

MiFID II: ESMA consults on systematic internalisers' quote rules

RTS 1 details MiFID II requirements on transparency for trading venues and investment firms in respect of shares, depositary receipts, exchange-traded funds, certificates and other similar financial instruments and the obligation for investment firms to execute transactions in certain shares on a trading venue or a SI.

ESMA proposes to clarify “prevailing market conditions”

MiFIR mandates ESMA to develop draft Regulatory Technical Standards (RTS) to specify further, in the context of the quoting obligations for SIs, “the determination of whether prices reflect prevailing market conditions”. ESMA finalised its proposal in September 2015 and RTS 1 was endorsed and published in the Official Journal on 31 March 2017.

Over recent months, the question has emerged whether the quotes of an SI can adequately reflect prevailing market conditions when those quotes do not reflect the minimum price increments (‘tick sizes’) applicable on-venue to the quoted financial instrument. In particular, for shares, depositary receipts and certain Exchange-Traded-Funds (ETFs), prices and quotes on Multilateral Trading Facilities (MTFs) and regulated markets will always have to comply with the minimum tick size regime of MiFID II.

ESMA considers it important to ensure a level playing field between different means of trading as envisaged by MiFID II/MiFIR. A competitive disadvantage would be created for trading venues compared to SIs if only on-venue orders and quotes have to comply with the minimum tick size regime. This could result in volumes currently traded on trading venues moving to OTC execution. Such an outcome appears likely in today’s technology driven environment where the order flow is automatically redirected to the best-priced quote, even if the quote only offers a very marginal price improvement. It is doubtful, however, that such an outcome would provide end-clients with real benefits as it would come at the expense of an artificial fragmentation of liquidity that may ultimately lead to a deterioration of the quality of price determination.

Therefore, ESMA proposes to amend Article 10 of RTS 1 to clarify that, for equity instruments subject to the minimum tick size regime under MiFID II RTS 11, SI quotes would only be considered to reflect the prevailing market conditions where those quotes reflect the price increments applicable to EU trading venues trading the same instruments.

Stakeholders are invited to provide feedback on this proposal by 25 January 2018. The input from stakeholders should help ESMA to finalise its amendments to RTS 1.