



European Securities and Markets Authority
CS 60747
201-203 Rue de Bercy
75021 Paris

29 April 2022

CONSULTATION PAPER ON ESMA'S OPINION ON THE TRADING VENUE PERIMETER

Dear Sir or Madam,

The European Financial Market Lawyers Group (**EFMLG**) is a group of senior legal experts from the EU banking sector dedicated to making analysis and undertaking initiatives intended to foster the harmonization of laws and market practices and facilitate the integration of financial markets in Europe. The members of the Group are selected amongst lawyers of major credit institutions based in the EU active in the European financial markets. The Group is hosted by the Legal Services of the European Central Bank.

The EFMLG is pleased to provide its high-level comments about the ESMA's Opinion on the trading venue perimeter (ESMA's Opinion). Namely, we would like to take this opportunity to focus on specific key issues addressed by the Opinion and to submit to ESMA attention our main concerns.

1. Interaction between trading interests and conclusion of contracts

From ESMA's Opinion we understand that, the mere interaction within a "system" between different trading interests is not only sufficient to consider it as "multilateral" (upon condition that all other three criteria mentioned in the Opinion are fulfilled), but also carries a decisive weight for a multilateral system to be regarded as a trading venue (**TV**). Further, we understand that the conclusion of a contract within the system is not required by ESMA as a pre-condition for a "system" to be regarded as "multilateral", and also does not represent a pre-condition that a firm must mandatorily satisfy to request to be authorized as TV for the system it operates. If our interpretation is correct and ESMA's Opinion indeed considers the element of 'interaction' a very important element and deems the element of 'concluding of contracts' of less importance, then this marks an important departure from the MiFID II regulatory framework currently in force and also from ESMA's interpretive guidance provided by ESMA in the past, which is still valid.

First and foremost, ESMA's Opinion seemingly implies a wide extension of the scope of the definitions of i) "Regulated Markets" ii) "Multilateral Trading Facility" (**MTF**) and iii) "Organized Trading Facility" (**OTF**) provided for by MiFID II and that, on their turn, are included within the definition of "TV" under MiFID II (that is drafted in exclusive and exhaustive terms). These three definitions share a fundamental feature: all envisage, as a key element, the conclusion of a contract and not the mere interaction between trading interests.

Secondly, insofar as ESMA's Opinion broadly stretches the scope of the three-itemized definition of "TV", it seemingly blurs the difference between the definitions of "executing orders", "Multilateral System" and "TV" and risks making the latter less meaningful. Under MiFID II, the three items included in the definition of "TV" are regarded as "Multilateral Systems" and must fulfill specific requirements for being defined as "TVs" including the common requirement that the bringing together or the interaction of multiple third-party buying and selling interests must result in the conclusion of a contract.

As for interpretive guidance¹, ESMA has provided a negative answer as to whether a TV can use its trading systems and platforms to arrange transactions that are then reported and ultimately executed on another TV noticing that the fundamental characteristic of a TV is to execute transactions. Thus, a TV is not allowed to arrange transactions without formalizing the execution of those transactions under its rules and systems. This Q&A seems overridden by ESMA's Opinion since this latter minimizes the relevance of the location where the final terms of a contract are concluded² and does not attach importance to the fact that interaction should be formalized under a pre-defined set of rules of the relevant TV.

2. Multilateral third party concept and the Robeco CJEU Judgement

As per ESMA's Opinion, systems where only two trading interests interact could be considered "in scope" provided that they are brought together under the rules of a third-party operator; according to ESMA, this interpretation is supported by the CJEU Robeco Judgement³.

In this specific respect, we would like to make three remarks. First, we question whether this judgement may provide sound legal basis *per se* since, inter alia, it was adopted in 2017 i.e. before MiFID II came into effect and OTFs were introduced and it dealt with a case of interpretation of MiFID I. Also, it was very fact-specific⁴. Secondly, ESMA's interpretation seems to suggest that this judgement relates to "one-to-one" interactions; however, in our view this judgement concerns "one-to-many" interactions⁵. Thirdly, ESMA's Opinion does not seem in line with currently in force MiFID II rules. Namely, among the conditions for authorization, MTFs and OTFs are required to have at least three materially active members or users, each having the opportunity to interact with all the others in respect to price formation.⁶

3. Difference between multilateral systems, single dealer systems and electronic communication tools.

We believe that multilateral systems must be appropriately distinguished from electronic platforms that are basically communication tools.

As highlighted by the Advocate General of the CJUE in his Opinion on Robeco case (paragraph 88) in respect of the EFS System operated by Euronext, "mere information channels for the transmission of orders" are different from "*systems in which financial instruments ... are traded and its activity is carried out in accordance with the rules established by the system operator (Euronext) in a trading manual.*"

For these purposes, we would welcome further guidance on the definition of "system" and "market operator". As set out in the CP on trading venue perimeter, a system must be understood as a common set of rules⁷ to

¹ Q&A n.7 Paragraph 5 "Multilateral and bilateral system" (Q&As on MiFID II and MiFIR market structures topic).

² An interaction sufficient to trigger the definition of "TV" is regarded by ESMA as existent even when the above-mentioned final terms are concluded outside of the system or facility (Paragraph 20 of ESMA's Opinion).

³ Judgement of the Court (Fourth Chamber) 16 November 2017, Robeco Hollands Bezit NV and Others v Stichting Autoriteit Financiële Markten (AFM).

⁴ Namely, it dealt with a system in which the participants were brokers representing investors and "open end" investment fund agents required to execute orders relating to their funds.

⁵ Paragraph 35 of the Robeco judgement states as follows: "the fact that, in a system (...) there is no trading between the various brokers or between the various investment fund agents is irrelevant so far as, within that system, the agents can conclude transaction with multiple brokers and vice versa".

⁶ Article 18 paragraph 7 MiFID II.

⁷ This interpretation is supported by point 19 of ESMA's consultation paper on trading venue perimeter "*In the context of Article 4(19) of MiFID II, a system must be understood as a set of rules that governs how third-party trading interests interact. Such rules or features could be contractual agreements or standard procedures that shape and facilitate interaction between participants' trading interests.*"

negotiate and conclude transactions on financial instruments, imposed by the system operator, to which all the participants in the system adhere without negotiation. In this regard the system operator has additional authorities compared to the participants. For instance, the operator has insight in the transaction data. Further, it is important to note that the participants have agreed with the operator to these rules that apply similarly for all participants *prior* to access to the platform / conclusion of a contract.

Also, from a client perspective it is important to differentiate between a multilateral system with a market operator and a software that is used by a regulated entity. Where a third party operator of a multilateral system has a user relationship with its users and has its tasks and responsibilities concerning these users in respect of the conclusion of transactions, a regulated entity that insources software or technical means that are used for bilateral trades only, has a client-relationship only with the client it transacts with and an outsourcing relationship with the provider of the software or technical means. The counterparty either signs up with the third party platform operator or agrees a contract with, for instance, a bank. In the latter the bank uses the technical means of a software under its own responsibility and outsourcing requirements.

Also, as MIFID is technology-neutral⁸, the definition of system should be separated and distinguished from the concept of electronic platform, so that it is clear that it should be irrelevant whether the trading subject to this system's rules, take place electronically or through any other channel.

Accordingly, if there are no common rules to conclude transactions in an electronic platform, but they are bilaterally agreed by their users or are the result of bilateral conversations based on standardised communication protocols not provided by the software developer (such as the FIX Protocol), this platform should not be considered a multilateral system but an electronic communication tool.

For instance, multiple parties may conclude transactions through the phone line, in bilateral voice conversations, but the phone line wouldn't qualify as a trading system as the phone company does not provide a trading system but a communication channel. The same criteria should apply to the electronic communication channels, as MIFID is technology neutral.

In line with the foregoing criteria, a 'single-dealer' system would be an electronic trading platform in which one dealer imposes a trading system (i.e. common trading rules) on all the other participants that intend to trade financial instruments with this dealer and this dealer arranges and manages this trading system. In this respect it would not be relevant whether the technology or software has been developed by this dealer/operator or by a third party (e.g. a software/IT provider).

4. ESMA's Opinion and MiFIR Review legislative proceeding

In the MiFID II Review Report on the functioning of the OTF (OTF Report) adopted in March 2021 and recalled by ESMA's Opinion, ESMA had envisaged two solutions: i) a short-term solution, by means of an Opinion clarifying the boundaries of TV authorization and ii) a long-term solution, by means of an amendment to Level 1 legislation i.e. moving the obligation set out in MiFID II in Article 1 paragraph 7 into MiFIR⁹.

⁸ Point 20 of ESMA's Consultation Paper on Trading Venue Perimeter: "*A system in ESMA's understanding is to be technology-neutral, hence the type of technology used or the fact that it is an automated or non-automated system, does not determine whether it is a system. The main criterion is whether there are specific rules concerning the interaction of multiple market participants to which participants shall adhere to.*"

⁹ With a view to ensuring more legal certainty, fostering EU-wide consistency and convergence in the application of the framework and avoiding any issues with transposition (Paragraph 25 of the OTF Report).

In the meantime, the 'moving' advocated by ESMA is already included in the legislative proposal on MiFIR Review adopted by the EC in November 2021. This legislative process has thus started. Although, the publication of an Opinion was not supported by the majority of respondents to ESMA OTF Public Consultation¹⁰, ESMA envisaged the publication of an Opinion in March 2021 to be finalized in a relatively short-term and as a solution that should precede (and not follow) the amendments to MIFIR.

Therefore, at this moment we do not see a compelling case / urgent reasons for the adoption of an Opinion from ESMA. Also, the absence of coordination and the different nature of the two envisaged measures (i.e. Opinion and legislative measures) does not benefit the legal certainty for market participants, but rather decreases that.

Members of the EFMLG would be delighted to meet you to discuss the issues raised in this letter. Please do not hesitate to contact me should you wish to arrange a meeting or if you have any questions.

Yours faithfully,



Fernando Conlledo Lantero

EFMLG

Vice-Chairman

¹⁰ As recognized by ESMA in its OTF Report (Paragraph 37 of the OTF Report).