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| 10 March 2020 |

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| Reply form for the Consultation Paper on MiFID II/ MiFIR review report on the transparency regime for non-equity and the trading obligations for derivatives |
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| Date: 10 March 2020 |

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the Consultation Paper on the transparency regime for non-equity instruments and the trading obligations for derivatives MiFID II/ MiFIR review report published on the ESMA website.

*Instructions*

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

* use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
* do not remove the tags of type <ESMA\_QUESTION\_CP\_MIFID\_NQT\_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
* if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

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

**Naming protocol**

In order to facilitate the handling of stakeholders’ responses please save your document using the following format:

ESMA\_CP\_MIFID\_NQT\_NAMEOFCOMPANY\_NAMEOFDOCUMENT.

e.g. if the respondent were ESMA, the name of the reply form would be:

ESMA\_CP\_MIFID\_NQT\_ESMA\_REPLYFORM or

ESMA\_CP\_MIFID\_NQT\_ANNEX1

***Deadline***

Responses must reach us by **19 April 2020.**

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading ‘Your input - Consultations’.

***Publication of responses***

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

***Data protection***

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the headings ‘Legal notice’ and ‘Data protection’.

# General information about respondent

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| --- | --- |
| Name of the company / organisation | London Metal Exchange |
| Activity | Regulated markets/Exchanges/Trading Systems |
| Are you representing an association? |  |
| Country/Region | UK |

# Introduction

Please make your introductory comments below, if any:

<ESMA\_COMMENT\_CP\_MIFID\_NQT\_1>

TYPE YOUR TEXT HERE

<ESMA\_COMMENT\_CP\_MIFID\_NQT\_1>

1. What benefits or impacts would you see in increased pre-trade transparency in the different non-equity markets? How could the benefits/impacts of such pre-trade transparency be achieved/be mitigated via changes of the Level 1 text?.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_1>

The LME is supportive of the policy objectives behind the enhanced pre- and post-transparency requirements placed on trading venues through MiFID II. The exchange believes that transparency, set at appropriate levels and within a framework that is tailored to the relevant market, would help to support the continued development of liquidity and encourage more on-exchange participation by a broader range of market participants. Together, these factors would have a net positive effect on the market ecosystem. However, in regard to the specific impact of the MiFID II transparency requirements, the LME considers the results to have had a mixed impact on commodity derivatives markets in particular.

The availability of a range of waivers, exemptions and deferrals from these transparency requirements underlines the European authorities’ acknowledgement that transparency is not necessarily appropriate or positive for a market in all circumstances. The LME agrees with this view and, although the LME also supports the availability of these waivers, exemptions and deferrals, it is important they are appropriately calibrated and reflective of how the underlying markets operate and are traded. For example, in commodity derivatives markets, contracts often take prolonged periods to develop self-sustaining and significant liquidity on the more fully transparent central limit order book. Additionally, in many cases, on-exchange contracts represent the culmination of a chain of OTC products, often structured to meet a specific participants’ demand (and in relation to which there is very little transparency at all). Given the importance to the commodity derivative markets of the underlying supply and demand dynamics, inappropriately structured and/or calibrated waivers, exemptions and deferrals risk negatively impacting this trade flow and consequently, risk resulting in more volume remaining in the less transparent off-exchange market. Therefore, it is important the structure and calibration of the MiFID II transparency framework is appropriate in the context of commodity markets and does not impact on this cycle to transparency.

Due to the current classification of systems in Annex 1 of RTS 2, specifically the catch-all “hybrid system”, the LME considers this cycle to be difficult to maintain as it breaks the intermediate step of trade registration and makes pure OTC trading relatively more attractive. If they remain unchanged, this could also have longer-term implications as exchanges will struggle to build liquidity in nascent contracts on a central limit order book and therefore ultimately achieving a high level of transparency in these instruments. This issue is also exacerbated by inappropriately calibrated waiver thresholds which leads to some contracts being classified as liquid (and therefore not being able to benefit from the illiquid waiver) when there is limited on screen liquidity. As a result, those trades which are relatively small in size (i.e. below Large in Scale threshold) are often unable to be transacted under the exchange rules as doing so would open the client up to significant price risk. Therefore, in certain instances there is a risk that requirements may have the opposite impact of increasing transparency in commodity derivatives.

Given all of the above and when considering commodity derivatives specifically, the LME does not believe that meaningful increased transparency has been achieved. Also, given inappropriately calibrated thresholds, the LME believes the requirements have actually reduced transparency in some instances as the relative benefits of trading OTC are increased when compared with on-exchange trading. The LME appreciates the difficulty in striking the right transparency balance with these requirements and would welcome further dialogue with industry to develop an appropriate solution that achieves the overall policy intent of the legislation without impacting the proper functioning of the market.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_1>

1. What proposals do you have for improving the level of pre-trade transparency available? Do you believe that the simplification of the regime for pre-trade transparency waivers would contribute to the improvement of the level of pre-trade transparency available?

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_2>

In terms of Level 1 amendments, the LME does not consider simplification to necessarily be a positive step. Although the removal of the SSTI waiver would benefit the market, it is critical that transparency requirements are specifically tailored to the underlying asset class given the idiosyncrasies that apply. Therefore, the LME advocates for a more granular approach that adequately captures these market nuances.

In addition, the LME believes the existing hedging exemption broadly works effectively and making it into a waiver would increase the associated administrative burden (and could have cost implications for the market) without furthering the ultimate policy objective. Further guidance from ESMA on its use could ensure a more consistent approach being adopted by market participants.

In regard to Level 2 changes for commodity derivatives, the LME considers the waiver thresholds to be inappropriately calibrated and, in some cases, has the unintended consequence of decreasing transparency in markets. Although this is acknowledged by ESMA, we would strongly encourage significant changes to how the waivers (specifically LIS and Illiquid) are structured with the use of different parameters. If ESMA is unable to take these steps, amending the thresholds would improve the outcome for trading of commodity contracts and, in the longer term, see more contracts classified as liquid and trading on central limit order books.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_2>

1. Are you supportive of ESMA’s proposal to delete the pre-trade SSTI-waiver? Would you compensate for this by lowering the pre-trade LIS-thresholds across all asset classes or only for selected asset classes? What would be the appropriate level for such adjusted LIS-thresholds? If you do not support ESMA’s proposal to delete the pre-trade SSTI-waiver, what should be the way forward on the SSTI-waiver in your view?

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_3>

The LME is supportive of its deletion and the subsequent lowering of LIS thresholds for all asset classes for a more effective and fairer transparency regime.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_3>

1. What are your views on the use of the SSTI for the SI-quoting obligations. Should it remain (Option 1) or be replaced by linking the quoting obligation to another threshold (e.g. a certain percentage of the LIS-threshold) (Option 2)? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_4>

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_4>

1. Would you support turning the hedging exemption into a limited negotiated trade waiver? If so, would you support Option 1 or Option 2? If not, please explain why.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_5>

Although the LME would welcome consistency in the use of the hedge exemption by market participants, increasing the number of waivers as part of the pre-trade transparency requirements would not be the optimal way to achieve this. Therefore, the LME is not supportive of turning the hedging exemption into a limited negotiated trade waiver. The LME considers this would add additional operational burden for the market for a potential issue that could be resolved by providing greater clarity on its use via further Q&As.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_5>

1. Do you agree with ESMA’s observations on the emergence of new trading systems and the proposed way forward requiring a Level 1 change and ESMA to issue an Opinion for each new trading system defining its characteristics and the transparency requirements? Would you have suggestions for the timeline and process of such Opinions? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_6>

The LME agrees with ESMA’s views that the trading systems outlined in Annex 1 are not sufficiently granular or flexible and potentially result in novel regulatory issues.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_6>

1. Do you agree with the proposal for the definition of hybrid system? Are there in your view trading systems currently not or not appropriately covered in RTS 2 on which ESMA should provide further guidance? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_7>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_7>

1. Do you agree with ESMA’s proposal to require SIs to make available data free of charge 15 minutes after publication? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_8>

The LME agrees with ESMA’s proposal to define that SIs also have to make available data free of charge 15 minutes after its publication. To improve the quality of published pre-trade transparency information, in particular in traditionally opaque markets, the requirements of SIs should be on the same level as those of trading venues. This would not only further level the playing field between SIs and trading venues but would also improve the overall level of pre-trade transparency in financial markets.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_8>

1. Would you see value in further standardising the pre-trade transparency information to increase the usability and comparability of the information? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_9>

The LME would support ESMA’s approach to further define requirements for making pre-trade transparency information more accessible and comparable. However, in order to ensure a level playing field across venues and increase transparency especially regarding SI trading, which is still very opaque, the proposed standardisation of pre-trade information should be applicable to all types of venues, including SIs. Together with the requirement for SIs to publish, their quotes free of charge after 15 minutes (as trading venues are required to do) this measure would be a significant step forward to increase pre-trade transparency.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_9>

1. Do you agree with ESMA’s assessment of the level of post-trade transparency and with the need of a more streamlined and uniform post-trade regime which does not include options at the discretion of the different jurisdictions? If not, please explain why and, where available, support your assessment with data.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_10>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_10>

1. Do you agree with this proposal? What would be the appropriate level of such a revised LIS-threshold in your view?

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_11>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_11>

1. In your view, should the real time publication of volume masking transactions apply to transactions in illiquid instruments and above LIS waiver (Option 1) or to transactions above LIS only (Option 2 and Option 3). Please elaborate. If you support another alternative, please explain which one and why.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_12>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_12>

1. Do you agree with the publication of the price and volume of all transactions after a certain period of time, such as two calendar weeks (Option 1 and 2) or do you support the two-steps approach for LIS transactions (Option 3)? Please explain why and provide any alternative you would support. Which is the optimal option in case a consolidated tape would emerge in the future?

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_13>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_13>

1. Do you agree with ESMA’s proposed way forward to issue further guidance and put a stronger focus on enforcement to improve the quality of post-trade data? Are there any other measures necessary at the legislative level to improve the quality of post-trade data? What changes to the transparency regime in Level 1 could lead to a substantial improvement of data quality?

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_14>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_14>

1. What would be the optimal transparency regime to help with the potential creation of a CTP?

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_15>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_15>

1. Do you agree with ESMA’s above assessment? If not, please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_16>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_16>

1. Are you of the view that the interpretation of TOTV should remained aligned for both transparency and transaction reporting? If not, please explain why.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_17>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_17>

1. Which of the three options proposed, would you recommend (Option 1, Option 2 or Option 3)? In case you recommend an alternative way forward, please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_18>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_18>

1. What is your view on the proposal to delete the possibility for temporarily suspending the transparency provisions? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_19>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_19>

1. Do you have any remarks on the assessment of Article 28 of MiFIR? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_20>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_20>

1. Do you have any views on the above-mentioned criteria and whether the criteria are sufficient and appropriate for assessing the liquidity of derivatives? Do you consider it necessary to include further criteria (e.g. currency)? Do you consider that ESMA should make use of the provision in Article 32(4) for asset classes currently not subject to the trading obligations? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_21>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_21>

1. Do you agree that a procedure for the swift suspension of the trading obligation for derivatives is needed? Do you agree with the proposed procedure? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_22>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_22>

1. Do you have a view on this or any other issues related to the application of the DTO?

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_23>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_23>

1. Do you have any views on the functioning of the register? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_24>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_24>

1. Do you agree that the current quarterly liquidity calculation for bonds is appropriate or would you be of the view that the liquidity determination of bonds should be simplified and provide for more stable results? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_25>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_25>

1. Do you agree with ESMA proposal to move to stage 2 for the determination of the liquidity assessment of bonds? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_26>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_26>

1. Do you agree with ESMA 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.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_27>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_27>

1. Do you agree with ESMA proposal to move to stage 2 for the determination of the pre-trade SSTI thresholds for bonds (except ETCs and ETNs)? Please explain.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_28>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_28>

1. What is your view on the current calibration of the ADNA and ADNT for commodity derivatives? Are there specific sub-asset classes for which the current calibration is problematic? Please justify your views and proposals with quantitative elements where available.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_29>

As previously noted, the legislation is designed not to ensure full transparency in all instruments but to ensure an appropriate degree of transparency that preserves the orderly price discovery processes in markets. The waivers available to trading venues evidence this. However, it is imperative these waivers and the thresholds set out within them are appropriately calibrated.

The LME considers that the current methodology has led to a significant number products being incorrectly classified as liquid, and thus becoming subject to significantly broader transparency requirements, which were previously reserved for developed markets. Specifically in regard to the thresholds for the illiquid waiver, the LME does not believe the current thresholds set out below are appropriate:

1. The average daily notional amount (ADNA) is greater than or equal to €10m; and
2. The average daily number of trades (ADNT) is greater than or equal to 10.

Taking ADNT first, a commodity derivative market is not considered to be liquid if 10 trades are executed each day. Given that trading is rarely uniformly distributed throughout the day, higher thresholds are a better basis for determining liquidity and, thus, anindication of the ability to find a counterparty in a relatively short period of time within a given trading day. As a result, we propose 100 for the ADNT for the metals sub-asset class.

Secondly, ADNA does not automatically reflect a significant number of trades and therefore a high level of liquidity. We support a proposal to look at trade frequency and standard size to determine liquidity, including aspects such as price and currency. As a result, we propose €100 million for the ADNA for the metals sub-asset class.

Third, commodity trading venues and market participants are also challenged by the fact that the LIS thresholds are set in Euro instead of lots. Prices do not determine theliquidity of a market and notional values do not reflect trading practice. Moreover, market participants typically hedge their production and consumption in trading in lots and not in notional value. Thus, although acknowledged to be difficult by ESMA, we recommend that the liquidity analysis is normalised to a base quantity unit that is native to the asset class. If not possible, we propose that the metals sub-asset class LIS pre-trade threshold floor is set at €50,000 and the trade percentile is set to 30%.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_29>

1. In relation to the segmentation criteria used for commodity derivatives: what is your view on the segmentation criteria currently used? Do you have suggestions to amend them? What is your view on ESMA’s proposals SC1 to SC3? In your view, for which sub-asset classes the “delivery/cash settlement location” parameter is relevant.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_30>

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<ESMA\_QUESTION\_CP\_MIFID\_NQT\_30>

1. What is your view on the analysis and proposals related to the pre-trade LIS thresholds for commodity derivatives? Which proposal to mitigate the counterintuitive effect of the current percentile approach do you prefer (i.e. keep the current methodology but modify its parameters, or change the methodology e.g. using a different metric for the liquidity criteria)? Please justify your views and proposals with quantitative elements where available.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_31>

As noted in previous responses, trade registration is an important way to allow transactions in illiquid/nascent commodity markets in the most transparent way. However, excessively high LIS thresholds lead market participants to revert to more bilateral trading outside transparent and supervised venues, and outside CCP clearing.

To avoid this from happening and to allow for a more natural move to ‘on venue’ trading, the current methodology for setting the LIS thresholds should be replaced with a more appropriately tailored and market-based approach. The LME welcomes ESMA’s assessment on the counterintuitive effects arising from the current percentile approach. We would suggest using a scaled approach based on variations in the liquidity distribution. However, should ESMA not find this feasible, we would also welcome a less comprehensive amendment of the methodology by recalibrating the current parameters.

<ESMA\_QUESTION\_CP\_MIFID\_NQT\_31>