Deutsche Bank
Global Equities

Global Market Structure – Europe

Execution Excellence

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MiFID II: What is new for buy side?

Pre and Post Trade Transparency- Equity Derivatives

Briefing Note

What is happening?

- MiFID II will introduce enhanced pre and post trade transparency obligations on trading venues and investment firms for trading in equity derivatives. For a general overview of obligations, see our document on Topic 6.
- Investment firms trading in instruments[1] traded on European trading venues (TOTV instruments) on a regular basis outside the rules of trading venue will need to register as a 'Systematic Internalisers' (SI) in those instruments. Unlike MiFID I, where registering as SIs is optional, MiFID II will make it mandatory, from September 2018, for firms to register as SIs where their OTC volumes in an instrument are substantial when compared with total EU trading in that instrument.
- Investment firms may elect to 'opt-up' as SIs in instruments even where their OTC volumes do not meet the defined thresholds. An Investment firm can elect to be an SI from 3rd January 2018.
- SIs are defined as 'execution venues' under MiFID II and will be subject to transparency obligations in respect of TOTV instruments.
- This document outlines the manner in which DB will meet its transparency obligations.

What are the pre trade transparency obligations on DB?

- Firms when acting as SIs, who agree to provide a quote, are required to make quotes in TOTV instruments public, for:
  - Instruments classified as 'liquid'; and
  - Where the requested quote size is below 'Size Specific to Instrument' (SSTI)

  Liquidity of an instrument is determined as per Article 13, RTS 2. See Appendix 1 for a list of equity derivatives considered to have a liquid market.

  ESMA's latest guidance provides SSTI thresholds for pre trade transparency purposes for equity derivatives.
- When acting as an SI, DB will publish eligible quotes via the Tradeweb system.
- Access to the Tradeweb system is available by contacting Europe.APA@tradeweb.com.

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[1] 'Instruments' includes shares, depositary receipts, ETFs, certificates (collectively referred to as 'equity like instruments') and bonds, structured finance products, emission allowances and derivatives (collectively referred to as 'non-equity instruments').

- Eligible pre trade quotes in TOTV instruments will be made public during Tradeweb's working hours.
- Eligible quotes will be provided by personnel operating on behalf of DB from EEA locations only. These quotes may be accessed by all clients, regardless of their location.

SSTI and Liquidity Assessment for Certain Equity Derivatives

- ESMA published SSTI and Large in scale (LIS) thresholds for 'liquid' equity derivatives. It is not clear whether they will also publish a list of equity derivatives which are deemed to not have a liquid market.
- Certain equity derivatives by default are considered to have a liquid market, and this includes stock index options, stock options, stock index futures and forwards, ETF options and ETF futures and forwards[2]. In the spreadsheet provided by ESMA for SSTI and LIS thresholds for liquid equity derivatives, only certain ISINs for such derivatives are enumerated. However, this does not mean that other such derivatives which are not specifically indicated in the spreadsheet are not considered to be liquid. For such derivatives, SSTI and LIS thresholds will be those applicable to the smallest average daily notional amount (ADNA) band for that sub-asset class.[3]
- For equity and portfolio swaps, liquidity is to be assessed periodically based on quantitative and qualitative criteria. Equity and portfolio swaps are not initially considered liquid by ESMA and they also do not appear in the spreadsheet provided for liquid equity derivatives. Therefore, on this basis, the industry wide consensus is that no equity and portfolio swaps are deemed liquid at this point in time. This position could change if ESMA make liquidity assessments for these instruments and publish thresholds for specific swaps that meet the liquidity criteria.

What are the post trade transparency (trade reporting) obligations for DB?

- Unlike pre trade transparency requirements which only apply to SIs, post trade transparency requirements are applicable to all investment firms that trade, on an OTC basis, instruments which ESMA considers to be TOTV.
- The post trade transparency obligations require Investment firms to publish, the ISIN, volume, price and time of trade, within 15 minutes of execution, subject to applicable deferrals (see below).
- Post trade transparency obligations apply to investment firms only when they trade on an OTC basis and when they trade on certain third country trading venues.
- The obligation to post trade report will always sit with the SI.
- However, where neither party to the trade is an SI, or where both parties to the trade are SIs; the seller of exposure is obligated to publish the post trade report.
- Trades concluded on EEA trading venues are reported by the trading venue and do not have to be re-reported by investment firms.
- For trades concluded by MiFID Investment firms on Third Country Venues: ESMA stated in its opinion on 'Determining Third Country Venues for the Purpose of Transparency under MiFID II/ MiFIR' that DB (along with other MiFID II firms) will be required to report transactions via its APA in TOTV instruments undertaken on a Third country trading venue that ESMA considers not having a 'similar' post trade transparency regime as EEA venues. Conversely, if the Third country venue is considered to have a 'similar' post trade transparency regime, then DB will not be required to re-report the transaction in the EEA.
- ESMA has stated that it will publish a list of Third country venues that it will consider 'similar' for post trade transparency purposes and has asked firms to nominate venues for inclusion.
- The above stated principles will apply to all transactions in TOTV instruments booked into DB group's entities located within the EEA.

Which transactions are eligible for deferrals?

- Regulators may allow trading venues and investment firms to delay the publication of trade reports on the basis of the type and size of the transaction.

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[2] See complete list in Table 6.1, RTS 2.
[3] Article 13(14), RTS 2. Thresholds provided in Table 6.2, RTS 2.

- National Competent Authorities decide which deferrals to grant and their length, therefore, deferrals may vary among jurisdictions.
- The deferral time ranges from 2 days to 4 weeks and also includes an aggregation option for certain instruments.
- In particular, deferrals may be granted for the following transactions:
  - Large in scale transactions
  - Transactions in illiquid instruments
  - Transactions larger than SSTI where an investment firm is dealing on own account other than on matched principal basis
  - Certain package transactions

How will ESMA decide what OTC derivatives are TOTV?

- ESMA in its opinion on 'OTC Derivatives Traded on a Trading Venue' noted that it is essential to delineate the OTC derivatives that are within the scope for pre and post trade transparency because they are less standardised and often arise from bilateral contracts between two counterparties.
- Under RTS 23, trading venues will be required to submit reference data for instruments traded on their platforms to their national competent authorities on a daily basis. National competent authorities will then relay this information to ESMA who will consolidate all reference data and publish.
- ESMA is of the view that only those OTC derivatives sharing the same reference data details (published per RTS 23) as the derivatives traded on trading venues should be considered to be TOTV.
- In this context, "sharing the same reference data details" should mean that the OTC derivatives should have matching/identical values as the ones reported in accordance with RTS 23 for derivatives admitted to trading or traded on a trading venue. Fields 5-12 are not to be included in TOTV assessment as those relate to information about the trading venue and the issuer.
- In this respect, ISDA has highlighted concerns around matching of fields. One of the fields that should match is the ISIN of the derivative. For OTC derivatives, ISIN generation does not take into account the fixed rate or strike price of the derivative. However, for TOTV determination, ESMA's approach requires the matching of the fixed rate and strike price fields also. This would effectively mean that there would be derivatives with the same ISIN but with different fixed rate/ strike price having different TOTV status. Besides, an instrument will not be identifiable as TOTV with only the help of its ISIN, because the ISIN does not capture all attributes in RTS 23.
- Therefore, in the interests of transparency, ISDA has suggested that TOTV should be aligned at the ISIN level. To achieve this, ISDA proposed that for some classes of OTC-derivatives, fixed rate and strike price should not be included in assessing whether the derivative is TOTV or not. ESMA has not thus far either endorsed or rejected this proposal.

Global Market Structure - Europe

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Appendix 1

Sub-asset classes deemed to have a liquid market- Annex III, Table 6.1, RTS 2

1. Stock index options
2. Stock index futures
3. Stock options
4. Stock futures/forwards
5. Stock Dividend options
6. Stock dividend futures/forwards
7. Dividend index options
8. Dividend index futures/forwards
9. Volatility index futures/forwards
10. Volatility index options
11. ETF options
12. ETF futures/forwards

Please note that Swaps are not considered to have a liquid market by default and liquidity determination for each sub-asset class of swaps has to be done in accordance with Table 6.1, Annex III, RTS 2.

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