European Securities and Markets Authority

Consultation Paper

RTS 2 Annual Review

12 May 2021 | ESMA70-156-4233

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

- respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by 11 June 2021.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Data protection'.

Who should read this paper?

This document will be of interest to all stakeholders involved in the securities and derivatives markets. It is primarily of interest to firms that are subject to MiFID II and MiFIR – in particular, investment firms and credit institutions performing investment services and activities and trading venues. This paper is also important for trade associations and industry bodies, institutional and retail investors and their advisers, and consumer groups, as well as any market participant because the MiFID II and MiFIR requirements seek to implement enhanced provisions to ensure the transparency and orderly running of financial markets with potential impacts for anyone engaged in the dealing with or processing of financial instruments.

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Acronyms used

CFD	Contracts For Difference
CP	Consultation Paper
ESMA	European Securities and Markets Authority
ETC	Exchange Traded Commodity
ETN	Exchange Traded Note
ILQ	Illiquid
LIS	Large in scale
MiFID I	Directive 2004/39 of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directive 85/611/EC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC
MIFID II	Directive 2014/65/EU of the European Parliament and the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU
MiFIR	Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012
MTF	Multilateral trading facility
NCA	National competent authority
OJ	Official Journal
OTF	Organised Trading Facility
RFQ	Request For Quote trading system
RM	Regulated market
RTS 2	Commission Delegated Regulation (EU) 2017/583 of 14 July 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards on transparency requirements for trading venues and investment firms in respect of bonds, structured finance products, emission allowances and derivatives.
SI	Systematic internaliser
SFPs	Structured Finance Products

1 Executive Summary

Reasons for publication

Under Article 17 of RTS 2 ESMA is required to analyse whether it is appropriate to move to the following stage in terms of transparency with regard to (i) the average daily number of trades (ADNT) threshold used for the quarterly liquidity assessment of bonds, and (ii) the trade percentile used for determining the pre-trade SSTI thresholds. If that move is deemed appropriate, ESMA shall submit to the Commission an amended version of the regulatory technical standard adjusting the thresholds for the relevant parameters. This consultation paper (CP) covers this mandate.

Contents

Section 2 deals with the review of the setting of (i) one of the parameters to assess bond liquidity and (ii) the percentile used to calculate the pre-trade SSTI thresholds for bonds and other non-equity instruments.

Next Steps

ESMA will consider the feedback it receives to this consultation in Q2 2021 and expects to publish a final report and submit, if necessary, draft technical standards to the European Commission for endorsement in July 2021.

Disclaimer

Data analyses based on data from the Financial Instruments Transparency System (FITRS) are based on data provided by trading venues, approved publication arrangements (APAs) and National Competent Authorities.

Therefore, ESMA has to rely on those reporting entities in respect of the completeness and accuracy of the submitted data. Delayed or incorrect provision of the relevant data may affect the completeness and accuracy of the information.

2 Introduction

1. Article 9(5)(d) of MiFIR required ESMA to develop draft regulatory technical standards to specify the pre-trade SSTI thresholds for all non-equity instruments. The system developed was based on annual recalibrations.

2. More specifically, the MiFIR transparency regime for non-equity instruments is currently subject to a four-stage phase-in for both, the determination of the liquidity status of bonds (based on the criterion 'average daily number of trades') and the level of the pre-trade SSTI threshold for bonds and most derivatives (based on trade percentiles). The details of the phase-in regime are set out in Article 17 of RTS 2.

3. Article 17(4) of RTS 2 requires ESMA to submit to the Commission an assessment of the operation of the thresholds for the liquidity determination of bonds and the trade percentiles determining the pre-trade SSTI-threshold by 30 July of each year, starting on 30 July 2019, until the final stage of the phase-in has been reached.

4. According to Article 17(5) of RTS 2 ESMA should take the following factors into account for such assessment:

    - The evolution of trading volumes in non-equity instruments covered by the pre-trade transparency obligations;
    - the impact on liquidity providers of the percentile thresholds used to determine the SSTI; and,
    - any other relevant factors.

5. Where, based on this assessment, ESMA considers that the thresholds should be adjusted to the next stage, it should submit an amended version of RTS 2 to the Commission as specified in Article 17(6) and 17(8) of RTS 2.

6. In 2020, ESMA published the RTS 2 Annual Report[1] where ESMA proposed to move to stage 2 for the liquidity assessment of bonds. The analysis revealed that moving to stage 2 would result in only a marginal increase in market transparency. ESMA's analysis did not reveal risks that such a move might result in liquidity providers retreating from the market or trading activity moving from trading venues to OTC trading. Most stakeholders responding to the consultation were supportive of the move to stage 2.

7. As far as the move to stage 2 for the pre-trade percentile for the SSTI threshold is concerned, ESMA concluded last year that for non-equity instruments other than bonds, the move to stage 2 was premature mainly due to data quality issues and because the first partial publication of the annual calculations for derivatives was done only in 2020. However, considering the limited pre-trade transparency available in bond markets and

[1] esma70-156-3300_mifid_ii_mifir_annual_report_under_commission_delegated_regulation_eu_2017.583_rts_2.pdf (europa.eu)

the availability of pre-trade waivers other than the SSTI, it was concluded that the move to stage 2 for the pre-trade SSTI threshold for bonds was appropriate and that such move would not negatively impact liquidity providers.

8. The European co-legislators approved ESMA's proposal to move to the second stage of the phase-in for bonds[2]. This second stage is applying since 15 April 2021 to the thresholds of both the liquidity determination of bonds and the pre-trade SSTI of bonds.

9. Despite stage 2 not yet being applied in the course of last year, the assessment this year should not be delayed as ESMA is required to perform an annual assessment by 30 July of each year and, as the legislative process to be completed will always imply a certain delay before the next stage of the phase-in will apply in practice.

10. In addition, ESMA would like to highlight that the RTS 2 Annual Report published in 2020 already highlighted that the increase in transparency in the market with the move to stage 2 for the parameter of the liquidity assessment would in all likelihood only be marginal and that the overall level of transparency would remain limited. Moreover, no significant negative impacts on the exposure of liquidity providers due to the slightly increased transparency could be identified, neither at the time when performing the analysis nor until spring 2021. This assessment was supported by the large majority of stakeholders replying to the consultation last year.

11. Therefore, this CP addresses the following questions:

- Should the average daily number of trades used to determine if a bond has a liquid market be set at 7 as provided for at stage 3 (instead of 10 as provided for at stage 2) (section 2.1)?

- Should the trade percentile to determine the SSTI pre-trade threshold for bonds be set to 50% as provided for at stage 3 (instead of 40% as provided for at stage 2) (section 2.2)?

- Should the trade percentile to determine the SSTI pre-trade threshold be set to 40% as provided for at stage 2 (instead of 30% as provided for at stage 1) for SFPs, interest rate derivatives, commodity derivatives, credit derivatives, C10 derivatives, CFDs, emission allowances and emission allowance derivatives (section 2.2)?

[2] Commission delegated regulation (EU) 2021/529 of 18 December 2020 establishing regulatory technical standards amending Delegated Regulation (EU) 2017/583 as regards adjustment of liquidity thresholds and trade percentiles used to determine the size specific to the instrument applicable to certain non-equity instruments (OJ L 106, 26.3.2021, p.47).

2.1 Average daily number of trades for the determination of bond liquidity

A. Analysis

12. The quarterly liquidity assessment for bonds (except ETCs and ETNs) is currently performed on the basis of three parameters:

- Average daily notional amount greater than or equal to EUR 100,000;
- Average daily number of trades greater than or equal to 10[3];
- Percentage of days traded over the period considered greater than or equal to 80%.

13. Under the different stages of the phase-in, the parameters for the average daily notional amount and the percentage of days traded would remain unchanged, but the average daily number of trades would be gradually reduced from 15 trades/day under stage 1 to 2 trades/day under stage 4 (see Table 1). When moving from stage 2 to stage 3, the average daily number of trades would be reduced from 10 to 7.

TABLE 1 LIQUIDITY DETERMINATION OF BONDS (EXCEPT ETCS AND ETNS)

Average daily notional amount	Average daily number of trades				% of days traded
EUR 100 000	Stage1	Stage2	Stage3	Stage4	80%
	15	10	7	2	

14. In order to assess the move to stage 3, ESMA has performed an analysis similar to that of last year[4]. In particular, Table 2 below displays the number of bonds considered to be liquid in the liquidity assessments from 2020Q1 to 2020Q4 using the stage 2 criterion (i.e. average daily number of trades equal to 10). This simulation includes UK-single listed instruments and data related to the trading activity executed in the UK across all bonds.

15. From Table 2 it is evident that most of the bonds classified as liquid are sovereign bonds, followed by corporate bonds. The analysis provided hereafter will focus on the absolute numbers of bonds that will be deemed liquid with the move to stage 3 rather than on the percentual increase to avoid misinterpretation due to changes of the total number of bonds that might occur over the year.

[3] The first liquidity assessment of bonds based on stage 2 will occur on 1 May 2021.
[4] The lower number of bonds compared to last year is due to the delisting of a relevant number of bonds in Q4 2019.

Table 2 Liquid Bonds per bond type, 2020Q1-2020Q4, based on the application of stage 2, with UK data

	2020Q1	2020Q2	2020Q3	2020Q4
Liquid	**1,463**	**1,211**	**1,042**	**922**
of which				
Convertible	8	6	4	2
Other public	71	40	44	30
Sovereign	667	584	508	514
Covered	23	13	14	6
Corporate	596	488	395	313
Other	79	64	63	41
Illiquid	**45,678**	**45,036**	**46,198**	**37,155**
Total	**47,141**	**46,247**	**47,240**	**38,077**
% of liquid bonds	*3.10%*	*2.62%*	*2.21%*	*2.42%*
Number of liquid bonds multi-listed in the EU and the UK	*1,431*	*1,183*	*1,016*	*919*
Number of illiquid bonds multi-listed in the EU and the UK	*32,123*	*33,131*	*34,402*	*32,328*

Source: FITRS

16. Table 3 provides the same results as the previous table but using the stage 3 criterion (i.e. average daily number of trades equal to 7). The consequence is that, compared to stage 2, the number of liquid bonds under the application of stage 3 would have increased in each quarter of 2020.

Table 3 Liquid Bonds per bond type, 2020Q1-2020Q4, based on the application of stage 3, with UK data

	2020Q1	2020Q2	2020Q3	2020Q4
Liquid	**2,152**	**1,792**	**1,440**	**1,263**
of which				
Convertible	23	15	7	3
Other public	98	53	59	45
Sovereign	868	750	655	647
Covered	44	29	24	6

Corporate	959	813	588	481
Other	131	109	91	65
Illiquid	**44,989**	**44,454**	**45,801**	**36,813**
Total	**47,141**	**46,246**	**47,241**	**38,076**
% of liquid bonds	*4.57%*	*3.87%*	*3.05%*	*3.32%*
Change of the number of liquid bonds compared to S2	*689*	*581*	*398*	*341*
Number of liquid bonds multi-listed in the EU and the UK	1,313	1,756	1,405	1,259
Number of illiquid bonds multi-listed in the EU and the UK	31,450	32,558	34,013	31,988

Source: FITRS

17. ESMA would like to highlight that the data used for the bond liquidity assessment from 1 May 2021 will exclude the data from the UK, as a consequence of Brexit.

18. Therefore, Tables 4 and 5 provide the same results, as Tables 2 and 3, excluding the data from the UK. Before moving to the results, it is important to stress that FITRS (the Financial Instruments Transparency System) does not provide data on a transaction basis with the identification of the counterparties. Therefore, the exclusion of the UK data consists of excluding the instruments which were single listed in the UK over the observation period. For multi-listed instruments, the trading activity recorded on UK trading venues, executed by UK systematic internalisers and OTC reported by UK APAs were also excluded. This methodology is the most conservative approach and is expected to underestimate the trading activity recorded in the EU after Brexit since UK APAs were also used by EU entities.

19. ESMA considers that these two analysed scenarios should therefore represent the maximum and the minimum changes that could be expected.

TABLE 4 LIQUID BONDS PER BOND TYPE, 2020Q1-2020Q4, BASED ON THE APPLICATION OF STAGE 2, WITHOUT UK DATA

	2020Q1	*2020Q2*	*2020Q3*	*2020Q4*
Liquid	*605*	*414*	*369*	*473*
of which				
Convertible	*1*	*1*	*0*	*0*
Other public	*44*	*23*	*17*	*18*
Sovereign	*239*	*206*	*185*	*240*
Covered	*2*	*0*	*1*	*1*

Corporate	*262*	*141*	*133*	*174*
Other	*40*	*32*	*23*	*25*
Illiquid	*22,876*	*23,375*	*23,123*	*28,126*
Total	*23,481*	*23,789*	*23,492*	*28,599*
% of liquid bonds	*2.58%*	*1.74%*	*1.57%*	*1.65%*

Source: FITRS

TABLE 5 LIQUID BONDS PER BOND TYPE, 2020Q1-2020Q4, BASED ON THE APPLICATION OF STAGE 3, WITHOUT UK DATA

	2020Q1	*2020Q2*	*2020Q3*	*2020Q4*
Liquid	*808*	*583*	*542*	*668*
of which				
Convertible	*1*	*1*	*0*	*0*
Other public	*58*	*26*	*25*	*31*
Sovereign	*318*	*276*	*264*	*324*
Covered	*4*	*0*	*2*	*1*
Corporate	*357*	*225*	*208*	*265*
Other	*49*	*40*	*30*	*32*
Illiquid	*22,674*	*23,206*	*22,950*	*27,931*
Total	*23,482*	*23,789*	*23,492*	*28,599*
% of liquid bonds	*3.44%*	*2.45%*	*2.31%*	*2.34%*
Change of the number of liquid bonds compared to S2	*203*	*169*	*173*	*195*

Source: FITRS

B. Conclusions and Proposals

20. The analysis above highlights that the current level of real-time pre- and post-trade transparency remains very low, as represented by the limited number of bonds subject to real-time transparency. Rather the transparency regime is still mainly driven by a high share of illiquid instruments which are not subject to real-time transparency.

21. One of the key objectives of MiFID II/MiFIR was to increase transparency and thereby improve the functioning of financial markets. In particular, a high level of real-time trade transparency is essential to provide investors with a comprehensive view on investment opportunities across the Union. This is of particular importance for financial institutions operating on a cross-border basis in a fragmented market environment with many competing execution venues.

22. Transparency is hence a key attribute of well-functioning markets, and, if appropriately calibrated, more transparent markets attract more liquidity thereby triggering a reinforcing feedback cycle, ultimately translating into lower trade execution costs. This can also be observed in other jurisdictions with a higher level of transparency, such as the regime for bond transparency in the US (TRACE) where the large majority of transactions are subject to real-time post-trade transparency. While initially there were concerns that such a highly transparent regime might expose liquidity providers to undue risk and thereby impair market liquidity, in practice these concerns have not materialised and investors have largely benefitted from the high level of transparency.

23. Moreover, a higher level of transparency assists firms in making sound risk management decisions. Furthermore, as markets becomes more liquid, the data input and output increase, ultimately fostering digitalisation and competition which also turn into better pricing for investors.

24. It appears doubtful that market participants will be able to reap the above benefits in the current market environment characterised by a very low level of transparency. For these reasons, ESMA already recommended in 2015 to apply the thresholds of stage 4 for the liquidity assessment of bonds.

25. As can be seen from Tables 4 and 5 the impact of moving to stage 3 would be limited and still only a very limited share of bonds would be considered liquid and therefore subject to real-time pre- and post-trade transparency. Moving to stage 3 would result on average in less than 3% of bonds being considered as liquid compared to about 2% of liquid bonds currently under stage 2. For comparison, ESMA estimates that about 2000 bonds (i.e close to 10% of all traded bonds) would be considered liquid under stage 4.

26. Moreover, orders and transactions that are large in scale (LIS) or above the SSTI will continue to be eligible for waivers and deferrals. In consequence, while the impact on liquidity of moving to stage 3 will be limited, ESMA also does not expect that the move to stage 3 would be accompanied by a negative market impact.

27. This is also confirmed in the analysis of the 2020 Annual Report of waivers and deferrals for non-equity[5] instruments which highlights the significant role that waivers and deferrals still have in the bond market.

28. For the reasons above and while the effects of the move to stage 2 could not be fully assessed in practice, ESMA does not see any justification to delay the move to stage 3. ESMA, therefore, recommends moving to stage 3 for the liquidity assessment of bonds.

Q1: Do you agree with ESMA's proposal to move to stage 3 for the determination of the liquidity assessment of bonds? Please explain.

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[5] https://www.esma.europa.eu/sites/default/files/library/esma70-156-3926_annual_report_2020_non-equity_waivers_and_deferrals.pdf

2.2 Trade percentile for the determination of the pre-trade SSTI threshold

A. Analysis[6]

29. Article 17 of RTS 2 requires ESMA to assess by 30 July of each year if the percentile to be used for the pre-trade SSTI threshold shall be changed and set to the value provided for in the following stage. For this report, ESMA therefore has to assess whether the transparency regime should move to stage 3 for bonds and to stage 2 for all non-equity instruments other than bonds.

Non-equity instruments other than bonds

30. Despite an improvement for many asset classes, the level of completeness and the quality of the data were still considered insufficient to perform the annual transparency calculations in the year 2020 for a number of instrument classes. ESMA constantly works with NCAs and reporting entities to improve data completeness and data quality in order to be able to perform such calculations for the full scope of instruments as soon as possible.

31. Considering that ESMA provided the first annual transparency calculations for non-equity instruments other than bonds in 2020 but only for a limited scope and that 2020 was a peculiar year due to Covid-19, ESMA still considers it premature to assess a move to stage 2 for those instruments at this point in time.

32. In addition, ESMA will have a full year of data related to the trading activity excluding the UK, which is a main pool of liquidity for certain derivatives, only in 2022. For all those reasons, ESMA considers that at this point in time it is not in a position to properly assess the impact of moving to the following stage for the pre-trade SSTI threshold for non-equity instruments other than bonds.

Bonds

33. As far as bonds (excluding ETCs and ETNs) are concerned, ESMA performed the annual transparency calculations related to the determination of the pre- and post-trade LIS and SSTI thresholds since 2019.

34. Consequently, in order to determine if the value of the pre-trade SSTI threshold should be changed ESMA has performed a simulation of what the value of such threshold would be using a trade percentile of respectively 50% and 40%, on the basis of data reported to FITRS in the year 2020.

35. The results of the analysis are presented in Table 6 below. The table also includes the results of using the stage 2 threshold based on 2018 data provided in the 2020 Annual

Review Report[7]. The results of last year simulation were relatively accurate as they are similar to the ones based on 2020 data with the exception of covered bonds and other public bonds.

36. The increase in value with the stage 3 percentile is relevant mainly for sovereign bonds and other public bonds. Considering that both types of bonds usually trade in big sizes, in the range of EUR 6 and 3 million respectively[8], it therefore appears to be appropriate to move to stage 3 as the impact on large sizes should be limited.

TABLE 6 PRE-TRADE SSTI THRESHOLDS, WITH UK DATA

Bond type	(data of year 2018) SSTI pre-trade_40%	(data of year 2020) SSTI pre-trade_40%[9]	(data of year 2020) SSTI pre-trade_50%
Corporate Bond	500,000	500,000	600,000
Convertible Bond	700,000	800,000	1,000,000
Other Public Bond	600,000	1,000,000	2,000,000
Covered Bond	1,500,000	500,000	700,000
Sovereign Bond	1,500,000	1,000,000	2,000,000
Other Bond	500,000	500,000	600,000

Source: FITRS

37. Table 7 provides the same analysis but, as for bond liquidity, the data from the UK is excluded[10] since the annual calculations for SSTI in bonds next year will include the trading activity of the EU only. Similarly, the major increases are expected for sovereign and other public bonds.

TABLE 7 PRE-TRADE SSTI THRESHOLDS, WITHOUT UK DATA

Bond type	(data of year 2018) SSTI pre-trade_40%	(data of year 2020) SSTI pre-trade_40%	(data of year 2020) SSTI pre-trade_50%
Corporate Bond	500,000	400,000	600,000
Convertible Bond	700,000	600,000	900,000
Other Public Bond	600,000	1,500,000	2,500,000
Covered Bond	1,500,000	400,000	600,000
Sovereign Bond	1,500,000	900,000	1,500,000
Other Bond	500,000	400,000	600,000

Source: FITRS

B. Conclusions and Proposals

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[7] esma70-156-3300_mifid_ii_mifir_annual_report_under_commission_delegated_regulation_eu_2017.583_rts_2.pdf (europa.eu)
[8] These figures were calculated before data corrections. The numbers will be re-calculated for the Final Report.
[9] The results might differ from the public results of the annual transparency calculations since this analysis was performed earlier and data corrections might have occurred in the meantime.
[10] Using the same methodology as in section 2.1

38. In conclusion, ESMA proposes for SFPs, interest rate derivatives, commodity derivatives, credit derivatives, C10 derivatives, CFDs, emission allowances and emission allowance derivatives not to move to stage 2 for the determination of the pre-trade SSTI threshold.

39. As far as bonds (excluding ETCs and ETNs) are concerned, the simulation provided in tables 6 and 7 using the stage 3 criteria provides for an increase on the SSTI threshold for all bond types, in particular for sovereign and other public bonds. Such increase would enhance pre-trade transparency in bond markets hence increasing liquidity in these markets and improving pricing efficiency. In addition, the fact that the bond market remains largely characterised by large size trades counterpoints to the argument that an increase in the pre-trade threshold could be prejudicial for end-investors.

40. ESMA does not consider that the move to stage 3 would expose liquidity providers to undue risk. More generally, over the last years a reduction in market making activity in fixed income markets could be observed. This development appears to be largely driven by an increased reluctance of market makers to be exposed to market risks as well as stricter prudential requirements aiming at ensuring that market exposures are subject to sufficient capital requirements. At the same time, a trend towards increased electronic trading as well as the development of new trading protocols, such as all-to-all trading platforms, can be observed, thereby compensating for the reduced contribution of market makers. Indeed, electronic trading platforms with a higher degree of transparency offer traders the possibility to communicate with hundreds of peers simultaneously and see and compare bids and offers real-time. In this increasingly open market, the ability to profit from information has become accessible to more and more market participants.

41. In view of these market developments, the role of the SSTI waiver aiming at protecting market makers and liquidity providers from undue risk has become somewhat less important.

42. Last but not least, in the Final Report on the MiFIR Review for non-equity instruments[11], ESMA considered that the removal of the pre-trade SSTI waiver and a lowering of the LIS threshold would lead to a more appropriate level of transparency. The move to stage 3 proposed in this consultation would not go as far as that recommendation but would nevertheless attempt to achieve a higher degree of pre-trade transparency in the bond market and to reinforce the level playing field between RFQ and voice trading systems that can benefit from the SSTI waiver and other types of trading systems that are not eligible for the SSTI waiver.

43. ESMA considers that under stage 3 the pre-trade SSTI threshold would still be sufficiently low to protect liquidity providers from potential market impact stemming from large orders, while ensuring that a higher share of liquid bonds would be subject to the MiFIR pre-trade transparency regime. Such increased transparency would contribute to more informed

[11] esma70-156-3329_mifid_ii_mifir_review_report_on_the_transparency_regime_for_non-equity_instruments.pdf (europa.eu)

investors, a better functioning price formation process and ultimately lower transaction costs for end investors.

44. Therefore, ESMA proposes to move to stage 3 for the determination of the SSTI threshold for bonds.

45. ESMA is aware that the move to stage 3 for both the determination of the liquidity assessment of bonds and of the pre-trade SSTI threshold for bonds (except ETCs and ETNs) proposed by ESMA in this CP may introduce divergent transparency requirements between the EU and the UK depending on future developments in the UK.

46. For example, investment firms may have to apply two different regimes when trading in the EU and the UK in multi-listed bonds which constitute the large majority of liquid bonds as highlighted in Tables 2 and 3 above.

47. However, this is one of the natural consequences of Brexit which cannot be determinative for the EU in the development of its transparency framework. Moreover, a higher degree of transparency, as highlighted above, is also expected to result in more integrated markets and lower transaction costs, which would strengthen European capital markets and contribute to the objective of the Capital Markets Union. Finally, ESMA considers that this analysis can be informative also for UK authorities and their future determinations on this matter.

48. ESMA considers that the evolution of financial markets since the application of MiFID II with increased competition and a trend towards more electronification in fixed income markets also validates that a move to stage 3 for both the liquidity assessment and the pre-trade SSTI threshold is adequate to further enhance market transparency. The statistics displayed in the tables above demonstrate that also at stage 2 overall bond market transparency still remains limited. Therefore, a move to stage 3 appears fully warranted to achieve an adequate level of transparency in bond markets as envisaged by the co-legislators in MiFID II.

Q2: Do you agree with ESMA's proposal not to move to stage 2 for the determination of the pre-trade SSTI thresholds for all non-equity instruments except bonds? Please explain.

Q3: Do you agree with ESMA's proposal to move to stage 3 for the determination of the pre-trade SSTI thresholds for bonds (except ETCs and ETNs)? Please explain.

3 Annexes

3.1 Annex 1 - Summary of questions

Q1: Do you agree with ESMA's proposal to move to stage 3 for the determination of the liquidity assessment of bonds? Please explain.

Q2: Do you agree with ESMA's proposal not to move to stage 2 for the determination of the pre-trade SSTI thresholds for all non-equity instruments except bonds? Please explain.

Q3: Do you agree with ESMA's proposal to move to stage 3 for the determination of the pre-trade SSTI thresholds for bonds (except ETCs and ETNs)? Please explain.

3.2 Annex 2 – Mandate

1. This Consultation Paper (CP) covers the reports to be delivered to the Commission under the following articles:

Article (9)(5)(d) of Regulation (EU) No 600/2014:

ESMA shall develop draft regulatory technical standards to specify the following:

[…]

(d) the size specific to the financial instrument referred to in paragraph 1(b) and the definition of request-for-quote and voice trading systems for which pre-trade disclosure may be waived under paragraph 1;

Article 17(4) to (9) of CDR (EU) 2017/583:

4. ESMA shall, by 30 July of the year following the date of application of Regulation (EU) No 600/2014 and by 30 July of each year thereafter, submit to the Commission an assessment of the operation of the thresholds for the liquidity criterion 'average daily number of trades' for bonds as well as the trade percentiles that determine the size specific to the financial instruments covered by paragraph 8. The obligation to submit the assessment of the operation of the thresholds for the liquidity criterion for bonds ceases once S4 in the sequence of paragraph 6 is reached. The obligation to submit the assessment of the trade percentiles ceases once S4 in the sequence of paragraph 8 is reached.

5. The assessment referred to in paragraph 4 shall take into account:

(a) the evolution of trading volumes in non-equity instruments covered by the pre-trade transparency obligations pursuant to Article 8 and 9 of Regulation (EU) No 600/2014;

(b) the impact on liquidity providers of the percentile thresholds used to determine the size specific to the financial instrument; and

(c) any other relevant factors.

6. ESMA shall, in light of the assessment undertaken in accordance with paragraphs 4 and 5, submit to the Commission an amended version of the regulatory technical standard adjusting the threshold for the liquidity criterion 'average daily number of trades' for bonds according to the following sequence:

(a) S2 (10 daily trades) by 30 July of the year following the date of application of Regulation (EU) No 600/2014;

(b) S3 (7 daily trades) by 30 July of the year thereafter; and

(c) S4 (2 daily trades) by 30 July of the year thereafter

7. Where ESMA does not submit an amended regulatory technical standard adjusting the threshold to the next stage according to the sequence referred to in paragraph 6, the ESMA assessment undertaken in accordance with paragraphs 4 and 5 shall explain why adjusting the threshold to the relevant next stage is not warranted. In this instance, the move to the next stage will be postponed by one year.

8. ESMA shall, in light of the assessment undertaken in accordance with paragraphs 4 and 5, submit to the Commission an amended version of the regulatory technical standard adjusting the threshold for trade percentiles according to the following sequence:

(a) S2 (40th percentile) by 30 July of the year following the date of application of Regulation (EU) No 600/2014;

(b) S3 (50th percentile) by 30 July of the year thereafter; and

(c) S4 (60th percentile) by 30 July of the year thereafter.

9. Where ESMA does not submit an amended regulatory technical standard adjusting the threshold to the next stage according to the sequence referred to in paragraph 8, the ESMA assessment undertaken in accordance with paragraphs 4 and 5 shall explain why adjusting the threshold to the relevant next stage is not warranted. In this instance, the move to the next stage will be postponed by one year.

3.3 Annex 3 - Draft RTS

COMMISSION DELEGATED REGULATION (EU) No …/..

of [date]

establishing regulatory technical standards amending Delegated Regulation (EU) 2017/583 as regards adjustment the liquidity thresholds and trade percentile used to determine the size specific to the instrument applicable to certain non-equity instruments

(Text with EEA relevance)

THE EUROPEAN COMMISSION

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012[12], and in particular the fourth subparagraph of Article 9(5) thereof,

Whereas:

(1) Commission Delegated Regulation (EU) 2017/583[13] sets out the transparency regime applicable to bonds, structured finance products, emission allowances and derivatives. In order to ensure a smooth implementation of this new regime, the application of certain transparency thresholds has been phased-in allowing in practice to gradually broaden the application of the new transparency obligations. This concerns, in particular the 'average daily number of trades' criterion used for the determination of bonds for which there is a liquid market as well as the trade percentiles used to determine the size specific to the instrument which allows for pre-trade transparency obligations to be waived.

(2) Under this phased-in approach, moving to the next stage is not automatic but based on an assessment that the European Securities and Markets Authority (ESMA) is required to submit annually to the Commission. The ESMA's assessment has to analyse the evolution of trading volumes for the concerned financial instruments under the current stage and to anticipate the possible impact a move to the next stage could have on both available liquidity and market participants. If appropriate, ESMA is required to submit, together with its report, a revised regulatory standard to move to the next stage.

(3) ESMA has conducted its assessment and, taking into account the limited level of transparency, the limited effects to competition in the market and the fact that the

[12] OJ L 173, 12.6.2014, p. 84.
[13] Commission Delegated Regulation (EU) 2017/583 of 14 July 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards on transparency requirements for trading venues and investment firms in respect of bonds, structured finance products, emission allowances and derivatives (OJ L 87, 31.3.2017, p. 229–349)

threshold would still be sufficiently low to protect liquidity providers from potential market impact stemming from large orders, considers that it is appropriate to move to stage S3 and accordingly amend Commission Delegated Regulation (EU) 2017/583 for bonds for which there is a liquid market and for the size specific to the instrument for bonds. This should increase the level of transparency available in the bond market without a negative impact on liquidity. ESMA considers that at this point in time there is not enough evidence to move to stage S2 for the size specific to the instrument for other classes of financial instruments.

(4) This Regulation is based on the draft regulatory technical standards submitted by ESMA to the Commission.

(5) ESMA has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the advice of the Securities and Markets Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council[14],

HAS ADOPTED THIS REGULATION

Article 1

Amendments to Delegated Regulation (EU) 2017/583

Article 17 of Delegated Regulation (EU) 2017/583 is amended as follows:

(a) paragraph 1 is replaced by the following:

'1. For determining the bonds for which there is not a liquid market for the purposes of Article 6 and according to the methodology specified in point (b) of Article 13(1), the approach for the liquidity criterion "average daily number of trades" shall be taken applying the "average daily number of trades" corresponding to stage S3 (7 daily trades).';

(b) paragraph 3 is replaced by the following:

'3. For determining the size specific to the financial instrument for the purposes of Article 5 and according to the methodology specified under point (b)(i) of Article 13(2), the approach for the trade percentile to be applied shall be used applying the trade percentile corresponding to the stage S3 (50th percentile).

[14] Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

For determining the size specific to the financial instrument for the purposes of Article 5 and according to the methodology specified under points (b)(ii) to (iv) of Article 13(2), the approach for the trade percentile to be applied shall be used applying the trade percentile corresponding to the stage S1 (30th percentile).'.

Article 2

Entry into force and application

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Commission

The President

Ursula von der Leyen