via the SSTI thresholds and the levels of the SSTI thresholds were appropriate.
129. According to respondents, the dichotomy identified in the data between SIs mainly quoting below SSTI and SIs mainly quoting above SSTI reflects the differences between SIs in terms of client base. SIs quoting mainly below SSTI typically serve retail clients, for which pre-trade transparency is important as they may have difficulties to gauge market values. On the other hand, SIs quoting mainly above SSTI are likely to serve institutional clients, who can rely on various sources of market data and have access to relevant liquidity providers (hence for which pre-trade transparency is of less importance). In that sense, respondents considered that the pre-trade transparency regime for SIs was appropriately framed.

#### Conclusions and proposals on Bonds’ quoting and trading activity in relation to the SSTI

130. The feedback received tends to confirm the conclusion drawn by ESMA’s analysis of the data, i.e. that SIs quote either mainly above the SSTI thresholds, or mainly below them (depending on their clients base), but that there is no significant quoting or trading activity “just beyond” those thresholds.

#### Detailed figures on bonds

Count	SI Code	Quoted volumes below SSTI	Quoted volumes ]100-101% SSTI <sup>1</sup>	Quoted volumes ]101-105%] SSTI <sup>1</sup>	Quoted volumes > 105% SSTI
1	SI 58	0.0%	0.0%	0.0%	100.0%
2	SI 37	0.0%	0.0%	0.0%	100.0%
3	SI 34	0.0%	0.0%	0.0%	100.0%
4	SI 28	0.0%	0.0%	0.0%	100.0%
5	SI 47	0.1%	0.0%	0.0%	99.9%
6	SI 39	0.1%	0.0%	0.0%	99.9%
7	SI 13	0.1%	0.0%	1.3%	98.6%
8	SI 50	0.1%	0.0%	0.0%	99.9%
9	SI 38	0.2%	0.0%	0.0%	99.8%
10	SI 31	0.3%	0.0%	0.0%	99.7%
11	SI 30	0.3%	0.0%	0.0%	99.7%
12	SI 1	0.3%	0.0%	0.0%	99.7%
13	SI 40	0.4%	0.0%	0.0%	99.6%
14	SI 15	0.8%	0.0%	0.0%	99.2%
15	SI 27	1.4%	0.0%	0.0%	98.5%
16	SI 41	1.7%	0.0%	0.1%	98.2%
17	SI 48	2.0%	0.0%	0.0%	98.0%
18	SI 49	2.4%	0.0%	0.0%	97.6%
19	SI 26	3.7%	0.0%	0.0%	96.3%
20	SI 9	9.5%	0.0%	0.0%	90.5%
21	SI 16	26.4%	0.0%	0.0%	73.6%
22	SI 2	33.3%	0.0%	0.0%	66.7%
23	SI 60	37.0%	0.0%	0.0%	62.9%
24	SI 4	72.5%	0.0%	27.5%	0.0%
25	SI 43	97.5%	0.0%	0.0%	2.5%
26	SI 23	100.0%	0.0%	0.0%	0.0%
27	SI 29	100.0%	0.0%	0.0%	0.0%

**Table 11: Bonds having a liquid market – Quoted volumes against SSTI**

Count	SI Code	Traded volumes below SSTI	Traded volumes ]100-101% SSTI <sup>1</sup>	Traded volumes ]101-105%] SSTI <sup>1</sup>	Traded volumes > 105% SSTI
1	SI 22	0.0%	0.0%	0.0%	100.0%
2	SI 40	0.0%	0.0%	0.0%	100.0%
3	SI 37	0.0%	0.0%	0.0%	100.0%
4	SI 34	0.0%	0.0%	0.0%	100.0%
5	SI 60	0.0%	0.0%	0.0%	100.0%
6	SI 28	0.0%	0.0%	0.0%	100.0%
7	SI 39	0.0%	0.0%	0.0%	100.0%
8	SI 50	0.1%	0.0%	0.0%	99.9%
9	SI 13	0.1%	0.0%	1.3%	98.6%
10	SI 38	0.2%	0.0%	0.0%	99.8%
11	SI 54	0.2%	0.0%	0.0%	99.8%
12	SI 30	0.3%	0.0%	0.0%	99.7%
13	SI 1	0.3%	0.0%	0.0%	99.7%
14	SI 48	0.3%	0.0%	0.0%	99.7%
15	SI 47	0.4%	0.0%	0.0%	99.6%
16	SI 49	0.6%	0.0%	0.0%	99.4%
17	SI 15	0.7%	0.0%	0.0%	99.3%
18	SI 41	0.7%	0.0%	0.0%	99.3%
19	SI 27	1.2%	0.0%	0.0%	98.8%
20	SI 16	2.3%	0.0%	0.0%	97.7%
21	SI 26	5.7%	0.0%	0.0%	94.2%
22	SI 9	23.1%	0.0%	0.0%	76.9%
23	SI 2	33.3%	0.0%	0.0%	66.7%
24	SI 4	81.4%	0.0%	18.6%	0.0%
25	SI 43	97.5%	0.0%	0.0%	2.5%
26	SI 23	100.0%	0.0%	0.0%	0.0%
27	SI 29	100.0%	0.0%	0.0%	0.0%

**Table 12: Bonds having a liquid market – Traded volumes against SSTI**

Count	SI Code	Number of Quotes below		Number of Quotes		Number of Quotes ]101-105%]		Number of Quotes > 105%	
		SSTI		]100-101% SSTI		]105%] SSTI		SSTI	
1	SI 37	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%	100.0%
2	SI 58	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%	100.0%
3	SI 28	1.4%	0.0%	0.0%	0.0%	0.0%	0.0%	98.6%	98.6%
4	SI 34	4.6%	0.0%	0.0%	0.0%	0.0%	0.0%	95.4%	95.4%
5	SI 39	6.9%	0.0%	0.0%	0.0%	0.0%	0.0%	93.1%	93.1%
6	SI 47	8.0%	0.0%	0.0%	0.0%	0.0%	0.0%	92.0%	92.0%
7	SI 50	12.1%	0.1%	0.0%	0.2%	0.0%	0.0%	87.7%	87.7%
8	SI 13	14.3%	0.0%	0.0%	7.1%	0.0%	0.0%	78.6%	78.6%
9	SI 31	15.9%	0.0%	0.0%	0.5%	0.0%	0.0%	83.6%	83.6%
10	SI 38	26.3%	0.2%	0.0%	0.0%	0.0%	0.0%	73.5%	73.5%
11	SI 40	28.6%	0.0%	0.0%	0.0%	0.0%	0.0%	71.4%	71.4%
12	SI 9	30.0%	0.0%	0.0%	0.0%	0.0%	0.0%	70.0%	70.0%
13	SI 30	32.2%	0.0%	0.0%	0.1%	0.0%	0.0%	67.7%	67.7%
14	SI 1	39.9%	0.0%	0.0%	0.0%	0.0%	0.0%	60.1%	60.1%
15	SI 15	45.8%	0.0%	0.0%	0.0%	0.0%	0.0%	54.2%	54.2%
16	SI 41	47.7%	0.0%	0.0%	0.6%	0.0%	0.0%	51.7%	51.7%
17	SI 27	48.5%	0.0%	0.0%	0.3%	0.0%	0.0%	51.2%	51.2%
18	SI 26	49.2%	0.0%	0.0%	0.1%	0.0%	0.0%	50.7%	50.7%
19	SI 49	57.9%	0.0%	0.0%	0.0%	0.0%	0.0%	42.1%	42.1%
20	SI 2	63.2%	0.0%	0.0%	0.0%	0.0%	0.0%	36.8%	36.8%
21	SI 48	76.4%	0.0%	0.0%	0.2%	0.0%	0.0%	23.4%	23.4%
22	SI 16	85.7%	0.0%	0.0%	0.0%	0.0%	0.0%	14.3%	14.3%
23	SI 43	95.8%	0.0%	0.0%	0.0%	0.0%	0.0%	4.2%	4.2%
24	SI 4	96.4%	0.0%	0.0%	3.6%	0.0%	0.0%	0.0%	0.0%
25	SI 60	97.2%	0.0%	0.0%	0.0%	0.0%	0.0%	2.7%	2.7%
26	SI 23	100.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
27	SI 29	100.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

**Table 13: Bonds having a liquid market – Number of quotes against SSTI**

Count	SI Code	Number of trades below		Number of trades		Number of trades ]101-105%]		Number of trades > 105%	
		SSTI		]100-101% SSTI		]105%] SSTI		SSTI	
1	SI 22	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%	100.0%
2	SI 37	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%	100.0%
3	SI 40	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	100.0%	100.0%
4	SI 28	1.9%	0.0%	0.0%	0.0%	0.0%	0.0%	98.1%	98.1%
5	SI 39	3.1%	0.0%	0.0%	0.0%	0.0%	0.0%	96.9%	96.9%
6	SI 34	4.6%	0.0%	0.0%	0.0%	0.0%	0.0%	95.4%	95.4%
7	SI 54	8.3%	0.0%	0.0%	0.1%	0.0%	0.0%	91.6%	91.6%
8	SI 50	11.0%	0.1%	0.0%	0.1%	0.0%	0.0%	88.8%	88.8%
9	SI 60	11.2%	0.0%	0.0%	0.0%	0.0%	0.0%	88.8%	88.8%
10	SI 13	14.3%	0.0%	0.0%	7.1%	0.0%	0.0%	78.6%	78.6%
11	SI 47	16.2%	0.0%	0.0%	0.0%	0.0%	0.0%	83.8%	83.8%
12	SI 30	32.2%	0.0%	0.0%	0.1%	0.0%	0.0%	67.6%	67.6%
13	SI 49	33.3%	0.0%	0.0%	0.0%	0.0%	0.0%	66.7%	66.7%
14	SI 41	35.9%	0.0%	0.0%	0.0%	0.0%	0.0%	64.1%	64.1%
15	SI 38	39.0%	0.0%	0.0%	0.0%	0.0%	0.0%	61.0%	61.0%
16	SI 15	39.8%	0.0%	0.0%	0.0%	0.0%	0.0%	60.2%	60.2%
17	SI 1	40.5%	0.0%	0.0%	0.0%	0.0%	0.0%	59.5%	59.5%
18	SI 27	54.3%	0.0%	0.0%	0.3%	0.0%	0.0%	45.4%	45.4%
19	SI 9	60.0%	0.0%	0.0%	0.0%	0.0%	0.0%	40.0%	40.0%
20	SI 2	63.2%	0.0%	0.0%	0.0%	0.0%	0.0%	36.8%	36.8%
21	SI 26	63.3%	0.0%	0.0%	0.1%	0.0%	0.0%	36.6%	36.6%
22	SI 16	66.7%	0.0%	0.0%	0.0%	0.0%	0.0%	33.3%	33.3%
23	SI 48	82.5%	0.0%	0.0%	0.1%	0.0%	0.0%	17.4%	17.4%
24	SI 43	85.7%	0.0%	0.0%	0.0%	0.0%	0.0%	14.3%	14.3%
25	SI 4	98.0%	0.0%	0.0%	2.0%	0.0%	0.0%	0.0%	0.0%
26	SI 23	100.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
27	SI 29	100.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

**Table 14: Bonds having a liquid market – Number of trades against SSTI**



### 4.1.3 Derivatives

#### Analysis

131. The following paragraphs provide an analysis of trading and quoting activity in relation to the SSTI thresholds for derivatives. The analysis could only be performed for interest rate, equity and securitised derivatives for the following reasons:

- Credit derivatives: only 7 SIs provided data and out of those, only 2 reported volumes on liquid instruments. In addition, the number of quotes and trades reported by those 2 SIs was very limited. This coverage was considered insufficient to allow for a meaningful presentation;
- Commodity derivatives: only 2 SIs provided data, and this was only on illiquid instruments;
- FX derivatives: instruments in this asset-class are all considered not to have a liquid market hence the analysis in relation to SSTI is irrelevant;
- No data was reported for the remaining asset classes (C10 derivatives, CFDs, Emission allowances, Emission allowances derivatives).

132. Irrespective of the type of derivatives presented below, and both for traded and quoted volumes, the same feature as for bonds is observed: there is very little (if any) activity close to the SSTI thresholds, i.e. between 100% and 105% of those thresholds. Instead, the activity as measured by volumes is in most cases concentrated above 105% of the SSTI thresholds or, for a few SIs, concentrated below those thresholds.

133. In addition, the analysis based on the number of quotes and number of trades, which provides a representation that is not tilted by the actual size of the transaction, leads to a similar result as the analysis based on volumes: there are little (if any) quotes and trades close to the SSTI thresholds.

134. As a result, based on the data collected for interest rate, equity and securitised derivatives, there is no evidence of significant quoting and trading activity just beyond the SSTI thresholds. It follows that the data does not suggest any intention to circumvent the pre-trade transparency obligation via the SSTI thresholds (i.e. by quoting “just beyond” the threshold).

135. For interest rate derivatives, the analysis of the number of quotes/trades (Table 17 and Table 18.) leads to a similar conclusion as for bonds: the percentage of quotes and trades below SSTI varies from 0% from some SIs to 100% for other SIs, with a relatively smooth distribution of SIs in the middle (this should however be nuanced by the small number of SIs in the sample). This means that, as measured by number of quotes/trades, some SIs are subject to pre-trade transparency for all their activity, others are not subject to it at all, and for others there is a mix of both.

136. For securitised derivatives (Table 25 and Table 26) the outcome seems slightly different, with more SIs subject to pre-trade transparency for an important proportion of their activity as measured by the number of quotes/trades. For credit and equity derivatives, a similar conclusion is more difficult to draw due to the limited number of SI included in the analysis.

#### Feedback to the CP

137. ESMA requested feedback on this analysis of derivatives data and the relation with the SSTI thresholds (Question 12). The responses to this question were largely the same as those collected in the previous question related to bonds. Most stakeholders commented that ESMA's findings were in line with industry expectations, that there was no evidence of circumvention of the pre-trade transparency regime via the SSTI thresholds and the levels of the SSTI thresholds were appropriate.

138. Several stakeholders also agreed with ESMA's statement in para. 89 of the CP that the level of the SSTI thresholds was so low for some asset classes that by construction almost any quote would be above SSTI. In those instances, the comparison between trade flows above and below the SSTI thresholds is somehow meaningless. Some suggested to remove the SSTI thresholds and align them with the levels of the LIS.

#### Conclusions and proposals on derivatives' quoting and trading activity in relation to the SSTI

139. As for bonds, the feedback received tends to confirm the conclusions deriving from ESMA's analysis of the derivatives data, i.e. that SIs quote either mainly above the SSTI thresholds, or mainly below them (depending on their client base), but that there is no significant quoting or trading activity "just beyond" those thresholds.

140. The sections below present the detailed numbers for each asset-class.

##### 4.1.3.1 Interest rate derivatives - quoting and trading activity in relation to SSTI

141. The analysis in relation to interest rate derivatives (IRD) is provided in the four tables below: quoted volumes in Table 15, traded volumes in Table 16, number of quotes in Table 17 and number of trades in Table 18.

142. Filtering the SIs that provided positive figures on liquid instruments reduced the population of SIs from 18 (as shown in Table 10) to 13 (for quote data) and 12 (for trade data). This means that a few SIs only reported positive volumes on illiquid interest rate derivatives.

Count	SI Code		Quoted volumes below SSTI		Quoted volumes ]100-101% SSTI <sup>1</sup>		Quoted volumes ]101-105%] SSTI <sup>1</sup>		Quoted volumes > 105% SSTI
1	SI 31	●	0.5%	●	0.0%	●	0.0%	●	99.5%
2	SI 28	●	0.6%	●	2.5%	●	0.0%	●	96.8%
3	SI 26	●	1.2%	●	0.0%	●	0.0%	●	98.8%
4	SI 48	●	1.2%	●	0.0%	●	0.0%	●	98.8%
5	SI 39	●	1.8%	●	0.0%	●	0.0%	●	98.2%
6	SI 50	●	2.4%	●	0.0%	●	0.0%	●	97.6%
7	SI 34	●	3.6%	●	0.1%	●	0.1%	●	96.3%
8	SI 1	●	7.4%	●	0.0%	●	0.0%	●	92.6%
9	SI 30	●	15.7%	●	0.9%	●	0.9%	●	82.5%
10	SI 38	●	17.4%	●	0.0%	●	1.3%	●	81.3%
11	SI 49	●	39.5%	●	0.0%	●	0.0%	●	60.5%
12	SI 24	●	100.0%	●	0.0%	●	0.0%	●	0.0%
13	SI 40	●	100.0%	●	0.0%	●	0.0%	●	0.0%

**Table 15: IRD having a liquid market – Quoted volumes against SSTI**

Count	SI Code		Traded volumes below SSTI		Traded volumes ]100-101% SSTI <sup>1</sup>		Traded volumes ]101-105%] SSTI <sup>1</sup>		Traded volumes > 105% SSTI
1	SI 26	●	0.0%	●	0.0%	●	0.0%	●	100.0%
2	SI 48	●	0.8%	●	0.0%	●	0.0%	●	99.2%
3	SI 28	●	1.2%	●	4.9%	●	0.0%	●	93.9%
4	SI 39	●	1.7%	●	0.0%	●	0.0%	●	98.3%
5	SI 54	●	2.2%	●	0.0%	●	0.0%	●	97.8%
6	SI 50	●	2.4%	●	0.0%	●	0.0%	●	97.6%
7	SI 34	●	3.6%	●	0.1%	●	0.1%	●	96.3%
8	SI 1	●	4.2%	●	0.0%	●	0.0%	●	95.8%
9	SI 30	●	15.6%	●	0.9%	●	0.9%	●	82.6%
10	SI 38	●	21.3%	●	0.0%	●	1.5%	●	77.2%
11	SI 49	●	29.7%	●	0.0%	●	0.0%	●	70.3%
12	SI 24	●	100.0%	●	0.0%	●	0.0%	●	0.0%

**Table 16: IRD having a liquid market – Traded volumes against SSTI**

SI Code	Number of Quotes below		Number of Quotes		Number of Quotes ]101-105%]		Number of Quotes > 105%	
	SSTI		]100-101% SSTI		105%] SSTI		SSTI	
SI 28	●	4.3%	●	8.7%	●	0.0%	●	87.0%
SI 31	●	11.5%	●	0.0%	●	0.0%	●	88.5%
SI 48	●	20.0%	●	0.0%	●	0.0%	●	80.0%
SI 50	●	22.2%	●	0.0%	●	0.0%	●	77.8%
SI 26	●	35.9%	●	0.0%	●	0.1%	●	64.0%
SI 34	●	40.3%	●	0.4%	●	0.4%	●	59.0%
SI 39	●	41.9%	●	0.0%	●	0.0%	●	58.1%
SI 30	●	56.7%	●	1.3%	●	1.0%	●	41.0%
SI 38	●	63.8%	●	0.0%	●	2.1%	●	34.0%
SI 49	●	66.7%	●	0.0%	●	0.0%	●	33.3%
SI 1	●	76.5%	●	0.0%	●	0.0%	●	23.5%
SI 24	●	100.0%	●	0.0%	●	0.0%	●	0.0%
SI 40	●	100.0%	●	0.0%	●	0.0%	●	0.0%

**Table 17: IRD having a liquid market – Number of quotes against SSTI**

SI Code	Number of trades below		Number of trades		Number of trades ]101-105%]		Number of trades > 105%	
	SSTI		]100-101% SSTI		105%] SSTI		SSTI	
SI 26	●	0.3%	●	0.0%	●	0.0%	●	99.7%
SI 28	●	7.7%	●	15.4%	●	0.0%	●	76.9%
SI 48	●	20.0%	●	0.0%	●	0.0%	●	80.0%
SI 50	●	22.2%	●	0.0%	●	0.0%	●	77.8%
SI 54	●	27.3%	●	0.1%	●	0.1%	●	72.5%
SI 34	●	40.3%	●	0.4%	●	0.4%	●	59.0%
SI 39	●	42.5%	●	0.0%	●	0.0%	●	57.5%
SI 1	●	44.8%	●	0.0%	●	0.0%	●	55.2%
SI 38	●	46.3%	●	0.0%	●	1.9%	●	51.9%
SI 30	●	56.5%	●	1.3%	●	1.0%	●	41.1%
SI 49	●	70.0%	●	0.0%	●	0.0%	●	30.0%
SI 24	●	100.0%	●	0.0%	●	0.0%	●	0.0%

**Table 18: IRD having a liquid market – Number of trades against SSTI**

#### 4.1.3.2 Equity derivatives - quoting and trading activity in relation to SSTI

143. The analysis in relation to equity derivatives (EQD) is provided in the four tables below: quoted volumes in Table 19, traded volumes in Table 20, number of quotes in Table 21 and number of trades in Table 22.

144. Filtering the SIs that provided positive figures on liquid instruments reduced the population of SIs from 8 (as shown in Table 10) to 6 (for quote data) and 5 (for trade data). This means that a couple of SI only reported volumes on illiquid equity derivatives.

Count	SI Code	Quoted volumes below SSTI	Quoted volumes ]100-101% SSTI <sup>1</sup>	Quoted volumes ]101-105%] SSTI <sup>1</sup>	Quoted volumes > 105% SSTI
1	SI 50	0.0%	0.0%	0.0%	100.0%
2	SI 58	0.1%	0.0%	0.0%	99.9%
3	SI 40	13.4%	0.0%	0.0%	86.6%
4	SI 43	27.7%	0.0%	0.0%	72.3%
5	SI 26	100.0%	0.0%	0.0%	0.0%
6	SI 49	100.0%	0.0%	0.0%	0.0%

Table 19: Equity derivatives having a liquid market – Quoted volumes against SSTI

Count	SI Code	Traded volumes below SSTI	Traded volumes ]100-101% SSTI <sup>1</sup>	Traded volumes ]101-105%] SSTI <sup>1</sup>	Traded volumes > 105% SSTI
1	SI 5	0.0%	0.0%	0.0%	100.0%
2	SI 50	0.0%	0.0%	0.0%	100.0%
3	SI 58	0.2%	0.0%	0.0%	99.8%
4	SI 40	13.3%	0.0%	0.0%	86.7%
5	SI 43	69.6%	0.0%	0.0%	30.4%
6	SI 26	100.0%	0.0%	0.0%	0.0%
7	SI 49	100.0%	0.0%	0.0%	0.0%

Table 20: Equity derivatives having a liquid market – Traded volumes against SSTI

Count	SI Code	Number of Quotes below SSTI	Number of Quotes ]100-101% SSTI <sup>1</sup>	Number of Quotes ]101- 105%] SSTI <sup>1</sup>	Number of Quotes > 105% SSTI
1	SI 50	2.8%	0.0%	0.0%	97.2%
2	SI 58	3.3%	0.0%	0.1%	96.6%
3	SI 43	35.4%	0.0%	0.0%	64.6%
4	SI 40	76.1%	0.1%	0.3%	23.6%
5	SI 49	100.0%	0.0%	0.0%	0.0%
6	SI 26	100.0%	0.0%	0.0%	0.0%

Table 21: Equity derivatives having a liquid market – Number of quotes against SSTI

Count	SI Code	Number of trades below		Number of trades		Number of trades ]101-105%]		Number of trades > 105%	
		SSTI		]100-101% SSTI		]105%] SSTI		SSTI	
1	SI 5	0.0%		0.0%		0.0%		100.0%	
2	SI 58	2.9%		0.0%		0.1%		97.0%	
3	SI 50	10.1%		0.0%		0.0%		89.9%	
4	SI 43	44.4%		0.0%		0.0%		55.6%	
5	SI 40	61.7%		0.1%		0.4%		37.7%	
6	SI 49	100.0%		0.0%		0.0%		0.0%	
7	SI 26	100.0%		0.0%		0.0%		0.0%	

**Table 22: Equity derivatives having a liquid market – Number of trades against SSTI**

#### 4.1.3.3 Securitised derivatives - quoting and trading activity in relation to SSTI

145. The analysis in relation to securitised derivatives (IRD), which are all considered to have a liquid market, is provided in the four tables below: quoted volumes in Table 23, traded volumes in Table 24, number of quotes in Table 25 and number of trades in Table 26.

Count	SI Code	Quoted volumes below SSTI		Quoted volumes ]100-101% SSTI <sup>1</sup>		Quoted volumes ]101-105%] SSTI <sup>1</sup>		Quoted volumes > 105% SSTI	
1	SI 39	0.0%		0.0%		0.0%		100.0%	
2	SI 58	5.5%		0.1%		0.3%		94.2%	
3	SI 44	13.0%		0.1%		0.2%		86.7%	
4	SI 48	25.0%		0.0%		0.3%		74.7%	
5	SI 43	42.6%		0.0%		0.0%		57.4%	
6	SI 26	45.0%		0.1%		0.5%		54.4%	
7	SI 46	80.0%		0.1%		0.5%		19.4%	
8	SI 31	100.0%		0.0%		0.0%		0.0%	
9	SI 38	100.0%		0.0%		0.0%		0.0%	

**Table 23: Securitised derivatives having a liquid market – Quoted volumes against SSTI**

Count	SI Code	Traded volumes below SSTI	Traded volumes ]100-101% SSTI <sup>1</sup>	Traded volumes ]101-105% SSTI <sup>1</sup>	Traded volumes > 105% SSTI
1	SI 39	0.0%	0.0%	0.0%	100.0%
2	SI 54	0.0%	0.0%	0.0%	100.0%
3	SI 44	9.2%	0.0%	0.1%	90.6%
4	SI 58	15.4%	0.1%	0.4%	84.1%
5	SI 48	32.9%	0.0%	0.5%	66.6%
6	SI 43	42.6%	0.0%	0.0%	57.4%
7	SI 26	51.1%	0.2%	0.7%	48.1%
8	SI 46	77.6%	0.2%	0.8%	21.3%
9	SI 28	95.1%	0.1%	0.3%	4.5%

Table 24: Securitised derivatives having a liquid market – Traded volumes against SSTI

Count	SI Code	Number of Quotes below SSTI	Number of Quotes ]100-101% SSTI <sup>1</sup>	Number of Quotes ]101- 105%] SSTI <sup>1</sup>	Number of Quotes > 105% SSTI
1	SI 39	0.0%	0.0%	0.0%	100.0%
2	SI 58	42.7%	0.2%	0.9%	56.2%
3	SI 43	80.0%	0.0%	0.0%	20.0%
4	SI 48	87.4%	0.0%	0.3%	12.4%
5	SI 44	96.5%	0.0%	0.1%	3.4%
6	SI 26	99.1%	0.0%	0.0%	0.9%
7	SI 46	99.5%	0.0%	0.0%	0.5%
8	SI 38	100.0%	0.0%	0.0%	0.0%
9	SI 31	100.0%	0.0%	0.0%	0.0%

Table 25: Securitised derivatives having a liquid market – Number of quotes against SSTI

Count	SI Code	Number of trades below SSTI	Number of trades ]100-101% SSTI <sup>1</sup>	Number of trades ]101- 105%] SSTI <sup>1</sup>	Number of trades > 105% SSTI
1	SI 39	0.0%	0.0%	0.0%	100.0%
2	SI 54	7.5%	0.0%	0.0%	92.5%
3	SI 58	45.8%	0.3%	0.9%	53.0%
4	SI 28	77.7%	0.0%	0.0%	22.3%
5	SI 43	80.0%	0.0%	0.0%	20.0%
6	SI 48	87.3%	0.0%	0.3%	12.3%
7	SI 44	96.1%	0.0%	0.1%	3.8%
8	SI 26	98.0%	0.0%	0.1%	1.9%
9	SI 46	99.3%	0.0%	0.1%	0.6%

Table 26: Securitised derivatives having a liquid market – Number of trades against SSTI

#### 4.1.4 Conclusions and proposals in relation to SSTI

146. As a conclusion to the above analysis, the data collected by ESMA for the purpose of the CP did not provide clear evidence of significant quoting or trading activity “just beyond” the SSTI threshold. Hence it does not appear that SIs would somehow artificially provide quotes at specific levels to make sure that they are not subject to the pre-trade transparency requirements for liquid instruments under Article 18(2).
147. In fact, when replying to the ad-hoc data collection exercise, a couple of SIs have provided explanations of two different natures which could shed some light on why, as we see in the data, there is virtually no trading and quoting activity very close to the SSTI thresholds.
148. First, the explanation could be that the level of the SSTI thresholds are, at least for some asset classes, so low that by construction almost any quote would be above the SSTI. This would be for instance the case for some equity derivative contracts (where the SSTI threshold is 20,000 EUR in many cases) where it has been evidenced that even quoting a single lot leads to such quote being above the SSTI threshold.
149. Second, another explanation for certain SIs could be that they provide quotes in relation to two distinct market segments, retail flow which tends to be well below the SSTI thresholds, and wholesale flow which would typically be significantly above the SSTI thresholds.
150. Overall, whether a quote is subject to pre-trade transparency depends on a series of factors: first the instrument should be traded on a trading venue (ToTV)<sup>16</sup>, second it should be liquid and third the quote should be above the SSTI threshold. While this paper does not measure the influence of the first two factors on the overall level of pre-trade transparency in non-equity traded on SIs, it suggests that the third one alone does not appear to be used by market participant to circumvent their obligations under Article 18(2).
151. Any reflections around the overall level of transparency (such as the liquidity determination or the level of the SSTI thresholds) is expected to be covered at a more general level (i.e. not for SI only) in the MiFID II/MiFIR report on transparency for non-equity instrument, expected to be published in Q3 2020. ESMA wishes to highlight that any change to the transparency regime may have an impact on the SI regime in Article 18 of MiFIR therefore it is important to perform a holistic review of the relevant Level 1 requirements.
152. With regards to the mandate covered in this report, i.e. the impact of the SSTI threshold on SI’s obligation to publish firm quotes in non-equity instruments, ESMA exposed in the CP that in the absence of obvious issues linked to possible circumvention of the pre-trade transparency obligations via the SSTI threshold, no change to the legal framework appeared necessary.

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<sup>16</sup> As explained in the Annex 6.3, for the purpose of this analysis all instruments have been considered ToTV.



## Feedback to the CP

153. In the CP, ESMA asked market participants their views on the influence of the SSTI thresholds on the pre-trade transparency framework for SI active in non-equity instruments, and whether any changes to the legal framework were necessary (Question 13).
154. Most stakeholders concluded that in the absence of an impact or influence of the SSTI thresholds on the pre-trade transparency framework for SIs active in non-equity instruments no change to the legal framework was needed at this stage.
155. This conclusion was supported by the fact that quotes provided by SIs mainly result from request for quotes from clients, hence SIs are not setting the volume of those quotes.
156. In addition, some SIs stream quotes in non-equities on a continuous basis, typically in the most liquid and widely traded non-equity instruments. For those instruments, prices are available on trading venues as well and liquidity providers are happy to trade on those quoted prices, especially for smaller volumes. Hence there is little to no incentive for SIs to provide quotes in those instruments for sizes just above the SSTI in order to avoid pre-trade transparency.
157. Some stakeholders proposed to change what they consider to be a complex system of variable thresholds to a fixed SSTI threshold, provided that the policy objective of protecting SIs against undue risk is still met. In their view, fixed thresholds would be easier for retail clients to understand, while wholesale clients have more resources to stay informed of changing variable thresholds.

### Proposals and conclusions on the influence of the SSTI thresholds on the pre-trade transparency framework for SIs active in non-equity instruments

158. The feedback received from stakeholders largely confirms ESMA's preliminary conclusions set out in the CP: there is no evidence that SIs would artificially provide quotes at specific levels to make sure that they are not subject to the pre-trade transparency requirements for liquid instruments under Article 18(2).
159. ESMA hence confirms its conclusion that in the absence of obvious issues linked to possible circumvention of the pre-trade transparency obligations via the SSTI threshold, no change to the legal framework appears necessary at this stage.
160. The proposals made in the responses to the CP going beyond the mandate of this report, such as overall changes to the way in which SSTI thresholds are calculated, or the relevance of SSTI thresholds as a whole, will be addressed in the broader context of the MiFIR review report on transparency for non-equity instruments.

## **4.2 Monitoring whether quoted prices reflect prevailing market conditions**

161. Article 19(1) of MiFIR states that "Competent authorities and ESMA shall monitor the application of Article 18 regarding [...] the degree to which the quotes reflect prevailing

market conditions in relation to transactions in the same or similar financial instruments on a trading venue.”. It also states that in the event of “significant quoting and trading activity [...] outside prevailing market conditions”, ESMA shall submit its report to the Commission in advance of the legislative deadline.

162. This mandate implies that ESMA collects on the one side information on quoted and traded prices and, on the other side, information on prevailing market conditions on the basis of transactions taking place on venue, and finally designs a methodology to compare those two to formulate a general assessment of whether there is any significant quoting and trading activity “outside” prevailing market conditions.

#### 4.2.1 Collecting ad-hoc data from SIs

163. To fulfil this mandate ESMA had initially envisaged to collect quoting and trading data, as well as market prices, directly from SIs for three main reasons. Firstly, data on individual quotes are not part of the transparency data which is submitted to ESMA under MiFIR. Secondly, the post-trade transparency data submitted to ESMA is aggregated per ISIN, trading day and reporting entity, hence there is no information at individual transaction level including on price.

164. Thirdly, the analysis of quotes that SIs are required to publish under Article 18(1) of MiFIR, which could be used in this context, would not allow for a thorough analysis because the quotes subject to publication only concern a limited subset of the total quoting activity (liquid instruments below SSTI) and would not cover the whole mandate. In addition, there is no centralised access point to those published quotes and they prove difficult to capture on a systematic basis (an issue that the recommendation in section 3.3.1.4 aims to address).

165. ESMA therefore initially produced a template to collect data from SIs on quoted and traded prices and whether they reflect prevailing market conditions, as it did to collect the data related to the first part of the mandate (i.e. whether there is a significant trading and quoting activity just beyond the SSTI threshold). When ESMA consulted SIs on this template over the summer 2019, the general feedback was that this exercise would be extremely complex, costly, time consuming or simply impossible.

166. For example, some SIs mentioned that they stored the market inputs used for the fair price but not the prices in the same or similar financial instruments on a trading venue. Others mentioned that there were several sources of “market data” (including sometimes both internal and external sources), and several ways to aggregate them, hence further guidance would be needed on how the “price prevailing market condition” should be calculated/provided.

167. Finally, some SIs also stressed that performing such analysis on a systematic basis (e.g. all quotes from all SIs for a given time period) would produce gigantic amounts of data, rendering the subsequent data analysis very complex. Taken the above feedback into account, ESMA had decided not to collect ad-hoc data from SIs in this context.

168. As suggested by some SIs, there could be alternative ways for ESMA to fulfil its mandate: one possibility would be to source this information from APAs, and the other one to retrieve the information published by SIs under Commission Delegated Regulation (EU) 2017/575 (RTS 27 on Best Execution). Those options, not mutually exclusive, are described below.

#### 4.2.2 Relying on data published under RTS 27

169. RTS 27 specifies inter alia the content, format and periodicity of data relating to the quality of execution to be published by execution venues (i.e. including SIs) in accordance with Article 27(3) of MiFID II (best execution).

170. ESMA has initiated a workstream to search, store and aggregate parts of the data published by SIs under RTS 27, in particular Table 3 of this RTS which includes data at a level of granularity that is compatible with the analysis required (i.e. transaction level).

171. The scope of the data published under RTS 27 would by definition not completely overlap with the data needed to cover ESMA's mandate for this report, in two ways: the data does not reflect quoting activity, but only trading activity (when a quote results in no trade, there is no obligation to report it under RTS 27); and SIs activity above the SSTI threshold is exempted from the reporting of intra-day transaction data (such as covered by Table 3) under RTS 27 (see recital 10 of RTS 27).

172. Although the intra-day data expected to be published is limited to four specific points in time for each day (9.30, 11.30, 13.30 and 15.30), ESMA considers that such time granularity would be sufficient for the analysis to be performed.

173. From the large sample of SIs' RTS 27 reports examined by ESMA, the main limit identified lies in the significant differences in the way SIs make their RTS 27 report publicly available.

174. Finally, Table 3 of RTS 27 mandates SIs to publish information on the "Best bid and offer or suitable reference price at time of execution", which could be considered equivalent to the "prevailing market conditions" and hence provide a valuable source of data for the analysis ESMA is expected to make. However, this specific column of Table 3 of RTS 27 is only mandatory in the situation where "no transactions occurred during the first two minutes of the relevant time periods<sup>17</sup>". The information from the RTS 27 reports alone would not enable a proper assessment of whether the quotes would reflect prevailing market conditions.

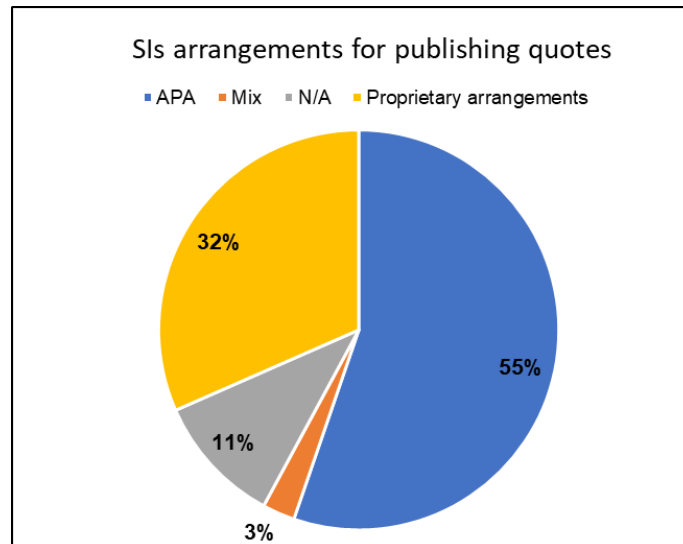
#### 4.2.3 Relying on APA data

175. APAs could be a source of information in two different ways. First, in relation to pre-trade data (hence information on SI quoting activity), some SIs are complying with their pre-trade transparency obligation under Article 18(1) by publishing quotes via an APA.

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<sup>17</sup> Article 4 point (a)(x) of RTS 27

APAs could hence constitute a centralised source of data in relation to quoted prices, with one limitation being that according to a survey performed by ESMA in November 2019 (covering 40 SIs), roughly only half of the SIs are using such publication arrangement (Figure 2).



**Figure 2: SIs arrangements for publishing quotes (source: SIs survey November 2019)**

176. The other SIs that responded to the survey indicated that they are fulfilling this obligation via a trading venue or making the pre-trade information available on their own website. In addition, as mentioned above, pre-trade publication is only mandatory for quotes in liquid instruments below SSTI, hence covering only one part of the Commission’s mandate.

177. Second, in relation to post-trade data (hence information on SI trading activity), ESMA could leverage on Article 21 of MiFIR which requires SIs to make public the volumes and prices of all their non-equity transactions through an APA. Opting for this data source would, of course, limit the analysis to trading activity but would cover a broader scope of transactions and instruments compared to pre-trade data, as the APA post-trade reporting is not limited to transactions in liquid instruments below SSTI.

#### 4.2.4 Market data source

178. None of the data sources described above, i.e. RTS 27 reports and APA data, appear to be a reliable source of data concerning the “prevailing market conditions in relation to transactions in the same or similar financial instruments on a trading venue”.

179. Based on a preliminary assessment, the possibility to source this data from trading venues has been excluded due to complexity. It would indeed first require mapping each instrument with the (possibly numerous) trading venues on which it is available, then designing data requests which would be ad-hoc to each trading venue and finally re-aggregating the pricing data afterwards. Instead, ESMA is examining the possibility to use external data sources with pre-aggregated data from multiple trading venues, but the extent to which this will be sufficient to deliver a meaningful analysis is yet to be determined.

180. As explained above, ESMA is faced with multiple challenges when it comes to fulfilling the second part of the mandate on whether quoted/traded prices reflect prevailing market conditions. Several options have been identified as possible data sources, but all appear to have their own drawbacks. Choices have yet to be made as regards the scope of the data set (both in terms of instruments, number of SIs and time period) with the view to strike a balance between the representativeness of the sample and its complexity, having in mind the impact on affected stakeholders' as well as ESMA's resources.

#### Feedback to the CP

181. In the CP, ESMA asked market participants their view on the best way for ESMA to fulfil the mandate related to whether quoted and traded prices reflect prevailing market conditions (Question 14). Market participants overall agreed that there is no simple or obvious solution available in order to fulfil ESMA's mandate. Among the responses received, none recommended using RTS 27 data. Data from RTS 27 was deemed unsuitable because, as discussed above, trade level data is published only in some narrow scenarios and in very diverse formats.

182. With respect to the possible use of APA data, respondents highlighted that indeed APA's data is broad as it includes both pre- and post-trade data. However, respondents noted that not all SIs use APAs and that APAs are not required to aggregate data. Even where data would be available, SIs are not subject to pre-trade transparency obligations when they quote above SSTI, which narrows the scope of the analysis.

183. Regarding the possibility of fulfilling ESMA's mandate through a data request to SIs and trading venues (TVs), some respondents highlighted that if such choice was made the data request should be sent for few, narrowly selected timeslots. In ESMA's view, this would hinder the purpose of the data request as it would limit data availability and not lead to a meaningful analysis.

184. Some respondent suggested that ESMA discusses the relation between quotes and prevailing market conditions directly with SIs, recommending a qualitative approach rather than a quantitative one.

#### 4.2.5 Conclusions and proposals in relation to prevailing market conditions

185. The feedback received from stakeholders confirms ESMA's preliminary view that data currently available through APAs and RTS 27 publications is not suitable to fulfil ESMA's mandate with respect to the degree to which SIs' quotes reflect prevailing market conditions in relation to transactions in the same or similar financial instruments on a trading venue.

186. In light of the responses received, ESMA considers that a suitable way to fulfil its mandate would be to rely on a qualitative analysis, relying on the feedback received from SIs to the data request performed in July 2019. In this data request, SIs were asked to explain how they ensure that quoted prices reflect current market conditions.

187. Overall the responses received highlighted that SIs ensure that their quoted prices are in line with prevailing market condition either by directly using the prices available on TVs as an input for their quotes, or by indirectly using such prices (or in some cases the price of the underlying) as input to their pricing models.
188. Several SIs stated that for those financial instruments where SIs directly compete with trading venues, SIs necessarily take into account on-venue pricing when offering quotes and that quotes are marked against TV prices. SIs which continuously stream quotes in RFQ systems sometimes strictly replicate the trading venues' order book, to ensure that their quotes are in line with market conditions. Others have tools to compare their quotes with on-venue pricing with the same objective.
189. Furthermore, SIs stressed that they might aggregate multiple sources of pricing (e.g. RMs, MTFs and OTFs) in order to ensure that their quotes represent the best available prices. The responses also highlighted that best execution policies, internal pricing policies, as well as pricing models (which are audited and authorised) ensure that quoted prices reflect the current market conditions.
190. Finally, some mentioned that when the SI is a market-maker on a product they have issued, the quote itself is the prevailing market price.
191. Overall, ESMA considers that undertaking a full quantitative assessment at this stage would create disproportionate costs (both to market participants and ESMA) compared to the potential benefit. This position might be revisited upon the establishment of a (pre-trade) consolidated tape, as suggested in some responses to the CP, as the data necessary to fulfil this mandate would then likely be available in the appropriate shape.
192. As of today, relying on the qualitative feedback provided by SIs, ESMA considers that SIs appear to have procedures and systems in place to ensure that their quoted prices are in line with the prevailing market conditions. ESMA further notes that there is no evidence or complaint from SI users pointing to a different conclusion. ESMA will continue to monitor the relation between quoted prices and prevailing market conditions as part of its overall supervisory convergence mandate, e.g. via qualitative surveys encompassing a larger set of SIs.

## 5 Summary of proposals

193. ESMA proposes to:
- 1) Allow SIs to withdraw quotes at any time (and not only under “exceptional market conditions”), by amending Article 18(3) of MiFIR.
  - 2) Simplify the requirements applicable to quotes in liquid non-equity instruments, by deleting in MiFIR: Article 18(5), the first paragraph of Article 18(6) and Article 18(7);
  - 3) Set out at Level 2 the requirements for SIs in non-equity instruments for publishing their quotes, via an amendment to Commission Delegated Regulation (EU) No 2017/567,



which would extend to non-equity instruments the requirements currently applicable to equity instrument (Article 13 of Commission Delegated Regulation (EU) No 2017/567);

- 4) Simplify the requirements applicable to quotes in illiquid non-equity instruments, by deleting Article 18(2) of MiFIR.

## 6 Annexes

### 6.1 Annex 1: Feedback from the Consultation Paper

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

With two exceptions, none of the respondents considered it necessary to further clarify what a firm quote is. Most of them considered that there was a clear understanding among market participants, SIs and clients of what a firm quote was.

Many respondents were also concerned that introducing a new definition that would not be aligned with market practices would be a source of additional costs and would further complicate the rule.

A couple of respondents said they understood a firm quote to be an executable quote.

One responded that there is sufficient clarity in the market as to the meaning of a firm quote, in particular given ESMA’s Q&A on MiFID II and MiFIR Transparency topics.

One respondent referred to the SSR of 2012 where “firm quotes” are mentioned, without having required any need for further clarification.

The minority view was expressed by a trading venue that supported clarifying that all quotes provided by SIs that contain all necessary information in order to agree on a trade have to be considered a “firm quote” to help levelling the transparency regime playing field between SIs and multilateral trading venues. Another stakeholder noted that “firm quote” allows for multiple interpretations, with each SI adopting different conventions that best suit their needs but did not explicitly call for a clarification of the term.

**Q 2: (For SI clients) As a SI client, do you have easy access to the quotes published, i.e. can you potentially trade against those quotes when you are not the requestor? Do you happen to trade against SIs quotes when you are not the initial requestor? How often? If it varies across asset classes, please explain.**

Seven stakeholders responded from an SI client perspective. About half of them considered that the market has no need for pre-trade data from SIs with respect to non-equity instruments. Institutions/clients typically have a business relationship with a limited number of SIs, and no one would be willing to bear the costs of entering into a new relationship just to benefit from a “better quote”. As regards the quotes published by SIs they already have a relationship with, clients will always ask directly for a quote as the quote is priced considering the characteristics



of each client. In addition, clients turn to SIs for specific demands, which are of no use for other clients.

Some stakeholders stressed that pre-trade quotes are indeed difficult to access due to the variety of channels that can be used but even easier access would not make much difference considering their limited usefulness. Those stakeholders further stressed that pre-trade transparency is only a burden that prevent small and medium-sized firms from registering as SIs, thereby reducing market competition. Two respondents noted that quotes are indeed available but confirmed that clients would rather trade on published axes and inventory rather than MiFIR based SI quotes.

One buy-side firm noted that most of the bilateral negotiations seem to be carried out via voice or via Bloomberg chat, without knowing most of the time whether trading with the counterparty takes place under the SI regime, so pre-trade transparency is not helpful.

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

Apart from three respondents, all stakeholders provided negative feedback on the non-equity SI pre-trade transparency framework for liquid instruments based on multiple grounds.

A large majority of respondents stressed that there is no demand for SI quotes due to the bespoke nature of each request. Buy-side firms (market participants/institutional investors) continue to use consistently updated market data streams for the purposes of price discovery, together with axes and runs published by dealers as a source of information for price discovery. Quotes just disappear in a black hole whilst being a burden for SIs.

One stakeholder further stressed that there is no point in having as a regulatory objective to have the quotes accessed by other clients due to their bespoke nature. Having those quotes used for price discovery would require clients to build multiple data feeds with their SIs, which they will not do. According to this respondent, SI quotes may only be useful in the context of a pre-trade consolidated tape. Another respondent noted that quotes are made public almost at the same time as the resulting transactions. It is therefore almost impossible to trade on those quotes, which are difficult to access in the first place. Only the more sophisticated market players may take advantage of those quotes for their own trading and pricing strategies. Many respondents stressed that pre-trade is anyhow limited to a very small number/percentage of instruments qualifying as ToTV that are liquid.

Based on the above, some respondents suggested deleting Article 18 to focus on post-trade transparency.

Many respondents expressed concerns about the scope of pre-trade transparency rules for OTC derivatives and the uncertainty/burden arising from the ToTV concept which should be reconsidered. A couple of respondents suggested disapplying pre-trade transparency rules to all OTC derivatives.





Other concerns expressed relate to bond liquidity misclassification, to the need to review pre-trade transparency calibration for some derivatives (e.g. IR options, commodity derivatives), to increase SI thresholds to concentrate on larger, more meaningful SIs and to disconnect SI status from post trade transparency rules.

Two respondents noted that the CP did not evaluate the level of pre-trade transparency being provided by SIs for package transactions and call for an amendment to Section 4, Question 4(c) of ESMA's Q&A on MiFID II and MiFIR transparency topics on this topic, which leaves too much room for circumvention by SIs.

One respondent insisted on the poor data quality of the pre trade data and suggested that additional level of standardization of ISINs, CFI codes etc. would help addressing the issue.

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

Seven stakeholders responded to this question. Most respondents noted most non-equity instruments are illiquid and that most SIs benefit from a waiver. Therefore, no quote is available to clients. A couple of stakeholders stressed that they have no interest in the bespoke quotes provided to another client and that the focus should be on post-trade transparency, also referring to their responses to Question 2 and 3.

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

Half of the respondents to this question benefitted from an illiquid pre trade transparency waiver, while one did not.

All respondents not benefitting from the waiver stressed that the cases where they have been asked by another client to disclose a quote in illiquid instruments were rare or negligible. Like for liquid instruments, clients do not have an interest in a quote that would have been tailor made to another client request, and even more so in illiquid instruments.

One respondent mentioned the risks associated with "quote fishing" practices by those with no intention to trade that could compromise the trading strategies and hedging abilities of the parties involved in a bilateral transaction.

**Q 6: Do you consider that there is an unlevel playing field between SIs and multilateral trading venues active in non-equity instruments, in particular with respect to pre-trade transparency? If so, please explain why and suggest potential remedies.**

The vast majority of stakeholders who responded to this question either directly or through their trade association were banks/sell side firms. They stressed that MiFIR recognises the need for transparency requirements to be calibrated for different types of financial instruments



taking into account the interest of issuers and market liquidity, hence the different rules that apply to trading venues and SIs.

According to those respondents, SIs are at a disadvantage compared to trading venue because they have to give access to their quotes to other clients, firm quotes 'available to other clients' and 'enter into transactions' under the published conditions (although acknowledging that they have managed risks through their commercial policy). Furthermore, their quotes are not anonymous. Article 18 should therefore be amended to level the playing field between SIs and trading venues by deleting Article 18(6), (7) as well as (5). Another source of unlevel playing field quoted is the burden arising from the uncertain application of the SI regime to non-ToTV instruments. Sell-side firms also anticipated the trading venues' responses by stressing that the concerns arising from network of SIs are only relevant for the equity space, not for non-equities.

Trading venues considered that they were at a disadvantage compared to SIs. They first noted that the distinction between bilateral trading and multilateral trading is being blurred due the setting up of network of SIs, which ESMA is invited to further look into. It was also noted that some SIs do not comply with the prohibition, when dealing on their own account, from entering into matching arrangements with entities outside their group to carry out de facto riskless back-to-back transactions through arrangements with third party liquidity providers. Trading venues also claimed that BCN trading volumes under MiFID I have shifted to SI reported trading instead of moving to multilateral trading venues, which demonstrates the failure of MiFID II to move more trading to lit venues. This analysis was also supported by another stakeholder who pointed at increased complexity and market fragmentation under MiFID II. To address the issues identified, some trading venues suggested mandating trading below LIS on RMs, MTFs, and OTF (with a 100,000 EUR threshold for bonds and securitised derivatives).

One trading venue further noted the unlevel playing field arising from the fact that it is unclear whether SIs must formally apply for a waiver, whereas TV waivers as subject to in-depth scrutiny by NCAs and ESMA.

**Q 7 (for SIs who are also providing liquidity on trading venues): What are the key factors that determine whether quote requesters (your clients) want to receive the quote through the facilities of a trading venue or through your own bilateral trading facilities?**

Most respondents quoted the size of the trade and the liquidity of the instrument as key differentiating factors for trading on an SI or a trading venue. Large size trade in low liquidity instruments would be executed with SIs, while trading venue would attract trades in more liquid instruments such as equity derivatives or retail bond trading. According to those respondents, trading with SIs in large size minimise the risk of information leakage. Clients would also turn to SIs for illiquid instruments where no pricing is available, when the trade is part of a complex trading strategy or in times of market volatility/uncertainty. Some respondents also referred to lower execution fees and trading costs, and sometimes settlement costs, compared to on-venue trading.

Some respondents noted that trading venues offer the benefit of a fast transaction process and Straight Through Processing, which is valuable for smaller trades.



One respondent has noted an increase in liquidity provision by market makers/SIs on trading venues as trading on trading venues makes it easier to comply with regulatory requirements (transparency, transaction reporting). Trading on trading venues also facilitates compliance with best execution requirements.

**Q 8: What is your view on the proposal to simplify the requirements in relation to SI quotes in liquid non-equity instruments under Article 16(6) and 18(7)?**

Apart from three stakeholders, all respondents supported the deletion of Article 18(6) and 18(7), noting that the requirement to trade with other clients on the quote displayed does not apply to dealers/market makers on trading venues. A couple of respondents further noted that the deletion of Article 18(6) and 18(7) will just result in the current de facto situation implemented through the commercial policies of the majority of SIs, building as well on ESMA's Q&A that allows the SI to trade on the displayed quote with one client only. Some respondents commented or reiterated earlier comments that the quote provided by an SI responds to a specific client's requests and therefore cannot be extended to other clients

Some respondents suggested to also delete Article 18(5). If the SI is no longer required to trade with other clients at the displayed quote, then there is no need for the SI to "give access" to its quotes. In their views, the publication of the quote would be enough. Two stakeholders further suggested to get rid of pre-trade transparency requirements altogether for SIs and focus on post-trade transparency.

The two trading venues that responded to the question were opposed to the deletion of Article 18(6) and 18(7). One trading venue stressed that although trading on the quote displayed with only one client may indeed be the actual SI behaviour, this is not in line with the MiFID objectives. Deleting Article 18(6) and 18(7) would make SIs like any other investment firm while qualifying as execution venues. According to this trading venue, the requirement to trade on the quote published with other clients when that quote is below SSTI allows for appropriate risk management by SIs. The other trading venue considered that a quote against which only a subset of a SI's clients is entitled to trade decreases transparency and liquidity available to the overall market. A quote provided to one client, without the requirement to allow other clients to participate in the execution at this price is bilateral trading and must be avoided below LIS thresholds.

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

A majority of responded supported the deletion of Article 18(2), which is considered overly complex and providing little benefit. However, most of those respondents could not support Option 3 as they did not understand what the supervisory convergence tool mentioned in this Option was referring it or were concerned by the additional burden thus created for NCAs and SIs. Option 1 ("do nothing") therefore appeared as their fall-back solution. Some respondents supported Option 1 (do nothing) but nonetheless felt attracted by the deletion of Article 18(2) and said they could consider Option 3 if further clarity was provided on the supervisory convergence tool considered. A couple of respondents were just satisfied with the "do nothing approach".



Some respondents supported Option 3 provided that the supervisory convergence tool mentioned does not prove more burdensome for SIs than the existing Article 18(2) requirements. One banking association agreed with Option 3 provided that those tools are limited to the monitoring of the instruments' classification by SIs (liquid versus illiquid instruments) based on the list of liquid instruments created and periodically updated by ESMA itself. In contrast, one respondent understood that under Option 3, SIs would now oversee determining the liquidity status of non-equity instruments instead of ESMA, which he did not agree with.

Two trading venues were the only stakeholders supporting Option 2 (align the regime for liquid and illiquid instruments, with a waiver for illiquid instruments) in support of more transparency. They also both understood that Option 2 would include a formal waiver application for SIs, which they supported to reduce the unlevel playing field with multilateral trading venues for which the difference in the transparency regime for liquid and illiquid instruments is managed through the application for related waiver for illiquid instruments.

One trading venue further referred to ESMA's consultation paper on equity instruments and supports the approach to remove the pre-trade transparency waivers (non-liquid waiver) except for LIS and OMF also for bonds and securitized derivatives.

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

Stakeholders were split as to whether Level 2 should be amended to further specify the publication arrangements for SI quotes.

About half of the respondents, including banking federations, did not support the proposal to specify in Commission Delegated Regulation (EU) No 2017/567 the arrangements to be met by SIs for publishing quotes, in line with the arrangements to be met for the publication of quotes in equity instruments. The arguments put forward are the lack of convincing regulatory arguments to do so and the additional costs and administrative burden entailed.

The other half supported ESMA's proposal to provide more clarity and legal certainty. However, a couple of them noted that there are elements of Article 13 which relate to equities and are not readily applicable to the bond market and recommended that ESMA reviews Article 13 to ensure that its provisions are practicable in respect of the bond markets.

Three stakeholders (of which one in the first general comment section) noted that the CP suggested to further clarify the concept of exceptional circumstances under which an SI may suspend providing quotes but that there was no question asked on this proposal. One respondent agreed with the proposal. Another one considered that the clarification was not necessary as pre-trade transparency only applies anyway when the SI agrees to provide a quote. The last one stressed that it was important not to copy paste the rules for equities but to ensure that those circumstances are relevant for the different parts of the non-equity market. On many bond and derivatives markets, liquidity is provided by SIs that trade against own account and the exceptional circumstances should relate to distressed situations where that is no longer possible.



Separately, a couple of respondents expressed concerns that SI data (the published prices) are considered by the trading venues to be “unlawful” derived data (from the trading venues own published prices) infringing on the trading venues intellectual property rights to those prices. At present, many venues do not allow SIs to publish this information on the SIs’ webpages or through an APA unless they pay the venues for the data, i.e. SIs need to pay venues for complying with their legal requirements as SIs under MiFID/MiFIR. In practice, this has forced SIs not only to restrict the access to the information on their webpages to a limited number of logged in clients but also to pay unjust fees for the SIs’ compliance with MiFIR. Those respondents suggested that the Commission and ESMA further investigate the matter.

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

Most stakeholders commented that ESMA’s finding were in line with industry expectations, that there was no evidence of circumvention of the pre-trade transparency regime via the SSTI thresholds and the levels of the SSTI thresholds were appropriate.

According to respondents, the dichotomy identified in the data, between on one side certain SIs mainly quoting below SSTI; and on the other side other SIs mainly quoting above SSTI, reflects the differences between SIs in terms of client base. SIs quoting mainly below SSTI typically serve retail clients, for which pre-trade transparency is important as they may have difficulties to gauge market values. On the other side, SIs quoting mainly above SSTI are likely to serve more active clients, who can rely on various sources of market data and have access to relevant liquidity providers (hence for which pre-trade transparency is of less importance). In that sense, respondents considered that the pre-trade transparency regime for SI was appropriately framed.

One stakeholder commented that bond trading remained opaque and that there was no increase in transparency following MiFIDII/MiFIR, as most trading activity occurs OTC or between bank/SI and retail clients. According to this stakeholder, there should be an obligation to trade bonds below LIS in transparent multilateral markets. This would significantly reduce market fragmentation, add liquidity and increase pre- and post-trade transparency, particularly for retail investors.

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

The responses to this question (on derivatives) were largely the same as those collected in Question 11 (on bonds): for derivatives markets, most stakeholders commented that ESMA’s finding were in line with industry expectations, that there was no evidence of circumvention of the pre-trade transparency regime via the SSTI thresholds and the levels of the SSTI thresholds were appropriate.

Several stakeholders also agreed with ESMA’s statement in para. 89 of the CP, i.e. that the level of the SSTI thresholds were so low for some asset classes that by construction almost any quote would be above SSTI. In those instances, the comparison between trade flows above and below the SSTI thresholds is somehow meaningless. Some suggested to remove the SSTI thresholds and align them with the levels of the LIS.



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

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

The responses received overall highlighted that there is no simple or obvious solution available in order to fulfil ESMA's mandate. With respect to the possible use of RTS 27 data, no respondent recommended the use of such data. The most common reasons for which RTS 27 data is considered as unsuitable are: (i) the fact that data is published in very diverse formats, and trade level data is published only in some narrow scenarios; (ii) the scope does not overlap; (iii) RTS 27 data is not used by clients of SIs; (iv) it is not suitable for FX, as FX data is published quarterly and most of the fields are not applicable; (v) there is an absence of an obligation to report quotes in those instances where they actually result in no trade entailing that a mismatch may exist between quoting activity and trading activity.

One respondent suggested that the publication of RTS 27 data shall be harmonised both in terms of content and format.

The majority of respondents highlighted that APA data is broader than other sources and could be useful to understand if SI quotes reflect prevailing market conditions. Nevertheless, responses also highlighted that there could be shortcomings also in the use of APA data as: (i) not all SIs use APAs; (ii) APAs are not required to aggregate data; (iii) SIs are not subject to PTT obligations when they quote above SSTI.

One respondent suggested standardising the format of submission of data for APAs.

Few respondents suggested that ESMA discusses with market participants the relation between quotes and prevailing market conditions, recommending a qualitative approach rather than a quantitative one. Furthermore, few respondents argued that the introduction of a consolidated tape (CTP) could help to monitor whether quoted and traded prices reflect prevailing market conditions. Nevertheless, one respondent highlighted that the introduction of a CTP could worsen data availability problems if governance and operations requirements are not calibrated adequately, because consumers would use inadequate data.

Few participants suggested that ESMA proceeds with a data request to SIs and TVs. This would entail a request of data to SI for selected time slots, and a request of data to TVs.

## **6.2 Annex 2: Legal Mandate**

Article 19(1) of MiFIR:

### **Monitoring by ESMA**

1. Competent authorities and ESMA shall monitor the application of Article 18 regarding the sizes at which quotes are made available to clients of the investment firm and to other market participants relative to other trading activity of the firm, and the degree to which the quotes reflect prevailing market conditions in relation to transactions in the same or similar financial instruments on a trading venue. By 3 January 2019, ESMA shall submit a report to the Commission on the application of Article 18. In the event of significant quoting and trading activity just beyond the threshold referred to in Article 18(6) or outside prevailing market conditions, ESMA shall submit a report to the Commission before that date.

## 6.3 Annex 3: Data collection exercise

### 6.3.1 Quality of reference data

194. In terms of quality of the reference data, ESMA performed some consistency checks. Minor adjustments were made to the data submitted when such adjustments were straightforward as described below.
195. In relation to the LIQUIDITY flag, ESMA changed the liquidity flag as reported by SI based on the sub-asset class reported, in the following cases:
  - Securitised derivatives should all be LIQUID as per Article 13(1)(a)(i) of RTS 2;
  - Equity derivatives different from “Other Equity derivatives”, “Swap” and “Portfolio swap” should all be LIQUID as per Table 6.1 of Annex III of RTS 2
  - SFP should all be ILLIQUID as per the transitional transparency calculations
196. Other sub-asset classes have a fixed liquidity status (e.g. all FX derivatives are illiquid, all derivatives in the “Other” category are illiquid) but there were no instances of misreporting for those cases.
197. In relation to the field “WAIVER”, which indicates whether the quotes are subject to a waiver under Article 18(3): since this waiver is only available to quotes in illiquid instruments, ESMA changed the flag from “WAIVER” to “NA” on all liquid instruments.
198. SI have been asked to segment the data provided based on whether the instrument was traded on a trading venue (ToTV) or not. For the analysis presented in the CP this breakdown has not been considered for the following reasons:
  - For bonds (including ETCs and ETNs) as well as interest rate derivatives, virtually all volumes have been reported as ToTV hence the exclusion of “non-ToTV” data would not have made a difference to the analysis;
  - For other derivatives on the contrary, the exclusion of “non-ToTV” data would have led to a significant cut in an already limited sample of data and would have rendered any analysis quite difficult. Given that this CP does not address the question of the ToTV



definition, and that whether an instrument is ToTV may be subject to changes over time, it has been considered reasonable to assess the data irrespective of the ToTV status.

### 6.3.2 Quality of quantitative data

199. In terms of quality of the quantitative data, the following data analysis should be understood with the following caveats in mind:

- Only a subset of SIs has been invited to provide data even though the overall number of SIs who participated in the exercise is meaningful (about 1/3 of the total SI population);
- SIs who reported data flagged that retrieving the data ex post as framed in the data request has been a complex exercise and they have not always been able to retrieve data for all their activity.
- Some SIs have not reported data in relation to asset classes that are illiquid (e.g. FX).
- The assumptions and methodologies that SIs have used to aggregate quoting data are not always known and are likely to differ from one SI to another. This is relevant for SIs that are streaming quotes on a continuous basis or reproducing the order book of a trading venue. Some have calculated quoted volumes by considering each change of price/quantity as a new quote, leading to extremely high quoted volumes (which are out of proportion compared to their traded volumes, or to the quoted volumes of other SIs). Other SIs have merged quotes with identical quotes details within a specific time period.

200. ESMA also performed a consistency analysis between (1) the traded volumes reported in the ad-hoc data request; and (2) those reported to FITRS by the same SIs over the same period. For bonds, the results turned out satisfactory with a high consistency rate<sup>18</sup>, with however non-negligible differences between SIs (some reported higher volumes in FITRS, others reported higher volumes in the ad-hoc data request). In addition, the total volumes reported under the ad-hoc data request represented roughly 60% of the total FITRS volumes reported by all SIs over the same time period, indicating a reasonable coverage of the ad-hoc data sample.

201. For interest rate derivatives and securitised derivatives, the consistency rate as described above also turned out reasonable however the coverage was much lower than in the case of bonds. For equity derivatives, the number of common SI between the two datasets was too small to come up with a meaningful comparison.

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<sup>18</sup> Sum of (Volumes reported under the ad-hoc data) divided by Sum of (Volumes reported in FITRS) for the month of June 2019, across SI that have reported in both systems.





202. Such consistency checks on *quoted* volumes were not possible as no other source of data could be identified for the comparison.

203. Taking the above considerations into account, another possible way forward would have been to re-specify the data request and gather data from additional SIs. However, having heard the feedback from SIs on the complexity of retrieving the data already provided, as well as the deadline for providing the report to the Commission, ESMA considered that this would have been disproportionate and lengthy, and opted instead to work on the basis of the data as provided, subject to the corrections and caveats mentioned above.