



MiFID II pre and post trade transparency

Damian Carolan and Sidika Ulker

12 October 2017

Agenda

1	Overview of the MiFID II transparency regime
2	Extraterritorial considerations in respect of EU regulation
3	Extraterritorial reach of the MiFID II transparency requirements
4	Questions?

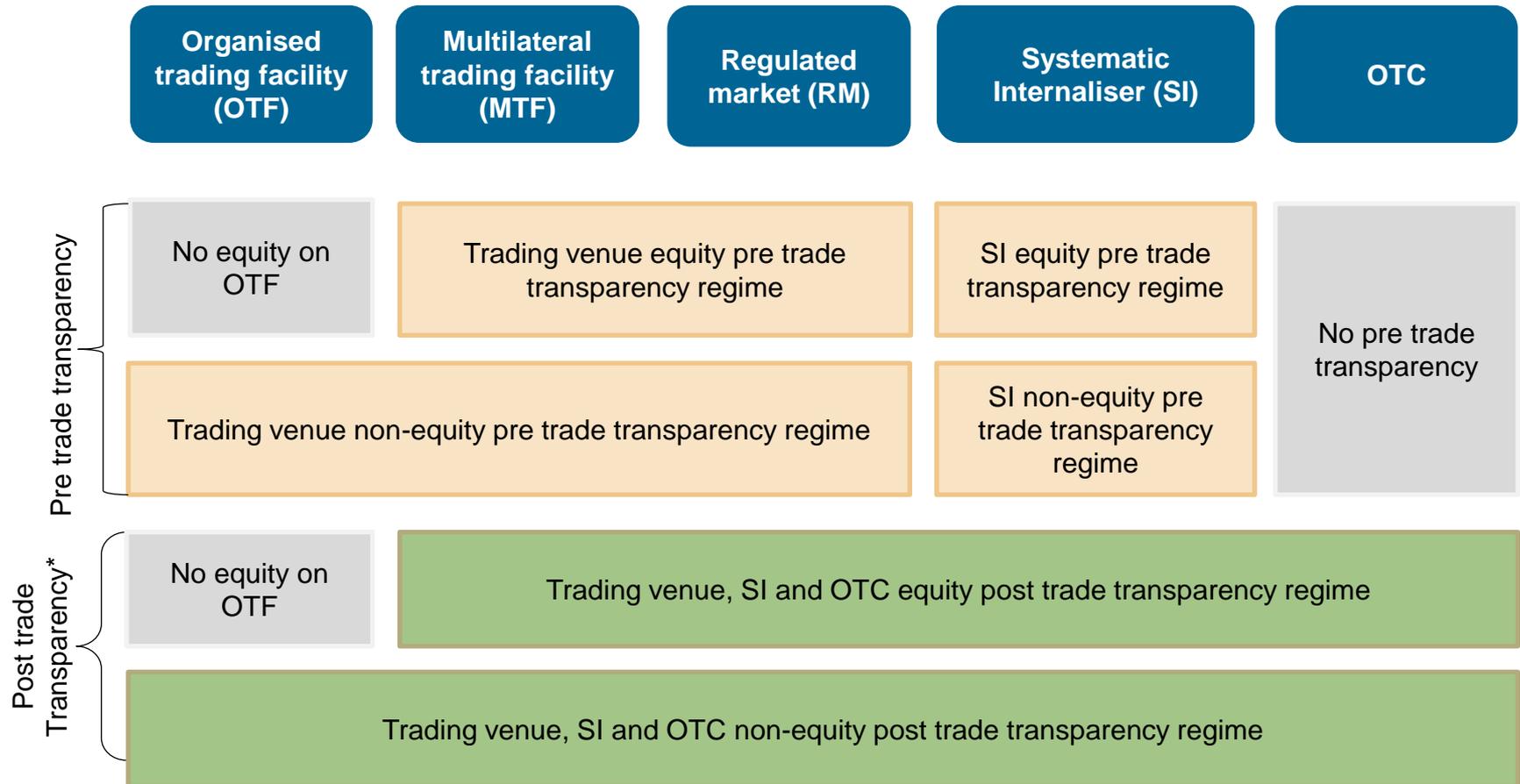
Overview of the transparency regime

MiFID II EU market structure



- **Multilateral system:** system or facility in which multiple third party buying or selling trading interests in financial instruments which are able to interact in the system.
- **Trading venues (i.e. RMs, MTF, OTFs) are multilateral systems**
- **Mandatory SI regime:** where investment firms deals on own account when executing client orders meet SI thresholds in respect of financial instruments/classes of financial instruments, they must be an SI in respect of those financial instruments/classes of financial instruments
- **Optional SI regime:** investment firms may opt in to become SIs in respect of financial instruments
- **OTC:** residual category

MiFID II transparency regime



*Central principle that there should be only a single trade report for a transaction chain

Pre trade: SI – equity and equity-like

- Equity instrument in which an SI
- Equity instrument is ToTV
- Quote is smaller than SMS

Scope?

- Must disclose quotes to clients upon request
- Can determine clients to whom give access to quotes on basis of commercial policy

- Minimum quote size $\geq 10\%$ SMS
- Make public two-way quotes on a regular and continuous basis during normal market hours
- Quotes must reflect prevailing market conditions
- Quotes must be easily accessible on a reasonable commercial basis
- Must execute orders received from clients at quoted prices
- Can determine clients to whom give access to quotes on basis of commercial policy

Illiquid?

Liquid?

Pre trade: SI – non-equity

- Bonds, structured finance products, emission allowances and derivatives
- Instrument/class (as appropriate) in which an SI
- Instrument is ToTV
- Quote is smaller than SSTI
- Client asks for quote and SI agrees to provide a quote

Scope?

- Can decide whom to give access on the basis of commercial policy and in an objective non-discriminatory way
- Non-discriminatory limits on number of transactions with clients
- Public and available in a manner that is easily accessible on a reasonable commercial basis
- Quotes must reflect prevailing market conditions

Access to quotes?

- Quote must be made public
- Quote must be made available to other clients on an executable basis

Liquid?

- Must disclose quotes to clients upon request
- Can determine clients to whom give access to quotes on basis of commercial policy
- Obligation may be waived

Illiquid?

Post trade – equity

- **Conclusion** of a transaction
- Share, depository receipts, ETFs, certificates and other similar financial instruments
- Instrument is ToTV
- For transactions concluded outside a trading venue, certain transactions are excluded

Scope?

- Give access to the arrangements they employ for making public the information on reasonable commercial terms and on a non-discriminatory basis
- Make available separately from pre trade
- Make information public on a reasonable commercial basis and ensure non-discriminatory access

Additional venue obligations?

- Publish Annex I Tables 3 and 4 RTS 1, including price, volume, time of transaction Close to real time as technically possible and in any case within one minute
- Publication waterfall applies
- **Investment firms trading OTC or through SI must publish through an APA**

Obligation?

- Competent authority discretion
- Large in scale trades – minimum qualifying size
- End of trading day publication if trade more than 2 hours before end of trading day. Otherwise, noon the next day
- Regime of the publication entity applies

Deferrals?

Post trade – non-equity

- **Conclusion** of a transaction
- Bonds, structured finance products, emission allowances and derivatives
- Instrument is ToTV
- For transactions concluded outside a trading venue, certain transactions are excluded

Scope?

- Give access to the arrangements they employ for making public the information on reasonable commercial terms and on a non-discriminatory basis
- Make available separately from pre trade
- Make information public on a reasonable commercial basis and ensure non-discriminatory access

Additional venue obligations?

- Publish Annex II Tables 2 and 3 RTS 2, including price, volume, time of transaction Close to real time as technically possible and in any case within 15 minutes
- Publication waterfall applies
- **Investment firms trading OTC or through SI must publish through an APA**

Obligation?

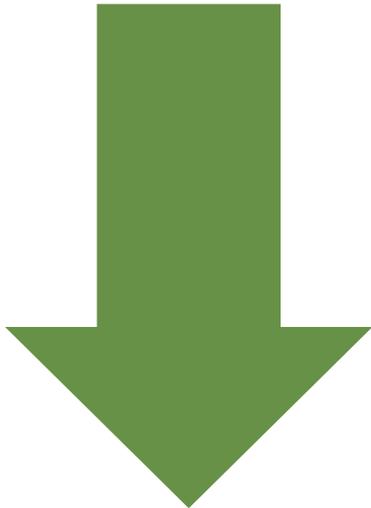
- Competent authority discretion
- Large in scale trades, SSTI for non-MPT trades, illiquid instruments, order management facility
- T+2 deferral if no supplementary deferral
- Supplementary deferral: (a) price information before T+2; (b) extended volume deferral; (c) aggregation

Deferrals?

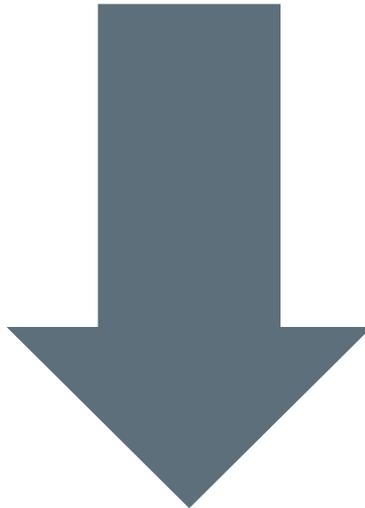
*Extraterritorial considerations in respect
of EU regulation*

Non-EU entities that may have an EU nexus

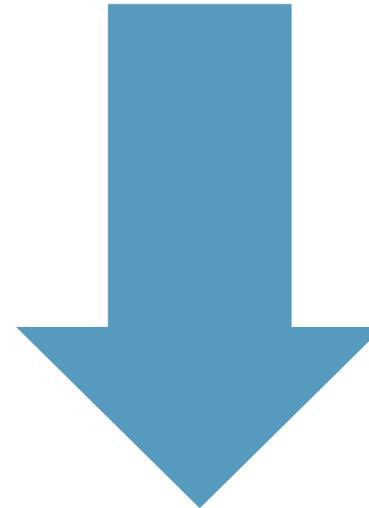
**Non-EU legal
entity
interacting
with the EU***



**Non-EU legal
entity with an
EU branch**



**EU legal
entity with a
third country
branch**



EU nexus

***Local licensing issues will need to be considered**

Basis of the EU's extraterritorial reach

The EU's ability to legislate extraterritorially is based on principles of international law. There are various types of EU nexus which potentially brings business in scope, such as:

EU incorporated MiFID regulated entity (e.g. where an entity is acting through a non-EU branch but the rules are expressed to apply to the legal entity without restriction)

Impact on EU markets (e.g. where there is a foreseeable effect on EU secondary markets)

Non-EU entity has EU clients/counterparties

Trading in respect of EU products

Interaction with EU infrastructure (e.g. trading on EU platforms)

Issuing and listing products on EU markets

Ways EU's extraterritorial reach could impact third country entities

- **Directly applicable obligations**
- **Indirectly applicable obligations**
 - Applicable to counterparties
 - Applicable to trading venues
 - Applicable to products
 - EU behaviour (e.g. reliance on EU trading desks)
- **Environmental impacts**

Changes to EU infrastructure that impacts the interaction of the third country entity with that infrastructure

Note: This presentation does not address the third country equivalence regime under MiFIR

*Extraterritorial reach of the MiFID II
transparency requirements*

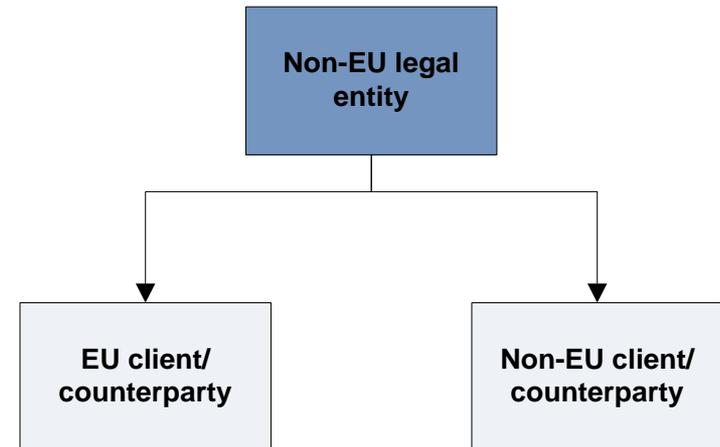
Extraterritorial reach of MiFID II pre and post trade transparency

1	Who?
2	What?
3	When?

Non-EU legal entity interacting with the EU market (no EU branch)

Direct impacts

- Transparency requirements do not apply to non-EU investment firms
 - Pre trade transparency applies to SIs and EU trading venues
 - Post trade transparency applies to EU authorised investment firms and market operators
- Local licensing considerations relevant if providing execution services to EU clients



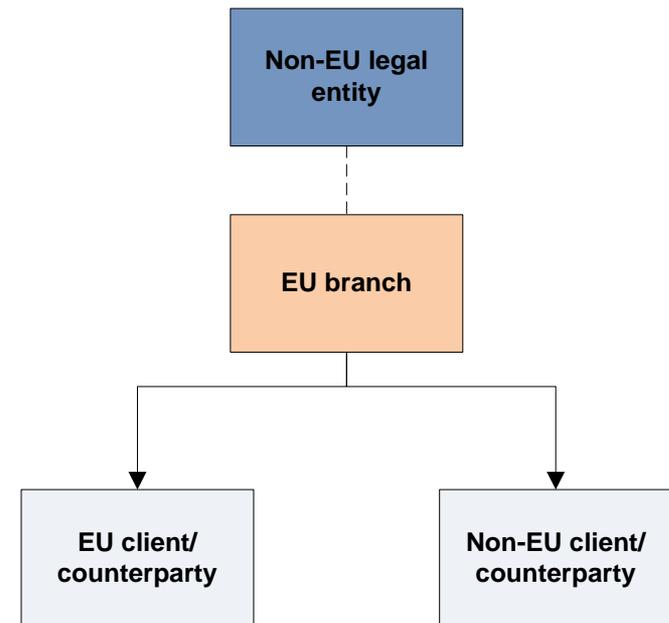
Indirect impacts

- EU counterparties and trading venues could be subject to the transparency requirements

Non-EU legal entity with an EU branch

Direct impacts

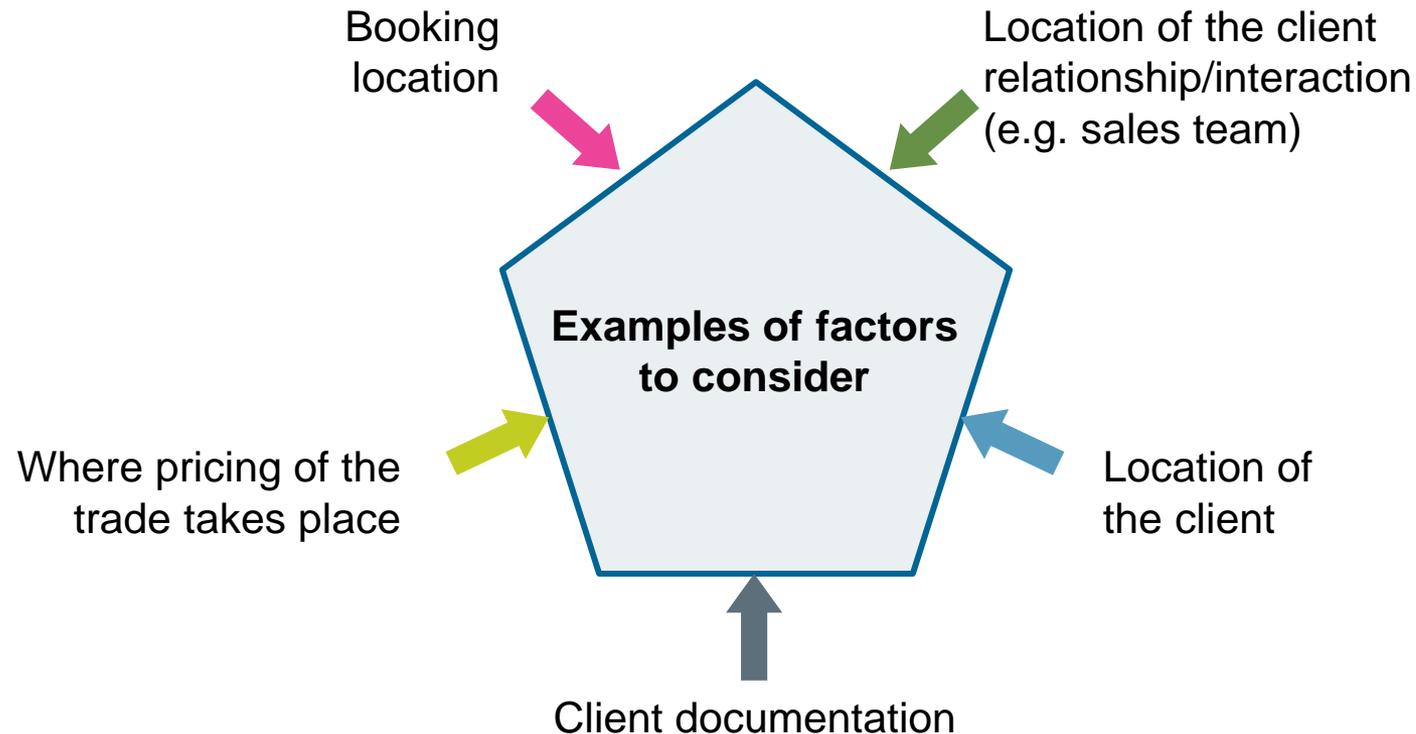
- Transparency requirements do not apply to non-EU investment firms
- EU branch will be subject to the local regulatory regime
 - “*No better off*” principal: expect local regimes to require EU branches to undertake SI calculations and comply with the transparency requirements
 - Should consider when activities constitute “branch business”



Indirect impacts

- EU counterparties and trading venues could be subject to the transparency requirements

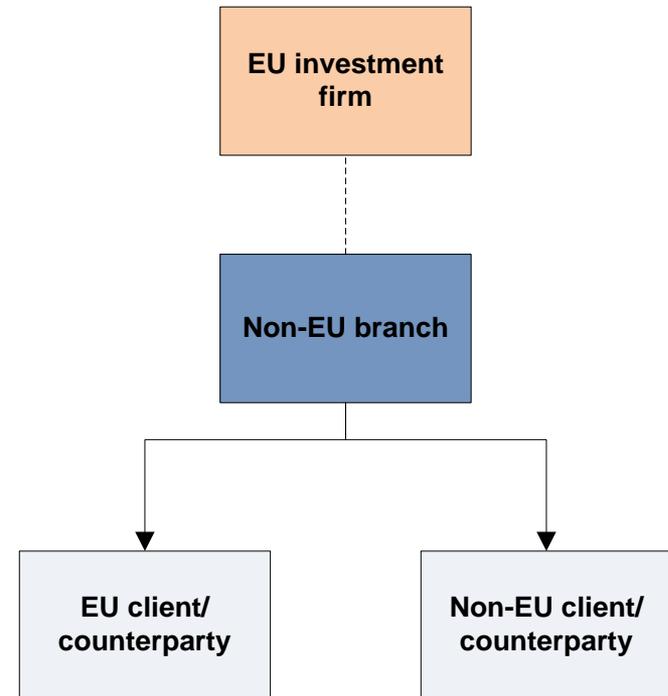
Examples of factors to consider when determining whether execution activity is “branch business”



EU investment firm with a third country branch

Direct impacts

- Rules are not clear as to whether or how the rules apply to non-EU branches (there is conflicting guidance under MiFID I)
- Rules are expressed at legal entity level without restriction
- *EU clients*
 - EU passporting legislation does not contemplate non-EU branches of EU firms providing services back into the EU
 - Home state/local law needs to be considered for exceptional cases
- *Non-EU clients*
 - Arguable pre trade applies to SIs and post trade to EU investment firms even where activity undertaken in non-EU branch
 - May need to consider non-EU branch trades in SI calculations



Extraterritorial reach of MiFID II pre and post trade transparency

1	Who?
2	What?
3	When?

Instruments in respect of which pre and post trade transparency apply

- Pre and post trade transparency apply in respect of instruments “*traded on a trading venue*” (**ToTV**)
- Expect shares and bonds that are made available for trading on EU trading venues to be in scope
- ESMA has provided guidance on the meaning of ToTV for OTC derivatives*:
 - OTC derivatives that share same reference data details as derivatives traded on a trading venue considered to be ToTV
 - Sharing same reference details means sharing the same values as ones reported by trading venues under the reference data obligations (except fields 5 to 12)

Impact

- Shares dual-listed in Europe within scope
- Bonds and shares only need to be made available for trading by one MTF or OTF (relevant for bonds) to be within scope
 - MTFs and OTFs may not have formal listing procedures
 - OTFs are likely to be interdealer brokers, which traditionally offer a broad scope of products
- OTC derivatives may be within scope

*<https://www.esma.europa.eu/file/22204/download?token=-DLnIjMW>

Extraterritorial reach of MiFID II pre and post trade transparency

1	Who?
2	What?
3	When?

Counterparties and clients – pre trade transparency

- Quotes must be made available to clients (in accordance with the requirements)
- For non-equities, the pre trade obligations are triggered when a client requests a quote and the investment firm agrees to provide the quote
- ESMA Q&A for SI calculations on the meaning of “*executing client orders*”:
 - an investment firm is executing client orders if dealing with a counterparty that is not a financial institution authorised or regulated in the Union or under national law of a Member State; or
 - when the counterparty is not a financial institution, one party is always acting in a client capacity

Impact

- Possible that the ESMA guidance on the meaning of “*executing client orders*” applies more broadly
 - Intragroup trades should be considered
 - Trades with non-EU financial institutions may be considered to be trades with non-financial institutions

Counterparties and clients – post trade transparency

- Investment firms trading off-venue must make public the details of the transaction according to the waterfall in the RTS
- ESMA guidance* that for a transaction concluded on a non-EU trading venue, the firm does not need to publish the trade if the venue is considered to be equivalent for the purposes of post trade transparency (ESMA will maintain a list)

Impact

- Certain transactions on third country trading venues will not fall within the MiFID II post trade transparency regime (whilst others will)

*https://www.esma.europa.eu/sites/default/files/library/esma70-154-165_smsc_opinion_transparency_third_countries.pdf

Timing – non-equity post trade transparency

- For non-equity post trade transparency, ESMA Q&A has clarified that transactions that take place outside daily trading hours of trading venues should be made public before the opening of trading of trading venues on the next trading day:
- “*Daily trading hours*” has been clarified to mean the trading hours of the trading venues trading the (relevant) instruments
- Where there is more than one trading venue trading the instrument, investment firms/APAs are expected to check whether the transaction took place during trading hours of any of the (relevant) trading venues

Impact

- Practical issues checking the daily trading hours of all relevant trading venues
- Publication timing of “out of hours” transactions need to be considered
- Issues regarding APA service hours

Questions?

These are presentation slides only. The information within these slides does not constitute definitive advice and should not be used as the basis for giving definitive advice without checking the primary sources.

Allen & Overy means Allen & Overy LLP and/or its affiliated undertakings. The term partner is used to refer to a member of Allen & Overy LLP or an employee or consultant with equivalent standing and qualifications or an individual with equivalent status in one of Allen & Overy LLP's affiliated undertakings.

Appendix

Pre trade: venues – equity and equity-like

- Applicable to RMs and MTFs
- Extended to cover shares, depositary receipts, ETFs, certificates and other similar FI ('equity and equity like')
- AIOIs within scope
- Transaction with a member of the ESCB for financial stability purposes are exempt

Scope?

Subject to national discretion

- Reference price waiver
- Negotiated transactions waiver
- Large in scale orders
- Orders held in trading venue's order management facility

Waivers?

- Current bid and offer prices and depth of trading interests at those prices
- Available on a continuous basis during normal trading hours
- Calibrated by trading system
- Reasonable terms and non-discriminatory
- Free of charge after 15 minutes
- Pre and post trade provided separately

Action?

- In respect of reference price and negotiated price waivers
- Total volume of all Union trading in that instrument in previous 12 months subject to waivers capped at (i) 4% per trading venue and (ii) 8% across all Union venues

Cap?

Pre trade: trading venues – non-equity

- Applicable to all trading venues
Bonds, structured finance products, emission allowances and derivatives
- AIOIs in scope

Scope?

Subject to national discretion

- Large in scale orders
- Orders held in order management facility
- For RFQ/voice trading systems, AIOIs above SSTI
- Illiquid instruments

- Current bid and offer prices and depth of trading interests at those prices
- Available on a continuous basis during normal trading hours
- Calibrated by trading system
- Reasonable terms and non-discriminatory
- Free of charge after 15 minutes
- Pre and post trade provided separately
- Indicative prices to be published where a waiver other than SSTI applies

Waivers?

Action?

- Derivative transactions of NFCs entered into for hedging purposes
- Transaction with a member of the ESCB for financial stability purposes
- Money market instruments

Exempt?