



**Exemption for market making activities and primary market operations
under Regulation (EU) 236/2012 of the European Parliament and the
Council on short selling and certain aspects of credit default swaps
(ESMA/2012/580)**

A response paper by the Futures and Options Association

OCTOBER 2012

EXEMPTION FOR MARKET MAKING ACTIVITIES

ESMA Consultation Paper (2012/580)

1. Introduction

- 1.1 This response is submitted on behalf of the Futures and Options Association (“the FOA”), which is the principal European industry association for 160 firms and organisations engaged in the carrying on of business in futures, options and other derivatives. Its international membership includes banks, financial institutions, brokers, commodity trade houses, energy and power market participants, exchanges, clearing houses, IT providers, lawyers, accountants and consultants (see Appendix 1).
- 1.2 The FOA has seen the joint response to ESMA prepared by AFME and ISDA and fully supports the observations, recommendations and concerns raised therein.
- 1.3 We have emphasised below the high-level issues of concern to FOA’s members, which are aligned with those described in the AFME/ISDA response. We have not provided detailed responses to the specific questions asked by ESMA and instead support the specific responses provided by AFME/ISDA in their response document.

The FOA’s key points:

2. ESMA’s Guidelines should be aligned with the intention and spirit of the Level 1 text

- 2.1 The FOA notes Recital 26 of the EU’s Short Selling Regulation (SSR), which states:
“Market making activities play a crucial role in providing liquidity to markets within the Union and market makers need to take short positions to perform that role. Imposing requirements on such activities could severely inhibit their ability to provide liquidity and have a significant adverse impact on the efficiency of the Union markets. Furthermore market makers would not be expected to take significant short positions except for very brief periods. It is therefore appropriate to exempt natural or legal persons involved in such activities from requirements which could impair their ability to perform such a function and therefore adversely affect the Union markets.”

In FOA’s view, ESMA’s proposed Guidelines are not aligned with the acknowledgement in the Level 1 text above on the crucial role market making activities play in providing liquidity to markets within the EU. The exemption in the SSR for market making activities is being interpreted by ESMA so narrowly that it may be of limited use to FOA firms. This is particularly concerning for firms facilitating client business, as this function was specifically included in the definition of “market making activities” in the Level 1 text.
- 2.2 As an example, ESMA has proposed that firms must provide specific details of each instrument on which market making activities are carried out. This means that to secure the exemption, firms must seek exemptions for a very wide universe of financial instruments, in many cases involving thousands of pages of ‘ISINs’ on lists which will

need to be continuously updated. The process appears to be unwieldy and ineffective for competent authorities as well as for firms (for whom the cost of building the alert systems to update ISIN lists is as onerous as complying with the SSR without an exemption). A better approach, and one we understand the Level 1 text envisaged given the reference to “activities”, would be to focus on the activities a firm is actually performing in connection with financial instruments.

- 2.3 The FOA believes that the 30 day notification requirement in Article 17(6) of the SSR also shows that policy-makers intended to create an activities-based market making exemption, because the 30 day notification does not work in situations where an ISIN is not available in time, or where the transaction may not be known about 30 days in advance. An ‘instrument class by instrument class’ approach is urged instead (e.g. EU sovereign bonds, EU equities and derivatives), instead of notifying the competent authority at the individual ISIN or contract level.

3. Short amount of time available

- 3.1 We are aware that ESMA is under considerable pressure in terms of the Short Selling Regulation work and other dossiers. That being said, it is very concerning that the proposed market maker exemption Guidelines were published only weeks before firms are to notify Competent Authorities of their intention to use the exemption, and only a month before the entry into force of the actual Short Selling Regulation on 1 November 2012. The absence of certainty in terms of the final Guidelines means that firms must implement changes to their internal processes, and IT system changes, based on a ‘best guess’ of what the final requirements will be.

4. Market making scope and ESMA’s proposed 90% quoting obligation

- 4.1 The FOA does not agree with ESMA’s analysis in paragraph 55 of the consultation paper that the words “a regular and on-going presence on the market” in Article 2(1)(k)(i) of the SSR means that “market making activities should on a monthly basis be undertaken for at least 90% of the overall trading time on a given financial instrument”. Requiring firms to quote at competitive prices for 90% of the overall trading time on a given financial instrument, regardless of the asset class or prevailing market conditions, is overly prescriptive and arbitrary (and not in the Level 1 text). This 90% requirement is not a one-size-fits-all metric for all markets, and in particular is not appropriate for derivative markets.

5. Dialogue with ESMA

- 5.1 The FOA and its members would like to be part of a dialogue with ESMA on the issues raised in our response and in the AFME/ISDA response, which we strongly support. We would welcome an opportunity to meet with ESMA to discuss these concerns in more detail.

APPENDIX 1

LIST OF FOA MEMBERS

FINANCIAL INSTITUTIONS

ABN AMRO Clearing Bank
N.V.
ADMISI
Altura Markets S.A./S.V
AMT Futures Limited
Jefferies Bache Limited
Banco Santander
Bank of America Merrill Lynch
Banca IMI S.p.A.
Barclays Capital
Berkeley Futures
BGC International
BHF Aktiengesellschaft
BNP Paribas Commodity
Futures
BNY Mellon Clearing
International
Citadel Derivatives Group
(Europe)
Citigroup
City Index
CMC Group Plc
Commerzbank AG
Crédit Agricole CIB
Credit Suisse Securities
(Europe)
Deutsche Bank AG
ETX Capital
FOREX.COM UK
FXCM Securities
GFI Securities
GFT Global Markets UK Ltd
Goldman Sachs International
HSBC Bank Plc
ICAP Securities Limited
IG Group Holdings Plc
International FC Stone Group
JP Morgan Securities
Liquid Capital Markets
London Capital Group
Macquarie Bank
Mako Global Derivatives
Marex Spectron
Mitsubishi UFJ Securities
International Plc
Mizuho Securities USA, Inc
London
Monument Securities
Morgan Stanley & Co
International
Newedge Group (UK Branch)
Nomura International Plc
Rabobank International
RBC Europe Limited
Saxo Bank A/S
Scotiabank Europe
S E B Futures
Schneider Trading Associates
S G London
Standard Bank Plc
Standard Chartered Bank
Starmark Trading
State Street GMBH London
Branch
The Kyte Group
The RBS
UBS Limited
Valbury Capital Ltd
Vantage Capital Markets LLP
Wells Fargo Securities

**EXCHANGE/CLEARING
HOUSES**

APX Group
CME Group, Inc.
Dalian Commodity Exchange
European Energy Exchange
AG
Global Board of Trade
ICE Futures Europe
LCH.Clearnet Group
LMAX Limited
MCX Stock Exchange
MEFF RV
Nasdaq OMX
Nord Pool Spot AS
NYSE Liffe
Powernext SA
RTS Stock Exchange
Shanghai Futures Exchange
Singapore Exchange
Singapore Mercantile
Exchange
The London Metal Exchange
The South African Futures
Exchange
Turquoise Global Holdings

**SPECIALIST COMMODITY
HOUSES**

Amalgamated Metal Trading
BASF SE. EIL
Cargill Plc
ED & F Man Capital Markets
Glencore Commodities
Gunvor SA
Hunter Wise Commodities LLC
Koch Metals Trading Ltd
Metdist Trading Limited
Mitsui Bussan Commodities
Natixis Commodity Markets
Noble Clean Fuels
Phibro GMBH
J.P. Morgan Metals
Sudcen Financial
Toyota Tsusho Metals
Triland Metals
Vitol SA

ENERGY COMPANIES

BP International IST
Centrica Energy
ChevronTexaco
ConocoPhillips Limited
E.ON EnergyTrading SE
EDF Energy
EDF Trading Ltd
International Power plc
Petro Ineos Trading Ltd
Phillips 66 TS Limited
National Grid Electricity
Transmission Plc
RWE Trading GMBH
Scottish Power Energy Trading
Shell International
SmartestEnergy Limited

**PROFESSIONAL SERVICE
COMPANIES**

Ashurst LLP
ATEO Ltd
Baker & McKenzie
Berwin Leighton Paisner LLP
BDO Stoy Hayward
Cadwalader, Wickersham &
Taft LLP
Clifford Chance
Clyde & Co
CMS Cameron McKenna
Deloitte
FfastFill
Fidessa Plc
Freshfields Bruckhaus Deringer
Herbert Smith LLP
Holman Fenwick Willan LLP
ION Trading Group
JLT Risk Solutions Ltd
Katten Muchin Rosenman LLP
Linklaters LLP
Kinetic Partners LLP
KPMG
McDermott Will & Emery LLP
Mpac Consultancy LLP
Norton Rose LLP
Options Industry Council
Orrick, Herrington & Sutcliffe
LLP
PA Consulting Group
R3D Systems Ltd
Reed Smith LLP
Rostron Parry
RTS Realtime Systems
Shearman & Sterling (London)
LLP
Sidley Austin LLP
Simmons & Simmons
SJ Berwin & Company
SmartStream Technologies
SNR Denton UK LLP
Speechly Bircham LLP
Stellar Trading Systems
SunGard Futures Systems
Swiss FOA
Trading Technologies
Traiana Inc
Travers Smith LLP
Trayport