

Answer of MOSAIC FINANCE to the consultation paper over exemption for market making activities and primary operations under regulation (EU) 236/2012

Mosaic Finance is an investment service provider established in Paris and regulated by Banque de France. It is a leading market making firm on equity derivatives, member of most derivative exchanges in Europe.

Q1: Do you agree with the above approach regarding the definition and scope of the exemption for market making activities?

We agree with the approach.

Q2: No opinion

Q3: Do you agree with general principles applicable to persons intending to make use of the exemption under article 17(10) of the Regulation ?

We see a contradiction between article 26 and article 41 of the "Consultation Paper"

Article 26 states that "the notifying person is not required (...) to be recognized as market maker or liquidity provider under the rules of that trading venue or market. Neither is there a requirement to have a separate contractual obligation to carry out market making activities."

Article 41 on the contrary states the "person (...) must (...) comply with the general rules and particular requirements for market making activities imposed by the trading venue (...)"

Q4: Do you agree with principles applicable to persons carrying out market making activities in accordance with article 2(1)(k)(i) of the Regulation ? In your view which of the two options in paragraph 44 should apply to quotes entered when carrying out market making activities ? Do you see other alternative to the two options proposed?

Concerning exemption for hedging of related instruments, and particularly options on stocks, bid and offer quotes cannot be maintained on all related options of a particular stock for technical reason. Indeed on a particular stock, the trading venue creates new related instruments (with new exercise prices and new expiries) on a regular base, following the movement of the stock. Several hundred of options are usually listed on one particular stock, most of which are "out of the money" and bear no volume. Trading venues impose the market makers to send quotes on a limited number of options (usually 9 strike prices and up to one year maturity) to qualify for market maker status. This restriction intends to limit the number of messages sent to the market, limited in their capacity of admitting quotes in their central order book.

However, though a market maker will be imposed to quote on a limited number of options, he can at any time trade options that are not in this restricted number of options on which he has obligations to quote (the most liquid one).

When the market maker hedges the exposure of his portfolio by buying or selling stocks, he does it globally, being unable to relate his hedging to each individual option he has in portfolio.

For related instruments, exemption of declaration of short position should then be defined not on an instrument by instrument basis, but for all related instruments (options) on the underlying stock.

Therefore we suggest that the status of market maker on stock options be defined in accordance with the one given by the biggest derivative markets (Eurex, Liffe), imposing to quote for a specific underlying at least 7 options "out of the money" and "2 options in the money" on expiries up to 13 months.

We favor option 2 (maximum spread acceptable) of article 44.

Q5: Do you agree with the principle applicable to persons carrying out market making activities in accordance with article 2(1)(k)(ii) of the Regulation?

We agree with these principles. However the definition of "client" must be extended to orders from client transmitted indirectly through a third party (broker). Indeed "clients" can submit request for quotes directly to a trading firm or indirectly by using a broker who will proceed to an auction with several market makers in order to find the best price. It is important to extend this definition for transparency and best execution purpose.

Q6: Do you agree with the qualifying criteria for the comparable size of orders?

We do not agree with this criteria at least concerning related instruments for several reasons :

- The minimum quantity required by the exchanges to fulfill the market makers obligations are fixed quantities. Any other criteria such as the ATS could lead to send quote with quantities which would be in breach of these obligations.
- As Market Makers quote tens of options on the same underlying, if the quantity is set at the ATS and if the ATS is significantly bigger than the one required by the exchange, the risk for the market maker is when his several quotes are "hit" at the same time (creating a big hedging position)
- The sensibility (delta) of each option to the movement of the underlying differs from 0 to 100%. The ATS is then not relevant for options.

We suggest to adopt the quantity defined by the exchanges in their "market making scheme" which have been set after years of negotiation between market makers and the exchanges.

Q7: Do you agree with the qualifying criteria for competitive price of orders

For related products such as options (who are generally very illiquid products), there are no quotes in the order book apart from market maker's. Consequently the average bid/ask spread observed on each option is the one imposed by the exchange in their market maker scheme.

We are then in favor of applying the exchange's obligation in term of spread as the criterium.

Q8: Which option do you favor ?

See answer to question 7

Q9: Do you agree with the qualifying criteria for ongoing presence on the market? Do you think different criteria should apply when conducting market making activities in sovereign debt?

For related products such as options a presence of 90% is not realistic and generally the market making scheme of the exchanges suggest a minimum of 80%. Moreover this percentages needs to be monitored not only on a monthly base but as an average on all the options traded on all the underlying for each country of origin.

Q10: Do you agree with ESAM approach towards assessment of notification of intent to make use of the exemption?

We agree with this approach.

We suggest that where a person is party to a market making contract, evidence should mainly be provided by the reports issued by the exchange, which have developed ad hoc monitoring tools.

Q11:

No opinion

Q12:

No opinion

Q13: Do you agree that the above information needs to be provided in the notification form? Should historical data be also provided with the notification form?

We agree with the information needed.

We think that providing historical data would give rational grounds to the competent authorities to authorize the requirement of exemption.

Q14: Do you agree with a period of 6 months after application of the guidelines for revising and assessing notifications made before entry into force of the Guideline?

We Agree

IMPORTANT NOTICE: article 74 of the consultation paper states that in exceptional circumstances the competent authority may exempt market making activities from the measures. We would like to point out that when market making on derivatives, the short position taken on the underlying to cover the related instruments (options or futures) can be for a period of time as long as the expiry of the related instrument. As a consequence, depending on the liquidity of the related products, it will not be in all cases possible for the market maker on such instruments to unwind his position and will oblige him to keep the short position he took as a hedge.

Q15: do you agree that a list of market makers and authorized primary dealers published on the ESMA website according to article 17(13) should at least include the above information?

We do agree.