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

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The Committee on Economic and Monetary Affairs adopted the report by MARKUS FERBER (EPP, DE) on the proposal for a Regulation of the European Parliament and of the Council on markets in financial instruments and amending Regulation [EMIR] on OTC derivatives, central counterparties and trade repositories.

The parliamentary committee recommends that the European Parliament's position adopted at first reading under the ordinary legislative procedure should amend the Commission's proposal as follows:

New category of organised trading facility: to make European markets more transparent and efficient to level the playing field between various venues offering multilateral trading services it is necessary to introduce a new category of **organised trading facility (OTF)** for bonds, structured finance products, emissions allowances and derivatives and to ensure that it is appropriately regulated and applies non-discriminatory rules regarding access to the facility.

The operator of an OTF should be subject to requirements in relation to the **sound management of potential conflicts of interest and non-discriminatory execution** and should not be allowed to execute in the OTF any transaction between multiple third-party buying and selling interests including client orders brought together in the system against his own proprietary capital.

Transparency obligations: all organised trading should be conducted on regulated venues with maximal pre- and post-trade transparency. **Appropriately calibrated** transparency requirements should therefore apply to all types of trading venues, and to all financial instruments traded thereon.

Timely pre- and post-trade transparency requirements taking account of the different characteristics and market structures of specific types of instruments other than shares should thus be introduced and adapted as necessary so as to be workable for request-for-quote systems, whether automated or involving voice trading. Only those financial instruments which are bespoke in their design or insufficiently liquid would be outside the scope of the transparency obligations.

Exclusions from the scope of the Regulation: in the interests of legal certainty, the following exclusions are specified:

- While it is important to regulate currency derivatives including currency swaps which give rise to a cash settlement determined by reference to currencies in order to ensure transparency and market integrity spot currency transactions should not fall within the scope of this Regulation;
- It is likewise important to clarify that contracts of insurance in respect of activities of classes set out in Annex I to Directive 2009/138/ECon the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) are not derivatives for the purposes of this Regulation if entered into with a Union or third-country insurance or reinsurance undertaking.
- Furthermore, while risks arising from algorithmic trading should be regulated the use of algorithms in post-trade risk reduction services does not constitute algorithmic trading.

Ensuring uniform applicable conditions between trading venues: to this end, the **same pre- and post-trade transparency requirements** should apply to the different types of venues. The transparency requirements should be **proportionate and calibrated** for different types of instruments, including equities, bonds, and derivatives, taking into account the interests of investors and issuers, including government bond issuers, and market liquidity. The requirements should also be calibrated for different types of trading, including order-book and quote-driven systems such as request for quote as well as hybrid and voice broking systems, and take account of issuance, transaction size and characteristics of national markets.

Systematic internalisers: these are defined as investment firms which, on an organised regular and systematic basis, deal on own account by executing client orders bilaterally outside a regulated market, an MTF or an OTF.

In order to guarantee the quality of the price formation process, the Regulation **limits the circumstances in which OTC trading can be carried out outside a systematic internalise**r.

Systematic internalisers may decide to give access to their quotes only to their retail clients, only to their professional clients, or to both. They should not be allowed to discriminate within those categories of clients but should be entitled to take account of distinctions between clients, for example in relation to credit risk. Systematic internalisers are not obliged to publish firm quotes in relation to transactions in equity instruments above standard market size and in non-equity instruments above retail market size.

Trading activities conducted outside regulated execution venues: the Regulation should ensure that **as much trading as possible which occurs outside regulated execution venues takes place in organised systems to which appropriate transparency requirements apply** while ensuring that large scale and irregular transactions can be concluded.

This Regulation is not intended to prohibit or limit the use of bespoke derivative contracts or make them excessively costly for non-financial institutions. Therefore, the assessment of sufficient liquidity should take account of market characteristics at national level including elements such as the number and type of market participants in a given market, and of transaction characteristics, such as the size and frequency of transactions in that market. In addition, this Regulation is not intended to prevent the use of post-trade risk reduction services.

Investor protection: in order to ensure the orderly functioning and integrity of financial markets, investor protection and financial stability, it is necessary to provide a mechanism for monitoring of the design of investment products and for powers to prohibit or restrict the marketing, distribution and sale of any investment product or financial instrument giving rise to serious concerns regarding investor protection, the orderly functioning and integrity of financial markets.

Where certain conditions are met, the competent authority or, in exceptional cases, European Securities and Markets Authority (ESMA) should be able to impose a prohibition or restriction on a precautionary basis before an investment product or financial instrument has been marketed, distributed or sold to clients.

Details of transactions: the details of transactions in financial instruments should be reported to competent authorities through a system coordinated by ESMA, to enable them to detect and investigate potential cases of market abuse, to monitor the fair and orderly functioning of markets, as well as the activities of investment firms.

The reports should use a **legal entity identifier** in line with the G-20 commitments.

To enable oversight by all the relevant competent authorities, the Commission should also report on whether the content and format of the reports are sufficient to (i) detect market abuse; (ii) expose priorities for monitoring given the vast amount of data reported; (iii) indicate whether the identity of the decision-maker responsible for the use of an algorithm is needed; and (iv) define the specific arrangements needed to ensure robust reporting of securities lending and repurchase agreements.

Besides, the marking of short sales provides useful supplementary information to enable competent authorities to monitor levels of short selling.

Third-country firms: the new regime should (i) harmonize the existing fragmented framework; (ii) ensure certainty and uniform treatment of third-country firms accessing the Union; (iii) ensure that an assessment of effective equivalence has been carried out by the Commission in relation to the regulatory and supervisory framework of third countries; and (iv) provide for a comparable level of protections to clients in the Union receiving services by third-country firms and reciprocal access to third-country markets.

In applying this regime, the Commission and Member States should **prioritise the areas covered by the G-20 commitments and agreements with the Union's largest trading partners** and should have regard to the central role that the Union plays in worldwide financial markets and ensure that the application of third-country requirements: (i) does not prevent Union investors and issuers from investing in or obtaining funding from third countries or (ii) does not prevent third-country investors and issuers from investing, raising capital or obtaining other financial services in Union markets unless this is necessary for objective and evidence-based prudential reasons.

The provisions of this Regulation regulating the provision of services or undertaking of activities by third-country firms in the Union should not affect the possibility for persons established in the Union to receive investment services by a third-country firm in the Union at their own exclusive initiative or for Union investment firms or credit institutions to receive investment services or activities from a third-country firm or for a client to receive investment services from a third-country firm through the mediation of such a credit institution or investment firm.