ICI Global Response to MiFID/MiFIR ESMA Consultation

Section 2.15 – Legitimacy of inducements to be paid to/by a third person

Q79. **Do you agree with the proposed exhaustive list of minor non-monetary benefits that are acceptable? Should any other benefits be included on the list? If so, please explain.**

ICI Global is concerned that the end result of ESMA's proposed advice may be to ban portfolio managers from acquiring value-adding investment research from dealing commission on the grounds that such arrangements constitute an inducement. We disagree that the purchase of investment research from dealing commissions should be characterised as an inducement under Article 24(6) of MiFID II and believe that banning its purchase from dealing commission was not the intention of the co-legislator. We recommend that ESMA consider an approach that focuses on the management of conflicts of interest and also conduct a thorough impact analysis before proposing changes.

The purpose of using dealing commission arrangements to buy investment research – which is a globally adopted model – is to provide investment managers with valuable research to inform their investment decision making process for the benefit of their clients. Receipt of research is not an inducement but a service *knowingly* paid for by the client to enhance the quality of the service in the best interests of the client. As such, dealing commission arrangements to pay for research are different to other arrangements that may be characterised as inducements that influence the recipient's behaviour in a way that is detrimental to its clients. Accordingly, we do not agree that the acquisition of research from dealing commission should be viewed as an inducement for these purposes, and should be outside the scope of the inducements provisions.

Instead, we believe dealing commission arrangements for the purchase of research should be analyzed as an arrangement that potentially poses conflicts of interest. Any conflicts can, in our view, be addressed proportionately through a combination of (i) governance and oversight of commission spend; and (ii) effective disclosure, rather than adopting a ban on the use of dealing commission to buy research (specific suggestions for oversight and controls are discussed below in the section on Elimination of Benefits Resulting from Existing Regime). Underpinning any changes to the use of dealing commission for research, we recommend recognizing that portfolio managers owe a fiduciary duty to investors to ensure that their accounts are managed and money is spent consistently with this duty. As such, managers must manage conflicts of interest. The approach taken by ESMA could be seen as essentially removing portfolio managers from their role as fiduciaries in this area, and undermining their ability to act as fiduciaries in other areas.

ICI Global stresses that, as discussed below, the European approach ultimately adopted could have a wide-ranging impact on the European and global investment management industry, the sell side and clients. As such, we recommend that ESMA reconsider its approach and conduct an extensive impact analysis before proposing changes. We urge ESMA to consider an approach that focuses instead on the management of conflicts of interest.

Disagree with ESMA's Exhaustive List of Non-Monetary Benefits

We do not agree with ESMA's proposal that the Commission should introduce an exhaustive list of minor non-monetary benefits that would be acceptable. An exhaustive list is not stipulated by the Level 1 Directive, is not sought by the Commission in its request for advice and risks the omission of items that would nonetheless satisfy the criteria set out in the Level 1 Directive (i.e., benefits capable of enhancing the quality of service provided to clients and of a scale and nature such that they could not be judged to impair compliance with the firm's duty to act in the best interests of the client). This is particularly the case because, as discussed below, the impacts of what is being proposed are unexamined and could have significant consequences. We do, however, support the idea of having a list of minor non-monetary benefits that would be deemed to be acceptable – we believe this would be helpful, provided this is indicative and non-exhaustive, and is expressed to be without prejudice to the qualitative criteria set out in Level 1.

We welcome the fact that ESMA recognises that, in principle, financial analysis could constitute a minor non-monetary benefit and we believe that this should be contemplated in the non-exhaustive list of non-monetary benefits that can be considered to be minor. However, we disagree with ESMA's conclusion in its commentary that, based on the intention of the "minor non-monetary benefits" exemption, any research that involves a third party allocating valuable resources to a specific portfolio manager (such as providing tailored, bespoke or rationed research or privileged access to research analysts) cannot be considered a minor non-monetary benefit. Indeed, ESMA's own draft technical advice refers to the fact that information (including financial research) could be generic in nature or *personalised to reflect the circumstances of an individual client*.

Before ESMA provides final advice that affects the receipt of research by MiFID investment firms, a thorough and in-depth impact analysis should be conducted examining the effects on (1) investment firms and their clients (including regulated funds, and their investors) and (2) the availability, accessibility, and quality of research that would be provided under the changed regime. As described below, we are concerned that the effect of the Level 1 ban on the acceptance of benefits together with the nature of ESMA's proposed advice on research as a minor non-monetary benefit would have significant negative, and unintended, consequences that would harm certain investment firms, small and medium-sized issuers, and small or niche research providers.

Accordingly, we propose that ESMA consider that research not be dealt with under the inducements provisions. If ESMA feels compelled to address the acquisition of research through dealing commission under the inducements provisions, it is our view that it should be permitted given that such arrangements, subject to the management of conflicts of interest, can actually support an investment firm's duty to act in the best interest of its clients. Any list of non-monetary benefits that are acceptable should be non-exhaustive and should demonstrate the types of non-monetary benefits that meet the requirements of Article 24(8) of the Level 1 text.

A. Proper Impact Analysis is Needed Regarding Any Change to the Existing Research Regime

A change to the research and dealing commission regime of the magnitude contemplated by ESMA in its interpretation of the Level 1 text should be undertaken only after a proper impact analysis that thoroughly considers the benefits and consequences of the proposed changes. We recognize that ESMA has stated that it is preparing an impact assessment for the technical standards and undertaking a data gathering exercise to support its technical advice and we assume that this will include a fulsome analysis of the impact, including any benefits, of its proposed changes to the interpretation of research and the use of dealing commission.

Based on information publicly available, there is no record in the negotiations over MiFID Level 1 text necessitating the outcome being put forth by ESMA. The original Commission text did not include reference to non-monetary benefits; rather, inclusion of a prohibition on non-monetary benefits was added by Parliament and Council at a later stage. While the Commission produced an impact analysis in October 2011, it includes neither non-monetary benefits nor research, and merely states that, with respect to a ban on inducements for portfolio managers, the Commission expects overall one-off cost implications of about €131 million, and on-going costs of €3.7 million.

The public record demonstrates no consideration or intention of the co-legislators to introduce the proposed constraint on the use of dealing commission to pay for research. ESMA should not, in these circumstances, reach an interpretation that is not reflected in the legislators' intent. Considering the potentially significant negative impacts of ESMA's proposed interpretation, we strongly urge ESMA to refrain from interpreting the Level 1 text in this manner and instead to undertake a thorough impact analysis, with public input, to fully understand the effect on investment firms and their clients, as well as on the market and firms providing research. We believe that such an analysis will demonstrate that dealing with the linkage between research and dealing commission under relevant conflicts of interest requirements rather than the inducements provision is the appropriate and best way forward.

B. Significant Negative Consequences

In our view, restricting potentially allowable research to only the most widely distributed and generic research would have significant negative consequences that would disproportionately harm the provision of research, small and medium-sized issuers, small or niche research providers, and certain investment firms.

1. Challenges for Global Investment Firms

Many global investment firms currently operate trading and research platforms that are fully integrated in order to take advantage of economies of scale, for personnel reasons, and/or for operational alignment. These firms have incurred substantial costs to establish operations in the EU, anticipating that the global practice of using commissions to pay for research would remain consistent cross border. These firms may apply the same requirements to all their trading and research operations for purposes of global consistency. This is currently possible because existing regulatory regimes on the acquisition of research through dealing commission in the U.S., Europe and the rest of the world are sufficiently similar to permit a this approach. In our opinion, this is for good reason, with the benefits of acquiring research from dealing commission having been generally acknowledged.

In an increasingly connected cross border financial world, it becomes extremely difficult to accommodate European rules on dealing commission that differ markedly from those adopted elsewhere. Given the global nature of much of investment management, there are many different combinations of circumstances – the clients' jurisdictions, the investment firm's and their affiliates' jurisdictions, and the trading jurisdiction. The adoption of very different European rules would cause significant operational complexity, increased compliance burdens and costs, with significant disruption to the efficient and effective provision of research across funds and clients at a global level. It also would increase the cost of operating EU subsidiaries and servicing EU clients. Global investment firms would have to decide whether it is possible to maintain some type of integrated research and trading platform which accommodates the proposed European approach, or whether to bifurcate their approach to deal with different regulatory regimes.

In reality, it would be very challenging for investment firms to maintain integrated research and trading platforms. First, the existing regulatory regimes in other jurisdictions may make it difficult or expensive to accommodate the EU changes. Second, market participants in non-EU jurisdictions may be reluctant to operate under the EU's provisions with respect to only certain transactions (i.e., transactions for that firm), whether due to operational complexity, financial impact, or other reasons. Third, the operational complexity and the compliance burden may be too great to justify.

Conversely, it may be equally challenging for different parts of a global investment firm to comply with regulatory regimes for research and the use of dealing commission that vary greatly. Such an approach would be operationally challenging with significant compliance burdens and costs. Neither ESMA nor the co-legislators have considered or attempted to quantify these costs, but we believe they would be substantial. We also believe the end result would be increased fragmentation of service provision with the likely impact being increased costs and reduced research for European clients.

For large international firms, the inability to continue to use dealing commission to acquire research could be a significant disincentive to doing business in Europe.

2. Impact on Small and Medium-Sized Enterprises

We are also concerned that ESMA's proposed advice would harm small and medium-sized enterprises themselves. If investment firms are precluded from using dealing commission to obtain research of any real value, the availability of high quality research, particularly research relating to smaller and medium-sized enterprises that are not widely followed, may be drastically reduced. This concern was recognized in the IOSCO 2007 Final Report on Soft Commission Arrangements.[1] To the extent there is a contraction of the research provided on such an issuer, this may lead to lower liquidity in the shares of such issuer and wider spreads in the issuer's shares. An increase in the bid/offer spreads would increase the trading/investment cost for investors, thereby making investment in such issuers less desirable. Such a result would be contrary to the EU's recent efforts to promote investment in small and medium-sized enterprises.

3. Competitive Disadvantage for EU Firms and Their Clients

ESMA's proposed advice would also impact the international competitiveness of EU firms, and potentially harm their clients, including regulated funds and their investors. If these changes are made at only an EU level, EU firms would be at a disadvantage compared to U.S., Asian, and other investment firms that are not subject to these requirements and may continue to use dealing commission for permissible research. EU firms would need to pay for such research themselves, charge clients explicitly for research, or create research in-house.

It is incorrect to assume that banning bundled commission payments in Europe would lead to the end of dealing commission arrangements elsewhere. In Hong Kong, dealing commissions are permissible so long as there is a demonstrable benefit to the client. In the U.S., investment managers are permitted to use dealing commissions for research services provided the elements of Section 28(e) of the Securities and Exchange Act of 1934 are met. Specifically, an investment firm is permitted to cause an account to pay more than the lowest available commission if the firm makes a good faith determination that the amount of commission is reasonable in relation to the value of brokerage and research services provided by the broker and so long as the research services assist the investment firm in the investment decision-making process.

Further, EU investment firms and their clients may also be disadvantaged with respect to the receipt of brokerage services from brokers located outside the EU. Because the EU would severely restrict the use of dealing commission for research (essentially requiring unbundling), EU firms may find it challenging, or not possible, to separate the execution and research services provided by brokers that are not required to unbundle and do not typically do so. In certain jurisdictions, the brokerage industry may be unfamiliar with unbundling or simply be unwilling to unbundle. In such cases, the commission rate may not be reduced if the EU investment firm, complying with its legal requirements, declines research or other services typically provided by the broker as part of its bundled offering.

[1] See Soft Commission Arrangements for Collective Investment Schemes, Final Report, Report of the Technical Committee of IOSCO, available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD253.pdf, at 8.

Although the EU firm could arguably seek to transact with a broker that can accommodate its situation, this may not be possible where brokerage options are limited (and where the potential research that could be provided would, in reality, unlikely impact the investment firm's choice of execution venue).

In addition, global investment firms may currently aggregate trades for clients in multiple jurisdictions in order to take advantage of economies of scale and treat client orders equitably. To the extent that a global firm no longer aggregates trades for MiFID clients and trades them on an execution only basis, these clients may be disadvantaged. The impact of how transactions for clients of EU firms are traded could reduce the attractiveness of the EU as a location for investment firm operations.

4. Detrimental Impact on Small and Medium-Sized Investment Firms

If ESMA's proposed advice is adopted, we expect that small and medium-sized managers would be disproportionately and adversely impacted. Specifically, small and medium-sized investment managers with more limited financial resources may be unable to absorb the costs of buying research or producing it in house. Due to their size and stature, these firms may also be unable to negotiate terms to pay for research with hard dollars that are equal to those of large firms. Consequently, small and medium-sized firms may ultimately have reduced access to research, whether it is bespoke written reports, meetings with research analysts, or other currently permitted services. This more limited access would consequently damage their business and potentially hurt their clients. A decrease in small and medium-sized firms could ultimately be harmful to consumers as it would reduce industry competitiveness and choice for investors.

5. Impact on Small and Niche Research Providers

Specialist and independent research houses that provide valuable (but relatively expensive) research into emerging market companies, small and medium-sized enterprises, or otherwise expensive-to-research issuers could also be detrimentally impacted if the existing arrangements are disturbed. The number of firms that provide research on such issuers may therefore decline. This will ultimately impact asset managers, too, as they will have more difficulty obtaining high quality research on these securities.

A narrower range of views about stocks from a reduced number of research providers could lead to a reduction in liquidity, and significantly limit information in the marketplace. Investors are better served when more rather than less information and opinions are available in the marketplace because broadly available higher quality information results in more efficient markets and better price discovery.

6. Elimination of Benefits Resulting from Existing Regime

The current regime for the provision of research on a bundled basis has many benefits; ESMA's advice may eliminate some or all of these benefits to the detriment of investment firms and their clients. Among the benefits of the current bundled brokerage regime is broad coverage and availability of research due to economies of scale. In today's environment, having many research providers promotes the availability of multiple perspectives. Because the marginal cost of research is relatively low, research also may be provided to a large number of users, allowing both producers and consumers of the research to benefit from economies of scale. This broad coverage benefits both investment firms that rely solely on outside research, as well as firms with substantial in-house research capability, as they provide the benefit of another perspective. In addition, greater coverage of stocks also helps to keep markets well-informed and functioning most efficiently. This also benefits small and medium-sized investment firms that would otherwise not be able to obtain such research.

We believe the interests of investment firms and clients can be aligned under a bundled dealing commission regime. Investment firms seek to negotiate commission rates that provide clients with best execution and appropriate access to research; they have incentives to avoid paying unduly high commission rates because the cost of commissions affects the performance of a fund or client portfolio. Similarly, the current regime provides investment firms with a degree of flexibility and discretion regarding the valuation of and payment for research. This flexibility benefits clients by helping to ensure that investment firms do not pay (or overpay) for research that they do not value. In addition, under the current model, research providers bear the fixed expenses related to research, and investment firms are able to switch research providers without downside financial risk. This model benefits investments firms as well as investors because investment firms are able to utilize a large quantity of research for the benefit of investors, and only pay for the research they find useful.

We believe a fixed price model may have the effect of reducing research available to managers, and thus providing less information for the investment decision-making process. This would not be in the best interest of investors. Although research is currently paid for out of commissions, managers are disincentivised from overpaying brokers because this would impact the manager's performance figures (which are very significant to investors).

Further, the current global regulatory environment for dealing commission - in which bundled brokerage is permitted - allows investment firms to establish and thereby provide clients with benefits from its global relationships. As described above, however, a significant divergence in regulatory approaches will creates challenges and burdens for global platforms, to the detriment of clients.

In our view, the bundled brokerage model can continue to provide an effective and efficient way of providing access to execution and research services at a competitive rate if it is combined with appropriate oversight and controls, which may include:

a) Regular review of the type and value of research paid for with dealing commission.
b) Adoption of research budgets or other mechanisms to monitor the amount of dealing commission spent on research. These should be set at suitable frequency, typically not less than once a year. Clear controls should be in place to determine how and when any such research budgets or other mechanisms are altered.

c) Separation of trading and investment functions i.e., the trading desk should focus on seeking best execution when dealing with brokers, and the research portion of the commissions should be guided by the investment staff utilizing the research.
d) Commission sharing agreements (CSAs), which eliminate the need to direct trades to a particular broker in order to pay for research from that broker. CSAs allow the buy-side to recognize brokers who produce good research, without being under any obligation to recognize them by directing trades to them.
e) Commission recapture arrangements to claw back commissions once budgets are reached.
f) Creation of a committee that sets broad policy direction, and reviews decisions of working groups.
g) Reports to clients on the use of commissions to assist clients in understanding client commission practices.

ESMA may wish to consider whether addressing the use of dealing commissions for research under the Commission's request for advice on the conflicts of interest provisions of MiFID (Articles 16(3) and 23) would be more appropriate.

Q82. Do you anticipate any additional costs in order to comply with the requirements proposed in this chapter? If yes, please provide details.

Please see our response to Question 79 in which we outline our concerns with the potential significant negative consequences, and associated costs, with implementation of ESMA's proposed advice on research as a non-monetary benefit.

Q81. Do you agree with the non-exhaustive list of circumstances and situations that NCAs should consider in determining when the quality enhancement test is not met? If not, please explain and provide examples of circumstances and situations where you believe the enhancement test is met. Should any other circumstances and/or situations be included in the list? If so, please explain.

ICI Global recognizes that the MiFID Level 1 text treats inducements provided to independent advisers and non-independent advisers differently. In our view, this solution is not at all desirable because, despite other regulatory constraints on non-independent advisers, it creates the probability of unjustifiably different levels of protection, disclosure and transparency for the client buying similar products through different types of advisers. We believe that the EU must move to a more seamless and reasoned treatment of the receipt of inducements by all advisers so as to ensure that different standards of transparency, disclosure and protection cannot risk leading to customer detriment.

Section 2.7 – Product Governance

Q14. Should the proposed distributor requirements apply in the case of distribution of products (e.g. shares and bonds as well as over-the-counter (OTC) products) available on the primary market or should they also apply to distribution of products on the secondary market (e.g. freely tradable shares and bonds)? Please state the reason for your answer.

ICI Global believes that it is neither practical nor appropriate to extend the product governance requirements to the distribution of products on the secondary market. Many shares and bonds available on the secondary market are not, in fact, manufactured by a MiFID investment firm but rather issued by a non-financial company. Provided the issue complies with requirements under the Prospectus Directive and appropriate listing requirements, we do not see the need to extend the product governance rules to these types of instruments.

In the case of certain financial instruments that are manufactured by MiFID investment firms and traded on the secondary market, such as ETFs, distributors/advisers often invest their clients through the secondary market as these are listed instruments with active trading on an exchange. Distributors do not contract or transact directly with the ETF and there is often no direct link or visibility between the manufacturer of the ETF and the advisory entity acquiring shares in the ETF on behalf of its clients. In these cases, it would be impractical and not sensible for the manufacturer of the ETF to police and monitor the activities of distributors on the secondary market, when they do not have a contractual relationship with them.

Q15. When products are manufactured by non-MiFID firms or third country firms and public information is not available, should there be a requirement for a written agreement under which the manufacturer must provide all relevant product information to the distributor?

ICI Global agrees with ESMA that product distributors should obtain from product manufacturers, including non-MiFID firms, the information necessary to ensure distribution to the relevant target market. We believe, however, that it is not necessary for ESMA to require the parties to go through the formality of entering into a written agreement. The formal process of entering into such an agreement (particularly with non-EU firms) may be time-consuming and costly and without a significant benefit, as MiFID suitability provisions already require the distributor to satisfy itself that it has sufficient information on the product that it is recommending to its clients. It is already in the business interest of the product manufacturer and distributor to provide and receive this information as needed; this should not be further regulated through Level 2 measures.

Q.16 Do you think it would be useful to require distributors to periodically inform the manufacturer about their experience with the product? If yes, in what circumstances and what specific information could be provided by the distributor?

ICI Global believes that the obligation for distributors proposed by ESMA in paragraph 21 of the advice in Section 2.7 is sufficient. Any further specific obligation risks conflating the responsibilities of the product manufacturer and distributor.

We believe that the responsibilities of product manufacturers and product distributors should be clearly separated. Paragraph 15(iii) of the analysis implies that distributors may have a duty to supply the manufacturer with copies of any promotional material of the distributor. We disagree with a regulatory outcome that would lead to the manufacturer ensuring that the distributor is complying with its own regulatory obligations. It is the responsibility of the distributor to ensure that its promotional or marketing materials meet the required regulatory standards.

Q.19 Do you consider that there is sufficient clarity regarding the requirements of investment firms when acting as manufacturers, distributors or both? If not, please provide details of how such requirements should interact with each other.

<u>Application to UCITS and AIFs</u>

ICI Global believes that the draft technical advice lacks clarity in certain respects regarding the application to and obligations of product manufacturers.

As an initial matter, we are concerned that ESMA's analysis contemplates the potential application of the MiFID product governance provisions to the manufacturers of UCITS and AIFs. UCITS and AIFs are explicitly exempted from regulation under MiFID in Article 2(1)(i); they are instead governed by separate EU legislation that imposes specific requirements on the fund management process in relation to fund managers and, in the case of UCITS, on the individual product. Managers of UCITS or AIFs that provide ancillary investment services in addition to the management of UCITS or AIFs are bound by MiFID provisions on internal organization and conduct of business only in relation to those ancillary services.

We recommend that ESMA clarify (including through deletion of paragraph 17 in the analysis) that the product manufacturing provisions do not apply to UCITS or AIFs. This result would treat equally UCITS and AIFs that are created by fund managers that are licensed to provide ancillary services in addition to their core activity of collective portfolio management with those that are created by UCITS or AIF-licensed managers that are not at all subject to MiFID. A different result would lead to disparate treatment of UCITS or AIFs depending on the licensing of the manufacturer; this result does not make sense, and is not necessary considering the regulations to which these products or their managers are already subject.

Proportionate and Flexible Application Needed

In our view, it is important for ESMA to provide advice that allows for a proportionate, flexible, and not overly-prescriptive approach to compliance with the product governance obligations. In the analysis section, ESMA notes that the measures should be applied in an appropriate and proportionate manner, in line with the MiFID proportionality principle, to different national legal and economic models. With this important principle in mind, we urge ESMA to include a provision in the technical advice itself reflecting this point, such as "These proposals should be applied in an appropriate and proportionate manner taking into account the nature, scale, and complexity of the investment firm."

More specifically, we are concerned with paragraphs 7 and 8 in the technical advice, which describe the product manufacturer's obligation to identify a target market for each product, including identifying groups of investors for whom the product is not compatible. These requirements appear to be based on the assumption that products -- including UCITS and AIFS to the extent they are determined to be in scope -- are always designed for an identifiable target market. In fact, however, certain products are not designed for a particular target market, but rather are a product specifically created to provide exposure to a particular or niche sector of the market and are intended as only a portion of an investor's portfolio. In this circumstance, the "target market" for this product is any potential investor for whom exposure of some amount is suitable in the context of the investor's overall investment strategy. The draft advice does not at all recognize or account for these types of products or scenarios. We urge ESMA to revise the advice with this in mind.

Obligations of Distributors with Respect to UCITS

ESMA's advice outlines the obligations for product distributors to ensure that products and services they intend to offer are compatible with the characteristics, objectives, and needs of an identified target market. We recommend that ESMA include a paragraph specifying that a distributor may consider the typical UCITS investor profile statement in considering whether the UCITS is compatible with the characteristics, objectives, and needs of its clients. This recommendation is supported by the following factors: (i) the UCITS Directive regulates funds designed for sale to the public, (ii) UCITS are required to produce a Key Investor Information Document that includes information about the essential characteristics of that UCITS so that investors are able to understand the nature and risks of the fund, and (iii) UCITS are already required in their prospectus to include a profile of the typical investor for whom the UCITS is designed.

Section 2.21 – Best Execution

Q101. Do you have any additional suggestions to provide clarity of the best execution obligations in MiFID II captured in this section or to further ESMA's objective of facilitating clear disclosures to clients?

ICI Global believes that additional transparency is needed regarding the execution of trades provided by investment firms. To that end, we support strengthening information provided to clients regarding execution. Specifically, we believe additional transparency is needed regarding the order routing and execution practices of market participants. In many cases, investors are in a position to obtain the necessary routing and execution data from investment firms and trading venues. We are concerned, however, that many investors are not privy to this level of transparency.

At a minimum, we recommend that investment firms be required to provide certain standardized information about an execution including the type of execution venue used, the capacity in which the trade was executed, and each destination to which an order was routed. Increased information regarding payments and other incentives provided or received to direct order flow to particular trading venues also would be valuable. Such increased transparency should assist in better understanding conflicts of interest that exist and would allow investors to make better informed investment decisions.

We are concerned that investment firms may interpret ESMA's requirement to provide "relevant information on the execution policies of the entities that they have selected to execute transactions" as simply requiring them to forward their brokers' execution policy on to clients wholesale. Given that execution policies can often be long and complex, we believe such an interpretation may not be particularly helpful to investors. ICI Global therefore recommends that ESMA require investment firms to provide clients, for example, with a summary of the policy which is set out in a helpful and easily digestible form for clients.

3. Transparency

3.1. Liquid market for equity and equity-like instruments

Q109. Do you agree with the liquidity thresholds ESMA proposes for equities? Would you calibrate the thresholds differently? Please provide reasons for your answers.

ICI Global agrees in principle with the proposed liquidity thresholds. The determination of what is liquid, however, will have an impact on many other aspects of how trading occurs in the markets. For example, the new liquidity thresholds will impact the trading obligation for shares and the new equity waiver regime. ESMA must ensure that the new thresholds do not negatively impact the manner in which investors trade large blocks of securities. We therefore urge ESMA to take a conservative approach in defining the new criteria for defining liquid shares, particularly the threshold for the free float.

4.3. Reasonable commercial basis (RCB)

Q154. Would these disclosure requirements be a meaningful instrument to ensure that prices are on a reasonable commercial basis?

Ensuring that prices for trading data are reasonable is critical for investors. ICI Global believes that data charges in the EU are currently too high, particularly in comparison to those in the United States. We therefore support ESMA for consulting on how to ensure that prices are at a reasonable level.

Requiring full transparency by venues of their data pricing could prove valuable towards ensuring that prices are fair, reasonable, and non-discriminatory. Such a requirement also could assist investors in comparing costs across trading venues.

Q156. To what extent do you think that comprehensive transparency requirements would be enough in terms of desired regulatory intervention?

While increased transparency could prove to ensure that prices are provided on a reasonable commercial basis, we are skeptical that transparency alone will reduce the current excessive market data costs. We therefore urge ESMA to review the operation of the definition of reasonable commercial basis to determine whether other/additional options are necessary.

Q162. Within the options A, B and C, do you favour one of them, a combination of A+B or A+C or A+B+C? Please explain your reasons.

ICI Global believes ESMA should impose a combination of options A, B, and C. We also stress that another solution to addressing the need for providing market data on a reasonable commercial basis is to establish a consolidated tape. The lack of a consolidated tape makes it difficult for investors to get a complete picture of available liquidity and accurate price and volume information. ICI Global therefore strongly supports bringing together market data through a consolidated tape.

5. Micro-Structural Issues

5.1. Algorithmic and high frequency trading (HFT)

Q167. Which would be your preferred option? Why?

ICI Global believes that whatever option is chosen, it must be sufficiently targeted and take account of the various methods that investors utilize to execute orders. We are concerned that many tools utilized by investors to manage or make internal investment decisions could inadvertently be included in the definition and, in turn, could inappropriately be included in regulations that are crafted based on this definition. It would therefore be helpful if ESMA could clarify the HFT definition so as to ensure that it does not capture any aspects of the trading process which is not the focus of additional requirements.

We believe a combination of Options 1 and 2 may be appropriate as elements of both options are relevant to the definition of HFT. In addition, we believe ESMA should take additional factors into account when clarifying the definition of HFT. Specifically, we believe there are other factors that distinguish HFT from algorithmic trading such as ending the day in as close to a flat position as possible.

Q168: Can you identify any other disadvantages of the options put forward?

ICI Global believes that the proposed two messages per second intraday message rate in Option 1 may be too low. We are concerned that such a rate may sweep in certain algorithms utilized by investors when trading. The difference between high frequency and non-high frequency trading is currently measured in milliseconds, not full seconds. Setting a message rate of two messages per second could therefore pull in non-high frequency traders into the scope of a regulatory regime intended to apply to high frequency traders.

Q169: How would you reduce the impact of the disadvantages of the options put forward?

As discussed in Q167, we believe that Options 1 and 2 can be combined, in addition to the consideration of additional factors in determining what is HFT, particularly the fact that high frequency traders will generally end the day with a flat or near-flat position.

2. Investor Protection

2.3 Best execution - publication of data related to the quality of execution by trading venues for each financial instrument traded

Q8. Do you agree data should be provided by all the execution venues as set out in footnote 24? If not, please state why not.

ICI Global strongly supports requiring Regulated Markets, MTFs, OTFs, SIs, market makers and other liquidity providers to provide data on the quality of the execution of transactions. Information regarding execution quality is critical to investors in making decisions on how to route and execute their trades.

Q13. Do you agree that trading venues should publish the data relating to the quality of execution with regard to a uniform reference period, with a minimum of specific reporting details and in a compatible format of data based on a homogeneous calculation method? If not, please state why.

ICI Global agrees that all trading venues should publish the data with standard reference periods and in a compatible format.

Q14. Is the volume of orders received and executed a good indicator for investment firms to compare execution venues? Would the VBBO in a single stock published at the same time also be a good indicator by facilitating the creation of a periodic European price benchmark? Are there other indicators to be considered?

We believe the volume of orders received and executed could be useful information for market participants to compare execution venues.

2.4. Best execution - publication of data by investment firms

Q29. Do you agree that in order to allow clients to evaluate the quality of a firm's execution, any proposed standards should oblige the firm to give an appropriate picture of the venues and the different ways they execute an order?

Given the complexities of the current market structure and the associated difficulties in assessing market performance for investors, ICI Global believes that one of the areas in which action will be critical is the need for improved information to investors about the order routing and execution practices of investment firms. Improved information would allow investors to make better informed investment decisions and, in turn, facilitate best execution.

Q34. Do you agree that the investment firms should publish the data relating to their execution of orders with regard to a uniform reference period, with a minimum of specific reporting details and in a compatible format of data based on a homogeneous calculation method? If not, please state why.

As we stated in our response to Q13, ICI Global agrees that all trading venues should publish the data with standard reference periods and in a compatible format.

Q44. What information on conflicts of interest would be appropriate (inducements, capital links, payment for order flow, etc.)?

ICI Global believes that information regarding conflicts of interest in order routing and execution would be extremely valuable for investors in making trading decisions. Specifically, it would be valuable to investors to have information regarding payment for order flow as well as whether a trading venue is associated with the investment firm, both potentially raising conflicts of interest. Information regarding payments made through rebates utilized by trading venues, i.e., the maker-taker model, also would be significant.

3. Transparency

3.1 Pre-trade transparency - Equities

<u>Large in Scale Waivers</u>

Q48. Do you agree with ESMA's view that ADT remains a valid measure for determining when an order is large in scale compared to normal market size? If not, what other measure would you suggest as a substitute or complement to the ADT? Please provide reasons for your answer.

Waivers, such as the large in scale waivers, are important for certain orders utilized by investors. Any changes to the waivers, therefore, must be carefully crafted to not create difficulties for investors when executing orders.

We do not consider ADT to be the appropriate measure for the Large In Scale (LIS) waiver, primarily because it does not take into account fluctuations in liquidity. Instead, we recommend basing the calculation on Average Daily Volume (ADV). We believe this is a better representation of market activity for LIS than ADT.

Q60. Do you agree with ESMA's opinion that stubs should become transparent once they are a certain percentage below the large in scale thresholds? If yes, at what percentage would you set the transparency threshold for large in scale stubs? Please provide reasons to support your answer.

ICI Global believes that stubs should remain protected by the large in scale waiver. Displaying stub orders could provide indications of large in scale activity which, in turn, could be detrimental to trading by investors in size. Imposing full transparency requirements on order stubs also would be complex to implement in practice and would add very little in terms of useful transparency data to the market.

3.2 Post-trade transparency - Equities

Q74. Do you agree that the content of the information currently required under existing MiFID is still valid for shares and applicable to equity-like instruments? Please provide reasons for your answer.

Post-trade transparency is critically important to investors in making investment decisions and decisions regarding order routing and execution. We believe the content of the information currently required under existing MiFID remains valid.

Q76: Do you think that the current post-trade regime should be retained or that the identity of the systematic internaliser is relevant information which should be published? Please provide reasons for your response, distinguishing between liquid shares and illiquid shares.

ICI Global believes that the publication of the identity of SIs could provide market participants with an overview of liquidity pools in relation to an instrument, which could be helpful information for traders. At the same time, we recognize that it might also allow other market participants to take advantage of the knowledge that a significant SI has accumulated risk in a particular instrument, and use that knowledge to form an undesirable trading strategy.

Q77. Do you agree with the proposed list of identifiers? Please provide reasons for your answer.

In general, ICI Global supports a more detailed set of flags identifying transactions carried out under each of the permissible waivers from pre-trade transparency. We believe such identifiers could improve the information content of trade reports and assist competent authorities in monitoring the extent to which waivers from pre-trade transparency are used.

Q79. Do you support the proposal to introduce a flag for trades that benefit from the large in scale deferral? Please provide reasons for your response.

We support the use of a flag in conjunction with the deferred publication of trades that benefit from the large in scale waiver.

Q85. Which of the two options do you prefer in relation to the deferral periods for large in scale transactions (or do you prefer another option that has not been proposed)? Please provide reasons for your answer.

Of the options provided, we would prefer Option B as it allows deferred publication for the largest transactions from late in the day (15:00 or later) to noon of the next trading day, instead of prior to the next trading day. Such deferred publication is necessary to avoid negative consequences for firms executing large trades late in the day.

Q89. Do you have concerns regarding deferred publication occurring at the end of the trading day, during the closing auction period?

As discussed in Q85, we prefer Option B which provides for deferred publication until noon the following day for the reason that such publication would have a price distorting effect during the closing auction period.

Q191: Is the requirement that real time monitoring should take place with a delay of maximum 5 seconds appropriate for the risks inherent to algorithmic trading and from an operational perspective? Should the time frame be longer or shorter? Please state your reasons.

ICI Global supports the effective monitoring of algorithmic trading activity. Such monitoring should take place with as minimal a time delay as possible. We are concerned, however, that a maximum delay of five seconds may prove too short for some investment firms. Instead of identifying a specific timeframe for the real time monitoring of algorithmic trading activity, we recommend that "real time" should be fixed in relation to the complexity of the system generating the order and other risk controls in place.

Q192: Do you agree with the definition of "T+1"' in relation to market monitoring of algorithmic trading activity by investment firms?

As discussed in our response to Q191, instead of identifying a specific timeframe for the real time monitoring of algorithmic trading activity, we recommend that "real time" should be fixed in relation to the complexity of the system generating the order and other risk controls in place (e.g., the list of pre-trade controls referenced at 208-209). We therefore would not recommend the imposition of a specific timeframe, such as T+1.

Q197: Do you agree with the approach described above regarding the application of the proportionality principle by investment firms? Please elaborate.

ICI Global strongly supports the preservation and application of the proportionality principle to investment firms, i.e., that the systems and controls of investment firms should take into account the nature, scale and complexity of their business. As ESMA notes, there is a wide range of investment firms that would be captured by future regulation and that the risks stemming from algorithmic trading activities are not homogeneous across all firms.

We support the proposal that investment firms should carry out on a regular basis a detailed and robust self-assessment of their activities, which allows the firm to identify, in operational terms, how it should apply the proportionality principle to its own situation.

We agree that the self-assessment should be subject to sign-off by the management body and should be reviewed. We do not believe, however, that subjecting the self-assessment to audit by the firm's internal audit function or by an independent third party audit adds meaningful value. Being answerable to management and regulatory bodies should be sufficient, particularly for low complexity algorithms.

4.2. Organisational requirements for investment firms (Article 17 MiFID II)

Q199: Do you agree with a restricted deployment of algorithms in a live environment? Please elaborate

In general, ICI Global believes a robust compliance and risk management program is critical given the prominence of the use of algorithms. We therefore strongly support the initial and ongoing testing of systems used for algorithmic trading to ensure that risks to firms and to the market as a whole are appropriately managed.

Regarding a restricted deployment of algorithms in a live environment, while we believe ESMA's proposed "controlled roll out requirement" may be appropriate for a new algorithm whose functioning has not yet been observed in a live environment, or for an algorithm which has undergone a material change or restructuring, it should not apply to existing algorithms which have undergone more minor changes, or to algorithms which are being rolled out onto new trading venues after those algorithms have already been observed to be functioning well on an existing trading venue.

Q202: Do you agree with ESMA's approach regarding the conditions under which investment firms should make use of non-live trading venue testing environments? Please elaborate.

ICI Global strongly supports robust testing practices to ensure the safety and resiliency of the markets. Nevertheless, given that there is the potential for testing on non-live trading venue environments to become mandatory for investment firms, we believe that the testing facilities provided by trading venues should be required to be adequate for these purposes or subject to objective standards which apply across all venues, and that testing facilities should be offered either at cost or free of charge for all market participants trading through the venue.

Q205: Do you agree with **the proposed monitoring and review approach? Is a twice yearly review, as a minimum, appropriate?**

ICI Global supports an investment firm having in place systems and risk controls to ensure that its trading systems are resilient, have sufficient capacity, and do not function in a manner that may create or contribute to a disorderly market. Among the proposals set forth by ESMA, we generally support a requirement that investment firms implement "kill button" abilities. We believe, however, that such a blunt instrument be reserved solely for emergency situations, and should be used only as a last resort.

Q206: To what extent do you agree with the usage of drop copies in the context of monitoring? Which sources of drop copies would be most important?

ICI Global supports a requirement for the use of drop copies in the context of monitoring. Such post trade reports would allow investment firms to independently confirm both their orders and trades, and to confirm their overall positions. Post-trade reports also have the potential to mitigate the impact of malfunctioning pre-trade risk controls or algorithms, particularly if they are made available and utilised on a low-latency basis. Thus, we believe that drop copies, along with other post-trade reports, have an important role to play in monitoring and reconciliation by investment firms.

Q207: Do you agree with the proposed approach?

ICI Global supports measures being taken to ensure the security of trading systems and algorithms. We are concerned, however, that ESMA's approach to this issue is overly prescriptive. We believe that investment firms should be given a certain amount of flexibility to implement the new regime in a manner that is proportionate and tailored to the risks faced by their businesses.

Q208. Is the proposed list of pre trade controls adequate? Are there any you would add to or remove from the list?

As we stated in our response to Q207, investment firms should have some discretion over which risk limits should be applied in any given situation, depending on an assessment of individual trading strategies and market conditions. While such pre-trade controls may be helpful on an individual basis and in specific circumstances, the proportionality principle should govern which controls are appropriate to be applied in any given situation.

Q209: To what extent do you consider it appropriate to request having all the pre-trade controls in place? In which cases would it not be appropriate? Please elaborate.

ICI Global believes that investment firms should be granted a degree of discretion so that they can tailor pre-trade risk controls to their specific trading strategies and to changing market conditions. Requiring all firms to comply with a general list of controls without allowing them a degree of discretion over the form and application of each control may in fact result in inadequate or poorly adapted controls which are less fit for purpose than the status quo.

Q213: Trade reconciliation – should a more prescriptive deadline be set for reconciling trade and account information?

ICI Global believes that ESMA should not set a more prescriptive deadline for reconciliation of trade and account information.

Q214: Periodic reviews – would a minimum requirement of undertaking reviews on a half-yearly basis seem reasonable for investment firms engaged in algorithmic trading activity, and if not, what would be an appropriate minimum interval for undertaking such reviews? Should a more prescriptive rule be set as to when more frequent reviews need be taken?

ICI Global believes that half yearly reviews should not be required unless warranted. Annual reviews would be more appropriate.

Direct Electronic Access

Q215. Are there any elements that have not been considered and / or need to be further clarified here?

In general, ICI Global supports due diligence by investment firms offering DEA on their DEA clients. Due diligence by a firm is an important factor in the provision of direct electronic access, and it is in the interest of all parties to ensure that both the DEA user and the DEA provider have suitable controls in place to avoid any form of disruption to fair and orderly trading. At the same time, we must ensure that the scope of any regulations in this area does not unnecessarily impact the various methods that investors use to trade securities through investment firms or lead to unintended consequences for institutional investors using DEA, particularly regarding the confidentiality of trading information.

Q216. What is your opinion of the elements that the DEA provider should take into account when performing the due diligence assessment? In your opinion, should any elements be added or removed? If so, which?

ICI Global is concerned about the language in paragraph 95 which states that, when analysing algorithms provided by the client, the investment firm should, in addition to the source code and the functioning of the algorithm, also take into account the client's process to develop or purchase the algorithms. We do not believe that client source codes should be within the scope of a DEA provider's due diligence requirements. Revealing such codes to a DEA provider can compromise the confidentiality of the trading practices of a DEA client and represents sensitive intellectual property. In addition, we note that the sheer size of source codes and the amount of data that would have to be transmitted to DEA providers would make the proposed requirement extremely burdensome to implement in practice. We therefore believe that the other factors listed for consideration by a DEA provider will be sufficient to satisfy the provider's due diligence requirements.

Pre-Trade Controls When Providing DEA

Q219. Do you agree with the above approach? Please elaborate.

ICI Global supports investment firms applying pre-trade controls when providing DEA. We reiterate our comments, however, made in Q216, that such controls should not include a DEA client providing the source code and other granular information on the specific algorithm to the DEA provider.

Monitoring of DEA Users

Q220. Do you agree with the above approach, specifically with regard to the granular identification of DEA user order flow as separate from the firm's other order flow? Please elaborate.

ICI Global supports the monitoring of DEA users to prevent instances of market abuse. We are concerned, however, about any requirement that would compromise the confidentiality of algorithms utilized by the DEA user, such as the need to register individual algorithms with DEA providers. We do not feel that it is appropriate for a DEA provider to have knowledge of the specific deployment of algorithms by its clients. As an alternative, we believe that DEA users can provide representation to DEA providers relating to their testing procedures and the use of their algorithms.

Q221. Are there any criteria other than those listed above against which clearing firms should be assessing their potential clients?

ICI Global does not believe that additional due diligence criteria is necessary given that ESMA's proposal covers the normal due diligence which clearing firms would perform on their members. It also is unclear why the due diligence category of "trading patterns and strategy" is required. We believe the broad wording of this category of information could result in clearing firms requiring the disclosure of proprietary information relating to algorithmic trading strategies.

4.3 Organizational Requirements for Trading Venues

Q229: Do you agree with requiring trading venues to perform due diligence on all types of entities willing to become members/participants of a trading venue which permits algorithmic trading through its systems?

ICI Global supports requiring trading venues to perform the appropriate due diligence on all entities applying to become members/participants of a trading venue, regardless of the type of activity in which the member is involved.

Q232. Do you agree with the list of parameters to be monitored in real time by trading venues? Would you add/delete/redefine any of them? In particular, are there any trading models permitting algorithmic trading through their systems for which that list would be inadequate? Please elaborate.

In general, we believe it is critical that trading venues monitor the performance of the market in real time so as to be able to react in a timely manner to any disruption that may arise.

<u>Trading Venue's Capacity</u>

Q234: Do you agree with the above approach?

ICI Global agrees. ESMA's proposed measures are positive in that they are intended to reinforce and improve the capacity of trading venues. The proposed measures should therefore ensure a better service for market participants trading through the venues (given, for example, that overloading of the venue's capacity could lead to slower functioning).

<u>Ensuring Resilience of trading systems</u>

Q237: Do you agree with the list of abilities that trading venues should have to ensure the resilience of the market?

ICI Global agrees. Regarding the use of "kill switches," we believe that while utilizing a kill switch may at times be necessary, it should remain a last resort in light of the potential unintended consequences of its use for market participants.

Q239: Which in your opinion is the degree of discretion that trading venues should have when deciding to cancel, vary or correct orders and transactions?

ICI Global believes that there should be a clear and predictable set of rules setting out when trading venues will exercise their power to cancel, vary or correct transactions, with limited discretion for trading venues. Such a set of rules will help to maintain market certainty in the event of volatile trading conditions.

Q240: Do you agree with the above principles for halting or constraining trading?

ICI Global supports the proportionate use of market halts as a mechanism to allow participants to adjust to extreme market conditions. We believe, however, that halts should be used only after the failure of other pre-trade risk measures and as a last resort to prevent market disruptions. In addition, we note that the proposals refer to halt mechanisms being applied in different "phases of trading." We believe that stronger safeguards should apply to the use of trading halts closer to the end of the business day, so that there is less risk of market participants being left with positions which they are unable to offset following use of the halt mechanism.

Q241: Do you agree that trading venues should make the operating mode of their trading halts public?

ICI Global supports the requirement for trading venues to publish the process for implementing trading halts on grounds of market certainty. While we believe that trading halts can be a useful tool in certain situations to ensure the resiliency of trading systems, we also believe that other mechanisms also can be implemented to achieve the same results with possible less consequences on the markets and market participants, such as so called "limit-up/limit-down" mechanisms and price collars.

4.5 Order-to-transaction ratio (OTR)

Q290: Do you agree with the types of messages to be taken into account by any OTR?

ICI Global strongly supports the imposition of an OTR to assist in preventing any market disruptions from occurring. We have recommended on several occasions that regulators examine whether a fee should be imposed on cancelled orders above a certain ratio of orders to executed transactions, designed to discourage the current risk free use of certain types of orders and to protect the integrity of the markets' infrastructure. We believe an OTR would facilitate orderly trading conditions on trading venues by controlling the number of orders members may send to the trading venue, thereby ensuring the capacity of the latter is not exceeded. We agree that all messages related to an order should be taken into account under any OTR regime as this can help to achieve these goals. If all messages are taken into account by an OTR, the OTR should be set sufficiently high to account for legitimate trading practices, such as cancelling and modifying orders in the normal course of business.

Q291: What is your view in taking into account the value and/or volume of orders in the OTRs calculations? Please provide:

i. reasoning for your opinion;

ii. the pros and cons of taking those parameters into account; and

iii. an indication of a possible methodology to factor in value and/or volume.

ICI Global believes that only the volume of orders should be taken into account in OTR calculations. Taking into account the value of orders would not achieve the purpose of the OTR, i.e., to control the number of orders members may send to the trading venue. In addition, taking into account the value of orders would make the calculation of the OTR more complex than necessary.

Q298: What is your view regarding an activity floor under which the OTR regime would not apply and where could this floor be established?

ICI Global generally supports the application of an activity floor under which the OTR regime would not apply. We recognize that the application of such a floor would likely be a positive outcome for smaller traders, who would not have to spend time and resources on checking their messaging levels against the OTR. Nevertheless, we are concerned that such a floor could weaken the operation of the OTR overall. As such, if ESMA institutes an activity floor, the operation of such a floor should be monitored to ensure that market participants are not circumventing the goals of the OTR regime overall.

Q299: Do you agree with the proposal above as regards the method of determining the OTR threshold?

ICI Global believes that given that the OTR is intended to safeguard against trading venues' capacity being overloaded, trading venues may be best placed to determine the level at which the OTR is set, as opposed to a "one size fits all" approach imposed by ESMA.

<u>Market Maker Exemption</u>

Q304: What are your views in this regard? Please explain.

ICI Global believes that market makers should be exempt from the OTR regime. We therefore support Option (ii) of maintaining the current practice in granting an exemption for market makers and other liquidity providers.

4.6 Co-location rules

Q305: What factors should ESMA be considering in ensuring that co-location services are provided in a 'transparent', 'fair' and 'non-discriminatory' manner?

ICI Global supports requirements for trading venues to ensure that their co-location services are provided in a transparent, fair and non-discriminatory manner. Significantly, the fees charged to market participants must be uniform between market participants using the same services and should not discriminate against different classes of market participants. In addition, the conditions for provision of co-location services should be transparent. For example, co-location providers should disclose whether they or third parties offer co-location services on a priority basis other than first available. Providers also should publish clear and understandable information about their services and the prices attaching to such services.

4.7 Fee structures

Q306: Do you agree with the approach described above?

ICI Global supports ESMA's proposal that market participants meeting the same criteria should be able to access the same system of fees and rebates from the trading venue in a non-discriminatory manner.

Q310: Are there other incentives and disincentives that should be considered?

ICI Global believes that the current rebate system utilized by trading venues, i.e., the maker-taker model, should considered in this context as it can create conflicts of interest in the routing and execution of investor orders. Specifically, an investment firm's interest may be in maximizing economic inducements by capturing liquidity rebates associated with the "maker-taker" pricing model which can lead to routing decisions that may be at odds with their clients' interest in obtaining best execution.

There have been renewed calls around the globe for an examination of the maker-taker model. ICI Global has for some time called for an examination of the benefits and drawbacks of rebates to learn more about the effects of this practice on investors and the markets. We have noted that investment firms can be incentivized to make routing decisions based on the availability and amount of rebates offered by an exchange. At the same time, the benefits of rebates to investors are doubtful -- investors do not receive these rebates directly and arguably also do not receive the benefits of rebates indirectly. We therefore have recommended that regulators work with the exchanges and other market participants to, at the very least, establish a pilot program where a certain set of securities would be prohibited from being subject to rebates.

Q323: Do you agree that an OTR must be complemented with a penalty fee?

ICI Global supports enforcing the OTR through the imposition of a penalty fee.

Q324: In terms of the approach to determine the penalty fee for breaching the OTR, which approach would you prefer? If neither of them are satisfactory for you, please elaborate what alternative you would envisage.

While we do not have a strong preference of the two options presented, we do believe that Option B might ensure a more uniform application of the OTR regime and, more importantly, prevent situations of regulatory arbitrage.

Q326: Would you apply economic penalties only when the OTR is systematically breached? If yes, how would you define "systematic breaches of the OTR"?

ICI Global agrees that minor and administrative breaches should not be subject to the imposition of penalties. Nevertheless, an OTR regime must be sufficiently stringent to ensure that market participants that are cancelling orders that fall within the OTR cannot circumvent the purpose of the OTR.

3.11 The Trading Obligation for Derivatives

Q168: Do you agree that there should be consistent categories of derivatives contracts throughout MiFIR/EMIR?

In general, categories of derivatives contracts should be consistent in EMIR and MiFIR to make compliance with the two regimes easier for market participants.

There will be a link between those classes of derivatives that are declared subject to the EMIR clearing obligation and those that are declared subject to the MiFIR trading obligation. Under Article 32 of MiFIR, ESMA is required to draft technical standards specifying "which of the class of derivatives declared subject to the clearing obligation . . . or a relevant subset thereof shall be traded on [trading venues]." In addition, those derivatives that become subject to mandatory clearing are more likely to be sufficiently liquid to be included within the scope of the trading obligation.

Nevertheless, in some cases it may be appropriate to further divide classes of derivatives declared subject to clearing into sub-classes for the purpose of assessing whether mandatory trading would be appropriate. In particular, the trading obligation should only be imposed on the subset of cleared derivatives that is the most liquid to ensure that trading is not driven to other markets as a result of concerns surrounding risks associated with low volume (*e.g.,* limited market, pricing information, flexibility, etc.).

During the public consultation that is required to be conducted under Article 32, ESMA should specifically request comment on whether the proposed classes of derivatives are adequately narrow in scope to avoid imposing a trading obligation on derivatives contracts that are not sufficiently liquid.

Finally, we would expect ESMA's power to declare derivatives subject to the MiFIR trading obligation in the absence of the EMIR clearing obligation to be used infrequently, if at all, given the unlikelihood that a class of derivatives that is not subject to mandatory clearing would be sufficiently liquid to be suitable for the trading obligation.

Q169: Do you agree with this approach to the treatment of third countries?

ESMA is intending to align the application of MiFID II with the application of EMIR in relation to transactions considered to have a "direct, substantial and foreseeable effect" in the European Union. Under EMIR, there are two situations in which transactions between two non-EU counterparties may have a direct, substantial, and foreseeable effect within the European Union. The first situation involves OTC derivatives contracts that are entered into by a third country counterparty benefiting from a guarantee issued by an EU guarantor that is a financial counterparty. The second situation involves transactions between two non-EU entities operating through EU branches if both entities would be financial counterparties if they were established in the European Union.

Because the market is now familiar with the scope of EMIR with respect to transactions between third country entities and the EMIR regime applies in a fairly well-defined set of circumstances, ICI Global supports taking a similar approach in connection with the MiFIR trading obligation.

Q170: Do you agree with the proposed criteria based anti-avoidance procedure?

ICI Global supports consistency between EMIR and MiFIR in relation to the criteria for transactions where it is considered necessary or appropriate to impose the trading obligation to prevent the evasion of MiFID II. As discussed in response to Q169, the market is now familiar with the EMIR standards, which we believe apply in a sufficiently well-defined set of circumstances to promote market certainty.

Q171: Do you think it would be reasonable for ESMA to consult venues with regard to which classes of derivatives contracts are traded on venue? Do you think venues would be well placed to undertake this task?

Article 32(2)(a) of MiFIR provides that, for the trading obligation to take effect, the relevant class of derivatives "must be admitted to trading or traded on at least one trading venue." ESMA will need to obtain data on which classes of derivatives are being traded or have been admitted to trading on trading venues. However, in paragraph 16 of Section 3.11 of the Discussion Paper, ESMA states that "in assessing whether a class of derivatives was admitted to trade in the EU, ESMA could ask venues to notify ESMA of those classes of derivative which the venue thought were appropriate for the trading obligation." ESMA goes on to state that "this could be a way of injecting industry views into the formation of any technical standard."

In ICI Global's view, the requirement in the Level 1 text that a class of derivatives be admitted to trading or traded on a trading venue is simply a question of fact. Therefore, although it may be appropriate for ESMA to gather data from trading venues on which derivatives fall within this category, it would be inappropriate to go further and specifically ask trading venues to notify ESMA of which classes of derivatives the venues "think are appropriate" for inclusion within the scope of the trading obligation. Trading venues have a vested economic self-interest in derivatives being declared subject to mandatory trading, which may influence their views on the classes that "should" be subject to the trading requirement. Therefore, ICI Global strongly believes that the determination of the classes of derivatives subject to the trading obligation should not be initiated by trading venues. ESMA, rather than the trading venues, should take the lead on this process with appropriate industry input. Trading venues along with other market participants will have an opportunity to comment on whether particular classes of derivatives should be subject to mandatory trading during the public consultation process.

Finally, we also strongly believe that ESMA should place greater weight and consideration on the liquidity analysis than on the venue test because the issue of liquidity is of primary importance to the Impact that mandatory trading will have on the market in a particular class of derivatives.

Q172: The discussion in section 3.6 on the liquid market for non-equity instruments around 'average frequency', 'average size', 'number and type of active market participants' and average size of spreads is also relevant to this chapter and we would welcome respondent's views on any differences in how the trading obligation procedure should approach the following:

- **(i) whether 'average frequency' should be understood to refer to the number of trades over a given time period, the number of days on which trading occurred over that time period or both;**
- **(ii) the extent to which the given time period will need to vary by asset class;**
- **(iii) whether the 'average size' should be based on the notional and the number of trades in the given period, the notional and the number of trading days, or some other measure; and**
- **(iv) the most appropriate data for calculating 'spreads'.**

In general, ESMA appears to be considering aligning the criteria for what would be considered a liquid market in the context of the trading obligation with what would be considered a liquid market in the context of the transparency obligation. Although alignment of the two regimes would have the advantage of simplicity and uniformity, using the same definition of liquidity for the purposes of transparency and for the trading obligation may not always be appropriate given the different consequences that follow from a class of derivatives being considered "liquid" in each context. In particular, it may be appropriate to assess the liquidity of narrower categories of derivatives for the purposes of the trading obligation given the significance of imposing the trading obligation and the difficulties involved in removing classes of derivatives from its scope. In any event, it should never be the case that the trading obligation is imposed on a class of derivatives that is not also subject to transparency requirements because of the difficulties that would be involved for market participants in complying with the trading obligation in the absence of reliable market data.

In relation to "average frequency of transactions," ICI Global recommends combining an analysis of the number of trades over a given period with the number of days on which trading occurred over the relevant time period. A transaction should only be considered liquid if there are a large number of trades occurring in a consistent way throughout the year. Taking into account both criteria will ensure that derivatives that are, for example, subject to seasonal fluctuations (*i.e.,* such that there is not a liquid market at certain times of the year) will not be caught by the scope of the trading obligation. As minimum criteria, ICI Global members believe that an instrument must be trading a minimum number of times per day and every day to be considered liquid. Similarly, we note that under the current MiFID regime a share will only be classified as liquid if it is traded daily.

Moreover, the look-back period over which ESMA should assess liquidity should vary for different types of derivatives because overall liquidity may be affected by numerous factors. For example, for certain FX instruments, there may be more trading at the end of the month for rebalancing of portfolios and there may greater volume of trading of certain commodity derivatives during particular seasons.

In relation to calculation of "average size," ESMA should focus the analysis on the notional and the number of trading days rather than the notional and the number of trades in the given period. Calculating average size based only on the number of transactions undertaken over a given period may (as ESMA itself notes at 3.6 of the Discussion Paper) ignore uneven distributions of transactions over time. However, ESMA should not entirely disregard the total notional divided by number of transactions because this figure will give a more accurate assessment of the average size of each transaction executed during the relevant period.

Q174: Do you have any suggestions on how ESMA should consider the anticipated effects of the trading obligation on end users and on future market behaviour?

ESMA should consider the costs of imposing mandatory trading because these costs will ultimately be passed on to end users (and to investors in the case of Regulated Funds) and should consider any potential impact on liquidity fragmentation and pricing. ESMA should in particular analyze the effect of the trading obligation on large in scale transactions. ESMA should use its power to determine whether a sub-class of derivatives is only liquid for transactions below a certain size pursuant to Article 32 of MiFIR to exclude large in scale transactions from the scope of the trading obligation. Subjecting large in scale transactions to the trading obligation may result in these transactions receiving a lower quality of execution. ICI Global supports the use of empirical analysis in forecasting the effect of the trading obligation; a "pilot programme" may be useful in testing which classes of derivatives should be subject to mandatory trading. We encourage ESMA to look to the experiences of other jurisdictions that already have a mandatory trading regime to assess the likely impact on European markets.

Clearly, a comprehensive public consultation where end users have the opportunity to fully assess and respond to ESMA's proposals will aid ESMA in assessing the anticipated effect of the trading obligation on end users. For that reason, we recommend a public comment period of 60 days, but in no event fewer than 30 days.

Ultimately, it will be difficult to fully predict the effect of the trading obligation on trading in each class of derivatives. For this reason, we recommend that ESMA phase in the trading obligation slowly and assess the effect of mandatory trading on the most liquid classes of derivatives before considering other, less liquid classes. In addition, it would be helpful to end users for a transition period to be put in place each time the trading obligation is declared for a particular class of derivatives. Market participants will need time to update their systems and procedures to comply with the trading obligation. It also is important that other trading venues that do not currently provide a market for the relevant class of derivatives are given the opportunity to make those derivatives available to trade. We recommend a minimum phase-in period of 180 days after a trading obligation determination is finalized before the trading obligation becomes effective.

Q175: Do you have any other comments on our overall approach?

Generally, ICI Global supports the G-20 commitment to have standardised derivatives traded on regulated trading venues. The implementation of this important reform, however, must be balanced against the need to ensure that any class of derivatives that is declared subject to the trading obligation is sufficiently liquid. This is particularly important given the time-consuming process involved in removing classes of derivatives from the scope of the trading obligation.

Specifically, ICI Global has concerns about mandating trading of a class or sub-class of derivatives that may not be sufficiently liquid, which could ultimately result in more limited trading in such contracts. A Regulated Fund, for example, may simply be unable to trade in a particular derivative for which the trading obligation has been imposed because there is limited or no trading in that derivatives contract in the regulated venues. Limited trading also could negatively affect the pricing of the derivative, indirectly raising costs to fund investors. Therefore, as discussed in response to Q174, market participants should be given an adequate period of time to digest properly and fully comment on any proposals for mandatory trading during the public consultation period.

Article 34 of MiFIR provides that the register of derivatives that are subject to the trading obligation maintained on ESMA's website is to be "exhaustive and unequivocal" in nature. We believe the Article requires that the classes of derivatives declared subject to the trading obligation be defined with sufficient detail to ensure that there is no market uncertainty as to which instruments fall within or outside the scope of the trading obligation.

As ESMA notes in the Discussion Paper, its power to remove classes of derivatives from the scope of the trading obligation following a sharp drop in liquidity is limited by the time-consuming process of drafting and submitting draft regulatory technical standards for consultation. ICI Global considers it unfortunate that the Level 1 text of MiFIR does not provide for a more expedited method of removing derivatives from the scope of the trading obligation and that there is no provision for ESMA or national competent authorities to suspend the trading obligation on an emergency, temporary basis. National competent authorities, however, have the ability to suspend transparency requirements following a similar drop in liquidity. ICI Global prefers to see a more efficient process for suspension of the trading obligation adopted in the future. In the meantime, we appreciate that ESMA (particularly given the lack of suspension power) recognizes that the trading obligation should only be applied to those classes of derivatives that are reasonably expected to remain liquid over time. We also recommend that ESMA monitor the liquidity of classes of derivatives periodically so that the process of suspending or amending the scope of the trading obligation can be commenced as soon as there are indications that a class of derivatives may no longer be suitable for mandatory trading.

ICI Global also urges ESMA to consider the impact of Article 33 of MiFIR on entities that are established outside of the EU and that are required to operate in compliance with the regulatory regime of a jurisdiction in which they are not established. Article 33 of MiFIR allows counterparties to comply with an equivalent non-EU regulatory regime rather than with the MiFIR trading obligation, but only where one of the counterparties is "established" in the relevant non-EU jurisdiction. ICI Global urges ESMA and other regulators to interpret this provision or extend its application to cover situations where entities are subject to the laws of an equivalent non-EU jurisdiction even if they are not established in that jurisdiction. Otherwise, entities located in offshore jurisdictions that are less likely to be declared equivalent may have to comply with competing regulatory regimes in executing their transactions (*e.g.,* MiFIR and the Dodd Frank Act).

In light of all of these concerns, we recommend that ESMA take a cautious approach to adopting and phasing in the trading obligation. We suggest that ESMA start with the most liquid derivatives contracts that are subject to the clearing obligation and provide market participants adequate time to prepare to trade those contracts through the regulated trading venues. As discussed in the answer to Q174, there should be adequate consultation and implementation periods.

Finally, we understand that ESMA has not yet considered fully the cross-border implications of these obligations. We urge ESMA to address these important issues in a future consultation paper and propose how these obligations would apply to cross-border transactions on which there may be conflicting trading requirements. As we have noted to ESMA and to international regulators in other contexts, given that many derivatives transactions are conducted across multiple jurisdictions, we support efforts for real and meaningful coordination among regulators on how derivatives regulations will be applied to market participants that engage in cross-border transactions.

3.6-3.10 Pre-Trade and Post-Trade Transparency for Derivatives

Q113: Should the concept of liquid market be applied to financial instruments (IBIA) or to classes of financial instruments (COFIA)? Would be appropriate to apply IBIA for certain asset classes and COFIA to other asset classes? Please provide reasons for your answers.

COFIA and IBIA have different strengths in determining liquidity for transparency purposes. COFIA would be less costly and easier to apply in practice, whereas IBIA would (at least in some cases) likely produce a more accurate assessment of the liquidity of each individual instrument. The success of the COFIA approach would largely depend on the sub-categories of instruments established by ESMA. As we discuss below, features such as maturity and underlying asset and currency would be relevant in ensuring that the instruments in each sub-category have a similar liquidity profile. If the sub-categories of financial instruments used in the COFIA approach were sufficiently granular to be homogenous in terms of liquidity, the COFIA approach could work effectively. However, for certain instruments (such as exotics) it may be impossible to form a sub-categorisation that would ensure a uniform liquidity profile or the sub-categories may be so narrow as to make the exercise meaningless. In these cases, we suggest that the IBIA approach be used.

Any liquidity assessments should be reviewed periodically given that the liquidity profile of a class or sub-class of instruments can change quickly over time; such a review process appears particularly important in the COFIA approach.

With respect to the determination of liquidity thresholds, which applies to both COFIA and IBIA, ICI Global prefers ESMA's first option of setting up a specialist working group to determine the threshold based on data analysis and consultation with stakeholders. We urge ESMA, however, to consult on the criteria that the working groups will utilize to set the thresholds. ESMA's second option of setting a coverage ratio would presumably always force a certain percentage of transactions within each class of instruments to be transparent, regardless of whether this level was appropriate based on empirical analysis.

In this context, ESMA refers to the CFTC approach of setting block sizes for derivatives using the 67% of total notional methodology. Although the issue of liquidity is clearly relevant to the CFTC block trade regime, it would be more appropriate for ESMA to consider this approach in the context of the "large in scale" waiver/deferral regime under MiFID II rather than in determining whether a class of derivatives was sufficient "liquid" for transparency purposes.

ICI Global also notes that the CFTC confirmed that setting the threshold at 67% would result in only 6% of trades being considered as block trades subject to a time delay. In our view, a similar threshold operating across all non-equity financial instruments would be too high, particularly in those markets lacking in depth and liquidity. Although ICI Global would much prefer any threshold to be set based on consultation with stakeholders and an analysis of market impact rather than pure policy grounds, if ESMA does decide to implement a coverage ratio we would suggest at least initially setting a lower threshold (*e.g.,* 50%), with a phase-in period for more illiquid sub-categories of instruments.

Q116: Do you think that, in the context of the liquidity thresholds to be calculated under MiFID II, the classification in Annex 3.6.1 is relevant? Which product types or sub-product types would you be inclined to create or merge? Please provide reasons for your answers.

In general, it is positive that the classification set out in Annex 3.6.1 sub-divides overall classes of instruments into granular sub-categories. At a minimum, ICI Global, however, recommends that sub-categories of financial instruments be classified according to the most granular portion of the table (*i.e.,* "other potential liquidity sub-categories") given that this portion of the table would sub-divide instruments based on features such as maturity and underlying asset and currency, each of which can have a significant effect on liquidity.

As an overall comment, it is not currently clear how multi-legged or packaged transactions would fit into the Annex 3.6.1 classifications. We also question whether the class of "exotics" is too broad (particularly given that the table does not currently include any "sub-product types" in relation to exotic derivatives).

Q117: Do you agree with the proposed approach? If not, please provide rationales and alternatives.

ICI Global supports the ability of national competent authorities to temporarily suspend transparency requirements where appropriate. In our view, the transparency suspension powers are essential emergency powers to be used when transparency has become damaging in the context of a particular market (*i.e.,* given a substantial drop in liquidity of the relevant instrument). Therefore, regulators should have the ability to exercise these powers quickly and simply. Requiring the submission of detailed reasoning in addition to an analysis of data on average daily turnover by authorities before they exercise the temporary suspension power may cause delay that may be detrimental to the markets. Although we believe the data provided to ESMA should provide adequate evidence of a drop in liquidity, ESMA should not be prescriptive regarding the quantitative information that must be submitted to it.

Despite the potential utility of the temporary suspension powers, we are concerned by the fact that there is no equivalent "emergency" power to temporarily suspend the derivatives trading obligation. If transparency requirements are suspended but the trading obligation is not, it could leave market participants in the difficult position of being forced to trade through trading venues on the basis of little or no market data.

Q122: Do you agree with the description of voice trading system? If not, how would you describe a voice trading system?

We generally consider that voice trading systems would be trading systems where transactions between members are arranged through voice negotiation. However, given the importance of this definition to the MiFIR transparency regime (*i.e.,* voice trading systems will benefit from a higher number of pre-trade transparency waivers), we encourage this description to be interpreted as extending to those hybrid systems where orders are first routed to a broker (*e.g.,* by telephone), even if execution may later take place via electronic means.

ESMA also should consider the role of instant messaging in interacting with brokers, given that instant messaging may perform a very similar role to traditional telephone conversations.

As a general matter, ICI Global is concerned that it is very unclear how pre-trade transparency requirements will work in the context of voice trading systems.

Q124: Do you think that the information to be made public for each type of trading system provides adequate transparency for each trading system?

As described in greater detail in answer to Q146, public disclosure of responses to a Regulated Fund's request for a quote (in a request-for-quote system) and bids and offers of any members of a regulated venue (in a voice trading system) can raise significant issues, including frontrunning and information leakage. We, therefore, emphasize the need for ESMA to provide appropriate waivers from the pre-trade transparency requirements.

Q136: Do you support the use of flags to identify trades which have benefitted from the use of deferrals? Should separate flags be used for each type of deferral (e.g. large in scale deferral, size specific to the instrument deferral)? Please provide reasons for your answer.

ICI Global is concerned about the use of flags during the deferral period specifically indicating, for example, that an order is large in scale. The use of such explicit flags may increase the risk of market participants trading against entities seeking to hedge their exposure.

Q146: Do you think that one universal deferral period is appropriate for all non-equity instruments which do not have a liquid market or that the deferrals should be set at a more granular level, depending on asset class and even sub asset class. Please provide reasons for your answer.

It may be appropriate to distinguish among instruments falling within the "illiquid" category. For example, where it would take more than one trading day to source an offsetting transaction in particularly illiquid markets, the deferral period should presumably reflect this longer timescale.

As a general comment, ICI Global supports post-trade transparency but believes ESMA must take into account the potential impact on the derivatives market. Publication of information regarding transactions in illiquid contracts or of a large size before a dealer has an adequate time to lay-off those risks could provide an opportunity for those seeking to profit from this knowledge to attempt to extract a higher premium from the dealer to offset those positions. If the offsetting transactions become more difficult and costly, dealers will raise the costs to compensate for the increased risks in hedging their positions. This higher cost, in turn, will be passed on to Regulated Funds and their investors.

Deferred publication will allow dealers that provide liquidity to Regulated Funds to be able to offset the risks of their positions at a reasonable cost. If dealers are unable to offset risk effectively, they may be deterred from engaging in transactions in the first place. The resulting decrease in market liquidity would ultimately have an impact on end users.

Premature publication of large transactions also may force Regulated Funds to break up large trades into smaller orders, which will create market inefficiencies and potentially diminish liquidity. In addition, opportunistic market participants may piece together information about a fund's holdings or trading strategy, which could lead to frontrunning of a Regulated Fund's trades.

Q147: Do you agree with the proposal that during the deferred period for non-equity instruments which do not have a liquid market, the volume of the transaction should be omitted but all the other details of individual transactions must be published? Please provide reasons for your answer.

The transaction price also should be masked to avoid information leakage.

Q151: Do you agree with the proposed option? Which option would be more suitable for the calibration of the large in scale requirements within an asset class?

ESMA is consulting on two options for "calibration" of the large in scale waiver: (i) Option 1, where instruments would be grouped into several different "bands" according to their average daily turnover (used as a measure of liquidity). The higher the average daily turnover, the higher the minimum threshold above which an order could be considered as being large in scale; and (ii) Option 2, where thresholds would be set for individual asset classes without any consideration of liquidity within the asset class, on the assumption that the asset class would only cover instruments with "homogenous patterns of liquidity."

Option 1 appears preferable (as ESMA notes) because it would most accurately predict the status of each individual instrument caught by the non-equities transparency regime. Option 1 would ensure that more illiquid instruments (when assessed on an instrument-by-instrument basis) would benefit from the most generous waiver and deferral regimes, given that the threshold for an order to be considered large in scale would be reduced for less liquid instruments. However, ICI Global acknowledges that Option 2 would be cheaper and less costly to implement and that it would make it easier for trading venues and market participants to keep track of when transactions are likely to benefit from transparency waivers and deferrals.

For Option 2 to function effectively, the sub-categories of instruments concerned would have to be set at a sufficiently granular level to ensure that only instruments with "homogenous patterns of liquidity" are included in each class.

Given the above considerations, ICI Global would support the use of Option 2 only in those cases where ESMA is able to set meaningful sub-categories of instruments that are effectively homogenous in terms of liquidity. In those cases where ESMA is unable to form sub-categories of instruments with the same liquidity profile (this situation may admittedly be rare, but it may, for example, apply to more unusual or exotic instruments), Option 1 should be used.

Q152: Do you consider there are reasons for opting for different options for different asset classes? Please provide arguments.

See our response to Q151.

Q153: Do you agree that the choice between the two options should be consistent with the approach adopted for the assessment of liquidity? If not, please provide arguments.

ESMA should not necessarily use the exact same approach for the large in scale waivers as the approach taken for the liquidity assessment. In particular, even if the COFIA approach is adopted in relation to the liquidity assessment, the classes of instruments that are appropriate for use in relation to COFIA may not be fully appropriate for use in relation to the large in scale regime. For example, although two different categories of derivatives within the same asset class may have the same level of "liquidity," what should be considered "large in scale" may be different for each category; thus, the sub-categories established for the purposes of assessing liquidity may in practice require some additional calibration for purposes of the large in scale threshold.

Therefore, the assessment of large in scale transactions (including setting "large in scale" thresholds) should be undertaken separately from the assessment of their liquidity. As such, the large in scale approach does not need to be consistent with the approach adopted for the assessment of liquidity.

Q156: In your view, which option would be more suitable for the determination of the large in scale thresholds? Please provide arguments.

ICI Global believes it would be preferable to compute the large in scale threshold based on a statistical measure of the central tendency (*e.g.,* based on the mean of the distribution of the overall trading size for each class) rather than setting a more policy-orientated "coverage ratio." Setting a specific coverage ratio could result in unintended consequences and could expose a significant proportion of transactions to transparency requirements, even where it is not suitable.

In this context, ESMA cites the CFTC's thresholds for block trades, which are intended to ensure that 67% of traded volume is transparent. As discussed in our response to Q113, we consider that a threshold of 67% across all non-equity financial instruments (which would result in imposing the transparency requirements on 94% of the trades) would be too high. If a coverage ratio were to be set, it would be better to at least initially set the ratio lower (at 50% for example) to assess market impact.

Q160: Do you think that the condition for deferred publication of large in scale transactions currently applying to shares (transaction is between an investment firm that deals on own account and a client of the investment firm) is applicable to non-equity instruments? Please provide reasons for your answer.

A condition that only large in scale transactions that are entered into between an investment firm that deals on own account and a client of the investment firm are eligible for post-trade deferral would be too restrictive.

Q163: Do you agree with the proposal that the size specific to the instrument should be set as a percentage of the large in scale size? Please provide reasons for you answer.

ICI Global considers that setting the size specific to the instrument threshold as a percentage of the large in scale size may be appropriate if, as ESMA states, the size specific to the instrument threshold is set at a level below the large in scale threshold. The size specific to the instrument regime is clearly intended to cover a different and additional set of transactions that would ordinarily fall outside of the large in scale regime, but which might nevertheless expose liquidity providers to undue risk in hedging their transactions.

ICI Global considers it vital that the size specific to the instrument regime is set at an appropriate level given that public disclosure of responses to a Regulated Fund's request for a quote (in a request-for-quote system) and bids and offers of any members (in a voice trading system) can raise significant issues regarding frontrunning and information leakage. A Regulated Fund also could suffer from "signaling" regarding the potential transaction. Thus, we recommend that ESMA conduct studies to identify disclosure levels that will not affect pricing or best execution and will not impair market liquidity in this context.

7. Commodity Derivatives

Q493: Should the regime for subsidiaries of a person other than entities that are wholly owned look to aggregate on the basis of a discrete percentage threshold or on a more subjective basis? What are the advantages and risks of either approach? Do you agree with the proposal that where the positions of an entity that is subject to substantial control by a person are aggregated, they are included in their entirety?

ICI Global generally agrees with ESMA's proposals in relation to aggregation and supports ESMA's proposed approach of looking primarily at direct parent/subsidiary relationships in the context of aggregation. Article 57 of MiFID II requires position limits to be set "on the basis of all positions held by a person and those held on its behalf at an aggregate group level." That is, the position limits apply at the legal entity level, together with parent/subsidiary undertakings of that legal entity. In this regard, investment funds are individual persons/trading counterparties holding positions. Therefore, for an investment fund, the positions of an individual investment fund would be subject to the relevant limits. Moreover, the positions of two or more investment funds would not be aggregated with each other simply on the basis of being managed by a common investment manager.

Q537: What are your views on these three alternative approaches for reporting the positions of an end client where there are multiple parties involved in the transaction chain? Do you have a preferred solution from the three alternatives that are described?

ICI Global disagrees with ESMA's first option of each investment firm in the execution chain passing details of the end client up the chain in "plain language" (*e.g.,* using the client's LEI code). ICI Global is concerned about the identity of the end client being revealed to intermediaries along the chain and about the potential for information leakage. Therefore, ICI Global recommends that ESMA adopt one of the two remaining options, which are designed to protect the identity of the end user.