

Markets in financial instruments; OTC derivatives, central counterparties and trade repositories

2011/0296(COD) - 20/10/2011 - Legislative proposal

PURPOSE: to adopt new rules for more sound, transparent and efficient EU financial markets (over the counter 'OTC' derivatives, central counterparties and trade repositories).

PROPOSED ACT: Regulation of the European Parliament and of the Council.

BACKGROUND: the **Markets in Financial Instruments Directive (MiFID) (Directive 2004/39/EC)**, in force since November 2007, is a core pillar in EU financial market integration. It establishes a regulatory framework for the provision of investment services in financial instruments (such as brokerage, advice, dealing, portfolio management, underwriting etc.) by banks and investment firms and for the operation of regulated markets by market operators. It also establishes the powers and duties of national competent authorities in relation to these activities.

The result after 3.5 years in force is more competition between venues in the trading of financial instruments, and more choice for investors in terms of service providers and available financial instruments, progress which has been compounded by technological advances. Overall, transaction costs have decreased and integration has increased.

However, **some problems have surfaced:**

- the benefits from this increased competition have not flowed equally to all market participants and have not always been passed on to the end investors, retail or wholesale;
- the market fragmentation implied by competition has also made the trading environment more complex;
- market and technological developments have outpaced various provisions in MiFID;
- the financial crisis has exposed weaknesses in the regulation of instruments other than shares, traded mostly between professional investors.

In line with the recommendations from the de Larosi re group and the conclusions of the ECOFIN Council of June 2009, **the revision of MiFID therefore constitutes an integral part of the reforms aimed at establishing a safer, sounder, more transparent and more responsible financial system.** It is also an **essential vehicle for delivering on the G20 commitment** to tackle less regulated and more opaque parts of the financial system, and improve the organisation, transparency and oversight of various market segments, especially in those instruments traded mostly over the counter (OTC), complementing the [legislative proposal](#) on OTC derivatives, central counterparties and trade repositories.

The proposal amending MiFID is **divided in two:**

- **this draft Regulation** on markets in financial instruments and amending Regulation [EMIR] on OTC derivatives, central counterparties and trade repositories;
- [the proposed Directive](#) on markets in financial instruments, repealing Directive 2004/39/EC of the European Parliament and of the Council.

IMPACT ASSESSMENT: policy options were assessed against different criteria: transparency of market operations for regulators and market participants, investor protection and confidence, level playing field for market venues and trading systems in the EU, and cost-effectiveness. Overall, the review of MiFID is estimated to generate one-off compliance costs of between **EUR 512 and EUR 732 million and ongoing costs of between EUR 312 and EUR 586 million**. This represents one-off and ongoing cost impacts of respectively 0.10% to 0.15% and 0.06% to 0.12% of total operating spending of the EU banking sector. This is far less than the costs imposed at the time of the introduction of MiFID.

LEGAL BASIS: Article 114 of the Treaty on the Functioning of the European Union (TFEU).

CONTENT: the proposed Regulation sets out requirements in relation to the disclosure of trade transparency data to the public and transaction data to competent authorities, removing barriers to non-discriminatory access to clearing facilities, the mandatory trading of derivatives on organised venues, specific supervisory actions regarding financial instruments and positions in derivatives, and the provision of services by third-country firms without a branch.

A central aim of the proposal is to **ensure that all organised trading is conducted on regulated trading venues**: regulated markets, multilateral trading facilities (MTFs) and organised trading facilities (OTFs). **Identical pre and post trade transparency requirements will apply to all of these venues**. The transparency requirements will be calibrated for different types of instruments, notably equity, bonds, and derivatives, and for different types of trading, notably order book and quote driven systems.

The main elements of the proposal are as follows:

- **Extension of transparency rules to equity like instruments and actionable indications of interests:** MiFID has established transparency rules, both pre and post trade that apply to shares admitted to trading on regulated markets, including when those shares are traded on an MTF or over the counter (OTC). The proposed provisions first extend the transparency rules applicable by these shares to equity like instruments such as depository receipts, exchange-traded funds, certificates and other similar financial instruments issued by companies. The extension of the transparency requirements will also cover actionable indications of interests (IOIs).
- **Increased consistency in the application of waivers to pre trade transparency for equities markets:** the proposed provisions will oblige the competent authorities to inform [ESMA](#) about the use of the waivers in their markets and ESMA will issue an opinion on the compatibility of the waiver with the requirements established in this Regulation and prospective delegated acts.
- **Extension of transparency rules to bonds, structured finance products and derivatives:** the proposal extends the principles of transparency rules up to now only applicable to equity markets to bonds, structured finance products, emission allowances and derivatives.
- **Increased and more efficient data consolidation:** the proposed provisions will contribute to reducing the cost of data by requesting trading venues, that is regulated markets, MTFs or OTFs to make post trade information available free of charge 15 minutes after the execution of the transaction, to offer pre- and post-trade data separately, and by giving the possibility to the Commission to clarify by delegated acts what constitutes a reasonable commercial basis. The proposal also requires investment firms to make public trades executed outside trading venues via Approved Publication Arrangements which will themselves be regulated in the Directive. This should significantly improve the quality of OTC data and consequently facilitate its consolidation.
- **Transparency for investment firms trading OTC including systematic internalisers:** the existing transparency rules for systematic internalisers will apply to shares and equity-like instruments, while new provisions would be introduced for bonds, structured finance products admitted to trading on a regulated market or for which a prospectus has been published, emission allowances and derivatives which are clearing-eligible or are admitted to trading on a regulated market or are traded on an MTF or an OTF.

- **Transaction reporting:** all transactions in financial instruments will need to be reported to competent authorities, except for transactions in financial instruments which are not traded in an organised way and are not susceptible to market abuse and cannot be used for abusive purposes. Competent authorities will have full access to records at all stages in the order execution process, from the initial decision to trade, through to its execution.
- **Trading of derivatives:** consistent with the requirements already proposed by the Commission (EMIR) to increase central clearing of OTC derivatives, the proposed provisions in this Regulation will require trading in suitably developed derivatives to occur only on eligible platforms, that is regulated markets, MTFs or OTFs. This obligation will be imposed on both financial and non financial counterparties exceeding the clearing threshold in EMIR.
- **Non-discriminatory clearing access:** the proposed provisions will prohibit discriminatory practices and prevent barriers that may prevent competition for the clearing of financial instruments.
- **Supervision of products and positions:** the proposed amendments will greatly increase the supervision of products and services by introducing the possibilities on the one hand, for competent authorities to set permanent bans on financial products or activities or practices with coordination by ESMA, and on the other hand, for ESMA to also temporarily ban products, practices and services. The proposed provisions in the Regulation introduce a role for ESMA to coordinate the measures taken at national level and specific powers to manage or limit positions for market participants.
- **Provision of investment services by third country firms without a branch:** the proposal creates a harmonised framework for granting access to EU markets for firms and market operators based in third countries in order to overcome the current fragmentation into national third country regimes and to ensure a level playing field for all financial services actors in the EU territory. The proposal introduces a regime based on a preliminary equivalence assessment of third country jurisdictions by the Commission. Third country firms from third countries for which an equivalence decision has been adopted would be able to request to provide services in the Union.

BUDGETARY IMPLICATIONS: the specific budget implications of the proposal relate to task allocated to ESMA. Total appropriations are estimated at **EUR 1 744 million from 2013 to 2015**.

DELEGATED ACTS: the proposal contains provisions empowering the Commission to adopt delegated acts in accordance with Article 290 TFEU.