

Deutsche Börse Group's Response
to
ESMA's Consultation on the Technical Standards specifying the
criteria for establishing and assessing the effectiveness of
investment firms' order execution policies

Eschborn, 16th October 2024

Question 1: Do you agree with the proposed categorisation of classes of financial instruments? And could the methodology based on, inter alia, the classification of financial instruments in the MiFID II RTSs 1 and 2 be used in the context of MiFID II transparency reporting be an alternative? Please state the reasons for your answers.

DBG generally agrees that investment firms shall distinguish between not only different classes of instruments but also between countries of primary listings for shares. In particular, for retail investors, it is important that investment firms consider different trading venues depending on the liquidity available on each platform and the prices, among other criteria. DBG cannot recommend a categorisation over another, but we believe it is important that this categorisation is consistent across investment firms to allow clients for easy comparisons.

Question 2: Do you believe that the current wording of the RTS is clear and sufficient with regard to the content of the order execution policy where an investment firm selects only one execution venue to execute all client orders? Or should the RTS provide for specific criteria to be taken into account when assessing if the selected venue achieves the best possible result in the execution of client orders? Please also state the reasons for your answer.

DBG does not believe that an order execution policy where an investment firm selects only one execution venue to execute all client orders is a viable option except when a particular product is offered only by a single venue; we are particularly concerned where the one execution venue in the best execution policy consists with a single intermediary counterpart of all orders on the trading venue, on the basis of an agreement between the broker and the execution venue. It is crucial that the best execution policies defined by investment firms participate to the level playing field between trading venues, promoted especially with the coming ban on payment for order flow. Regulation should support a healthy mix of order flows on trading venues by avoiding the segmentation of the retail flow and supporting price efficiency. In that sense it seems unlikely that any best execution policy with a single execution venue is fulfilling those objectives – again, excluding products proposed on one venue only.

We would recommend in particular that any kind of agreement between the investment firm and the execution venue shall be explicitly mentioned in the best execution policy of the investment firm including the selection criteria and rationale to ensure full transparency to their clients. Retail investors are particularly of concern here and we agree with the proposal that both in Article 4 and Article 5, ESMA distinguishes between retail and professional clients. We would also link this aspect to the clients' instructions in Q6 and caution against the possibility to route order to one venue under the cover of clients' instructions forfeiting de facto access to alternative execution venues.

Question 3: Do you agree with the proposed factor of “order sizes” respectively for retail and professional clients, to be considered in investment firms' selection of eligible execution venues in their order execution policy and internal execution arrangements (see Article 4(1)(d)(i) and ii) of the draft RTS)? If not, what alternative factor would you propose?

We prefer not to provide a response to this question at this time.

Question 4: Do you agree with ESMA's proposals for the specification of the criteria for establishing and assessing the effectiveness of investment firms' order execution policies? Please also state the reasons for your answer.

In general, DBG agrees with many of the specification of the criteria for both establishing and assessing the effectiveness of the investment firms' order execution policies, specified Article 3 and 7.

We furthermore would like to draw attention to the point that those criteria applied in the establishment vs. assessment parts of the execution policies are seemingly not entirely aligned, i.e., the factors deciding the criteria cannot be mapped one-to-one which makes it difficult to understand how the assessment of the best executions policy can be done practically. As an example, "levels of liquidity of execution venues" is a criterion in the assessment of the effectiveness of the order execution policy (Article 7) but, not in the establishment of the best execution policy (Article 3). It is not possible to assess the effectiveness of the execution policy by liquidity, if liquidity is not defined at all as a criterion for the establishment of the execution policy. So, specific to this example, "levels of liquidity of execution venues" should be included also in the establishment part of the execution policy for proportionality purposes. As a general comment, the criteria in the establishment and assessment of the best execution policies should be identical.

Regarding the proposals for the assessment of investment firms' order execution policies, DBG would have following comments:

- We do agree that the monitoring shall be at least once every 3 months. Especially in the case of policies with a single execution venue, the monitoring shall be frequent.
- Linked to the above point, whenever possible referring here to the number of venues where the relevant instrument is listed, we believe that the assessment of the best execution policy shall include a sufficient number of execution venues to compare to.
- Regarding the thresholds to monitor execution policies, it shall also be possible to ensure that those thresholds as well as the deviation of the execution results are not set at levels low enough to guarantee that the policy is de facto rarely reviewed and modified.

Moreover, we support that the consolidated tape data should be used to assess best execution policies. We would not, however, support the use of the consolidated tape for trading purposes given the latency issues it will present in the EU and as discussed during the political process in the context of L1. Furthermore, for the CTP to provide the data quality needed to become an integral part of trading/best execution monitoring, it will be of essence that any pending data quality issues (such as correct flagging and reporting, provision of correct and sufficiently granular time stamps) is solved beforehand. This may be a question of time and readiness of all affected parties alike, which ESMA should take into account. Quality issues should be addressed first before making the use of the CT mandatory (if at all) as the reference for defining, but especially for monitoring and assessing best execution.

Hence, we would recommend that ESMA further softens its references to the CT in respective Articles of the draft RTS wherever possible. As an example, we generally appreciate Art 7(2)(a) but consider that the wording could better indicate a level playing field. We would like to recommend as well that once the CTP has settled in as a trusted source of data, contributing data sources to the CTP (i.e.

trading venues) should continue to be considered trusted sources for best execution requirements under this regulation and on an equal standing with the CTP, while there should not be any compulsory usage of the CTP requested directly or indirectly. This could be especially important as well for smaller locally oriented investment firms not in need of a complete EU view.

Finally, it should be noted as well, that potentially not all venues will provide their data to the CTP (opt-in mechanism), hence, any mandatory use of the CTP may neither effective nor proportionate.

Question 5: Do you agree with ESMA's proposal that investment firms may rely on monitoring and assessments performed by third parties, such as independent data providers, as long as firms assess the processes of these third parties? Please also state the reasons for your answer.

While DBG strongly supports best execution requirements to ensure fair and trustful markets, we are not entirely convinced of ESMA's current proposal, including the potential outsourcing to third parties as it may come with unintended side effects. We agree, however, that outsourcing may become necessary, in case the RTS remains as is, as the new requirements defined by ESMA could extraordinarily burden especially smaller investment firms (i.e. through new IT requirements, additional complex processes and respective compliance) unless outsourcing may play a role. This again may have impact on the current market structure and trade executions, as those third parties may offer execution services themselves. Dependencies of especially smaller EU investment firms on Third Party Service Providers will be fostered and finally may result in potentially more executions off-exchange and in the dark.

While best execution applies to all asset classes alike, we feel that the requirements as regards cash equities and ETFs are especially demanding. While there are explicit links in the RTS as regards responsibilities and references to constant monitoring which will be highly challenging especially for smaller investment firms, there is a risk that ESMA creates an "indirect need to outsource" the execution business to third parties in order to ensure the full requirements in the area of cash equities are being met.

Furthermore, investment firms shall be cautious when using third parties as an ultimate reference data source, the more so in case such a third party offers trading services as well. Therefore, it is advisable to investment firms to cross check the data via different data sources whenever possible. It must nevertheless stay as the responsibility of the investment firm to properly assess the criteria for their best execution policies to ensure the best result for the client.

Question 6: Concerning the specific client instruction, should it be possible for an investment firm to pre-select an execution venue in the order screen, where the firm invites its clients to choose an executing venue out of multiple options? And if so, do you agree that only if the client chooses a different venue than the one pre-selected by the firm, the choice of execution venue does constitute a specific instruction? Please also state the reasons for your answer.

In the case of retail investors, it shall be mentioned that the order screen is decisive for the client. The way the trading venues are presented on the screen, especially the one at the top would have a much higher probability to be selected even if they do not offer the best outcome. The number of venues shown on the screen will also be important, where venues not visible on the first screen have

a low chance to be selected because the investor will not scroll down. We believe investment firm shall therefore be as transparent as possible and provide retail investors the clearest pictures regarding costs for each trading venues, potential agreements between the investment firm and the execution venue, etc. We could suggest the following:

- The order screen is blank i.e., it does not show any pre-selected trading venues to clients. However, it could display the daily average traded volume of a specific instrument in various venues to provide transparency in different options for the clients. Clients can choose any trading venue they would prefer.
- The order screen shows one pre-selected trading venue based on either investment firm's choice or client's own choice. The screen could also display the average daily traded volumes for a specific instrument traded also at other venues. This way the order screen can make the options at various venues transparent.

Question 7: Where an investment firm executes client orders by dealing on own account (including back-to-back trading), in light of the specificity of this execution model and since it is bound by the rules governing best execution, do you believe the current text is clear with regard to what kind of obligations investment firm applying such model should comply with? Or do you believe it would be useful to provide in the RTS list and explanations of information that should be included in the order execution policy, such as related to the method and steps to be taken by the firm to establish the price of client transactions in back-to-back trading, or the methodology for the firm's application of mark-ups or mark-downs in such order executions? Please also state the reasons for your answer.

We prefer not to provide a response to this question at this time.

Question 8: Are there any additional comments that you would like to raise and/or information that you would like to provide (for example, relevant information in relation to any expected costs and benefits arising from the proposals)?

DBG considers that there could be merit in requesting a standard format for the provision of a best execution policy and the provision of it on the investment firms' homepage, which would allow (retail) investors to make an informed decision when choosing their broker.