

BVI's response to the ESMA consultation paper on the trading obligation for derivatives under MiFIR (ESMA70-156-71)

BVI¹ takes the opportunity to present its views on the ESMA consultation paper on the trading obligation for derivatives under MiFIR:

Q1: *Do you agree with ESMA's assessment and proposed way forward for the criteria assessing the number and types of active market participants? If not, please explain your position and how you would integrate these elements into the liquidity test.*

We agree with ESMA's assessment that the minimum number of market participants of a class of derivatives subject to the trading obligation should be based on a more flexible approach allowing for some deviation where this is supported by the other liquidity criteria. However, ESMA should also take into consideration that the nature and the diversity of (active) market participants could have more prevalence than the computation of the number of market participants alone.

Q2: *Do you agree with the revised proposal not to exempt post-trade LIS transactions? If not, please explain and present your proposal.*

We disagree. Large derivative trades above the pre- and post-trade LIS threshold should be exempted from the trading obligation. The trading of large derivative (block) orders within the proposed waiver regime may influence the liquidity of the whole class of derivatives thereby hampering the flexibility of investment fund management companies to execute such big orders efficiently on behalf of highly regulated investment funds (UCITS/AIFs).

Q3: *Do you agree with this proposal? If not, please explain why and provide an alternative proposal for ESMA to populate and maintain the register.*

We disagree. ESMA should provide a register for the classes of derivatives which are subject to the trading obligation based on a golden source principle. Financial counterparties should have legal certainty on the list kept in the public register.

¹ BVI represents the interests of the German investment fund and asset management industry. Its 100 members manage assets of EUR 2.9 trillion in UCITS, AIFs and discretionary mandates. As such, BVI is committed to promoting a level playing field for all investors. BVI members manage, directly or indirectly, the investments for 50 million private clients in over 21 million households. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.



Q4: Do you agree with this proposal? Would you add other parameters e.g. day count convention of the floating leg, notional type (constant vs. variable), fixed rate type (MAC vs. MAC)? If yes, please explain why and provide the parameters.

Q5: For each Case, specify if you agree with the proposal of qualifying the sub-classes as liquid for the purpose of the trading obligation and if not, please explain why and provide an alternative proposal.

Q6: Would you also consider any of these possible sub-classes as liquid? Which other combinations of fixed leg payment frequency and floating leg reset frequency specifically would you consider to be sufficiently liquid?

Q7: For each Case, specify if you agree with the proposal of qualifying the sub-classes as liquid for the purpose of the trading obligation and if not, please explain why and provide an alternative proposal.

Q8: Would you also consider any of these possible sub-classes as liquid? Which other combinations of fixed leg payment frequency and floating leg reset frequency specifically would you consider to be sufficiently liquid?

Q9: For each case, specify if you agree with the proposal of qualifying the sub-classes as liquid for the purpose of the trading obligation and if not, please explain why and provide an alternative proposal.

Q10: Would you also consider the possible sub-classes here below as liquid? Which other combinations of fixed leg payment frequency and floating leg reset frequency specifically would you consider to be sufficiently liquid?

Q11: Do you agree with this proposal? If not, please explain why and provide an alternative proposal.

We agree.

Q12: Do you agree with this proposal? If not, please explain why and provide an alternative proposal.

The most liquid market segments of iTraxx Europe Main and iTraxx Europe Crossover as of series 17 are subject to the clearing obligation. Therefore, also the preselection of the liquidity has already taken place. We agree that the two CDS index classes are sufficiently liquid for the purpose of the trading obligation.

Q13: Do you agree to the proposed timeline? If not, please explain why and present your proposal.

We strongly disagree with the proposed timelines. The proposed parallel implementation of the phase-in approach's for category (1) and (2) do not give market participants, e.g. trading venues sufficient time to develop their offerings and trading frameworks for their market participants (e.g. buy-side clients). Firstly, trading venues have to develop their offerings (e.g. legal documentation) before buy-side clients can make a decision to which exchange, MTF or OTF they would like to connect to.

Furthermore, the suggested parallel implementation of the starting date for the trading obligation for category (1) and (2) on 3 of January 2018 is legally not in line with L1 as Article 32 para (1) (b) of MiFIR which requires ESMA to determine the dates from which the trading obligation takes effect including also the different phase-in approaches of the various categories of counterparties specified in EMIR.



We propose that the trading obligation for the categories of counterparties should only enter into force after six to nine months after at least two trading venues are registered in the ESMA register. This will give all financial counterparties (e.g. investment fund management companies) sufficient time to set up legal and operational arrangements with the trading venues, MTFs and OTFs. If the trading obligation applies between two financial counterparties within different categories of counterparties, the date from which the trading obligation takes effect for that derivative contracts should apply at the later date.

Highly regulated German investment funds (UCITS/AIF) belong mainly to clearing category (3) albeit a few funds are above the EUR 8 billion threshold calculated individually at fund level and are therefore classified within category (2). Our small and medium-sized members with a limited volume of clearing activity face difficulties to find clearing members and to set up legal and operational arrangements with them, accessing a CCP.

In the context of the EMIR review², we strongly support the proposal to relieve small financial counterparties (UCITS/AIFs) with a limited clearing volume from the clearing obligation by introducing a clearing threshold. We strongly share the evidence that for the smallest financial counterparties with a limited clearing volume such as most UCITS/AIFs (category 3) it is economically unfeasible to fulfil the clearing obligation. However, it needs to be ensured that an exemption of such firms is also reflected in MiFIR.

Therefore, we propose that small financial counterparties which are excluded from the EMIR clearing obligation are also exempted from the obligation to trade on a regulated market under MiFIR, as the latter would likely require them to centrally clear in any case.

Some German investment fund management companies have already significantly invested in the trading and clearing infrastructure to obtain trading access to regulated markets and indirect clearing access through a clearing member to a CCP before the compliance deadlines. Such management companies have already successfully tested the CCP clearing of e.g. the eligible IRS products and are therefore ready to start the mandatory clearing set in the RTS for category (3). Hence, financial counterparties (e.g. UCITS/AIF management companies) belonging to category (3) should be able to trade and (further) clear the envisaged IRS/CDS products on a voluntary basis before the trading and the clearing obligation take effect and should not be prevented from doing it.

² https://ec.europa.eu/info/law/better-regulation/initiatives/com-2017-208_en