28 August 2024

FIA EPTA response to the ESMA MiFIR Review Consultation on RTS 2 on transparency for bonds, structured finance products and emission allowances (ESMA74-2134169708-7241)

The European Principal Traders Association (FIA EPTA) represents Europe's leading Principal Trading Firms. Our members are independent market makers and providers of liquidity and risk-transfer for markets and end-investors across Europe. FIA EPTA works constructively with policy-makers, regulators and other market stakeholders to ensure efficient, resilient and trusted financial markets in Europe.

Our members support the objectives of the MiFIR Review to enhance pre and post trade transparency in non-equity instruments. Our members believe that fully operative and genuine post-trade transparency provides significant advantages for both retail and institutional investors such as better, more reliable pricing, lower transaction costs and better liquidity across all trade sizes, including the largest sized block trades. We point to academic studies analysing the impact of the US TRACE regime for corporate bonds and the positive impact on competition and price formation yielded from real time price and volume publication. In this regard, we support a post-trade deferral model which prioritises real time publication of price and volume with deferrals of no longer than End of Day, with any longer deferral period only being made available in respect of truly exceptional trades by reference to size.

An ambitious transparency regime will also support the success of the European consolidated tapes for bonds and derivatives by providing meaningful data for publication. A successful CT will further support the growth, resilience and competitiveness of European capital markets.

Supporting evolution towards a more ambitious transparency regime will also aid European competitiveness. Other major financial markets are currently exploring significant reforms to enhance transparency. In the US, FINRA has recently proposed reducing deferral periods under the TRACE system applicable to corporate bonds from 15 minutes to 1 minute[1]. For further information on the positive impact the TRACE regime has had on liquidity and price formation in the US corporate bond market, please see our response to question 13. The UK has also recently consulted on material reforms to non-equity transparency which will make a far greater proportion of traded volumes subject to real time publication.

In this regard, it is important that consideration is given to ensuring there is not material divergence in transparency thresholds or deferral periods with a view to ensuring the respective EU and UK consolidated tapes function in alignment to effectively ameliorate regional liquidity fragmentation.

[1] SR-FINRA-2024-004 | FINRA.org

FIA EPTA members support the ambition and simplicity embodied in ESMA's proposals regarding deferral periods and consider the data driven approach taken to calibrating thresholds has resulted in broadly sensible, pragmatic levels, subject to a few recommended adjustments addressed in our response below. We encourage ESMA to continue with this ambitious and data driven approach when undertaking their periodic review of deferrals as provided under MiFIR in order to realise the potential for more liquid and efficient non-equity markets embodied in the objectives of the MiFIR Review.

1. **Do you agree with the definition of CLOB trading systems proposed above? If not, please explain why.**

   Whilst the definitions of Continuous Lit Order Book and Frequent Batch Auctions/periodic auction trading systems appear to based on a view founded in equities markets, our members do not see any material issues with these insofar as they are relevant to matters dealt with in RTS 2, subject to our comments in response to question 2 below.

2. **Do you consider that the definition should include other trading systems? Please elaborate.**

   FIA EPTA members support the proposed definition of Continuous Lit Order Book ("CLOB"), in particular noting that it encompasses trading systems combining elements of a continuous auction trading system and periodic auction trading system. However, it is our understanding, in speaking with some ETD trading venues, that there are instances where the system that accepts pre-arranged trades subject to the rules of the trading venue is not considered to be part of the CLOB but is a separate and distinct trading system purely for crossing orders and thus would be considered a hybrid system (ie, "trading system not falling within the first five rows") under the current RTS 2. In order to ensure that pre-arranged trades submitted subject to the rules of a trading venue meet appropriate levels of pre-trade transparency (i.e., either by availing of a pre-trade transparency waiver or by being matched on the trading venue with a reasonable chance for other market participants to interact in a competitive way with the crossing as per ESMA Q&A 13[2]), the definition of CLOB should include any trading system that accepts pre-arranged trades (cross orders) subject to the rules of a trading venue that operates a CLOB.

   We would, also, recommend that ESMA remain open to the possibility of revisiting the definitions when it consults on proposed changes to RTS 2 concerning derivatives in case there are implications arising from those proposals that are not presently foreseeable.

3. **Do you agree that the description of periodic auction trading systems set out in Annex I of RTS 2 is relevant for specifying the characteristics of those trading systems in the revised RTS? If not, please elaborate.**

   No comment.

4. **Do you agree to use ESA 2010 to classify bond issuers If not, please explain and provide alternatives on how clarify how to classify sovereign, other public and corporate issuers.**

   FIA EPTA members support ESMA's proposals.

[2] *Page 71: https://www.esma.europa.eu/sites/default/files/library/esma70-872942901-35_qas_transparency_is-sues.pdf*

5. **Do you agree with the proposed LiS pre-trade thresholds for bonds? In your answer, please also consider the analysis provided in sections 4.2.1.**

   FIA EPTA members support ESMA's proposals.

6. **Do you agree with the proposed LiS pre-trade thresholds for SFPs and EUAs? In your answer, please also consider the analysis provided in section 4.2.2.**

   No comment

7. **Do you agree with the approach taken for the illiquid waiver for bonds, SFPs and EUA? If you disagree with how the liquidity threshold is determined, please include your comments in Q11 for bonds, Q14 for SFPs and/or Q17 for EUAs.**

   FIA EPTA members support ESMA's proposals.

8. **Do you agree with the changes to post-trade fields summarised in Table 5? Please identify the proposal ID in your response.**

   We support the proposed measures. In particular, the proposals to harmonise and improve the clarity of the trade reporting output of execution and publication venues are important measures to improve access and experience for reporting data consumers and to consequently improve price discovery. Similarly, measures to deprecate instrument reference data fields, where this information is already available in centralised sources (eg. FIRDS), would sensibly reduce the per trade reporting burden on reporting firms and increase the accuracy and consistency of instrument reference data provided to data consumers.

9. **Do you agree not to change the concept of "as close to real-time as technically possible"? If not, what would be in your view the maximum permissible delay?**

   Yes, we agree with not changing the concept of "as close to real-time as technically possible" and agree with ESMA that it is essential that the maximum permissible delay should only be used by market participants that, for technical reasons, are not able to achieve real-time publication. Where real-time publication is achievable, post-trade reporting should occur immediately and not be systematically/artificially delayed.

   Additionally, whilst we agree with ESMA's proposal to set the maximum delay at 5 minutes, we emphasise the importance of setting an expectation that this continue to be reviewed and adjusted downwards over time. Ongoing technological advancements and improved efficiency should result in overall faster publication with a reduction in technical reasons preventing real-time publication. The industry has shown its ability to adjust to a shorter timeframe as demonstrated by the permissible timeframe being adjusted downwards from 15 minutes to 5. Further, we observe the current FINRA proposals to reduce deferral periods under the US TRACE system applicable to corporate bonds from 15 minutes to 1 minute, demonstrating further reduction of publication times is not only desirable but also achievable[3]. Accordingly, we expect this trend to continue and be reflected in regulatory expectations.

10. **Do you agree with the changes proposed for the purpose of the reporting of OTC transactions?**

[3] SR-FINRA-2024-004 | FINRA.org

FIA EPTA members support ESMA's proposals.

11. **Do you agree with the liquidity thresholds set out in Table 7 above? If not, please provide an alternative approach.**

    FIA EPTA members broadly agree with the liquidity thresholds proposed by ESMA. We consider these to be generally reasonable and in line with accepted industry metrics.

    In addition, we agree that bond issuance amount outstanding is the appropriate criterion for assessing liquidity. This metric reflects the change in the liquidity profile of a particular issuance over time and is commonly used by fixed income indices.

12. **Do you agree with the proposed thresholds specified in the above Tables? If not, please justify by providing qualitative data to your analysis and differentiating per asset class.**

    FIA EPTA members agree with ESMA that the vast majority of transactions should be subject to real time reporting and that only a very small proportion of truly exceptional trades should be subject to the longest deferral period.

    Accordingly, we recommend that for corporate bonds the threshold for the maximum deferral period be set at EUR25 million to ensure only the most exceptional trades are captured. Referring to data published by Propellant.digital and ICMA for FY2023[4], in relation to EU Investment Grade corporate bonds, setting the threshold at EUR25 million would result in 6% traded notional falling within this category in contrast to 12% being captured when the threshold is at the proposed EUR15 million. This is a significant difference with 6% seemingly more appropriate as a reflection of trades to be considered truly exceptional. We would also suggest that the price deferral for category 3 corporate bonds is reduced from the End of Trading Day to 15 minutes.

    Whilst we do not disagree with using EUR50m as the higher threshold for sovereign bonds (at least as a starting point), EPTA members believe there is scope for this threshold to be considerably higher when one considers the market liquidity. For example, the main German bond future can have EUR200m on the Best Bid and Offer and, therefore, German bond trades up to that size can be immediately hedgable implying that the higher threshold for that German bond should be above EUR200m. We would, therefore, encourage ESMA to continue to set as ambitious levels as possible when it comes to reviewing these thresholds.

    In this regard we cite the premise that deferral periods should be based on the time a firm takes to hedge a position rather than the time to taken to economically unwind that position. We acknowledge that an important consideration in setting deferral thresholds is protecting capital at risk. However, balanced against the benefits to the market of greater transparency as the counter-point to capital protection, risk management is appropriately addressed via efficient hedging practices rather than exiting a position altogether.

    In addition, we strongly recommend that the publication thresholds should be set at "less than **or equal to**", not merely "less than". Trades sizes tend to towards round increments, particularly at the threshold levels proposed by ESMA. Therefore this distinction will have a

[4] ICMA-SMPC-report-European-Secondary-Bond-Market-Data-H2-2023-March-2024-190324.pdf (icmagroup.org)

significant impact at the margins in terms of the notional value subject to greater transparency.

By way of illustration, again using the Propellant.digital and ICMA data referred to above and regarding corporate bonds only, activity at trade sizes between 950k-999k and 1000001-1049999 is responsible for only 0.2% and 0.1% of notional respectively. However, trading at EUR1 million precisely is 6.1% of the traded notional.

Trade Size (EUR)	Percent of Total Notional (EUR)	Percent of Total Transaction Count
1,000,000	6.1%	4.9%
2,000,000	5.3%	2.1%
5,000,000	6.7%	1.1%
10,000,000	4.8%	0.4%
15,000,000	1.3%	0.1%
20,000,000	1.4%	0.1%

13. Do you agree with the maximum deferral period set out in the tables above?

FIA EPTA members are very supportive of ESMA proposal not to take up the maximum deferral period allowed under the text of the MiFIR Review and to only defer price publication until the end of the trading day with respect to large trades. Whilst in all cases, our members have a strong preference for publication of both price and volume information, we nevertheless see these proposals as a step in the right direction towards meeting the MiFIR Review's objectives of bringing greater transparency to non-equity markets. This timely provision of pricing information will aid trading and price discovery and contributes valuable simplicity to the regime.

In addition to supporting the objective of increasing transparency in aid of price formation, it will also make more data available to assess execution quality, enhance competition through reducing information asymmetry and enable sounder risk management through supporting more accurate data-driven decision making. Facilitating more timely publication of price and volume information will also support the value and efficacy of the bonds consolidated tape.

Longer deferral periods result in large information asymmetries forcing market participants to maintain wider spreads than would be needed if they had access to all relevant information. This results in liquidity deterioration and higher costs for end investors and is contrary to the objectives of MiFIR.

We see no logical justification for delaying price publication past End of Day and refer to the US TRACE model as demonstrating the effectiveness of an approach with real-time reporting of prices across all trade sizes. A four week deferral for publication of price and size is far too long even for the largest sized trades and presents no material difference from the existing transparency regime. We refer to the following studies which illustrate the benefits of a more ambitious transparency regime as represented by the US TRACE model:

- Bessembinder, H., et al., “Market transparency, liquidity externalities, and institutional trading costs in corporate bonds” (2006) Journal of Financial Economics, available at: https://www.researchgate.net/publication/222515781_Market_Transparency_Liquidity_Externalities_and_Institutional_Trading_Costs_in_Corporate_Bonds

- Edwards, A. K., et al., “Corporate bond market transaction costs and transparency” (2007) The Journal of Finance, available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=593823

- Goldstein, M. A., et al., “Transparency and liquidity: A controlled experiment on corporate bonds” (2007) Review of Financial Studies, available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=686324

- Asquith, P., et al., “The Effects of Mandatory Transparency in Financial Market Design: Evidence from the Corporate Bond Market” (April 2019), available at: https://www.nber.org/papers/w19417

- Jacobsen, S., et al., “Does trade reporting improve market quality in an institutional market? Evidence from 144A corporate bonds” (2018) at pages 1 and 7, available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3171056

We acknowledge that ESMA is empowered under the MiFIR Review pursuant to amended article 11(3)(h) to recalibrate deferral duration on a periodic basis with the aim of gradually decreasing it. We support this measure and encourage ESMA to be ambitious in its approach in order to realise the benefits of a more ambitious transparency regime as evidenced by the US experience. We believe a pragmatic and ambitious approach will be facilitated by the improved data available from the enhanced transparency regime and the emergence of the bond consolidated tape.

14. **Do you agree with a static determination of liquidity and determine that all SFPs are illiquid? If not, can you suggest any alternative methodology on how to define liquidity for SFPs?**

No comment

15. **Do you agree not to introduce changes to the threshold size currently applicable to SFPs as provided in RTS 2?**

No comment

16. **Do you agree with the maximum duration proposed?**

No comment

17. **Do you agree with a static determination of liquidity and determine that all EUA are liquid? If not, can you suggest any alternative methodology on how to define liquidity for EUAs?**

No comment

18. **Do you agree with the proposed framework for the deferral regime for EUAs? If not, please suggest an alternative methodology.**

    No comment

19. **Do you agree with the classification of ETCs and ETNs as types of bonds?**

    We support the proposal to continue to treat ETCs and ETNs as types of bonds where post-trade deferral thresholds are in line with ETFs.

20. **Do you agree with the liquidity determination for ETCs and ETNs. If not, please suggest an alternative approach to the liquidity determination.**

    We support the proposal. This is an appropriate simplification for reporting firms and report data consumers given the expected liquidity profile of instruments of this kind.

21. **Do you agree with the pre- and post-trade thresholds? If not, please suggest an alternative methodology.**

    We support the proposed new thresholds. We note that, as RTS 2 instruments, ETCs and ETNs would continue to be subject to a longer deferral period than ETFs. In the absence of supplementary deferrals, our view is that this T+2 deferral is appropriate given the illiquidity of the instrument and the generally narrower base of underliers exhibited by instruments of this kind.

22. **What is your view in relation to the implementation of the supplementary deferral regime for sovereign bonds?**

    No comment

23. **Do you agree not to make any changes to the temporary suspension of transparency obligations framework as it currently in RTS 2?**

    No comment

24. **Do you have any further comment or suggestion on the draft RTS? Please elaborate your answer.**

    No comment

25. **What level of resources (financial and other) would be required to implement and comply with the draft amended RTS and for which related cost (please distinguish between one off and ongoing costs)? When responding to this question, please provide information on the size, internal set-up and the nature, scale and complexity of the activities of your organisation, where relevant.**

    No comment