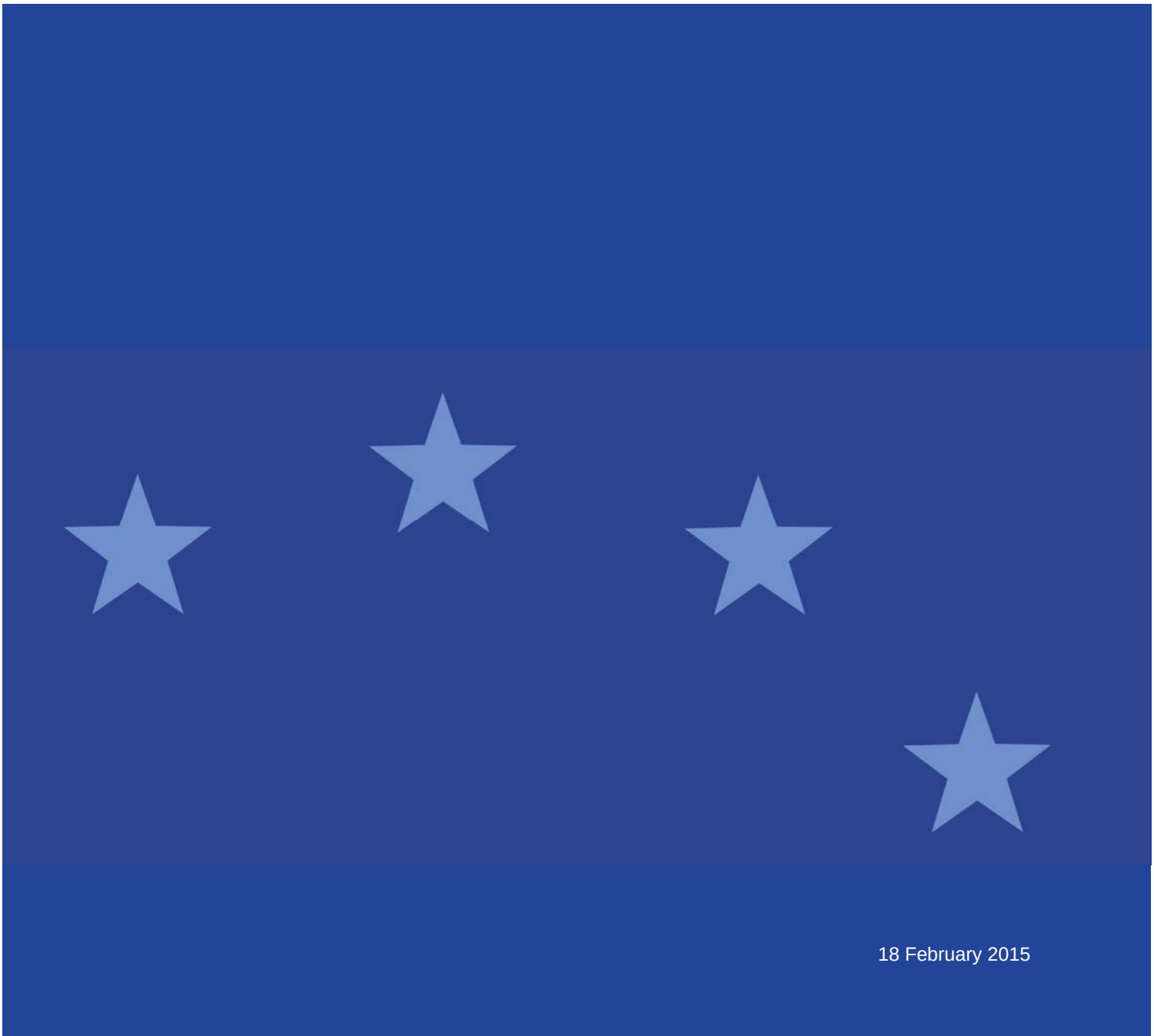
esma European Securities and Markets Authority

Reply form for the Addendum Consultation Paper on MiFID II/MiFIR



18 February 2015

European Securities and Markets Authority

Date: 18 February 2015

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the ESMA Addendum Consultation Paper on MiFID II/MiFIR, published on the ESMA website.

Instructions

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

- use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
- do not remove the tags of type <ESMA_ QUESTION_MIFID_ADD_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
- if you do not have a response to a question, do not delete it and leave the text "TYPE YOUR TEXT HERE" between the tags.

Responses are most helpful:

- if they respond to the question stated;
- contain a clear rationale, including on any related costs and benefits; and
- describe any alternatives that ESMA should consider

Naming protocol

In order to facilitate the handling of stakeholders responses please save your document using the following format:

ESMA_MiFID_ADD_NAMEOFCOMPANY_NAMEOFDOCUMENT.

E.g. if the respondent were ESMA, the name of the reply form would be:

ESMA_MiFID_ADD_ESMA_REPLYFORM or

ESMA_MiFID_ADD_ESMA_ANNEX1

To help you navigate this document more easily, bookmarks are available in "Navigation Pane" for Word 2010 and in "Document Map" for Word 2007.

Deadline

Responses must reach us by **20 March 2015.**

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input/Consultations'.

Publication of responses

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the headings 'Legal notice' and 'Data protection'.

General information about respondent

Name of the company / organisation	GFMA GFXD
Confidential[1]	☐
Activity	Banking
Are you representing an association?	Y
Country/Region	Europe

Introduction

Please make your introductory comments below, if any:

< ESMA_COMMENT_MIFID_ADD_1>

The Global Foreign Exchange Division (GFXD) of the Global Financial Markets Association (GFMA) welcomes the opportunity to comment on behalf of its members on the MiFID II/MiFIR Addendum Consultation Paper issued on the 18 February 2015.

The GFXD was formed in cooperation with the Association for Financial Markets in Europe (AFME), the Securities Industry and Financial Markets Association (SIFMA) and the Asia Securities Industry and Financial Markets Association (ASIFMA). Its members comprise 24 global Foreign Exchange (FX) market participants,[2] collectively representing more than 90% of the FX inter-dealer market.[3] Both the GFXD and its members are committed to ensuring a robust, open and fair marketplace and welcome the opportunity for continued dialogue with global regulators.

The FX market is the basis of the global payments system. The volume of transactions is therefore very high and these transactions are often executed across geographical borders. As reported by the Bank of International Settlements in their Triennial Central Bank Survey: Foreign Exchange Turnover in April 2014 over 75% of the market was traded by market participants across 5 key jurisdictions, hence the continued view from the GFXD that regulations should be harmonized at the global level. Cross border markets cannot operate in conflicting regulatory landscapes, and the natural outcome, should this be the case, is unwanted fragmentation of what is an already highly automated and transparent FX market.

The following summarises a number of the key elements of our response to the Consultation Paper (CP) including a specific summary of the key issues relevant to FX Prime Brokerage. As a summary, it is not exhaustive in terms of the depth and breadth of points covered and we refer to our answers to the Consultation Paper questions for further detail.

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The GFXD has strong concerns about the data used by ESMA in this CP and the approach ESMA has taken in calculating SSTI/LIS and liquidity. Our observations are outlined in section B below and our proposed alternative approach is set out in section A.

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[1] The field will used for consistency checks. If its value is different from the value indicated during submission on the website form, the latest one will be taken into account.

2 Bank of America Merrill Lynch, Bank of New York Mellon, Bank of Tokyo Mitsubishi UFJ, Barclays, BNP Paribas, Citigroup, Credit Agricole, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JP Morgan, Lloyds, Mizuho, Morgan Stanley, Nomura, Royal Bank of Canada, Royal Bank of Scotland, Société Générale, Standard Chartered Bank, State Street, UBS, Wells Fargo and Westpac

3 According to Euromoney league tables

[4] http://www.bis.org/publ/rpfx13fx.pdf

A. GFXD proposal for SSTI/LIS and liquidity definition

We believe that the trade reporting data available to ESMA does not reflect the FX market in Europe when compared to known and accurate market surveys. The GFXD proposal is therefore based on the October 2014 Bank of England semi-annual FX survey, which is widely accepted as a source by the FX industry, including central banks, as being representative of turnover within the FX market.

1. Liquidity definition:

- In our response to Q1 of the CP, we list the instruments, currency pairs and tenors that we believe to be liquid, the sum of which equates to 79% of the FX market in Europe.
- We do not believe that FX NDFs are liquid, nor are FX simple and FX complex exotic options.
- We suggest that ESMA considers that EMIR trade reporting data contains data reflecting the post execution status, including allocations etc which may distort several of the parameters used to measure liquidity (e.g., number of transactions). From 2018 onwards, a better approach may be to use a combination of data sources (including Central Bank data) to obtain a truer reflection of what is actually executed.

2. LIS and SSTI thresholds:

- We propose that LIS and SSTI thresholds should be different for pre- and post-trade obligations, due to the differing levels of risk facing market participants with each.

(a) LIS proposal:

- For 2018 onwards, we propose the following for FX:
  - Pre-trade: LIS threshold so that either 50% of the trades would lie below the threshold or 30% of the total volume traded for the relevant instrument would fall below the threshold.
  - Post-trade: LIS of 65% of the total volume traded for the relevant instrument would lie below the threshold.

(b) SSTI proposal:

- We propose that the SSTI threshold should either be set at either:
  - The median trade size (50th percentile of transaction sizes) for transactions below LIS in the relevant instrument; or
  - 10% of the LIS threshold for the relevant instrument (if ESMA prefers to retain a method based on the percentage of LIS).

B. Observations on the ESMA approach

The GFXD has presented the above proposal in response to concerns about the data that ESMA has used in the CP, and about its approach to the liquidity definition and LIS/SSTI thresholds. These concerns are summarised below.

1. Data Quality:

- We believe that the data presented by ESMA in the CP does not reflect the FX industry when compared to known and accurate market surveys, such as:

- The Bank of England semi-annual FX survey; and
- The Bank of International Settlements Triennial Central Bank Survey of FX Turnover.

- The use of EMIR trade reporting data from March-May 2014 is widely known to be inaccurate, including misclassification of financial instruments and mismatching financial details, such as notionals. This period is also deemed to be too short to capture a range of market events.
- We believe that the mapping of industry acknowledged financial taxonomies (i.e., the ISDA FX taxonomy) to EMIR trade reporting product ID fields is not sufficiently granular to represent the instruments traded in the FX market.
- ESMA have created a new FX 'product' to capture those FX instruments that do not easily map across to the EMIR trade reporting product ID fields:
  - FX spread-betting, which is usually used as a description of financial contracts for difference, has been used as a 'catch-all' by ESMA for those products mapped to the FX 'Other' product category under EMIR trade reporting. We suggest that spread-betting is included under MiFID Annex C9, Financial Contracts for Difference, whereas FX derivatives are included under MiFID Annex C4.
- Precious metals have been included within the FX analysis rather than the Commodities analysis.

2. Liquidity Definitions:

- GFXD does not agree with the ESMA liquidity definitions. The use of inaccurate trade data has lead to instruments being classified as liquid, that are usually illiquid and vice-versa:
  - The CP contains many deliverable currency pairs which have been included as non-deliverable forwards and many non-deliverable currency pairs which have been included as deliverable forwards.
  - Tenors expected to be liquid have not been included for some currency pairs and instruments (and vice-versa).
- The parameters used in the liquidity calibration were not fully reflective of the 4 defined parameters available to ESMA:
  - Data using bid-ask spreads and data on the types and numbers of market participants have been omitted.
  - Data on the number of trading days have yielded a result greater than 100%, influencing the overall categorisation.
  - Data on the number of trades per day and the notional amount per day have been arbitrarily set per instrument (e.g., 1 trade per day and EUR 10million for FX forwards) and are not reflective for a market with a high number of participants trading significant volumes, such as the FX market.

3. LIS and SSTI thresholds:

- GFXD does not agree with the thresholds set by ESMA.
- We believe that the LIS threshold should be calculated from 2018 onwards dynamically, but we do not agree that a floor should be applied.
- We believe that SSTI should not be arbitrarily set as 50% of LIS.

C: FX Prime Brokerage

The below updates the current discussion with a description of FX prime brokerage (FXPB) when considering transparency and transaction-reporting obligations under MiFID II/MiFIR.

FX prime brokerage activity has unique elements that are not present in bilateral transactions. Indeed, the FX Prime Broker (FXPB) is not present at the point of commitment to economic terms between the FXPB client and the executing broker or electronic platform (the "Price Maker"). This commitment to economic terms is a single price-formative event, but it gives rise to multiple transactions: the give-up trade and the mirror trade and in multi-FXPB arrangements, more transactions between prime brokers.

Further details on the FXPB structure are in the GFXD response to Question 138 of the 22 May 2014 ESMA MiFID II/MiFIR Discussion Paper (DP).

Pre-trade transparency, post-trade transparency and transaction reporting obligations under MiFID II have been identified as areas for further discussion and analysis:

1. Pre-Trade Transparency

*Does an FXPB fall within the definition of a Systematic Internaliser ("**SI**")?*

A "*systematic internaliser*" is defined in MiFID II/MiFIR as: an investment firm that, on an organised, frequent, systematic, and substantial basis, deals on its own account when executing client orders outside a regulated market, an MTF, or an OTF without operating a multilateral system.

The issue therefore becomes whether the investment firm is:

(i) on an organised, frequent, systematic and substantial basis;
(ii) dealing on own account; and
(iii) executing client orders.

An FXPB is not "executing client orders." The price-formation and execution of the transaction take place between the Price Maker and the client of the FXPB, acting as agent of the latter, pursuant to the agency authority granted to the client under the FXPB documentation. The **lack of execution of a client order by the FXPB** means that the FXPB does not act as an SI when accepting give-up transactions.

An important purpose of the regulation is to provide the market with accurate price discovery data. But, pursuant to RTS 9, the Price-Maker is already subject to the pre-trade transparency obligation in his capacity as an SI. Therefore, we conclude that the purpose of regulation is already satisfied, and that the FXPB should be exempted from any pre-trade transparency obligation.

Furthermore, the mirror transaction between the FXPB and its client (i.e. the identical but offsetting transactions between the FXPB and its client post acceptance of the give-up trade) should not be captured by the pre-trade-transparency regime. The mirror trade is executed at the same price as the give-up trade but only upon acceptance of the give-up trade by the FXPB (this creates a natural delay between price formation and the prime broker being 'in' the trade). Reporting could then result in the reporting of a stale price, thereby reporting erroneous information to the market. Furthermore, no SI will be involved in the mirror trade (note the above analysis concluding that the FXPB is not an SI). Therefore, the mirror trade should be exempted from the pre-trade transparency requirement.

A strict reading of the current MiFID II/MiFIR provisions would conclude that the trades are out-of-scope because no SI is involved in the price formation. The relevant provisions under RTS 9 provide:

"6. Where a transaction between two investment firms is concluded outside the rules of a trading venue, either on own account or on behalf of clients, the investment firm that sells the financial instrument concerned shall be responsible for making the transaction public through an Approved Publication Arrangement (APA).

7. By way of derogation to the previous paragraph, if only one of the investment firms party to the transaction is a systematic internaliser in the given instrument, that firm shall report the transaction, informing the seller of the action taken."

2. Post-trade transparency

Because the FXPB is not present at the time of the price formation of the give-up transaction and the existence of such trade is only even known by the FXPB once given-up by its client (usually by the end of the same business day and following matching notices from both the client and the Price Maker), the **FXPB is unable to report the give-up trade in real-time**. If an obligation to report was imposed, the FXPB would report stale data. Post-trade transparency requirements applied to FXPBs would be counter-productive because they would disseminate out-of-date information. The same analysis applies to the mirror trade whose price is formed at the same time the give-up trade is agreed between the FXPB client and the Price Maker.

The FXPB's reporting of stale pricing data to the public was a key consideration in the CFTC's decision to issue the no action relief letter #12-53 dated December 17, 2012 (http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/12-53.pdf) under which FXPBs have no real time public reporting obligation as long as that responsibility is allocated to a Price Maker that is a registered swap dealer.

MiFID II/MiFIR should avoid the intricate and time-consuming process engaged by the industry in the US to obtain the CFTC relief. It can be avoided if the FXPB is exempted from post-trade transparency obligations.

In this respect, RTS 9 does provide exemptions to OTC post-trade transparency obligations where there are "give-up" and "give-in" transactions. These terms are not defined for derivatives in the 19 December 2014 Consultation Paper but we understand it will follow the definitions provided for equity-like instruments under RTS 8, which provides:

"*a transaction where an investment firm passes a client trade to, or receives a client trade from, another investment firm for the purpose of post-trade processing*"

The FX Prime Brokerage industry understands that the above definition captures the give-up and mirror transactions involved in the FX Prime Brokerage structure. As result the FX Prime Brokerage trade will not be subject to post-trade-transparency obligations.

3. Transaction reporting

The FXPB industry must understand its transaction-reporting obligations.

In the "plain vanilla" FX Prime Brokerage relationship, the FXPB is involved in two different transactions: the give-up and mirror transaction. The current framework under EMIR requires the FXPB to report both

trades. This is inconsistent with the goals set-up by MiFID II/MiFIR. For example, when considering post-trade transparency, RTS 9 in its Chapter 2 section 8, provides the following:

> "*For those purposes two matching trades entered at the same time and for the same price with a single party interposed shall be considered to be a single transaction*".

Although it is arguable whether the give-up and mirror transactions are entered at the same time, they certainly have the same price that is crystallised (at the same time) when the FXPB client and the Price Maker agree on economic terms.

We are concerned by the discrepancy between the differing trade reporting rules for FXPBs under EMIR and MiFID II/MiFIR. The FXPB industry must have uniform reporting obligations under the two European regulations.

Under the Dodd Frank Wall Street Reform and Consumer Protection Act, for example, the FXPB reports the mirror transaction and the price-maker reports the give-up transaction. Adopting this approach would at least result in global-consistency.

We understand from Chapter 8.2 "Obligations to report transaction" of the 19 December 2014 MiFID II/MiFIR Consultation Paper outlines that counteracting market abuse is the key consideration of transaction-reporting. We argue that because the mirror transaction is executed at the same price as the give-up transaction (and based on the reporting of the give-up transaction by the Price Maker, the other option would be) to exempt the mirror trade from reporting obligations.

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We appreciate the opportunity to share our views on this consultation paper issued by ESMA. Please do not hesitate to contact Fiona McKane on +44 207 743 9317, email fmckane@gfma.org or Andrew Harvey on +44 207 743 9312, email aharvey@gfma.org should you wish to discuss any of the above.

< ESMA_COMMENT_MIFID_ADD_1>

Q1. Do you agree with ESMA's proposal for the definition of a liquid market? Please provide an answer detailed per asset class identified (deliverable forwards, non-deliverable forwards, options, swaps, spread betting contracts and futures) addressing the following points:

(1) Would you use different qualitative criteria to define the sub-classes? Please also specify if you agree in distinguishing or not distinguishing between deliverable and non-deliverable contracts. If you would distinguish between deliverable and non-deliverable contracts for other classes besides forwards, please provide your feedback as specific as possible with regard to the sub-classes that should be deemed liquid for deliverable contracts and those for non-deliverable contracts, pointing out the differences between the two sub-groups.

(2) Would you use different parameters or the same parameters (i.e. average number of trades per day and average notional amount traded per day) but different thresholds in order to define a sub-class as liquid?

(3) Would you define some specific classes declared as liquid in ESMA's proposal as illiquid (and vice versa)? Please provide reasons for your answer.

<ESMA_QUESTION_MIFID_ADD_1>
Q1. Do you agree with ESMA's proposal for the definition of a liquid market?

The GFXD does not agree with ESMAs definition of a liquid market. We consider that ESMA has used data that is not of sufficient quality, or contains too many incorrectly classified instruments, and as a consequence has made a proposal that contains many incorrect conclusions. We recommend that ESMA instead:

- Correct for the many issues arising from poor quality data or the incorrect classification of trades. ESMA should:
    - Only utilise data from EMIR trade repositories once ESMA can be sure that trades can be appropriately classified into correct classes, correcting the apparent misclassification of trades between the deliverable forward (FX forward), non-deliverable forward (NDF) FX swap and FX option classes.
    - ESMA's use of data to assess liquidity is from the period very shortly after the EMIR trade reporting requirement came into effect which has likely compounded ESMA's difficulties in performing analysis. The challenges that this reporting requirement presented to the industry have been widely publicised, and we are concerned that ESMA's dataset may, for example, contain duplicate trades or other erroneous data. ESMA may not wish to place full reliance on this dataset, or could compensate through the use of higher liquidity thresholds for the average frequency and average size of transactions liquidity parameters than might otherwise have been appropriate. Alternatively, ESMA could repeat its analysis on more recent trade repository data or use an alternate data source, which might be more accurate. Additionally, use of a dataset covering a longer period of time may produce more representative results, potentially less distorted by seasonal or short-

term factors. GFXD would be prepared to assist ESMA in repeating the analysis in order to incorporate the necessary corrections.

- In the absence of the necessary corrections, make a more conservative assessment of what is liquid in order to avoid permanent harmful impacts on the liquidity of those instruments incorrectly assessed.

- Remove the 'spread betting' class altogether, and instead allocate the trades into this class more granularly according to the specific nature of the transactions. The term 'spread betting' should not be used, and instead actual product types should be provided, according to market standard taxonomies. ESMA must make an appropriate determination of liquidity on each of the resultant sub-classes, a task with which GFXD is prepared to assist. Failing that, the 'spread betting' asset class should be re-labelled 'Others' and determined to be illiquid due to the non-homogeneity of the underlying instruments. We recommend that ESMA ceases to use this classification in conjunction with FX derivatives, as defined under MiFID annex C4.

- Consult on all product definitions via a specific public consultation and not introduce them as fact, such as in this MiFIR consultation. We draw specific reference to the process used by ESMA in its consultation on the delineation of FX spot and FX forward in May 2014 (http://gfma.org/correspondence/item.aspx?id=591). If ESMA decide not to separately consult the industry, then we strongly recommend that in order to complete Section 6 Annex III of RTS 9, ESMA leverages those provisions in the ISDA 1998 FX and Currency Option Definitions (and subsequent Supplements), as well as those available in other jurisdictions e.g., in the US Commodities Exchange Act. The GFXD would be prepared to assist ESMA as required.

- Seek to achieve its policy objective of ensuring transparency at the aggregate level of the FX derivatives asset class, and not attempt to find at least some liquid sub-classes in as many classes of FX derivatives as possible. Some classes are simply very illiquid or extremely heterogeneous. Appropriate and consistent use of liquidity thresholds across sub-classes when defined with comparable levels of granularity will ensure that illiquid classes are not incorrectly identified as liquid. If ESMA wishes to assess whether or not it has "captured" a sufficiently broad range of derivatives as liquid instruments, it should make this assessment at the aggregate level of the FX derivatives asset class, rather than at the level of each class or sub-class.

- Compensate for that fact that two of the key elements of the definition of a liquid market have not been taken into account, specifically: the number and type of market participants; and the average size of spreads. We understand why ESMA may have encountered difficulty incorporating these liquidity parameters, but MiFIR does require their consideration, and we therefore recommend that ESMA compensate for the potential misclassification of illiquid sub-classes as liquid through higher liquidity thresholds for those liquidity parameters actually used (i.e., average frequency and average size of transactions), than would otherwise have been possible had the full set of liquidity parameters been considered.

- Recognise package transactions as a distinct class of financial transactions and ensure that they are adequately provided for in the RTS.

- Make clearer and more specific compensation for the inadequacies in, and the errors of, the liquidity assessment, through setting lower LIS and particularly SSTI thresholds than might other-

wise have been possible had a more accurate determination of liquidity been utilized. This is of greatest importance where the liquidity assessment of the subclasses is most erroneous.

Below we explain in detail why we disagree with the ESMA proposal and propose an alternative using the Bank of England semi-annual FX survey.

(1) Would you use different qualitative criteria to define the sub-classes?

The GFXD would use different criteria to define the sub classes. Below, we discuss our observations across FX forward, FX swap, FX NDF and FX options and provide an alternative for consideration.

EMIR trade reporting and instrument mapping: We do not believe that EMIR trade reporting data has been categorized by ESMA to a sufficient degree of granularity to determine the liquidity of FX instruments. As per our response to the May 2014 MiFID Discussion Paper (DP), the GFXD believes that the FX instruments should be categorized as per Annex 3.6.1, included for ease in Figure 1 below. Our proposal allows the market to be considered in-line with the ISDA FX taxonomy which accurately represents how the market trades FX. For non-spot trades, participants report this data under the 'Product ID Value' field to the TRs, and we suggest that this data should be made available to ESMA for consideration. The current ISDA FX taxonomy does not contain a FX swap, due to the fact that FX swaps are reported as FX forwards and are linked with a 'link id'. Such an approach accommodates the varying booking methods used by market participants.

- The current ISDA FX taxonomy is as follows:
  - FX spot
  - FX NDF (non deliverable forwards) (Product ID Value: Foreign Exchange: NDF)
  - FX NDO (non deliverable options) (Product ID Value: Foreign Exchange: NDO)
  - FX forward (Product ID Value: Foreign Exchange: Forward)
  - FX vanilla options (Product ID Value: Foreign Exchange: Vanilla Options)
  - FX simple exotics (Product ID Value: Foreign Exchange: SimpleExotic)
  - FX complex exotics (Product ID Value: Foreign Exchange: ComplexExotic)

- EMIR trade reporting currently does not recognize this taxonomy. Instead trade repositories permit reporting firms map data submissions using the following EMIR reportable fields:
  - Product ID 1: CU (currency)
  - Product ID 2: FW (forwards), OP (options), SW (swap), OT (other)

- For example, DTCC maps their FX trade submissions as follows:
  - FX Spot – mapped to 'OT'
  - FX NDF – mapped to 'FW'
  - FX NDO – mapped to 'OP'
  - FX Fwd – mapped to 'FW'
  - FX Vanilla Option – mapped to 'OP'
  - FX Simple Exotic – mapped to 'OP'
  - FX Complex Exotic – mapped to 'OT'

ESMA also note that they have performed additional mapping of the data to the 'Other' bucket and have re-classified this as 'Spread-betting'. As discussed above, this is not appropriate to FX derivatives defined under MiFID Annex C4, so should be disaggregated and split by ESMA into the appropriate sub-product

classes for in order to achieve an appropriate determination of liquidity at a suitably granular level. Annex 2.1.1 paragraph vi on page 210 of the Consultation Paper (CP) defines how ESMA have re-pointed data and created the 'Spread-betting' bucket. We believe that this approach is not accurate and grossly misrepresents what should be included in the 'Other' bucket, namely FX complex exotic options, which represent approximately 2% of the FX market and are widely considered to be bespoke and illiquid in nature.

Figure 1: GFXD proposal for Annex 3.6.1 defining FX instrument categorization under MiFIR

Financial Instrument	**Product Types**	**Sub-Product Types**	**Recommended Liquidity sub-categories**
Foreign Exchange Derivatives	Futures	N/A	Currency Pair / Maturity
	Options	Non-Deliverable Option - NDO (only European type options are NDO - not any other FX options settled in non-deliverable currency)	
		Vanilla Option (European and American)	
	Forwards	Deliverable Forward	
		NDF	
	FX Swaps	Deliverable FX Swap	
		Non-Deliverable FX Swap	
	Others	Simple exotic (Barrier & Digital)	
		Complex Exotic	

The GFXD would also like to support the ISDA position on package transactions, a direct extract included below for ease which we consider should be applied generically to all non-Equity instruments:

START OF ISDA TEXT [Package transactions

a) Overview

ISDA would like to propose that ESMA considers specific and tailored treatment for package transactions as the Consultation Paper does not address how these transactions might be treated under the new framework. In response to the May 2014 DP, ISDA included a number of detailed comments on the nature of package transactions which we draw ESMA's attention to. We reiterate the points made in that response and put forward a proposal which we hope ESMA will find workable and flexible enough to apply for venue and SI transparency obligations and the derivatives trading obligation. This will preserve the market for package transactions and ensure that pricing and liquidity is not negatively impacted for end investors.

We believe that Level 1 text is flexible enough to empower ESMA to specify how package transactions are treated in order to determine if such transactions are liquid or "traded on a trading venue" (both for determining whether transparency obligations apply as well as determining whether the derivatives trading obligation applies). The Level 1 text clearly sets the foundation for the pre- and post-trade transparency regimes in non-equities by defining the asset classes – "bonds, structured finance products, emission allowances and derivatives" – on which the Level 2 measures must be built. However, ESMA has flexibility to define how, within these broad asset classes, to identify whether specific financial instruments (or combinations thereof) are to be considered "liquid" or "traded on a trading venue". ESMA has chosen to adopt COFIA as the basis for determining whether a liquid market exists – which suggests to us that ESMA is also empowered to tailor this approach to instruments which fall within one of the specified classes, but are part of a package transaction.

b) Advantages of package transactions to clients

Package transactions allow clients to reduce their transaction costs (i.e. a single transaction is less expensive to execute than multiple transactions) and manage their execution risk (i.e. a single execution alleviates timing and other mechanical/process type risks). They are tailored to provide risk-return characteristics in the form of a single transaction in an efficient and cost-effective manner to clients.

c) Challenges to trading package transactions without a tailored proposal

Below are some very realistic fact patterns which hopefully demonstrate that unless there is tailored treatment for package transactions which recognises that package transactions should be considered in their entirety when being assessed as subject to transparency requires and/or the derivatives trading obligation, there is a significant risk that such transactions may no longer be available to clients in the EU.

This will be due to the individual components being treated differently and inconsistently vs. each other when they are assessed against the relevant requirements which would negate the advantages highlighted above of trading package transactions. These challenges are likely to be particularly acute where one or more of the components of a package transaction includes derivatives subject to the trading obligation:

- If some components of a package transaction are traded on a trading venue but others are not.
- If some components of a package transaction are deemed liquid but others are not.
- If some components of a package transaction are above the relevant LIS or SSTI thresholds but others are not.
- If the components of a package transaction are below the relevant LIS or SSTI thresholds but together they behave similarly to a single transaction above the LIS or SSTI.
- If the package transaction contains a listed derivative which trades on a different trading venue to other components.

If ESMA fails to provide for the appropriate trading of packages, end investors will be required to trade the components independently, resulting in increased transaction costs and increased execution risks, which would seem to conflict with ESMA's policy objectives.

d) ISDA proposal

We would be keen to assist ESMA with the development of a workable regime for package transactions. We consider that the following proposals could both address the challenges we have described above. We have provided both proposals for ESMA's consideration as we recognise that, whilst Option 1 is a simpler proposal, Option 2 is more accurate.

Option 1:

1. Subject to point 3 below, if each component of a package transaction is liquid:
    a. The package transaction should be considered liquid; and
    b. If any one component is above the relevant threshold (LIS or SSTI) then the package transaction should be deemed to be above the threshold.
2. Subject to point 3 below, if the package transaction contains liquid and illiquid components:
    a. The package transaction should be considered illiquid; and
    b. If any one component is above the relevant threshold (LIS or SSTI) then the package transaction should be deemed to be above the threshold.
3. For the purposes of MiFIR Articles 8(1), 10(1), 18(1) and 18(2), all components of a package have to be tradable on a single venue in order for the package be considered "traded on a venue".
4. If the package transaction comprises ten or more component legs, the package transaction should be considered illiquid.

If ESMA, for pre-trade transparency purposes, would prefer to represent this in a table format, we propose the following table which reflects the above:

Table 11: ISDA Proposal for the calibration of Package Transactions for liquidity, Large in Scale, and Size Specific to the Instrument thresholds.

Type	Package type comprising:	Example	1. All components above LIS	2. All components above SSTI	3. At least one component above LIS	4. At least one component above SSTI	5. All components below LIS	6. All components below SSTI
A	Exclusively liquid derivatives in one derivative asset class[1]	2yr vs 10yr EUR swap	Package is above LIS and liquid	Package is above SSTI and liquid	Package is above LIS and liquid	Package is above SSTI and liquid	Package is below LIS and liquid	Package is below SSTI and liquid
B	Exclusively liquid securities	2yr vs 10yr Bund switch	Package is above LIS and liquid	Package is above SSTI and liquid	Package is above LIS and liquid	Package is above SSTI and liquid	Package is below LIS and liquid	Package is below SSTI and liquid
C	Liquid security(ies) and derivative(s) where the derivatives are from a single asset class[1]	Asset swap vs. cash bund	Package is above LIS and liquid	Package is above SSTI and liquid	Package is above LIS and liquid	Package is above SSTI and liquid	Package is below LIS and liquid	Package is below SSTI and liquid
D	Liquid & illiquid security(ies) and derivative(s) where the derivatives are from a single asset class[1]	10yr EUR swap vs. 10yr inflation swap	Package is above LIS and not liquid	Package is above SSTI and not liquid	Package is above LIS and not liquid	Package is above SSTI and not liquid	Package is below LIS and not liquid	Package is below SSTI and not liquid
E	Liquid derivative(s) & any liquid exchange traded derivative(s) in the same derivative asset class [1]	EFP transaction of swap vs. future	Package is above LIS and liquid[2]	Package is above SSTI and liquid[2]	Package is above LIS and liquid[2]	Package is above SSTI and liquid[2]	Package is below LIS and liquid[2]	Package is below SSTI and liquid[2]
F	Liquid security(ies) & any liquid exchange traded derivative(s) in the same derivative asset class [1]	Cash bund vs. Bund future basis trade	Package is above LIS and liquid[2]	Package is above SSTI and liquid[2]	Package is above LIS and liquid[2]	Package is above SSTI and liquid[2]	Package is below LIS and liquid[2]	Package is below SSTI and liquid[2]
G	Exclusively illiquid securi-ty(ies) or derivative(s)	10yr EUR inflation vs. 30yr GBP inflation	Package is above LIS and not liquid	Package is above SSTI and not liquid	Package is above LIS and Not liquid	Package is above SSTI and Not liquid	Package is below LIS and not liquid	Package is below SSTI and not liquid
H	10 or more components	Package of several swaps bundled for execution (e.g. 10yr EUR swap, 15yr EUR swap, 20yr EUR swap, 25yr EUR swap, and 30 yr EUR swap)	Package is above LIS and not liquid	Package is above SSTI and not liquid	Package is above LIS and not liquid	Package is above SSTI and not liquid	Package is below LIS and not liquid	Package is below SSTI and not liquid

[1] Interest Rate Derivatives, FX Derivatives, Commodity Derivatives, Equity Derivatives etc considered as distinct derivative asset classes.

[2] Assuming that ESMA agrees that, for the purposes of MiFIR articles 8(1), 10(1), 18(1) and 18(2), all components of a package have to be tradable on a single venue in order that the package be considered "traded on a venue". Otherwise, ESMA should deem packages including exchange traded derivatives to be not liquid. ISDA recommends that packages involving exchange traded derivatives should be executed using the wholesale trading facilities currently governed by venues' rulebooks

Option 2:

1. Subject to point 3 below, if each component of a package transaction is liquid:
    a. The package transaction should be considered liquid; and
    b. The percentage threshold for each individual component in a package transaction is equal to the notional of the relevant component expressed as a percentage of its relevant threshold (LIS or SSTI). If the sum of the percentage thresholds for all components in the package transaction is above 100%, then the package transaction (and each of its components) is above the relevant threshold (LIS or SSTI). See below for a more detailed explanation of the percentage threshold approach.
2. Subject to point 3 below, if the package transaction contains liquid and illiquid components:
    a. The package transaction should be considered illiquid; and
    b. The percentage threshold for each individual component in a package transaction is equal to the notional of the relevant component expressed as a percentage of its relevant threshold (LIS or SSTI). If the sum of the percentage thresholds for all components in the package transaction is above 100%, then the package transaction (and each of its components) is above the relevant threshold (LIS or SSTI). See below for a more detailed explanation of the percentage threshold approach.
3. For the purposes of MiFIR Articles 8(1), 10(1), 18(1) and 18(2), all components of a package have to be tradable on a single venue in order for the package be considered "traded on a venue".
4. If the package transaction comprises ten or more component legs, the package transaction should be considered illiquid.

The percentage threshold approach aims to, in a simple manner, replicate the package of instruments into a single instrument to test whether it would indeed be above the threshold (SSTI or LIS purposes) or not if it were traded as a single instrument.

Example: if an investor wishes to hedge cash flows at 5-year and 15-year points using EUR interest rate swaps, to create an accurate hedge the investor would trade a package of two EUR swaps at 5-year and 15-year maturities. Alternatively, the investor could enter into a single swap with an average 10-year maturity to try to replicate the risk profile but with less accuracy.

However, whilst the individual swaps in the package of swaps could each be below the relevant threshold, the equivalent single swap would have a larger notional and could therefore be above the threshold, as illustrated below. Given the 5-year and 15-year swaps are economically similar in nature, the pricing of one swap is likely to impact the pricing of the other. By not recognising this, ESMA could create an incentive for the market to trade in the equivalent single average instruments, rather than the package of instruments that provide a more accurate hedge: the result would be to provide a less perfect hedge, thereby retaining risk in the system.

The suggested percentage threshold approach provides a way to calibrate this and ensures that package transactions are not disproportionately disadvantaged.

The below table illustrates the example described above.

Table 12: Example of how the percentage threshold approach (Option 2) operates			
	More accurate hedge		Less accurate hedge
	EUR 5yr swap	EUR 15yr swap	EUR 10yr swap
Notional	60m	60m	120m
Threshold (SSTI or LIS)	100m	100m	100m
Percentage Threshold	60%	60%	120%

Table 11, prepared for Option 1, could easily be adapted for Option 2 if this is ESMA's preferred option and we would be happy to prepare this table if requested.

e) Safeguarding against avoidance

ISDA is aware that ESMA and national competent authorities may be concerned that adoption of our proposal may lead to market participants creating packages of instruments purely for the purposes of avoiding the transparency regime or the derivatives trading obligation. ISDA recognises these concerns and suggests that this could be achieved by defining a package and including, within the MiFID II/MiFIR framework, a mechanism that would support the monitoring (and therefore supervision) of the trading of packages. ISDA would welcome the opportunity to discuss these safeguards with ESMA in more detail.

1. Definition of package transaction

ISDA recommends that a "package transaction" be defined as a transaction comprising two or more components, each of which is a bond, structured finance product, emission allowance or derivative where:

(i) The components are priced as a "package" with simultaneous execution of all such components;
(ii) The execution of each component is contingent on the execution of the other components;
(iii) Each component must be able to stand alone and must be able to bear economic risk; and
(iv) Either:

i. the components are economically similar in nature such that the pricing of one component can affect the pricing of the other component; or
ii. the components must have a reasonable degree of correlation.

2. Post-trade transparency flag

With a view to assisting the monitoring of package transactions by supervisors, and as stated in our response to Question 74, ISDA recommends that an additional flag to be reported on trades that are components of package transactions be added to the list of flags set out in Table 2 of Annex II of RTS 9. We would also draw attention to our response to Question 218 where we suggest that ESMA may wish to consider including a "link ID" field in transaction reports (for the purposes of the Article 26 MiFIR transaction reporting regime). In ISDA's response to ESMA's recent consultation paper on the review of reporting technical standards under EMIR, we recommended the inclusion of a "link ID" field to link together trade reports of components of the same package. ESMA may wish to consider whether to incorporate such a field in the transaction reports required under the MiFIR transaction reporting regime as this would give supervisors greater visibility in respect of the usage of package transactions.] **END OF ISDA TEXT**

(2) Would you use different parameters or the same parameters but different thresholds in order to define a sub-class as liquid?

We do not believe that the approach used by ESMA in defining the Notional Amount/Number of trades a day is appropriate in its current state.

The FX market is global in nature and forms the basis of the global payments system, resulting is a very large number of market participants. It would be very easy for a financial instrument to be traded once a day but considered illiquid by market participants. Also, the definition of 'liquid market' in Article 2(17)(a) of MiFIR requires there to be "ready and willing buyers and sellers on a continuous basis". This requires there to be more than one buyer or seller in a market for a particular sub-class of instruments for that sub-class to be determined liquid. Specifically, two trades, or in some cases one trade per day, cannot be considered consistent with this definition.

Supporting ISDA in their response to the December 2014 CP, GFXD members believe that where a product is traded by a small number of participants, ESMA should seek to understand the composition of market participants before determining the final thresholds. For example, a market with ten active participants may have two sellers and eight buyers, or just one risk management provider amongst nine participants seeking risk management services.

(3) Would you define some specific classes declared as liquid in ESMA's proposal as illiquid (and vice versa)?

The GFXD would define some classes declared liquid by ESMA as illiquid and vice-versa and we explain why below.

ESMA have included on page 16 of the CP 2 charts which show the notional and trade distribution of FX derivatives, essentially summarizing the data used by ESMA in this CP.

It is immediately obvious that these charts do not mirror the data published in the Bank of International Settlements (BIS) Triennial Central Bank Survey of Foreign Exchange turnover (http://www.bis.org/publ/rpfx13fx.pdf), nor that published by the Bank of England in its semi-annual FX surveys (http://www.bankofengland.co.uk/markets/Pages/forex/fxjsc/default.aspx). Both of these sources are widely accepted by the FX industry (including Central Banks) as being representative of turnover within the FX markets, both sources reporting similar market splits by instrument traded and currency pairs.

Figures 2, 3, 4a/b and 5 below show the results of these data sources (Figure 5 comparing all 3) and it should be noted that ESMA themselves used the BIS data in their recent FX NDF Clearing CP, as illustrated in Figure 3.

It is clear that the product splits in Figure 2 (ESMA Addendum CP) are considerably different to those seen in Figures 3 and 4a/b (BIS and BoE) and the difference is even more obvious in Figure 5. The volume of each product is either considerably greater/smaller than expected and there is the addition of a new product, 'spread-betting' which was unexpected (and in fact misrepresentative), and is discussed in more detail elsewhere in Q1.

Figure 2: Extract from ESMAs MiFID Addendum Consultation Paper using EMIR trade reporting data

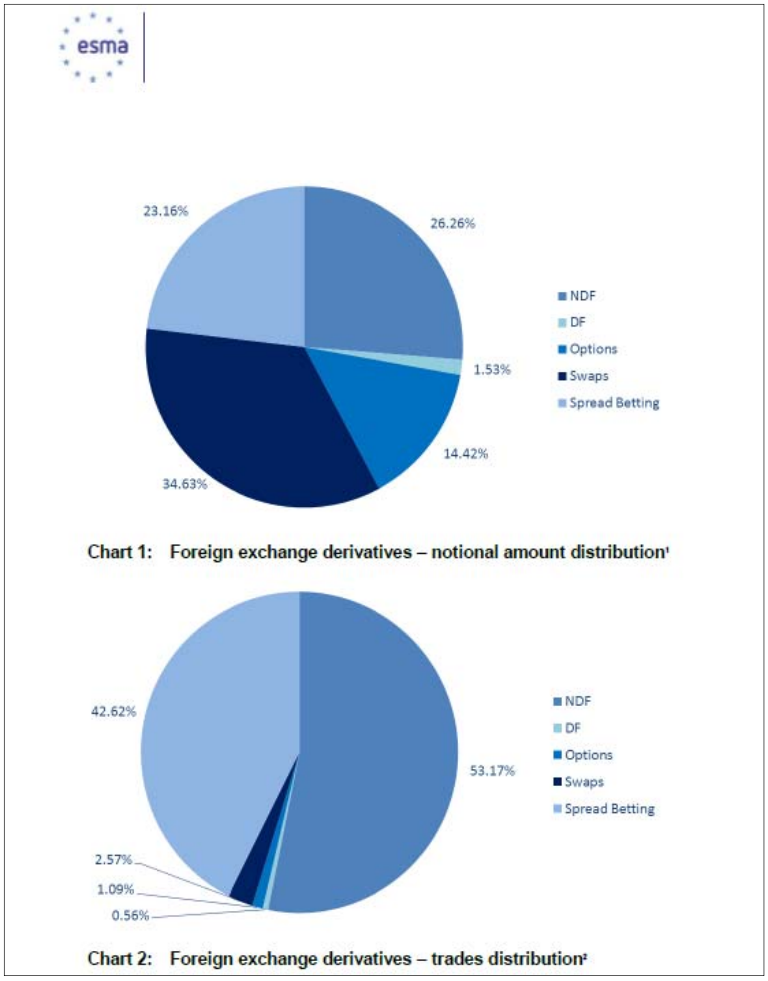


Figure 3: Extract from ESMAs FX NDF Clearing CP from October 2014 using BIS data

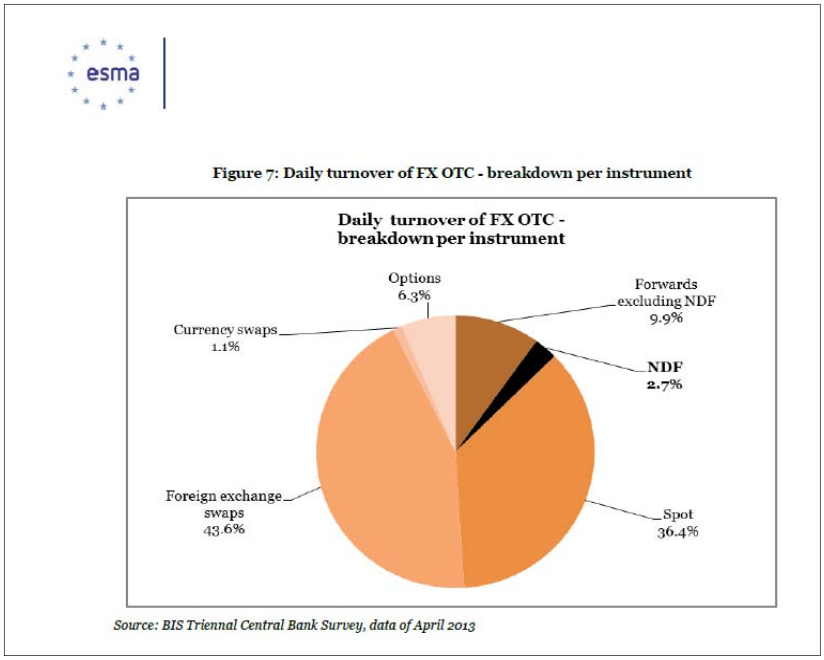


Figure 4a: Extract and Representation of the BoE April 2014 Semi-Annual FX Survey

Table 1

Reported UK foreign exchange market turnover by instrument[1]

Daily averages in billions of US dollars

Instrument	April 2014	October 2014
Spot transactions	795	1110
Outright forwards	179	236
Non-deliverable forwards	54	61
Foreign exchange swaps	1212	1041
Currency swaps	24	25
Foreign exchange options	129	196
Total foreign exchange turnover	**2393**	**2667**

[1] Adjusted for double counting of deals between survey contributors.
Totals may not sum due to rounding.
Daily averages are calculated assuming 20 working days in April 2014 and 23 working days in October 2014.

Figure 4b: Chart representation of Figure 4a (BoE Oct 2014 Semi-Annual FX Survey)

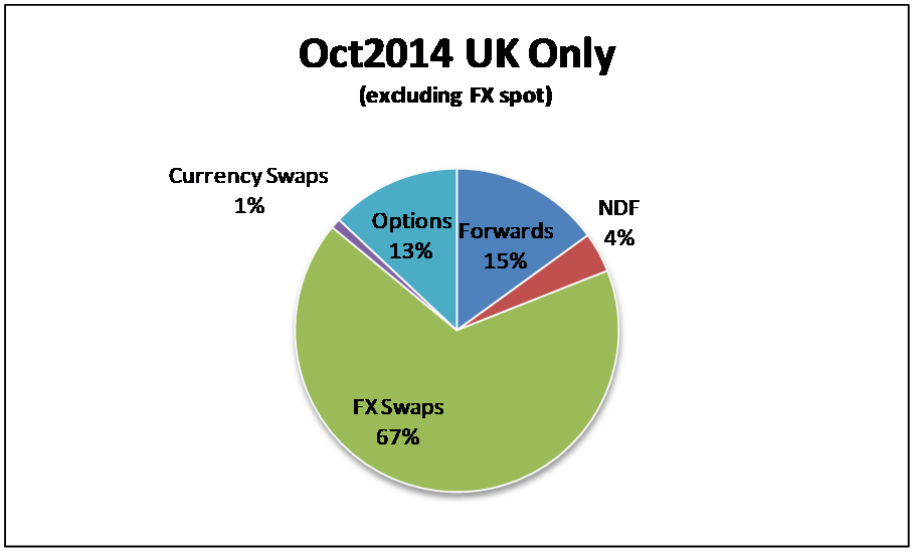
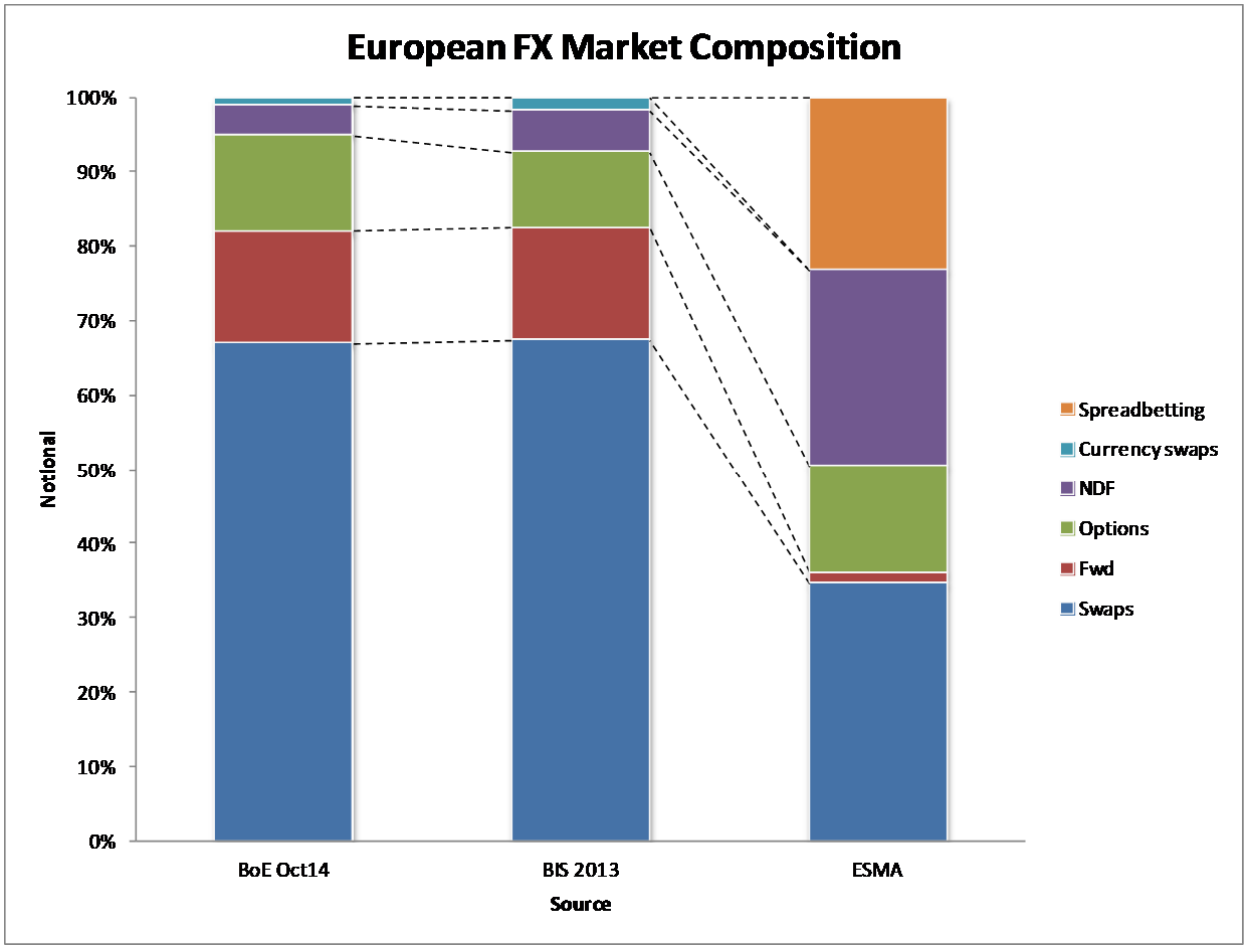


Figure 5: Comparative analysis between the ESMA CP, BIS and BoE data sets



Analysis of the underlying data, as provided in the charts on pages 22-163 of the CP, immediately illustrated examples of data inconsistencies, such as:

- Inclusion of deliverable currency crosses within the NDF bucket.
- Inclusion of non-deliverable currency crosses within the DF bucket.
- Inclusion of a new product category, Spread-betting, which appears to be being used by ESMA as a 'catch all' category for the EMIR trade reporting product category 'Other'. We also consider that there could be an overlap of this category with the Financial Contracts for Difference (CFD) product which is defined under MiFID Annex C9 and not C4 which is where FX derivatives are defined.
- Inclusion of precious metals within the FX data, which at best has the potential to result in confusing and conflicting rules between the FX and Commodities asset classes, and at worst creates unhelpful incentives to repackage economic exposure into different 'wrappers' in order to obtain different regulatory treatment. These commodity products should be removed from the requirements for FX products and addressed solely within the requirements for the Commodities asset class.

The impact of these data inconsistencies is that:

- Some FX instruments we had expected to be considered liquid have been classified as illiquid:
    - e.g., deliverable forward AUD crosses

- Some FX instruments which we had expected to be to be considered illiquid have been classified: as liquid
    - e.g., deliverable forward non-USD crosses

To illustrate the scale of these inconsistencies we have extracted the final deliverable and non-deliverable liquidity tables from the CP. Figure 6 illustrates the data from Table 48-Liquid NDF (which starts on page 329 of the CP) and Figure 7 illustrates Table 50-Liquid DF (which starts on page 336 of the CP).

Figure 6: MiFID Addendum CP Extract of FX non-deliverable forwards – liquid classes

NON-DELIVERABLE FORWARDS (NDF) - LIQUID CLASSES			
CURRENCY PAIR	TENOR	LIS (€)	SSTI (€)
AUD-EUR	from 1 day to 4 days	1,000,000	500,000
AUD-EUR	from 4 days to 7 days	1,000,000	500,000
AUD-EUR	from 7 days to 1 month	1,000,000	500,000
AUD-EUR	from 1 month to 3 months	3,500,000	1,750,000
AUD-EUR	from 3 months to 6 months	1,000,000	500,000
AUD-GBP	from 1 day to 4 days	1,000,000	500,000
AUD-GBP	from 4 days to 7 days	1,000,000	500,000
AUD-GBP	from 7 days to 1 month	1,000,000	500,000
AUD-GBP	from 1 month to 3 months	20,000,000	10,000,000
AUD-GBP	from 3 months to 6 months	1,000,000	500,000
AUD-JPY	from 1 day to 4 days	1,000,000	500,000
AUD-JPY	from 4 days to 7 days	4,000,000	2,000,000
AUD-JPY	from 7 days to 1 month	1,000,000	500,000
AUD-JPY	from 1 month to 3 months	8,500,000	4,250,000
AUD-JPY	from 3 months to 6 months	15,000,000	7,500,000
AUD-USD	from 1 day to 4 days	1,000,000	500,000
AUD-USD	from 4 days to 7 days	1,000,000	500,000
AUD-USD	from 7 days to 1 month	1,000,000	500,000
AUD-USD	from 1 month to 3 months	6,000,000	3,000,000
AUD-USD	from 3 months to 6 months	1,000,000	500,000
BRL-USD	from 1 day to 4 days	40,000,000	20,000,000
BRL-USD	from 4 days to 7 days	40,000,000	20,000,000
BRL-USD	from 7 days to 1 month	15,000,000	7,500,000
BRL-USD	from 1 month to 3 months	15,000,000	7,500,000
BRL-USD	from 3 months to 6 months	35,000,000	17,500,000
CAD-EUR	from 1 day to 4 days	1,000,000	500,000
CAD-EUR	from 4 days to 7 days	1,000,000	500,000
CAD-EUR	from 7 days to 1 month	1,000,000	500,000
CAD-EUR	from 1 month to 3 months	3,000,000	1,500,000
CAD-EUR	from 3 months to 6 months	1,000,000	500,000
CAD-GBP	from 1 day to 4 days	1,000,000	500,000
CAD-GBP	from 4 days to 7 days	1,000,000	500,000
CAD-GBP	from 7 days to 1 month	1,000,000	500,000
CAD-GBP	from 1 month to 3 months	30,000,000	15,000,000
CAD-USD	from 1 day to 4 days	1,000,000	500,000
CAD-USD	from 4 days to 7 days	1,000,000	500,000
CAD-USD	from 7 days to 1 month	1,000,000	500,000
CAD-USD	from 1 month to 3 months	1,000,000	500,000
CAD-USD	from 3 months to 6 months	1,000,000	500,000
CHF-EUR	from 1 day to 4 days	1,000,000	500,000
CHF-EUR	from 4 days to 7 days	1,000,000	500,000
CHF-EUR	from 7 days to 1 month	1,000,000	500,000
CHF-EUR	from 1 month to 3 months	8,500,000	4,250,000
CHF-EUR	from 3 months to 6 months	1,000,000	500,000
CHF-GBP	from 1 day to 4 days	1,000,000	500,000
CHF-GBP	from 4 days to 7 days	1,000,000	500,000
CHF-GBP	from 7 days to 1 month	1,000,000	500,000
CHF-GBP	from 1 month to 3 months	20,000,000	10,000,000
CHF-GBP	from 3 months to 6 months	1,000,000	500,000
CHF-JPY	from 1 day to 4 days	1,000,000	500,000
CHF-JPY	from 4 days to 7 days	1,000,000	500,000
CHF-JPY	from 7 days to 1 month	1,000,000	500,000
CHF-JPY	from 1 month to 3 months	25,000,000	12,500,000
CHF-JPY	from 3 months to 6 months	10,000,000	5,000,000
CHF-USD	from 1 day to 4 days	1,000,000	500,000
CHF-USD	from 4 days to 7 days	1,000,000	500,000
CHF-USD	from 7 days to 1 month	1,000,000	500,000
CHF-USD	from 1 month to 3 months	10,000,000	5,000,000
CHF-USD	from 3 months to 6 months	1,000,000	500,000
CLP-USD	from 7 days to 1 month	25,000,000	12,500,000
CLP-USD	from 1 month to 3 months	20,000,000	10,000,000
CLP-USD	from 3 months to 6 months	175,000,000	87,500,000
CNY-EUR	from 7 days to 1 month	15,000,000	7,500,000
CNY-EUR	from 1 month to 3 months	15,000,000	7,500,000
CNY-USD	from 1 day to 4 days	1,000,000	500,000
CNY-USD	from 4 days to 7 days	25,000,000	12,500,000
CNY-USD	from 7 days to 1 month	30,000,000	15,000,000
CNY-USD	from 1 month to 3 months	20,000,000	10,000,000
CNY-USD	from 3 months to 6 months	30,000,000	15,000,000
CNY-USD	from 6 months to 1 year	20,000,000	10,000,000
CNY-USD	from 1 year to 2 years	20,000,000	10,000,000
COP-USD	from 1 day to 4 days	175,000,000	87,500,000
COP-USD	from 4 days to 7 days	700,000,000	350,000,000
COP-USD	from 7 days to 1 month	70,000,000	35,000,000
COP-USD	from 1 month to 3 months	70,000,000	35,000,000
CZK-EUR	from 7 days to 1 month	15,000,000	7,500,000
CZK-EUR	from 1 month to 3 months	15,000,000	7,500,000
CZK-EUR	from 3 months to 6 months	1,500,000	750,000
DKK-EUR	from 1 day to 4 days	7,500,000	3,750,000
DKK-EUR	from 4 days to 7 days	7,500,000	3,750,000
DKK-EUR	from 7 days to 1 month	15,000,000	7,500,000
DKK-EUR	from 1 month to 3 months	100,000,000	50,000,000
DKK-EUR	from 3 months to 6 months	90,000,000	45,000,000
DKK-GBP	from 4 days to 7 days	20,000,000	10,000,000
DKK-GBP	from 7 days to 1 month	25,000,000	12,500,000
DKK-GBP	from 1 month to 3 months	25,000,000	12,500,000
DKK-USD	from 1 day to 4 days	1,000,000	500,000
DKK-USD	from 4 days to 7 days	70,000,000	35,000,000
DKK-USD	from 7 days to 1 month	15,000,000	7,500,000
DKK-USD	from 1 month to 3 months	15,000,000	7,500,000
DKK-USD	from 3 months to 6 months	4,000,000	2,000,000
DKK-USD	from 6 months to 1 year	20,000,000	10,000,000
EUR-GBP	from 1 day to 4 days	1,000,000	500,000
EUR-GBP	from 4 days to 7 days	1,000,000	500,000
EUR-GBP	from 7 days to 1 month	1,000,000	500,000
EUR-GBP	from 1 month to 3 months	20,000,000	10,000,000
EUR-GBP	from 3 months to 6 months	1,000,000	500,000
EUR-GBP	from 6 months to 1 year	1,000,000	500,000
EUR-GBP	from 1 year to 2 years	7,000,000	3,500,000
EUR-GBP	from 2 years to 3 years	35,000,000	17,500,000
EUR-HUF	from 1 day to 4 days	1,000,000	500,000
EUR-HUF	from 4 days to 7 days	15,000,000	7,500,000
EUR-HUF	from 7 days to 1 month	15,000,000	7,500,000
EUR-HUF	from 1 month to 3 months	30,000,000	15,000,000
EUR-HUF	from 3 months to 6 months	75,000,000	37,500,000
EUR-HUF	from 6 months to 1 year	15,000,000	7,500,000

NON-DELIVERABLE FORWARDS (NDF) - LIQUID CLASSES			
CURRENCY PAIR	TENOR	LIS (€)	SSTI (€)
EUR-JPY	from 1 day to 4 days	1,000,000	500,000
EUR-JPY	from 4 days to 7 days	3,000,000	1,500,000
EUR-JPY	from 7 days to 1 month	1,000,000	500,000
EUR-JPY	from 1 month to 3 months	10,000,000	5,000,000
EUR-JPY	from 3 months to 6 months	20,000,000	10,000,000
EUR-NOK	from 1 day to 4 days	8,000,000	4,000,000
EUR-NOK	from 4 days to 7 days	8,000,000	4,000,000
EUR-NOK	from 7 days to 1 month	2,000,000	1,000,000
EUR-NOK	from 1 month to 3 months	5,000,000	2,500,000
EUR-NOK	from 3 months to 6 months	3,500,000	1,750,000
EUR-PLN	from 1 day to 4 days	4,000,000	2,000,000
EUR-PLN	from 4 days to 7 days	4,500,000	2,250,000
EUR-PLN	from 7 days to 1 month	5,500,000	2,750,000
EUR-PLN	from 1 month to 3 months	7,000,000	3,500,000
EUR-PLN	from 3 months to 6 months	2,000,000	1,000,000
EUR-SEK	from 1 day to 4 days	9,000,000	4,500,000
EUR-SEK	from 4 days to 7 days	9,000,000	4,500,000
EUR-SEK	from 7 days to 1 month	5,000,000	2,500,000
EUR-SEK	from 1 month to 3 months	9,000,000	4,500,000
EUR-SEK	from 3 months to 6 months	2,500,000	1,250,000
EUR-USD	from 1 day to 4 days	1,000,000	500,000
EUR-USD	from 4 days to 7 days	1,000,000	500,000
EUR-USD	from 7 days to 1 month	1,000,000	500,000
EUR-USD	from 1 month to 3 months	2,000,000	1,000,000
EUR-USD	from 3 months to 6 months	1,000,000	500,000
EUR-USD	from 6 months to 1 year	1,000,000	500,000
EUR-USD	from 1 year to 2 years	4,000,000	2,000,000
EUR-USD	from 2 years to 3 years	20,000,000	10,000,000
GBP-HKD	from 4 days to 7 days	40,000,000	20,000,000
GBP-HKD	from 7 days to 1 month	8,500,000	4,250,000
GBP-HKD	from 1 month to 3 months	45,000,000	22,500,000
GBP-HUF	from 1 day to 4 days	1,000,000	500,000
GBP-HUF	from 4 days to 7 days	4,000,000	2,000,000
GBP-HUF	from 7 days to 1 month	6,000,000	3,000,000
GBP-HUF	from 1 month to 3 months	2,500,000	1,250,000
GBP-HUF	from 3 months to 6 months	45,000,000	22,500,000
GBP-JPY	from 1 day to 4 days	1,000,000	500,000
GBP-JPY	from 4 days to 7 days	1,000,000	500,000
GBP-JPY	from 7 days to 1 month	1,000,000	500,000
GBP-JPY	from 1 month to 3 months	35,000,000	17,500,000
GBP-JPY	from 3 months to 6 months	20,000,000	10,000,000
GBP-NOK	from 1 month to 3 months	25,000,000	12,500,000
GBP-NOK	from 3 months to 6 months	3,000,000	1,500,000
GBP-SEK	from 4 days to 7 days	5,000,000	2,500,000
GBP-SEK	from 7 days to 1 month	5,500,000	2,750,000
GBP-SEK	from 1 month to 3 months	45,000,000	22,500,000
GBP-USD	from 1 day to 4 days	1,000,000	500,000
GBP-USD	from 4 days to 7 days	1,000,000	500,000
GBP-USD	from 7 days to 1 month	1,000,000	500,000
GBP-USD	from 1 month to 3 months	15,000,000	7,500,000
GBP-USD	from 3 months to 6 months	1,000,000	500,000
GBP-USD	from 6 months to 1 year	1,000,000	500,000
HUF-USD	from 1 day to 4 days	1,000,000	500,000
HUF-USD	from 4 days to 7 days	225,000,000	112,500,000
HUF-USD	from 7 days to 1 month	30,000,000	15,000,000
HUF-USD	from 1 month to 3 months	40,000,000	20,000,000
HUF-USD	from 3 months to 6 months	40,000,000	20,000,000
IDR-USD	from 1 day to 4 days	20,000,000	10,000,000
IDR-USD	from 4 days to 7 days	15,000,000	7,500,000
IDR-USD	from 7 days to 1 month	350,000,000	175,000,000
IDR-USD	from 1 month to 3 months	10,000,000	5,000,000
IDR-USD	from 3 months to 6 months	10,000,000	5,000,000
INR-USD	from 1 day to 4 days	15,000,000	7,500,000
INR-USD	from 4 days to 7 days	25,000,000	12,500,000
INR-USD	from 7 days to 1 month	15,000,000	7,500,000
INR-USD	from 1 month to 3 months	7,500,000	3,750,000
INR-USD	from 3 months to 6 months	20,000,000	10,000,000
INR-USD	from 6 months to 1 year	40,000,000	20,000,000
INR-USD	from 1 year to 2 years	20,000,000	10,000,000
JPY-NZD	from 1 day to 4 days	1,000,000	500,000
JPY-NZD	from 4 days to 7 days	2,500,000	1,250,000
JPY-NZD	from 7 days to 1 month	1,000,000	500,000
JPY-NZD	from 1 month to 3 months	8,000,000	4,000,000
JPY-NZD	from 3 months to 6 months	3,000,000	1,500,000
JPY-USD	from 1 day to 4 days	1,000,000	500,000
JPY-USD	from 4 days to 7 days	6,000,000	3,000,000
JPY-USD	from 7 days to 1 month	1,000,000	500,000
JPY-USD	from 1 month to 3 months	20,000,000	10,000,000
JPY-USD	from 3 months to 6 months	30,000,000	15,000,000
KRW-USD	from 1 day to 4 days	75,000,000	37,500,000
KRW-USD	from 4 days to 7 days	55,000,000	27,500,000
KRW-USD	from 7 days to 1 month	35,000,000	17,500,000
KRW-USD	from 1 month to 3 months	20,000,000	10,000,000
KRW-USD	from 3 months to 6 months	575,000,000	287,500,000
MXN-USD	from 1 day to 4 days	2,000,000	1,000,000
MXN-USD	from 4 days to 7 days	9,500,000	4,750,000
MXN-USD	from 7 days to 1 month	2,500,000	1,250,000
MXN-USD	from 1 month to 3 months	6,500,000	3,250,000
MXN-USD	from 3 months to 6 months	2,000,000	1,000,000
MYR-USD	from 1 day to 4 days	15,000,000	7,500,000
MYR-USD	from 4 days to 7 days	30,000,000	15,000,000
MYR-USD	from 7 days to 1 month	20,000,000	10,000,000
MYR-USD	from 1 month to 3 months	15,000,000	7,500,000
NOK-USD	from 1 day to 4 days	1,000,000	500,000
NOK-USD	from 4 days to 7 days	15,000,000	7,500,000
NOK-USD	from 7 days to 1 month	3,500,000	1,750,000
NOK-USD	from 1 month to 3 months	225,000,000	112,500,000
NOK-USD	from 3 months to 6 months	2,000,000	1,000,000
NZD-USD	from 1 day to 4 days	1,000,000	500,000
NZD-USD	from 4 days to 7 days	1,000,000	500,000
NZD-USD	from 7 days to 1 month	1,000,000	500,000
NZD-USD	from 1 month to 3 months	1,000,000	500,000
NZD-USD	from 3 months to 6 months	1,000,000	500,000

NON-DELIVERABLE FORWARDS (NDF) - LIQUID CLASSES			
CURRENCY PAIR	TENOR	LIS (€)	SSTI (€)
PHP-USD	from 1 day to 4 days	10,000,000	5,000,000
PHP-USD	from 4 days to 7 days	10,000,000	5,000,000
PHP-USD	from 7 days to 1 month	15,000,000	7,500,000
PHP-USD	from 1 month to 3 months	8,000,000	4,000,000
RUB-USD	from 1 day to 4 days	1,000,000	500,000
RUB-USD	from 4 days to 7 days	25,000,000	12,500,000
RUB-USD	from 7 days to 1 month	3,500,000	1,750,000
RUB-USD	from 1 month to 3 months	15,000,000	7,500,000
RUB-USD	from 3 months to 6 months	10,000,000	5,000,000
SEK-USD	from 1 day to 4 days	1,000,000	500,000
SEK-USD	from 4 days to 7 days	15,000,000	7,500,000
SEK-USD	from 7 days to 1 month	8,000,000	4,000,000
SEK-USD	from 1 month to 3 months	9,500,000	4,750,000
SEK-USD	from 3 months to 6 months	1,000,000	500,000
TRY-USD	from 1 day to 4 days	1,500,000	750,000
TRY-USD	from 4 days to 7 days	1,000,000	500,000
TRY-USD	from 7 days to 1 month	1,000,000	500,000
TRY-USD	from 1 month to 3 months	6,500,000	3,250,000
TRY-USD	from 3 months to 6 months	1,000,000	500,000
TWD-USD	from 1 day to 4 days	15,000,000	7,500,000
TWD-USD	from 4 days to 7 days	20,000,000	10,000,000
TWD-USD	from 7 days to 1 month	20,000,000	10,000,000
TWD-USD	from 1 month to 3 months	15,000,000	7,500,000
TWD-USD	from 3 months to 6 months	35,000,000	17,500,000
USD-XAU	from 1 day to 4 days	1,000,000	500,000
USD-XAU	from 4 days to 7 days	1,000,000	500,000
USD-XAU	from 7 days to 1 month	1,000,000	500,000
USD-XAU	from 1 month to 3 months	125,000,000	62,500,000
USD-XAU	from 3 months to 6 months	125,000,000	62,500,000
USD-XAU	from 6 months to 1 year	1,000,000	500,000
USD-ZAR	from 1 day to 4 days	8,000,000	4,000,000
USD-ZAR	from 4 days to 7 days	8,000,000	4,000,000
USD-ZAR	from 7 days to 1 month	1,000,000	500,000
USD-ZAR	from 1 month to 3 months	9,000,000	4,500,000
USD-ZAR	from 3 months to 6 months	2,000,000	1,000,000

NDF

Precious metals

We have identified (grey highlight) in Figure 6 those currency crosses which are typically non-deliverable in nature and it is clear that there are many other crosses included in this category which rarely or never trade as non-deliverable forwards. It should be noted too that some of the LIS numbers, such as the COPUSD 700million, are actually higher than the notional/per day reported on page 30 of the CP (340million), again reflective of the data quality issues facing ESMA.

For ease we have also highlighted in blue those precious metals crosses (see comment above) which have also been included within the FX data. It is clear to us that the current ESMA analysis includes a large proportion of instruments which are rarely if ever traded as FX non-deliverables.

Figure 7: MiFID Addendum CP Extract of FX deliverable forwards – liquid classes

DELIVERABLE FORWARDS (DF) - LIQUID CLASSES			
CURRENCY PAIR	TENOR	LIS (€)	SSTI (€)
CAD-USD	7 days to 1 month	6,000,000.00	3,000,000.00
CAD-USD	1 month to 3 months	2,500,000.00	1,250,000.00
CHF-EUR	1 day to 4 days	20,000,000.00	10,000,000.00
CHF-EUR	4 days to 7 days	5,500,000.00	2,750,000.00
CHF-EUR	7 days to 1 month	8,500,000.00	4,250,000.00
CHF-EUR	1 month to 3 months	10,000,000.00	5,000,000.00
CHF-EUR	3 months to 6 months	15,000,000.00	7,500,000.00
CHF-USD	1 day to 4 days	15,000,000.00	7,500,000.00
CHF-USD	4 days to 7 days	4,500,000.00	2,250,000.00
CHF-USD	7 days to 1 month	4,500,000.00	2,250,000.00
CHF-USD	1 month to 3 months	10,000,000.00	5,000,000.00
CNH-USD	7 days to 1 month	25,000,000.00	12,500,000.00
CNH-USD	1 month to 3 months	40,000,000.00	20,000,000.00
DKK-EUR	7 days to 1 month	3,000,000.00	1,500,000.00
DKK-EUR	1 month to 3 months	4,500,000.00	2,250,000.00
EUR-GBP	1 day to 4 days	30,000,000.00	15,000,000.00
EUR-GBP	4 days to 7 days	7,000,000.00	3,500,000.00
EUR-GBP	7 days to 1 month	9,000,000.00	4,500,000.00
EUR-GBP	1 month to 3 months	10,000,000.00	5,000,000.00
EUR-GBP	3 months to 6 months	25,000,000.00	12,500,000.00
EUR-GBP	6 months to 1 year	8,500,000.00	4,250,000.00
EUR-JPY	1 day to 4 days	6,500,000.00	3,250,000.00
EUR-JPY	4 days to 7 days	5,000,000.00	2,500,000.00
EUR-JPY	7 days to 1 month	5,500,000.00	2,750,000.00
EUR-JPY	1 month to 3 months	4,500,000.00	2,250,000.00
EUR-JPY	3 months to 6 months	6,000,000.00	3,000,000.00
EUR-NOK	4 days to 7 days	5,000,000.00	2,500,000.00
EUR-NOK	7 days to 1 month	6,500,000.00	3,250,000.00
EUR-NOK	1 month to 3 months	1,000,000.00	500,000.00
EUR-PLN	7 days to 1 month	7,000,000.00	3,500,000.00
EUR-PLN	1 month to 3 months	2,500,000.00	1,250,000.00
EUR-RUB	1 day to 4 days	15,000,000.00	7,500,000.00
EUR-RUB	4 days to 7 days	15,000,000.00	7,500,000.00
EUR-RUB	7 days to 1 month	7,000,000.00	3,500,000.00
EUR-RUB	1 month to 3 months	3,000,000.00	1,500,000.00
EUR-SEK	1 day to 4 days	50,000,000.00	25,000,000.00
EUR-SEK	4 days to 7 days	5,000,000.00	2,500,000.00
EUR-SEK	7 days to 1 month	5,500,000.00	2,750,000.00
EUR-SEK	1 month to 3 months	4,000,000.00	2,000,000.00
EUR-SEK	3 months to 6 months	4,000,000.00	2,000,000.00
EUR-SEK	6 months to 1 year	3,000,000.00	1,500,000.00
EUR-USD	1 day to 4 days	10,000,000.00	5,000,000.00
EUR-USD	4 days to 7 days	10,000,000.00	5,000,000.00
EUR-USD	7 days to 1 month	6,500,000.00	3,250,000.00
EUR-USD	1 month to 3 months	7,500,000.00	3,750,000.00
EUR-USD	3 months to 6 months	4,500,000.00	2,250,000.00
EUR-USD	6 months to 1 year	3,000,000.00	1,500,000.00
EUR-USD	1 year to 2 years	5,000,000.00	2,500,000.00
EUR-USD	2 years to 3 years	20,000,000.00	10,000,000.00
GBP-USD	1 day to 4 days	7,000,000.00	3,500,000.00
GBP-USD	4 days to 7 days	6,000,000.00	3,000,000.00
GBP-USD	7 days to 1 month	15,000,000.00	7,500,000.00
GBP-USD	1 month to 3 months	15,000,000.00	7,500,000.00
GBP-USD	3 months to 6 months	75,000,000.00	37,500,000.00
GBP-USD	6 months to 1 year	20,000,000.00	10,000,000.00
INR-USD	7 days to 1 month	1,000,000.00	500,000.00
INR-USD	1 month to 3 months	1,000,000.00	500,000.00
JPY-USD	1 day to 4 days	10,000,000.00	5,000,000.00
JPY-USD	4 days to 7 days	7,500,000.00	3,750,000.00
JPY-USD	7 days to 1 month	10,000,000.00	5,000,000.00
JPY-USD	1 month to 3 months	7,000,000.00	3,500,000.00
JPY-USD	3 months to 6 months	3,500,000.00	1,750,000.00
JPY-USD	6 months to 1 year	75,000,000.00	37,500,000.00
JPY-USD	1 year to 2 years	85,000,000.00	42,500,000.00
NOK-SEK	7 days to 1 month	10,000,000.00	5,000,000.00
NOK-SEK	1 month to 3 months	6,500,000.00	3,250,000.00
NOK-USD	7 days to 1 month	15,000,000.00	7,500,000.00
NOK-USD	1 month to 3 months	5,500,000.00	2,750,000.00
SEK-USD	1 day to 4 days	7,500,000.00	3,750,000.00
SEK-USD	4 days to 7 days	5,500,000.00	2,750,000.00
SEK-USD	7 days to 1 month	8,500,000.00	4,250,000.00
SEK-USD	1 month to 3 months	6,500,000.00	3,250,000.00
SEK-USD	3 months to 6 months	9,500,000.00	4,750,000.00
SEK-USD	6 months to 1 year	6,000,000.00	3,000,000.00

NDF

We have used the same approach in Figure 7 as that used in Figure 6. Those currency pairs usually traded as non-deliverable are highlighted in grey. For ease we have also highlighted in blue those precious metal crosses (see comment above) which have also been included within the FX data. As mentioned in the paragraph above, it is very easy to see that the ESMA analysis includes instruments in non-deliverable currencies that are very rarely traded as deliverables, and that a large proportion of instruments that typically are not deemed liquid (e.g., non-USD crosses) in the normal course of trading have been categorized as liquid by ESMA. This is further demonstrated in the GFXD proposal at the end of our response to question 1.

We also strongly suggest that accurate data collected over a longer period than 3 months should be used to ensure a range of market events are captured within any calculations. However, the GFXD is aware that in our proposal below we have used data from a single month, October 2014, noting that this is more of a necessity to ensure the short consultation deadlines were met and we hope that ESMA will conduct a fuller analysis taking into consideration the issues we are raising.

For instance, the March-May2014 period used in this analysis contained specific CNY activity due to PBoC policy intervention as reported by Standard Chartered in the following research note, which may not be representative when considered over a longer period (https://research.standardchartered.com/configuration/ROW%20Documents/PBoC_delivers_a_decisive_band_widening_16_03_14_13_14.pdf).

We believe that the data should be collated once EMIR trade reporting is considered accurate and representative of actual trading patterns, including the correct mapping of FX instruments as traded by the market.

ESMA Approach – Data Quality Concerns

We have discussed above our initial observations concerning the quality of the data used by ESMA in its analysis in this CP. We believe it would be beneficial to expand on some of these themes.

Trade Reporting mismatches: EMIR trade reporting, unlike that in some other jurisdictions, is 2-sided in nature, meaning that both parties to a trade are required to report to a trade repository (TR). For FX, there are at least 6 trade repositories that have been registered in the EU, with the GFXD members all reporting to DTCC. The dual sided nature of reporting creates the need for both parties to validate that their submission matches that of their counterparty and this is usually performed via exception (or 'mismatching') reporting. During the first 3 months of data submissions (i.e., the extract used by ESMA in this CP), the ability for either party to check their submission for accuracy intra TR, or even inter TRs, did not exist due to the absence of any exception reporting. Even now, some 14 months since the go-live of EMIR trade reporting obligations, the availability of exception reporting is limited. ESMA therefore used mismatched trade data in their assessment of trading activity in Europe, impacting their assessment of notionals, financial instruments and volumes traded.

Trading period: Table 1 on page 17 of the CP illustrates a high-level assessment showing which FX product types are liquid. Footnote 5 on page 17 clearly states that the number of trading days for the period of data chosen for analysis was 65. However, Table 1 states that the number of trading days for each of the product types was above 65, and for NDFs was actually 92. We believe that the number of days traded should not exceed 100% which suggests that yet more of the data submitted to the TR was not representative. The number of days traded is a specific factor in the determination of liquidity, in that in order for a class of derivatives to be liquid, one of the categories assessed is the "number of days traded

greater than or equal to 80% of the available trading days in the period". We believe this is a further example impacting ESMA's ability to make an accurate liquidity assessment.

ESMA Approach – LIS/SSTI

We also believe that the relevant LIS/SSTI thresholds need to be set at a level appropriate to the liquidity (or illiquidity) of an instrument, and whilst our preference would be that ESMA make an accurate determination of liquidity, failing that we agree that ESMA can compensate to a degree through lower LIS and SSTI. It concerns us therefore that ESMA does not in practice make this compensation even though this is noted as a possibility. Furthermore, the proposed 50% SSTI/LIS ratio is arbitrary and we are concerned that it assumes a linear relationship between SSTI and LIS.

We propose two alternative solutions that would achieve a more appropriate SSTI (that would also compensate for an incorrect liquidity determination), a topic discussed in more details in our response to Question 2:

- SSTI be calibrated as the median trade size for trades below the LIS threshold in a given class; or
- A lower SSTI/LIS ratio of 10% should be used.

ESMA Approach – Ability to Re-calibrate

As referenced in the AFME and ISDA responses to the December 2014 MiFID CP, the GFXD shares the same concerns in that ESMA does not propose to recalibrate the liquidity assessment at all. In the May 2014 DP, ESMA stated (on page 125, paragraph 44) that "the liquidity of the sub-categories needs to be re-assessed periodically". Instead, it is now clear that ESMA proposes no such re-assessment. This decision also implies that ESMA has chosen not to utilise the market data that MiFIR (or EMIR) will make available to facilitate recalibration, which is an incomprehensible waste of the opportunity to refine the liquidity classification over time (particularly given the concerns over the EMIR trade repository data noted above).

This static determination is a serious weakness of ESMA's approach which implies that an incorrect initial assessment of liquidity will have permanent implications. We encourage ESMA to reconsider whether the COFIA can be recalibrated more regularly, as improved market data becomes available and to better reflect changing liquidity conditions. In the absence of regular and accurate recalibration, we urge ESMA to compensate through both a more conservative initial assessment of liquidity, and by calibrating the LIS and SSTI thresholds at lower levels. Finally, such a static approach will not leverage developments within the trade reporting requirements, most notably those being driven by ESMA as well as global standardisation through the use of the UPI.

GFXD Liquidity Proposal

The GFXD believes that due to the policy objectives of ensuring transparency at the aggregate level of the FX derivatives asset class, ESMA should not attempt to find at least some liquid sub-classes in as many classes of FX derivatives as possible. Some classes are simply very illiquid or extremely heterogeneous. For instance, the GFXD regards simple and complex exotic options as being illiquid, yet due to the current product mapping in the EMIR trade reporting data these would be deemed liquid.

We therefore propose the following alternative approach.

Data Source: As we have demonstrated above, we believe that the Bank of International Settlements (BIS) Triennial Central Bank Survey of Foreign Exchange turnover (http://www.bis.org/publ/rpfx13fx.pdf), and the Bank of England (BoE) semi-annual FX surveys (http://www.bankofengland.co.uk/markets/Pages/forex/fxjsc/default.aspx) accurately reflects the FX trading landscape in Europe. Both provide a level of granularity which enables the markets to be assessed to enable a practicable application by regulators and market participants alike as well as meeting policy objectives.

- Whilst the BoE survey captures the UK market only, it is important to understand that this represents 70% of the FX market in Europe (by notional traded) and is considered representative across Europe. Both data sources have been used over a number of years (BoE since 2008, for instance), with the data collection models being refined over time. These surveys are considered accurate by the FX industry, including central banks and ESMA (BIS was used by ESMA in the 2014 CP on FX NDF Clearing). This is obviously contrary to the EMIR trade repository data available to ESMA, which as we have discussed above is not considered in its current state to be representative of the European FX industry. We suggest that ESMA considers that EMIR trade reporting data contains data reflecting the post execution status, including allocations etc which may distort several of the parameters used to measure liquidity (e.g., number of transactions). From 2018 onwards, a better approach may be to use a combination of data sources (e.g., Central Bank data) to obtain a truer reflection of what is actually executed.

Results: Using the BoE October 2014 data, currency pairs and tenors were identified and agreed by GFXD members as being 'usually' liquid in the market (noting that this assessment was performed independently with the results then being applied to the BoE data) and have been highlighted blue in the following tables.

Each cell shows the notional reported in the survey in USD millions equivalent and is a direct extract from http://www.bankofengland.co.uk/markets/Pages/forex/fxjsc/default.aspx 'Results of the Semi-Annual FX Turnover Surveys, 2014 Results, October'.

We also noted that there was a considerable concentration of activity at the 3 month tenor. However, the BoE data only reports the 1-6 month tenor. Anecdotal feedback from the trading desks of GFXD members suggests that the liquidity of the 1-6 month tenor is actually concentrated within the 1-3 month range. As such, we have split the original 1-6 month tenor into a 1-3 month and 3-6 month tenors and have applied an 80/20 split to the 1-6 month tenor in-order to populate.

Figure 8: Liquid and illiquid FX deliverable forwards

3a. OUTRIGHT FORWARDS, Total Monthly Volume by Maturity Liquid

Millions of U.S. Dollars

1-6mth data split 80/20 between the 2 date ranges

	Maturity						
Currency Pair	**Less than 1 week**	**1 week to 1 month**	**1 month to 3 months**	**3 months to 6 months**	**6 months to 1 year**	**Over 1 year**	**Total**
U.S. DOLLAR versus							
Euro	894,772	309,274	336,540	84,135	25,366	17,489	
British pound	242,048	104,422	140,557	35,139	6,418	3,984	
Japanese yen	1,009,417	159,277	146,894	36,724	7,297	9,800	
Swiss franc	89,314	33,322	29,033	7,258	3,212	1,515	
Australian dollar	172,834	79,518	69,803	17,451	1,567	1,477	
Canadian dollar	86,569	35,022	41,462	10,366	1,424	5,119	
Norwegian krone	12,094	6,926	10,907	2,727	277	155	
Swedish krona	9,479	8,719	12,738	3,184	217	190	
New Zealand dollar	55,284	24,381	21,826	5,456	526	378	
South African rand	22,806	22,008	15,641	3,910	674	474	
Mexican peso	28,559	19,366	20,146	5,036	301	209	
Polish zloty	8,218	5,057	6,692	1,673	254	244	
Singapore dollar	29,683	17,409	15,844	3,961	492	1,733	
Russian ruble	31,420	5,011	10,616	2,654	1,992	923	
Turkish lira	23,686	24,590	24,762	6,191	488	296	
Brazilian real	7,701	2,343	2,950	737	11	160	
South Korean won	7,491	4,244	8,708	2,177	1,049	579	
Chinese yuan	19,011	14,186	24,382	6,095	5,283	4,526	
Indian rupee	6,071	7,753	14,901	3,725	1,121	811	
All other currencies	73,004	50,880	68,766	17,192	5,672	7,581	
EURO versus							
British pound	85,491	32,767	53,294	13,324	4,160	4,570	
Japanese yen	37,471	45,317	32,710	8,178	423	949	
Swiss franc	26,642	14,026	21,854	5,463	950	607	
Swedish krona	11,841	9,274	8,211	2,053	343	558	
Norwegian krone	14,043	14,730	12,985	3,246	104	116	
Polish zloty	4,788	4,563	7,042	1,760	443	242	
Canadian dollar	22,404	5,379	4,241	1,060	182	727	
Australian dollar	13,624	9,588	9,060	2,265	460	444	
All other currencies	25,957	18,490	17,419	4,355	3,491	1,334	
STERLING versus							
Japanese yen	14,546	80,581	9,187	2,297	670	326	
Swiss franc	6,636	1,997	3,273	818	285	249	
Australian dollar	10,487	2,897	3,296	824	303	418	
Canadian dollar	7,050	1,399	2,718	679	259	79	
All other currencies	13,069	4,353	6,011	1,503	1,237	900	
ALL OTHER CURRENCY PAIRS	62,264	33,365	24,602	6,151	1,568	1,144	
Total[a]	**3,185,774**	**1,212,434**	**1,239,070**	**309,768**	**78,519**	**70,306**	**6,095,871**
Blue total	**2,873,749**	**903,881**	**850,294**	**212,574**	**25,366**	**0**	**4,865,864**
%	**90.21%**	**74.55%**	**68.62%**	**68.62%**	**32.31%**	**0.00%**	**79.82%**

Figure 9: Liquid and Illiquid FX swaps

3b. FOREIGN EXCHANGE SWAPS, Total Monthly Volume by Maturity
Millions of U.S. Dollars

Liquid

1-6mth data split 80/20 between the 2 date ranges

Currency Pair	Maturity: Less than 1 week	1 week to 1 month	1 month to 3 months	3 months to 6 months	6 months to 1 year	Over 1 year	Total
U.S. DOLLAR versus							
Euro	6,826,644	1,017,434	1,163,500	290,875	131,273	94,240	
British pound	2,920,544	359,302	547,576	136,894	44,263	19,705	
Japanese yen	2,191,904	347,740	389,989	97,497	52,989	65,666	
Swiss franc	1,656,016	163,072	197,662	49,416	27,200	11,279	
Australian dollar	1,284,479	129,916	161,604	40,401	9,674	9,704	
Canadian dollar	619,833	71,626	103,958	25,989	8,508	13,248	
Norwegian krone	350,297	31,172	32,134	8,034	3,885	4,166	
Swedish krona	393,097	36,646	37,808	9,452	4,750	3,752	
New Zealand dollar	367,418	40,842	30,611	7,653	1,749	3,824	
South African rand	245,728	28,848	44,137	11,034	4,549	2,800	
Mexican peso	189,880	29,702	32,026	8,007	2,757	1,013	
Polish zloty	218,544	19,178	29,226	7,306	2,163	1,358	
Singapore dollar	211,555	29,416	24,322	6,081	4,311	3,630	
Russian ruble	177,241	20,760	26,784	6,696	7,725	6,839	
Turkish lira	384,583	64,792	64,575	16,144	5,255	2,817	
Brazilian real	488	1,415	2,648	662	0	0	
South Korean won	450	391	1,687	422	150	330	
Chinese yuan	114,499	20,731	21,934	5,484	10,446	20,035	
Indian rupee	1,966	1,644	2,049	512	148	1,197	
All other currencies	946,214	100,978	95,326	23,832	17,794	28,610	
EURO versus							
British pound	248,425	81,696	139,954	34,989	5,620	7,583	
Japanese yen	66,145	30,138	31,946	7,987	2,693	365	
Swiss franc	150,915	50,170	53,217	13,304	2,943	1,628	
Swedish krona	19,822	8,344	10,746	2,687	420	1,277	
Norwegian krone	12,735	5,468	9,362	2,341	562	160	
Polish zloty	10,690	10,520	11,386	2,846	214	883	
Canadian dollar	16,119	5,760	6,499	1,625	620	445	
Australian dollar	24,737	12,743	9,760	2,440	223	785	
All other currencies	97,177	36,064	38,214	9,553	3,420	2,810	
STERLING versus							
Japanese yen	37,951	6,397	13,798	3,449	476	69	
Swiss franc	24,884	4,306	12,713	3,178	1,255	111	
Australian dollar	9,733	4,728	3,769	942	9	20	
Canadian dollar	8,476	3,204	3,802	950	193	24	
All other currencies	10,284	7,383	10,902	2,726	473	481	
ALL OTHER CURRENCY PAIRS	245,357	17,890	23,179	5,795	1,494	694	
Total[a]	**20,084,830**	**2,800,416**	**3,388,805**	**847,201**	**360,204**	**311,548**	**27,793,004**
Blue total	**18,511,014**	**2,356,728**	**2,789,406**	**697,352**	**228,525**	**0**	**24,583,025**
%	**92.16%**	**84.16%**	**65.85%**	**16.46%**	**63.44%**	**0.00%**	**88.45%**

Liquid and illiquid FX options

GFXD members believe that as the FX options market is heterogeneous in nature, a dynamic liquidity calibration should be employed, and we note that ISDA recommended a similar approach in their submission to the December 2014 CP. This is reflected in our recommended asset classification under Annex 3.6.1 in the May 2014 DP, as well as being included above in Figure 1.

It is considered that the FX simple and complex exotic options are heterogeneous, illiquid in nature and represent approximately 15% of the total FX options market, itself believed to be approximately 6-8% of the overall FX market (including FX spot) or 13% if FX spot is excluded. With this in mind, we present 2 alternatives:

- Figure 10a uses the BoE options data as a whole, not distinguishing between simple and complex exotics and the rest of the FX options market (i.e., vanilla and NDO).

- Figure 10b, we have applied a consistent 85% ratio to include the FX vanilla options and NDO only (thus excluding simple and complex exotics).

Figure 10a: All options (FX vanilla options, NDO, simple and complex exotics)

3d. FOREIGN EXCHANGE OPTIONS, Total Monthly Volume by Maturity Liquid

Millions of U.S. Dollars

1-6mth data split 80/20 between the 2 date ranges

	Maturity						
Currency Pair	**Less than 1 week**	**1 week to 1 month**	**1 month to 3 months**	**3 months to 6 months**	**6 months to 1 year**	**Over 1 year**	**Total**
U.S. DOLLAR versus							
Euro	311,056	503,602	579,388	144,847	115,650	72,365	
British pound	39,953	74,570	79,516	19,879	19,425	6,899	
Japanese yen	118,675	277,057	442,018	110,504	80,965	122,783	
Swiss franc	22,543	25,736	60,282	15,071	27,225	22,896	
Australian dollar	34,740	54,293	86,535	21,634	18,033	7,159	
Canadian dollar	15,440	34,454	38,886	9,722	10,829	1,833	
Norwegian krone	1,703	2,423	4,240	1,060	752	196	
Swedish krona	637	1,964	3,456	864	717	89	
New Zealand dollar	13,344	17,212	21,918	5,480	6,486	2,902	
South African rand	3,520	6,802	9,077	2,269	2,238	2,463	
Mexican peso	2,466	8,632	12,606	3,151	1,144	2,517	
Polish zloty	208	483	1,965	491	704	168	
Singapore dollar	2,067	3,255	16,647	4,162	1,401	736	
Russian ruble	3,001	7,490	14,838	3,710	11,321	4,033	
Turkish lira	9,218	15,656	15,943	3,986	3,781	1,163	
Brazilian real	4,180	28,959	78,808	19,702	7,388	11,209	
South Korean won	4,618	11,945	10,071	2,518	2,394	1,063	
Chinese yuan	3,530	14,426	39,686	9,922	12,403	12,184	
Indian rupee	1,195	10,179	12,439	3,110	2,538	1,173	
All other currencies	14,287	43,551	74,758	18,690	37,964	23,123	
EURO versus							
British pound	20,043	36,006	65,922	16,481	20,635	4,110	
Japanese yen	10,642	13,140	30,186	7,547	5,767	4,209	
Swiss franc	4,454	23,589	112,511	28,128	17,082	2,316	
Swedish krona	6,161	5,907	6,059	1,515	2,410	584	
Norwegian krone	4,794	9,834	13,326	3,332	2,188	942	
Polish zloty	1,374	3,932	5,125	1,281	1,489	435	
Canadian dollar	1,219	1,171	5,159	1,290	793	244	
Australian dollar	1,894	4,717	8,648	2,162	866	1,182	
All other currencies	6,454	9,846	20,486	5,122	8,639	6,197	
STERLING versus							
Japanese yen	1,462	2,801	6,762	1,690	1,400	175	
Swiss franc	374	967	7,582	1,895	3,152	2,303	
Australian dollar	483	1,233	2,071	518	272	122	
Canadian dollar	41	581	839	210	727	323	
All other currencies	1,139	2,094	4,999	1,250	1,656	444	
ALL OTHER CURRENCY PAIRS	11,149	26,193	47,208	11,802	14,665	8,766	
Total[a]	**678,064**	**1,284,700**	**1,939,964**	**484,991**	**445,099**	**329,306**	**5,162,124**
Blue total	**429,731**	**1,099,575**	**1,586,120**	**255,351**	**196,615**	**0**	**3,567,392**
%	**63.38%**	**85.59%**	**81.76%**	**52.65%**	**44.17%**	**0.00%**	**69.11%**

Figure 10b: Data for FX vanilla options and NDO only (85% of the data in Figure 10a)

3d. FOREIGN EXCHANGE OPTIONS, Total Monthly Volume by Maturity (Vanilla/NDO only) Liquid

Millions of U.S. Dollars

1-6mth data split 80/20 between the 2 date ranges

Currency Pair	Maturity: Less than 1 week	1 week to 1 month	1 month to 3 months	3 months to 6 months	6 months to 1 year	Over 1 year	Total
U.S. DOLLAR versus							
Euro	264,398	428,062	492,480	123,120	98,303	61,510	
British pound	33,960	63,385	67,589	16,897	16,511	5,864	
Japanese yen	100,874	235,498	375,715	93,929	68,820	104,366	
Swiss franc	19,162	21,876	51,240	12,810	23,141	19,462	
Australian dollar	29,529	46,149	73,555	18,389	15,328	6,085	
Canadian dollar	13,124	29,286	33,053	8,263	9,205	1,558	
Norwegian krone	1,448	2,060	3,604	901	639	167	
Swedish krona	541	1,669	2,938	734	609	76	
New Zealand dollar	11,342	14,630	18,631	4,658	5,513	2,467	
South African rand	2,992	5,782	7,715	1,929	1,902	2,094	
Mexican peso	2,096	7,337	10,715	2,679	972	2,139	
Polish zloty	177	411	1,670	418	598	143	
Singapore dollar	1,757	2,767	14,150	3,538	1,191	626	
Russian ruble	2,551	6,367	12,613	3,153	9,623	3,428	
Turkish lira	7,835	13,308	13,552	3,388	3,214	989	
Brazilian real	3,553	24,615	66,987	16,747	6,280	9,528	
South Korean won	3,925	10,153	8,561	2,140	2,035	904	
Chinese yuan	3,001	12,262	33,733	8,433	10,543	10,356	
Indian rupee	1,016	8,652	10,573	2,643	2,157	997	
All other currencies	12,144	37,018	63,545	15,886	32,269	19,655	
EURO versus							
British pound	17,037	30,605	56,034	14,009	17,540	3,494	
Japanese yen	9,046	11,169	25,658	6,415	4,902	3,578	
Swiss franc	3,786	20,051	95,635	23,909	14,520	1,969	
Swedish krona	5,237	5,021	5,150	1,288	2,049	496	
Norwegian krone	4,075	8,359	11,327	2,832	1,860	801	
Polish zloty	1,168	3,342	4,356	1,089	1,266	370	
Canadian dollar	1,036	995	4,385	1,096	674	207	
Australian dollar	1,610	4,009	7,351	1,838	736	1,005	
All other currencies	5,486	8,369	17,413	4,353	7,343	5,267	
STERLING versus							
Japanese yen	1,243	2,381	5,747	1,437	1,190	149	
Swiss franc	318	822	6,444	1,611	2,679	1,958	
Australian dollar	411	1,048	1,761	440	231	104	
Canadian dollar	35	494	713	178	618	275	
All other currencies	968	1,780	4,249	1,062	1,408	377	
ALL OTHER CURRENCY PAIRS	9,477	22,264	40,127	10,032	12,465	7,451	
Total[a]	**576,354**	**1,091,995**	**1,648,969**	**412,242**	**378,334**	**279,910**	**4,387,805**
Blue total	**365,271**	**934,639**	**1,348,202**	**217,049**	**167,123**	**0**	**3,032,284**
%	**63.38%**	**85.59%**	**81.76%**	**52.65%**	**44.17%**	**0.00%**	**69.11%**

NDF

As demonstrated above in Figure 4 (Extract and Representation of the BoE October 2014 Semi-Annual FX survey), the NDF market in Europe is approximately 4% of the total FX market. We do not believe that the NDF market has sufficient volume to be considered liquid and recommend that, like simple and complex exotic options, that NDF are deemed illiquid. However, we are aware that there may be incentives to include the FX NDF market within the liquid categories of FX instruments. Whilst we oppose this, noting that there are differing liquidity approaches for mandatory clearing obligations and the mandatory trading obligations which may ultimately include some FX NDFs, our members anecdotally consider that the 1 week to 1 month tenors of USDBRL, USDKRW and USDCNY FX NDFs would be more liquid than other NDF crosses/tenors. Due to the parameters reported in the BIS and BoE data subsets it is difficult for us to sensibly size the markets in these NDF currency pairs.

Spread-betting

We do not consider this to be a FX instrument under MiFID C4. ESMA admit so in the CP, notably in footnote 25 on page 210, which states “this code is not provided for by the legislation”. As such we have not performed any analysis and do not agree that this ‘bucket’ should be included within this FX section.

Instead, ESMA should either (i) remove this spread betting category and associated definition, and instead appropriately categorize the underlying instruments according to the nature of those instrument, and provide suitable definitions that permit straightforward identification of product type without creating overlapping classes, or (ii) define an 'Others' asset class, to be determined illiquid in its entirety due to the non-homogenous nature of this product set.

Summary

We believe the above proposal achieves the policy objectives in deeming a significant percentage of the European FX market liquid. Our calculations show that using October 2014 Bank of England (BoE) semi-annual FX survey that **79% of the European FX market would be deemed liquid** (calculations illustrated in Figure 11 below)

Figure 11: GFXD summary calculation determining the % of the European Market deemed liquid as per the October 2104 Bank of England semi-annual FX survey

	BoE Oct14	GFXD Liquidity Analysis (% of BoE Oct14)	GFXD Adjusted BoE Oct2014
FX Forwards	15%	80%	12%
FX Swaps	67%	88%	59%
FX Options (NDO & Vanilla only)	11%	69%	8%
Total*	93%		79%

*Remaining 7% NDF, Exotic options and Currency swaps

<ESMA_QUESTION_MIFID_ADD_1>

Q2. Do you agree with ESMA's proposal for foreign exchange derivatives? Please specify, for each sub-class (non-deliverable forwards (NDF), deliverable forwards (DF), FX options, FX swaps, spread betting and FX futures) if you agree on the following points providing reasons for your answer and, if you disagree providing ESMA with your alternative proposal:

(1) deferral period set to 48 hours

(2) size specific to the instrument threshold set as 50% of the large in scale threshold

(3) volume measure used to set the large in scale and size specific to the instrument threshold as specified in Annex II, Table 3 of draft RTS 9

(4) pre-trade and post-trade thresholds set at the same size

(5) large in scale thresholds: (a) state your preference for the system to set the thresholds (i.e. annual recalculation of the thresholds vs. no recalculation of the thresholds) (b) in the case of a preference for a system with no recalculation (i.e. option 1), provide feedback on the thresholds determined. In the case of a prefer-

ence for a system with recalculation (i.e. option 2), provide feedback on the thresholds determined for 2017 and on the methodology to recalculate the thresholds from 2018 onwards including the level of granularity of the classes on which the recalculations will be performed

(6) <u>for non-deliverable forwards (NDF) and spread betting contracts only:</u> express your preference for either "Alternative A" or "Alternative B". If you disagree with both ESMA's proposal provides your alternative proposal for the LIS threshold floor.

<ESMA_QUESTION_MIFID_ADD_2>
Q2. Do you agree with ESMA's proposal for foreign exchange derivatives?

For FX non-deliverable forwards (NDF), FX forwards, FX options and FX swaps, the GFXD does not agree with ESMA's proposals, each of which is discussed in more detail below.

(1) deferral period set to 48 hours

The GFXD does not support the 48 hour deferral and would like to reference the responses made by ISDA and AFME to question 78 of the December 2014 Consultation Paper (CP) - whilst we welcome ESMA's proposal to extend the length of the deferral period for transactions that are equal to or exceed LIS, equal to or exceed SSTI (if carried out on own account other than matched principal) and in illiquid instruments, we recommend that the deferral period be set at two business days. This is to ensure that transactions that occur close to the end of trading before a weekend/bank holiday get the full benefit of the deferral period (which they may otherwise not if the 48 hour period runs over the weekend).

As ISDA argued in their response to the May 2014 DP and responded accordingly in the December 2014 CP, the duration of volume masking is critical. If ESMA does not accept ISDA's proposal in response to Question 83 of the December 2014 CP (that a 12 week supplementary deferral period is required for volume omission in respect of trades which are both Illiquid and LIS) then we would urge ESMA to extend the post-trade deferral period to at least 7 days for trades that are both illiquid and LIS.

We believe that even two business days may provide challenges for certain types and sizes of transactions and especially so if the LIS and SSTI thresholds are not appropriately calibrated in the final rules. This challenge will be significantly worsened if NCAs do not implement the supplemental volume omission regime. Whilst we appreciate that it is within the discretion of individual NCAs to determine whether to implement a supplemental volume omission deferral regime, the GFXD urges ESMA to try and encourage as many NCAs as possible to adopt this regime.

(2) size specific to the instrument threshold set as 50% of the large in scale threshold

<u>Size specific at 50%</u>

We do not support the proposal that the SSTI threshold is set as 50% of the large in scale threshold and would like to reference the responses made by ISDA and AFME to question 78 of the December 2014 CP.

We believe that the proposal to set the SSTI threshold at 50% of the LIS threshold is arbitrary – there is no rationale for choosing 50% (as opposed to another percentage) and its link to the LIS threshold means

that the SSTI threshold is unlikely to result in 50% of trades in a sub-class actually falling below the SSTI threshold. The use of a 50% ratio does not appear to have factored in the elements required by MiFIR under Article 9(5)(d), specifically whether liquidity providers are able to hedge their risks, and the extent of retail participation (although we recognize the practical challenges of incorporating these factors).

Furthermore, as ESMA seems to view the waiver and deferral regimes as a way to reduce the detrimental impact of an illiquid instrument being incorrectly assessed as liquid, we urge ESMA to ensure that the LIS and SSTI thresholds are set at levels sufficiently low in order to compensate for inaccuracies in the liquidity calibration. We also note that in the US, the CFTC has adopted policy-based approach to calculate block sizes, but for FX is currently applying Initial Block Sizes (CFTC 17 CFR Part 43) until accurate data can be collated and assessed.

We propose instead that the SSTI threshold should either be set at either:

- The median trade size (50th percentile of transaction sizes) for transactions below LIS in the relevant sub-class; or
- 10% of the LIS threshold for the relevant sub-class (if ESMA prefers to retain a method based on the percentage of LIS)

The appeal of using the median size is that ESMA can be sure that half of transactions in any liquid sub-class would be subject to pre-trade transparency, and would not experience deferred publication. We consider it would accord better with a normal market transaction at which liquidity providers could be reasonably expected to hedge their risks (as per MiFIR Article 9(5)(d)). Furthermore, breaking the link to LIS would prevent the SSTI being skewed by individual, large transactions (which could result under ESMA's current proposal for LIS calibration).

For the following reasons, we urge ESMA adopt our recommendations for the pre-trade SSTI (although we encourage ESMA to also consider doing so for the post-trade SSTI):

- The risks to firms are more significant in the pre-trade context: a firm is putting its capital at risk and pre-trade disclosure of its quoted prices increases the possibility that the market will move against the firm before it is able to execute those transactions. This would lead firms to price in these risks resulting in worse pricing for end investors

- A 50% SSTI ratio would only permit an SI to undertake two trades before taking on risk equivalent to a Large in Scale transaction. If the policy objective is to encourage SIs to make their quotes available and executable to several clients then setting the SSTI threshold at a level which takes into account multiple transactions and still being able to maintain a given quote would enable ESMA to achieve such an objective

The risk is of a different nature in the post-trade context. At this stage, the firm has already committed its capital. The risk it faces at this stage relate to the management of its exposure (i.e., its ability to conduct a successful hedging strategy). However, again, if the ratio is set too high for post-trade purposes, the risks the systematic internaliser faces in managing its hedging strategy in relation to certain products will be reflected in wider prices being quoted to clients.

(3) volume measure used to set the large in scale and size specific to the instrument threshold as specified in Annex II, Table 3 of draft RTS 9

The GFXD agrees that FX trade notional is the correct measure.

(4) pre-trade and post-trade thresholds set at the same size

The GFXD supports the responses made by ISDA and AFME to this equivalent question in the December 2014 CP. We believe that there should be a different SSTI for pre-trade transparency and post trade transparency because:

- The risk associated with the post trade threshold is the time permitted for the market maker to unwind and hedge risk. The pre-trade risks to the market maker are much greater than the post trade risks because the price formation process can be interfered with:
    - Other dealers could price against the market maker with regards and result in a race to the bottom in pricing that does not reflect market risk. Further, the disclosure of prices pre-trade could result in predatory pricing practices; and
    - Other dealers could take contrarian positions against the market maker prior to execution, increasing the cost of hedging or unwinding of the market maker's risk.

  Therefore, we believe that the pre-trade SSTI should differ from post trade SSTI and that the levels should be much lower. We do not believe that introducing different thresholds for pre-trade and post-trade would make the regime too operationally complex

- For post-trade transparency, if the SSTI is set too high (further exacerbated for illiquid instruments that are incorrectly classified as liquid), the larger trades will be subject to real time transparency (without NCA discretion for deferral) and market makers will be unable hedge and unwind their positions. This will ultimately discourage market makers from committing capital to facilitate trades, resulting in less depth of liquidity and wider spreads, at the expense of investors

(5) large in scale thresholds

Data quality issues:

As per our response to the May 2014 DP, we believe that there should be globally harmonised approaches in calculating LIS or block sizes, especially relevant in FX due to the global nature of the market, with at least 75% of the market being traded by market participants across 5 key jurisdictions.

In order to simplify the implementation of a LIS number, we propose that ESMA should look to bucket, per sub-product (e.g., FX forward) as follows:

- Tenor bucket: less than 1 week; 1 week to 3 months; 3 months to 1 year; over 1 year

- CCY buckets: super major (USDEUR, USDJPY, GBPUSD); major (USDCHF, AUDUSD, USDCAD, NZDUSD,GBPEUR, EURJPY); sub-major (USDNOK, USDSEK, USDZAR, USDMXN, USDSGD, USDTRY, USDCNY, EURCHF, EURNOK, GBPJPY)

Having examined the data in the CP we have noticed 2 trends in the LIS data which we believe are not representative of the FX markets. We suggest that the LIS calculations as they are published are not accurate and should be recalibrated at the earliest instance using accurate and representative data.

LIS absolute values: There are multiple examples where the LIS number is not representative of the market traded, again due to the poor quality of the data used in the assessment. For instance, USDCOP

NDFs (4days to 7 days) have a LIS value of EUR 700million and USDCLP (3 months to 6 months) has a LIS value of EUR 175million. Both of these are many multiples greater than the LIS for the most liquid FX currency pairs, such as USDEUR and can be close to or more than the average daily notional amount per day that is stated in the liquidity assessment tables.

LIS comparative values per currency cross: On many of the instruments listed in the FX tables, the value of the LIS increases with tenor. This is contrary to what is seen in the market. Generally liquidity peaks around the 3 month tenor and drops off post that, yet there are many examples showing otherwise, e.g., GBPUSD deliverable forwards as per Table 50 of the CP.

GFXD proposal:

The GFXD supports a dynamic calibration model, re-calibrating both LIS/SSTI using the financial instrument classification (proposed below in Figure 12) at the Annex 3.6.1 level. It is essential that the LIS threshold is appropriately calibrated to ensure that end investors can continue to transact in large trade sizes. Requiring price disclosure of large trades would lead to a widening of bid-offer spreads, which may have a detrimental impact on investors wishing to trade at these large sizes.

As we have previous discussed, we are concerned with the quality of the data used in this CP, especially given the known quality issues with EMIR trade reporting. The GFXD partially supports the dynamic model proposed in Option 2, a policy based approach and we believe that this offers the best compromise given global (US, CFTC) transparency obligations.

For 2018 onwards, we propose the following for FX:

- Pre trade: LIS threshold so that either 50% of the trades would lie below the threshold or 30% of the total volume traded for that sub-class would lie below the threshold

- Post trade: LIS of 65% of the total volume traded for that sub-class would lie below the threshold

- We disagree with ESMA's proposal to include a 'floor' in Option 2. In our view, this goes beyond the Level 1 requirements

The above approach enables the FX market to be policy aligned across jurisdictions and we believe that the dynamic model proposed in Option 2 offers synergy with the CFTC approach where a similar policy based approach is used. However, we would like to clarify that whilst US transparency obligations have been calculated in a similar fashion to the above recommendation, trade data has yet to be analyzed with updated LIS (block) numbers being provided to the market. The FX market is currently reporting based on historical futures data rather than the latest data obtained from the CFTC SDR reporting and as such we are not able to accurately predict the impact on the markets if such an approach is adopted in practice.

We believe that accurate and reflective trade data should be collated and that this should be used to calibrate the LIS number, accommodating the larger risks faced by participants when complying with pre-trade obligations (see previous comments). We believe that use of a floor in 2017 essentially provides flexibility in the near term to compensate for the known inaccuracies of EMIR trade reporting. We also believe that ESMA should correct its proposed rounding method which systematically rounds the LIS and SSTI thresholds higher. Instead, ESMA should adopt simple mathematical rounding to the nearest round

number. In other words, Paragraph 3 of Article 11 of RTS 9 should be amended to "The threshold determined in accordance to paragraph (2) shall be rounded to the next nearest:".

Finally, we believe that thresholds should be applied at Annex 3.6.1 level, included below (with GFXD recommended amendments) in Figure 12.

Figure 12: GFXD proposal for Annex 3.6.1 defining FX instrument categorization under MiFIR

Financial Instrument	Product Types	Sub-Product Types	Recommended Liquidity sub-categories
Foreign Exchange Derivatives	Futures	N/A	Currency Pair Maturity
	Options	Non-Deliverable Option - NDO (only European type options are NDO - not any other FX options settled in non-deliverable currency)	
		Vanilla Option (European and American)	
	Forwards	Deliverable Forward	
		NDF	
	FX Swaps	Deliverable FX Swap	
		Non-Deliverable FX Swap	
	Others	Simple exotic (Barrier & Digital)	
		Complex Exotic	

6) for non-deliverable forwards (NDF) and spread betting contracts only: express your preference for either "Alternative A" or "Alternative B".

The GFXD agrees with Alternative B.

<ESMA_QUESTION_MIFID_ADD_2>

Q3. Which is your preferred option for the definition of a liquid market of single name CDS? Please provide an answer detailed per underlying issuer type identified (sovereign and corporate), addressing the following points:

(1) Would you use different qualitative criteria to define the sub-classes?

(2) **Would you use different parameters or the same parameters (i.e. average number of trades per day and average notional amount traded per day) but different thresholds in order to define a sub-class as liquid?**

(3) **Would you define classes declared as liquid in ESMA's proposal as illiquid (or vice versa)? Please provide reasons for your answer.**

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TYPE YOUR TEXT HERE
<ESMA_QUESTION_MIFID_ADD_3>

Q4. For all the other classes (CDS Index, Bespoke basket CDS, CDS index options and Single name CDS options): do you agree with ESMA's proposal for the definition of a liquid market? Please provide an answer detailed per contract type (CDS and CDS options), underlying type (index, single name, bespoke basket) and underlying identified, addressing the following points:

(1) **Would you use different qualitative criteria to define the sub-classes?**

(2) **Would you use different parameters or the same parameters (i.e. average number of trades per day and average notional amount traded per day) but different thresholds in order to define a sub-class as liquid?**

(3) **Would you define classes declared as liquid in ESMA's proposal as illiquid (or vice versa)? Please provide reasons for your answer.**

<ESMA_QUESTION_MIFID_ADD_4>
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Q5. Do you agree with ESMA's proposal for credit derivatives? Please specify, for each sub-class (single name CDS, CDS index, bespoke basket CDS, single name CDS options, CDS index options) if you agree on the following points providing reasons for your answer and, if you disagree providing ESMA with your alternative proposal:

(1) **deferral period set to 48 hours**

(2) **size specific to the instrument threshold set as 50% of the large in scale threshold**

(3) **volume measure used to set the large in scale and size specific to the instrument threshold as specified in Annex II, Table 3 of draft RTS 9**

(4) **pre-trade and post-trade thresholds set at the same size**

(5) **large in scale thresholds: (a) state your preference for the system to set the thresholds (i.e. annual recalculation of the thresholds vs. no recalculation of the thresholds) (b) in the case of a preference for a system with no recalculation (i.e.**

option 1), provide feedback on the thresholds determined. In the case of a preference for a system with recalculation (i.e. option 2), provide feedback on the thresholds determined for 2017 and on the methodology to recalculate the thresholds from 2018 onwards including the level of granularity of the classes on which the recalculations will be performed.

<ESMA_QUESTION_MIFID_ADD_5>
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Q6. Do you agree with ESMA's proposal for the definition of a liquid market? Please provide an answer detailed per class of derivatives (freight derivatives, emissions derivatives, weather derivatives and other exotic derivatives) and contract type identified (options, futures, forwards, swaps, others). If you do not agree with ESMA's proposal for the definition of a liquid market, please specify per class of derivatives and contract type identified:

- **your alternative proposal;**

(6) which qualitative criteria would you use to define the sub-classes;

(7) which parameters and related threshold values would you use in order to define a sub-class as liquid. Please, provide reasons for your answer.

<ESMA_QUESTION_MIFID_ADD_6>
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Q7. Which is your preferred option? Please express your preference either for "Alternative A" or for "Alternative B". If you disagree with both ESMA's proposals provide your alternative proposal by answering the following question.

<ESMA_QUESTION_MIFID_ADD_7>
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Q8. Please specify, for each class (defined as follows if you have stated your preference for Alternative A: freight derivatives, emissions derivatives, weather derivatives and other exotic derivatives. Defined as combination of underlying type and contract type if you have stated a preference for Alternative B: freight options, freight futures, freight forwards, etc.) if you agree on the following points providing reasons for your answer and, if you disagree, providing ESMA with your alternative proposal:

(1) deferral period set to 48 hours

(2) size specific to the instrument threshold set as 50% of the large in scale threshold

(3) **volume measure used to set the large in scale and size specific to the instrument threshold as specified in Annex II, Table 3 of draft RTS 9**

(4) **pre-trade and post-trade thresholds set at the same size**

(5) **large in scale thresholds: (a) state your preference for the system to set the thresholds (i.e. annual recalculation of the thresholds vs. no recalculation of the thresholds) (b) in the case of a preference for a system with no recalculation (i.e. option 1), provide feedback on the thresholds determined. In the case of a preference for a system with recalculation (i.e. option 2), provide feedback on the thresholds determined for 2017 and on the methodology to recalculate the thresholds from 2018 onwards including the level of granularity of the classes on which the recalculations will be performed.**

<ESMA_QUESTION_MIFID_ADD_8>
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Q9. Do you agree with the approach taken for shares where any CFD based on a liquid share would be considered as having a liquid market? More specifically, please provide feedback on the following:

(1) **Would you prefer to follow a similar approach as that proposed in option 2 on liquidity for equity derivatives (paragraph 90 page 132 of December CP), i.e. qualify all CFDs on equity as liquid irrespectively of the liquidity of the underlying?**

(2) **Would you have used different criteria to define the classes or sub-classes?**

(3) **Would you have used different parameters or the same parameters (i.e. average number of trades per day and average notional amount traded per day) but different thresholds in order to define a sub-class as liquid?**

(4) **Would you support extending the approach taken for shares to other equity (ETFs, depositary receipts and certificates) and equity-like instruments?**

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Q10. Do you agree with ESMA's proposal for the definition of a liquid market for CFDs on currencies? Please provide a feedback on the following in your answer:

(1) **Would you use different qualitative criteria to define the sub-classes?**

(2) **Would you use different parameters or the same parameters (i.e. average number of trades per day and average notional amount traded per day) but different thresholds in order to define a sub-class as liquid?**

(3) **Would you define sub-classes declared as liquid in ESMA's proposal as illiquid (or vice versa)? Please provide reasons for your answer.**

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Q11. Do you agree that CFDs on instruments other than equities and currencies are illiquid? If you do not agree with ESMA's proposal for the definition of a liquid market for those classes, please provide your alternative proposal specifying the following:

2. How would you define the sub-classes, i.e. which qualitative criteria would you use?

(4) **Which parameters and related thresholds would you use to classify a sub-class as liquid?**

(5) **Which sub-classes would you define as liquid?**

<ESMA_QUESTION_MIFID_ADD_11>
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Q12. Do you agree with ESMA's proposal for CFDs? Please specify, for each sub-class (CFDs on equity, CFDs on currency, CFDs on commodity, CFDs on bonds, CFDs on futures on equity and CFDs on options on equity, others) if you agree on the following points providing reasons for your answer and, if you disagree providing ESMA with an alternative proposal regarding:

(1) **deferral period set to 48 hours**

(2) **size specific to the instrument threshold set as 50% of the large in scale threshold**

(3) **volume measure used to set the large in scale and size specific to the instrument threshold as specified in Annex II, Table 3 of draft RTS 9**

(4) **pre-trade and post-trade thresholds set at the same size**

(5) **large in scale thresholds: (a) state your preference for the system to set the thresholds (i.e. annual recalculation of the thresholds vs. no recalculation of the thresholds) (b) in the case of a preference for a system with no recalculation (i.e. option 1), provide feedback on the thresholds determined. In the case of a preference for a system with recalculation (i.e. option 2), provide feedback on the thresholds determined for 2017 and on the methodology to recalculate the thresholds from 2018 onwards including the level of granularity of the classes on which the recalculations will be performed.**

<ESMA_QUESTION_MIFID_ADD_12>

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