Review of the Markets in Financial Instruments Directive

BMW AG: Questionnaire on MiFID/MiFIR 2 by Markus Ferber MEP

The questionnaire takes as its starting point the Commission's proposals for MiFID/MiFIR 2 of 20 October 2011 (COM(2011)0652 and COM(2011)0656).

All interested stakeholders are invited to complete the questionnaire. You are invited to answer the following questions and to provide any detailed comments on specific Articles in the table below. Responses which are not provided in this format may not be reviewed.

Respondents to this questionnaire should be aware that responses may be published.

Please send your answers to econ-secretariat@europarl.europa.eu **by 13 January 2012.**

Theme	Question	Answers
Scope	1) Are the exemptions proposed in Directive Articles 2 and 3 appropriate? Are there ways in which more could be done to exempt corporate end users?	The exemptions in Articles 2 and 3 present a step in the right direction with regard to the non-financial companies' usage of derivatives. We embrace the clarification of the term **"ancillary activities"** in art. 2 para. 3 MiFID. This ensures that non-financial corporate are able to deal on own account in commodity derivates without being confronted with the risk to be covered by the regulatory framework of MiFID / MiFIR. However, it is still vitally important to translate these exemptions into clear legal language, i.d. non-financial companies are using derivatives mainly for hedging purposes and are, therefore, exempted from MiFID / MiFIR. Furthermore, it is important that the interaction of the exemptions in art. 2 para. 1 lit. d and art. 2 para. 1 lit. i is clarified for commodity derivatives and emission allowances. The fundamental reason is to avoid uncertainty e.g. for

		firms that can benefit from the ancillary activity exemption but that are at the same time market makers, members of regulated markets or MTFs. Still, it is necessary to emphasize that corporates trading financial instruments besides commodity derivatives and emission allowances on own account can benefit from the ancillary exemption without any limitation. Besides that, we believe the term **"participants in a regulated market or MTF"** in art. 2 para. 1 lit. d (ii) is misleading because it might indicate that every market participant who deals in financial instruments on own account on regulated markets or MTFs is obliged to be authorized under MiFID / MiFIR. Thus, we suggest that "to participate" should be replaced by "to be admissible" for trading on regulated markets as defined for example in art. 16 of the German stock exchange act. This would guarantee that merely persons who gained admission to trade directly on regulated markets are excluded from the above mentioned exemption.
	2) Is it appropriate to include **emission allowances** and **structured deposits** and have they been included in an appropriate way?	In spite of the similarity to other categories of financial instruments (e.g. transferable securities), emission allowances are different due to several reasons: they do not confer financial claims against the public issuer of such allowances; and they do not represent titles to capital or titles to debentures or constitute forward contracts. Moreover, the primary purpose of emission allowances is not to serve as an investment product but to value the emissions of carbon dioxide by market prices and thereby to improve the cost-effectiveness of climate protection measures.

		Increasing transaction costs by expanding MiFID / MiFIR requirements on emission allowances will further hamper the efficiency of the ETS. These additional costs are not accompanied by any benefits especially regarding investor protection. Participants in emission trading are exclusively professional clients. Therefore, there is no reason to protect these investors by the MiFID / MiFIR rules.
	3) Are any further adjustments needed to reflect the inclusion of **custody** and **safekeeping** as a core service?	n.a.
	4) Is it appropriate to **regulate third country access to EU markets** and, if so, what principles should be followed and what precedents should inform the approach and why?	Regulating third country access to EU markets is appropriate to avoid any distortion of the competitive environment. However, no two regulatory regimes are identical in all respects. For this reason, equivalence should be defined in terms of intent rather than in terms of specific rules.
Corporate governance	5) What changes, if any, are needed to the new requirements on corporate governance for investment firms and trading venues in Directive Articles 9 and 48 and for data service providers in Directive Article 65 to ensure that they are proportionate and effective, and why?	n.a.
Organisation of markets and trading	6) Is **the Organised Trading Facility category** appropriately defined and differentiated from other trading venues and from systematic internalisers in the proposal? If not, what changes are needed and why?	In our opinion, the OTF category should exclude pure OTC trading (see questions 7 for our definition), especially the systems used exclusively for pure OTC trading of derivatives between non-financial counterparties. The rather broad definition of "organised trading facilities" might include platforms which are neither relevant for investor protection nor have an effect on financial stability. For instance, this applies for electronic platforms

		like 360T. The definition of OTF should therefore be restricted to "trading platforms" in the classical meaning.
	7) How should **OTC trading** be defined? Will the proposals, including the new OTF category, lead to the **channelling** of trades which are currently **OTC** onto organised venues and, if so, which type of venue?	OTC derivatives trading should be defined as opposite to the trading of standardised instruments. Most importantly, it should be acknowledged that derivatives used for hedging purposes only are not a threat to financial stability and should thus be allowed to be traded OTC in future. This would also take the heavy dependency of corporates on OTC derivatives into account. Since standardised derivatives eligible for trading on exchanges do not meet corporates' needs to effectively hedge risks resulting from their operative business, corporates need tailor-made OTC products in order to hedge effectively. Two different ways exist how OTC derivatives are negotiated between non-financial counterparties and their financial counterparty. 1) Larger transactions in particular are often agreed by phone. 2) For other derivatives (the "day-to-day-business") corporates use electronic platforms. These platforms include e.g. 360T, Currenex and Fxall. Apart from saving transaction costs these platforms offer further advantages: They offer transparency to the users enabling them to assess the soundness and fairness of the price formation process and to secure processes based on corporate needs. In spite of the fact that these platforms offer multilateral access they are not considered "trading platforms" due to the fact that trading by investors within a liquid secondary market does not take place. Trading on these platforms should be furthermore regarded as pure OTC trading and should be excluded from the

		scope of MiFID / MiFIR. However, the broad definition of an „organised trading facility (OTF)“ in MiFID / MiFIR poses the threat that these electronic platforms will be covered by the scope of MiFID / MiFIR (see also qu. 6). Eventually, this could lead to the undesired fact that non-financial companies are in the focus of MiFID / MiFIR, although they are exempted from the trading obligation according to art. 24 et seq. MiFIR. Certain problems arise from this indirect impact of MiFID / MiFIR especially regarding pre- and post-trade transparency requirements (art. 7 et seq. MiFIR) which also include „derivatives admitted to trading or which are traded on an MTF or an OTF” (art. 7 para. 1 and art. 9 para. 1 – see our answer to question 22 below).
	8) How appropriately do the specific requirements related to algorithmic trading, direct electronic access and co-location in Directive Articles 17, 19, 20 and 51 address the risks involved?	
	9) How appropriately do the requirements on resilience, contingency arrangements and business continuity arrangements in Directive Articles 18, 19, 20 and 51 address the risks involved?	
	10) How appropriate are the requirements for investment firms to keep records of all trades on own account as well as for execution of client orders, and why?	

	11) What is your view of the requirement in **Title V** of the Regulation for specified derivatives to be traded on **organised venues** and are there any adjustments needed to make the requirement practical to apply?	Our answers to questions 7 and 22 raise transparency issues which are also of importance for non-financial companies obliged to central clearing after crossing the clearing threshold. According to that, they are required to trade eligible derivatives as described in art. 24 et seq. MiFIR on regulated markets, MTFs or OTFs. It should be taken into consideration that these companies do not conclude derivatives exclusively for trading purposes but first and foremost use these instruments for hedging reasons. This matter should consequently be reflected by the definition determining which classes of derivatives should be subject to the trading obligation. The two criteria mentioned so far – "eligibility for clearing" (art. 26 para. 1 lit. a) and "sufficiently liquid" (art. 26 para. 3) – do not take these concerns adequately into consideration. We therefore recommend adding a further criterion which takes into account whether the purpose of the derivative transaction is hedging or not. The proposal could refer to the definition of "hedging" developed by ESMA / the EU-Commission within EMIR. This would ensure that derivative transactions which are eligible to be settled on electronic platforms as mentioned in our answer to question 7 but are not eligible for trading are exempted from the trading obligation. The problem regarding transparency obligations could be circumvented thereby. The suggested amendment would also not create problems with regard to supervisory requirements and investor protection (see our answer to question 22). We therefore suggest amending art. 26 para. 3 as follows: […] ***(d) the specifics of the derivative (e.g. whether they are be-***

		spoke in their design or used for hedging purposes as defined by ESMA / EU-Commission in Regulation [ ] (EMIR)).
	12) Will SME gain a better access to capital market through the introduction of an MTF SME growth market as foreseen in Article 35 of the Directive?	
	13) Are the provisions on non-discriminatory access to market infrastructure and to benchmarks in Title VI sufficient to provide for effective competition between providers? If not, what else is needed and why? Do the proposals fit appropriately with EMIR?	
	14) What is your view of the powers to impose **position limits**, alternative arrangements with equivalent effect or manage positions in relation to commodity derivatives or the underlying commodity? Are there any changes which could make the requirements easier to apply or less onerous in practice? Are there alternative approaches to protecting producers and consumers which could be considered as well or instead?	We strongly support the view, that **mandatory position limits** set by market operators are not justified. Nowadays market operators already apply such limits from case to case in order to secure the efficiency of markets. As the proposed obligation is very detailed it would limit the discretion and flexibility of market operators to react appropriate to certain market conditions. Consequently, art. 59 MiFID should be deleted. In particular, the **real-time reporting requirement** is very costly for corporates and does not offer any additional benefits. EMIR already requires market participants to report their derivative transactions to trade repositories. Double reporting should be avoided as stated in recital 29 MiFIR. Therefore, we suggest to delete art. 60 para. 2.

Investor protection	15) Are the new requirements in Directive Article 24 on independent advice and on portfolio management sufficient to protect investors from conflicts of interest in the provision of such services?	
	16) How appropriate is the proposal in Directive Article 25 on which products are complex and which are non-complex products, and why?	
	17) What if any changes are needed to the scope of the best execution requirements in Directive Article 27 or to the supporting requirements on execution quality to ensure that best execution is achieved for clients without undue cost?	
	18) Are the protections available to eligible counterparties, professional clients and retail clients appropriately differentiated?	
	19) Are any adjustments needed to the powers in the Regulation on product intervention to ensure appropriate protection of investors and market integrity without unduly damaging financial markets?	
Transparency	20) Are any adjustments needed to the pre-trade transparency requirements for shares, depositary receipts, ETFs, certificates and similar in Regulation Articles 3, 4 and 13 to make them workable in practice? If so what changes are needed and why?	
	21) Are any changes needed to the pre-trade transparency requirements in Regulation Articles 7, 8, 17 for all organised	

	trading venues for bonds, structured products, emission allowances and derivatives to ensure they are appropriate to the different instruments? Which instruments are the highest priority for the introduction of pre-trade transparency requirements and why?	
	22) Are the **pre-trade transparency requirements** in Regulation Articles 7, 8 and 17 for trading venues for bonds, structured products, emission allowances and derivatives appropriate? How can there be appropriate calibration for each instrument? Will these proposals ensure the correct level of transparency?	The high transparency requirements will affect corporate hedging strategies in a negative way for a variety of reasons (see question 7: non-financial end users use derivatives mainly to cover risks connected to the underlying business): 1) The publication of an order book including bespoke derivatives with individual agreed characteristics regarding maturity and volume does not seem to be very meaningful. An "order book" for these derivatives would generally comprise one order, namely that from the non-financial company requesting a bespoke transaction on these electronic platforms. Besides the administrative burden for the platform operator to publish these order books it is not comprehensible what value the information provided should have for end users. On the contrary especially in narrow markets, the transparency obligation might bear the risk that all market participants would be able to identify the non-financial company and thus there hedging strategy. This in turn would increase prices and raise hedging expenses. 2) Additionally, non-financial companies participating in derivative transactions are considered as professional clients and therefore do not need the same degree of protection as in secondary markets where retail or institutional investors are involved.

		3) Neither does any justification exist for transparency requirements in MiFID / MiFIR on the part of supervisory authorities. EMIR already provides the obligation for market participants to report derivative transactions to trade repositories. For these reasons, we suggest to restrict the pre- and post-trade-transparency obligations of art. 7 and 9 MiFIR to counterparties which are subject to the trading obligation in art. 24 et seq. This would exempt non-financial companies with a stock of derivatives not exceeding the clearing threshold defined in EMIR and would also take into account recital 12 MiFIR which explicitly outlines that OTC-derivatives are not covered by the transparency regime. Articles 7 para. 1 and 9 para. 1 regarding pre- and post-transparency on regulated markets, MTFs and OTFs should be amended as follows: Art. 7 para. 1: Regulated markets and investment firms and market operators operating an MTF or an OTF based on the trading system operated shall make public prices and the depth of trading interests at those prices for orders or quotes advertised through their systems for bonds and structured finance products admitted to trading on a regulated market or for which a prospectus has been published, emission allowances and for derivatives ***which are subject to the trading obligation as referred to in Art. 24.*** […] The aforementioned exemption should also cover transparency requirements for systematic internalisers (art. 17 and 20). Given that the EU-Commission has announced to widen the scope of

		the definition for systematic internaliser we assume that many financial counterparties of corporates will be covered by these provisions when MiFIR / MiFID is adopted. Therefore, the problems regarding transparency mentioned above are also relevant in regard to systematic internaliser.
	23) Are the envisaged waivers from pre-trade transparency requirements for trading venues appropriate and why?	
	24) What is your view on the data service provider provisions (Articles 61 - 68 in MiFID), Consolidated Tape Provider (CTPs), Approved Reporting Mechanism (ARMs), Authorised Publication Authorities (APAs)?	
	25) What changes if any are needed to the post-trade transparency requirements by trading venues and investment firms to ensure that market participants can access timely, reliable information at reasonable cost, and that competent authorities receive the right data?	Please, see answer to question 22.
Horizontal issues	26) How could better use be made of the European Supervisory Authorities, including the Joint Committee, in developing and implementing MiFID/MiFIR 2?	
	27) Are any changes needed to the proposal to ensure that competent authorities can supervise the requirements effectively, efficiently and proportionately?	
	28) What are the **key interactions** with **other EU financial services legislation** that need to be considered in develop-	From the corporate perspective, the intended extensive expansion of supervisory powers (product intervention and position

	ing MiFID/MiFIR 2?	mangement, art. 31,32 MiFIR) could arbitrarily affect our risk management practices. We are also afraid that possible exemptions in the European Market Infrastructure Regulation (EMIR) might be contradicted by MiFID/MiFIR II. Due to the far-ranging definition of these supervisory rights and vague definition of the circumstances triggering these measures we are concerned that the sole possibility of applying these instruments could deter non-financial companies from mitigating their operative risks by means of derivatives. In order to guarantee consistency with EMIR, derivatives of non-financial companies which are not obliged to clear should be exempted from the above mentioned supervisory measures. This would be consistent with the common understanding that OTC derivatives of non-financial companies are used for hedging purposes and therefore do not increase systemic risks. Therefore, we recommend the following amendments in art. 31 para. 1 lit. b and art. 32 para. 2 lit. e: ***[…] Derivative transactions of non-financial counterparties which are not subject to the clearing obligation as defined in Art. 5 para. 1 of Regulation […] (EMIR) shall be exempted from the prohibition or restriction.*** The same logic applies to position limits imposable by ESMA (Art. 35 MiFIR) or local authorities (Art. 72 MiFID).
	29) Which, if any, interactions with similar requirements in major jurisdictions outside the EU need to be borne in mind and why?	

	30) Is the sanctions regime foreseen in Articles 73-78 of the Directive effective, proportionate and dissuasive?	
	31) Is there an appropriate balance between Level 1 and Level 2 measures within MIFID/MIFIR 2?	
Detailed comments on specific articles of the draft Directive		
Article number	**Comments**	
Article ... :		
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