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

2011/0296(COD) - 26/10/2012 - Text adopted by Parliament, partial vote at 1st reading/single reading

The European Parliament adopted by 497 votes to 20, with 17 abstentions, **amendments** to 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 matter was referred back to the committee responsible for reconsideration and the vote was postponed until a subsequent plenary session.

The main amendments adopted by Parliament are the following:

Scope: the Regulation should apply to credit institutions authorised under Directive 2006/48/EC and investment firms authorised under the new MiFID Directive where the credit institution or investment firm is providing one or more investment services and/or performing investment activities, and to market operators.

Organised trading facility (OTF) means a multilateral system or facility, which is not a regulated market, a multilateral trading facility or a central counterparty, operated by an investment firm or a market operator, in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in the system in a way that results in a contract in accordance with the provisions of Title II of the new MIFID Directive.

This new category should be **appropriately regulated and apply 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.

Parliament favours the introduction of timely pre- and post-trade transparency requirements taking account of the different characteristics and market structures of specific types of instruments other than shares. These should be 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 internaliser**.

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.

Market data: these data should be easily and readily available to users. In this context, approved publication arrangements should be used to ensure the consistency and quality of such data and to enable the delivery of a consolidated tape for post-trade data.

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 text underlines that **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 provide for a comparable level of protection to clients in the Union receiving services from third-country firms as well as **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.