Deutsches Aktieninstitut

ESMA consultation on draft regulatory / implementation technical standards regarding MiFID II / MiFIR

Response of Deutsches Aktieninstitut, 2 March 2015

Summary

ESMA's proposed technical standards should not hamper companies' need to finance their business and to hedge risks stemming from their commercial or treasury financing activities. Deutsches Aktieninstitut[1] is of the opinion that recognising this guiding principle is also a prerequisite for a consistent implementation of a Capital Markets Union as identified by the EU Commission as a major source for growth and innovation in the EU.

We kindly ask ESMA to consider this in particular with regard to the following aspects:

Exemption for ancillary activities

Thresholds: The thresholds determining the ancillary activities are very low and we are concerned that major market participants will leave the market with unintended consequences for the liquidity. As a result, bid/offer spreads and hence prices for the respective instruments will rise, to the detriment of end-users. In addition, ESMA does not provide an empirical analysis of how these thresholds are derived. Therefore, we urge ESMA to conduct a sound analysis in order to adequately calibrate the thresholds. Without a thorough impact analysis, ESMA should set the thresholds on a higher level to avoid unforeseen, unintended consequences.

Privileged transactions: Companies are required by law (especially due to the requirements of the European Emission Allowances System) to hold emission allowances. These instruments should be – like risk-mitigating derivatives – acknowledged as privileged transactions. Emission allowances hold for these purposes can be easily identified as they are considered as "own use" instruments or accounted under "non-current assets: intangible assets" in accordance with existing accounting rules.

De minimis exemption: According to the proposed "de minimis exemption" non-financial companies not exceeding a market activity threshold of 0.25 % are not required to calculate the second threshold regarding the capital employed. Although the threshold should be reassessed as well, this exemption is very helpful and should be preserved in general. To allocate capital for certain activities or transac-

[1] Deutsches Aktieninstitut (identification number: 38064081304-25) represents the entire German economy interested in the capital markets. The about 200 members of Deutsches Aktieninstitut are listed corporations, banks, stock exchanges, investors and other important market participants. Deutsches Aktieninstitut keeps offices in Frankfurt, Brussels and in Berlin.

tions is a notion only common for financial institutions complying e.g. with capital/own fund requirements, or commodity firms with separate trading entities. However, this is not the case for most other non-financial companies. The MiFID requirement to assume allocated capital for certain activities would cause an additional administrative burden which is not justified especially for companies far away from exceeding the thresholds (as they are using derivatives almost exclusively for risk mitigating purposes). The de minimis exemption is also covered by the level-1-text as Art. 2(4) only states that ESMA "***may*** determine that the capital employed […]", which is not excluding alternative solutions.

Calculation of the trading activity test: It is unclear if ESMA intends to provide data especially regarding the overall market activity. The latter is necessary as market participants do not have access to all existing trade repositories to calculate the respective figures. Therefore, figures regarding the overall market activity in the respective asset classes should be provided centrally by ESMA or the national supervisory authorities which have access to the data collected on trade repository levels.

Position limits for commodity derivatives

Macro, portfolio or proxy hedging: We miss a clear statement that macro, portfolio or proxy hedging, which is a widespread risk-mitigating technique among non-financial companies, are acknowledged as "risk-mitigating" under the position limits regime as well. Therefore, ESMA should unambiguously state that the hedging exemption under the position limit is in line with the hedging definition under EMIR and the respective Q&A drafted by ESMA.

Notification process: The proposed notification process for the hedging exemption is too complex and does not reflect risk management practice. In the interest of both market participants and competent authorities the procedure should be designed much leaner, and in aggregated form (e.g. weekly or monthly summary). Reference could be made to reports provided by the relevant EMIR trade repositories which already include the information given by the company whether the derivative in question is for risk-mitigating purposes or not.

Acknowledging OTC derivatives: Finally, ESMA should clarify that exposures to risk-mitigating OTC derivatives agreed by financial institutions and non-financial companies can be taken into account in determining the net position under the limit regime notwithstanding such contracts do not constitute economic equivalent OTC contracts. While we in principle agree with ESMA's view to keep the scope of "economic equivalence" narrow, we are clearly concerned that end-users could not make use of their exemptions for risk-mitigating transactions in practice because financial institutions would not offer them due to their own position limits.

Position reporting

Coherent reporting standards should avoid double reporting between different regulations, especially regarding EMIR. Therefore, the obligation for end-users to report their positions daily to the venue operator should be as lean as possible. This means that data already available in the trade repositories or in other sources (especially for emission allowances) should be used for reporting purposes as far as possible.

Transparency for non-equity instruments / derivatives

The transparency requirements for derivatives could seriously interfere with the risk management strategy of non-financial companies using tailor-made or bespoke derivatives. Therefore, the transparency regime should reasonably reflect the peculiarities of these derivatives by. Recital 1 and recital 5 of the draft RTS 9 clearly states that the transparency requirements should ensure that investors are adequately informed and that primary market transactions are not covered by the provisions of this regulation. Derivatives used by non-financial companies for risk-mitigating purposes are by and large not fully fungible, standardized instruments. They are contracts bilaterally agreed with their banking partners. Secondary markets with “active” investors do not exist for these derivatives. Therefore, ESMA should state that derivatives that are not traded on a secondary market are excluded from the transparency requirements.

At least, ESMA should adjust the details proposed for deferred post-trade publication. The 48 hours deferral period for transactions which are illiquid, large in scale or above the size specific for the instrument are too short. The deferral period for illiquid instruments should be extended to 5 days after the day of the execution at the minimum. In addition, a waiver, especially when temporary, should not reveal selective information like the price immediately, or it is superfluous from the very beginning. Therefore, no details should be published during the deferral period, which is also the approach chosen by the U.S. CFTC. Otherwise, the regulation challenges the level playing field between the U.S. and the European industry.

Tick size regime and unexecuted order to transaction ratio

Listing on stock exchanges provides access to an important source of capital to finance growth and employment. A prerequisite for the willingness of investors to invest in shares and to provide capital for the company is the ability to sell the shares at any time at fair prices in the secondary market. For this purpose, liquidity and integrity of capital markets is of utmost importance to ensure that a fair price fixing process is available. ESMA should reflect this guiding principle in the tick size regime and the rules regarding the unexecuted order to transaction ratio. Well-balanced rules should ensure an efficient market infrastructure and should not harm market liquidity.

Answers to selected questions

Transparency regime for derivatives

Q61. Do you agree with ESMA's proposal for the definition of a liquid market? Please provide an answer for each of the asset classes identified (FRA, Swaptions, Fixed-to-Fixed single currency swaps, Fixed-to-Float single currency swaps, Float -to- Float single currency swaps, OIS single currency swaps, Inflation single currency swaps, Fixed-to-Fixed multi-currency swaps, Fixed-to-Float multi-currency swaps, Float -to- Float multi-currency swaps, OIS multi-currency swaps, bond options, bond futures, interest rate options, interest rate futures) addressing the following points:

(1) Would you use different criteria to define the sub-classes (e.g. currency, tenor, etc.)?

(2) Would you use different parameters (among those provided by Level 1, i.e. the average frequency and size of transactions, the number and type of market participants, the average size of spreads, where available) or the same parameters but different thresholds in order to define a sub-class as liquid (state also your preference for option 1 vs. option 2, i.e. application of the tenor criteria as a range as in ESMA's preferred option or taking into account broken dates. In the latter case please also provide suggestions regarding what should be set as the non-broken dates)?

Deutsches Aktieninstitut is of the opinion that the approach applied by ESMA to cover all derivatives under the transparency regime – irrespective whether they are traded or not – does not adequately reflect risk management practice in non-financial companies. It is important for ESMA to understand that OTC derivative markets – including contracts executed on MTFs or OTFs – are different from markets for securities and in particular for shares: These are no fully fungible and standardized transactions. They are requested by individual customers when required. Like loan contracts, leasing contracts, saving account contracts etc. these derivative transactions are contracts bilaterally agreed between clients and banks. Trading of the derivatives in question on secondary markets does not take place. From the perspective of trading on a secondary market these instruments are illiquid per se. There is also no investor involved who should be protected. On contrary, especially for larger transactions or transactions referring to an illiquid underlying it is likely that transparency will distort the price formation process to the detriment of the end-user. If an order is split up into smaller buckets (which is a common practice for the

above mentioned transactions), orders executed at a later stage will become remarkably more expensive. The reason for this is that it is unlikely that various end-users demand a "bespoke" derivative at the same time. The supply side can therefore conclude that the split orders can be attributed to the same end-user. As a result, prices will increase which makes risk management more expansive.

The legislator acknowledged these particularities by exempting derivative transactions of non-financial counterparties that are objectively measurable as reducing risks directly relating to the commercial activity or treasury financing activity from the pre-trade transparency requirements according to Art. 8(1) MiFIR.

Therefore, Deutsches Aktieninstitut asks ESMA to clarify that derivative contracts not traded on a secondary market are not in the scope of the transparency regime. This would be in line with recital 5 of draft RTS 9 which clearly states that the transparency regime does not apply to primary market transactions. In addition, recital 1 of draft RTS 9 underlines that the transparency rules should ensure that investors are adequately informed. Since there is no investor involved in such transactions, there is no reason for investor protection.

At least, for reasons of consistency in the methodology ESMA should adequately consider the characteristics of derivative contracts in its liquidity analysis. The term "trading" should not be confused with the conclusion of a derivative contract between the end-user and the bank. Both are different actions that should be treated differently. Therefore, derivatives that are "only" concluded between the contract partners and not traded furthermore should be deemed as illiquid per se.

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

Please refer to our answer above to Q61(2).

Q66. Do you agree with ESMA's proposal for the definition of a liquid market? Please provide an answer detailed per contract type, underlying type and underlying identified, addressing the following points:

(1) Would you use different qualitative criteria to define the sub-classes? In particular, do you consider the notional currency as a relevant criterion to define sub-classes, or in other words should a sub-class deemed as liquid in one currency be declared liquid for all currencies?

(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?

Please refer to our answer to Q61.

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

Please refer to our answer to Q61.

Q67. Do you agree with ESMA's proposal for the definition of a liquid market? Please provide an answer detailed per contract type, underlying type and underlying identified, addressing the following points:

(1) Would you use different qualitative criteria to define the sub-classes? In particular, do you consider the notional currency as a relevant criteria to define sub-classes, or in other words should a sub-class deemed as liquid in one currency be declared liquid for all currencies?

(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?

Please refer to our answer to Q61.

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

Please refer to our answer to Q61.

Q68. Do you agree with ESMA's proposal for the definition of a liquid market? Please provide an answer detailed per contract type 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?

Please refer to our answer to Q61.

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

Please refer to our answer to Q61.

Q72. ESMA seeks further input on how to frame the obligation to make indicative prices public for the purpose of the Technical Standards. Which methodology do you prefer? Do you have other proposals?

Deutsches Aktieninstitut refers to ESMA's discussion on the waiver for financial instruments for which there does not exist a liquid market (see p. 214). ESMA states that the waiver for derivatives not subject to the trading obligation is eligible for "derivatives subject to the clearing obligation but for which ESMA has determined that they shall not be subject to the trading obligation". We miss the statement that the waiver should be eligible ***also*** for derivatives ***not*** subject to the clearing obligation. For reasons of clarity ESMA should introduce the latter as well.

Q75. Do you agree with ESMA's proposal? Please specify in your answer if you agree with:

(1) a 3-year initial implementation period

(2) a maximum delay of 15 minutes during this period

(3) a maximum delay of 5 minutes thereafter. Please provide reasons for your answer.

No, Deutsches Aktieninstitut does not agree with the proposed process to adjust the maximum delay period to 5 minutes after three years automatically. ESMA should conduct an impact study in order to assess whether a real time transparency with a five minutes delay is adequate without affecting the markets negatively. If this is the case the period could be reduced.

Q76. Do you agree that securities financing transactions and other types of transactions subject to conditions other than the current market valuation of the financial instrument should be exempt from the reporting requirement under article 21? Do you think other types of transactions should be included? Please provide reasons for your answers.

Yes, Deutsches Aktieninstitut agrees, as double reporting should be avoided.

Q78. Do you agree with ESMA's proposal for interest rate derivatives? Please specify, for each sub-class (FRA, Swaptions, Fixed-to-Fixed single currency swaps, Fixed-to-Float single currency swaps, Float -to- Float single currency swaps, OIS single currency swaps, Inflation single currency swaps, Fixed-to-Fixed multi-currency swaps, Fixed-to-Float multi-currency swaps, Float -to- Float multi-currency

swaps, OIS multi-currency swaps, bond options, bond futures, interest rate options, interest rate 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

Deutsches Aktieninstitut assumes that derivative contracts concluded between the bank and the end-users are exempted from the transparency regime, if these instruments are not traded on secondary markets. At least, these contracts should be acknowledged as illiquid per se (see our answer to Q61).

Against this background, the deferral period of 48 hours for illiquid contracts is not sufficient. Especially derivative contracts that refer to an illiquid underlying (e.g. Nordic currencies) or instruments used for the hedging of bigger transactions (e.g. a M&A transaction) transparency might distort price mechanisms. As in those cases orders are split into smaller parts, orders executed at a later stage will become remarkably more expensive. The reason for this is that it is unlikely that various end-users demand a "bespoke" derivative contract at the same time. The supply side can therefore conclude that the split orders can be attributed to the same end-user. As a result, prices will increase which makes risk management more expansive.

In order to avoid a negative price impact it often takes days or more to complete the respective transaction. The deferred publication regime should appropriately consider this. Therefore, ESMA should extend the deferral period to 5 days after the day of the execution at the minimum at least for illiquid contracts.

For LIS and SSTI waiver we consider the deferred period of 48 hours as appropriate. Nevertheless, we ask ESMA to clarify that 2 days means 2 ***business*** days in order to counterbalance weekends and public holidays.

With regard to LIS thresholds, our view is that ESMA should recalibrate the LIS on a regular basis. However, we do not fully agree with option 2 as proposed. As an alternative, we suggest that the most relevant measure of the LIS threshold is trade count as distributed over the notional value of trades. We do not support the use of the volume measure set out in option 2. The determination of whether a transaction is large relative to the market should not be combined with the volume of trading in that market. We also disagree with ESMA's proposal to include a "floor" in option 2. In our view, this goes beyond the requirements set out in the level-1-text.

Finally yet importantly, ESMA proposes that competent authorities should have the option that other details besides those relating to the volume should be revealed immediately under the post-trade waiver. ESMA should be aware that these details would also affect the pricing process as described above. If the underlying itself is

illiquid, e.g. an emerging market currency or an unusual long maturity, the customer is at risk to be taken advantage of by traders even without mentioning the requested volume. A waiver, especially if applied only temporary, should not reveal selective information. Otherwise, it is superfluous from the very beginning. Therefore, no details should be published during the deferral period, which is also the approach chosen by the U.S. CFTC. If not, the level playing field between the U.S. and the European industry would be challenged.

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

ESMA seems to view the waiver regime for LIS and SSTI as a way to reduce the detrimental impact of an illiquid instrument that is incorrectly classified as liquid. Against this background, we urge ESMA to ensure that the LIS and SSTI thresholds are set at levels sufficiently low to ensure a more accurate reflection of which classes of instruments should be subject to the transparency obligations. In this regard the proposal to calculate the SSTI threshold as 50% of the respective LIS is too high. A level of 10% to 15% of LIS would be more adequate for SSTI, for both pre- and post-trade transparency.

Q83. Do you agree with ESMA's proposal in relation to the supplementary deferral regime at the discretion of the NCA? Please provide reasons for your answer.

Deutsches Aktieninstitut agrees principally. Nevertheless, we want to reiterate our concerns regarding the disclosure of information during the deferral period (please see our answer to Q78).

Ratio of unexecuted orders to transactions

Q109. Do you agree with the proposed regulatory technical standards? Please provide reasons for your answer.

In our view, listing on a stock exchange provides access to an important source of capital to finance growth and employment for companies. A prerequisite for the willingness of investors to invest in shares and to provide capital for the company is the ability to sell the shares at any time at fair prices in the secondary market. For this purpose, liquidity and integrity of capital markets is of utmost importance to ensure that a fair price fixing process is available.

Rules like the unexecuted order to transaction ratio (OTR) should ensure the efficiency of the market infrastructure as a prerequisite for issuers to finance their

business. Nevertheless, ESMA should also be aware that algorithmic traders increase trading volume and hence liquidity on secondary markets that improves companies' access to capital markets. Therefore, the OTR should leave venue operators enough discretion to adjust the rules respectively in order to ensure the liquidity provision by algorithmic traders.

Taking this into account ESMA should consider at least the following:

- ESMA should introduce a floor element as this is necessary to account for illiquid instruments.
- The OTR should not include indicative orders/quotes. Especially market makers use indicative quotes as an "invitatio ad offerendum" which should not be confused with an order directly placed in the trading system. If indicative orders/quotes would be regarded as orders the business model of market makers would be harmed to the detriment of the liquidity in the market.
- In general, market making activity should not be restricted by the OTR. Especially in illiquid markets quotes provided by market makers often do not meet a corresponding order on the other market side leading to a transaction. Under those circumstances the OTR for market maker is high per se. In order to not impair the provision of liquidity by market makers venue operators should have the permission to apply derogatory regimes for all venue participants involved in a reasonable quoting activity;
- We do not agree with the approach of ESMA to calculate the maximum OTR by taking into account the trading activity of the last year. Due to the evolving market environment trading volume is not a steady figure. Therefore, venue operators shall be in control of setting the permitted maximum OTR based on its considerations regarding system capacity and market conditions.

Tick sizes

Q123. Do you agree that the average number of trades per day should be considered on the most relevant market in terms of liquidity? Or should it be considered on another market such as the primary listing market (the trading venue where the financial instrument was originally listed)? Please provide reasons for your answer.

No, Deutsches Aktieninstitut does not agree. In our view listing on a stock exchange provides access to an important source of capital to finance growth and employment for companies. A prerequisite for the willingness of investors to invest in shares and to provide capital for the company is the ability to sell the shares at any time at fair prices in the secondary market. For this purpose, liquidity and integrity of capital markets is of utmost importance to ensure that a fair price fixing process is available.

Against this background, the tick size regime should not affect liquidity negatively and should not increase costs of using capital markets for financing purposes. We are concerned that the one-size fits all approach of ESMA will result in tick sizes that are often too large resulting in a significant increase of bid-offer spreads. Consequently, trading of shares will become more costly for investors, which will decrease liquidity and the attractiveness for companies to access stock markets for financing purposes.

Therefore, we ask ESMA to introduce an approach which is more proportionate and which better reflects the specifics of the respective instruments. According to the question posed above we think that the definition of "relevant market" should not be restricted to instruments traded on venues, but should also capture instruments traded OTC and by Systemic Internalisers.

Q124. Do you believe a more granular approach (i.e. additional liquidity bands) would be more suitable for very liquid stocks and/or for poorly liquid stocks? Do you consider the proposed tick sizes adequate in particular with respect to the smaller price ranges and less liquid instruments as well as higher price ranges and highly liquid instruments? Please provide reasons for your answer.

No, Deutsches Aktieninstitut does not agree. As pointed out in our answer to Q123 we are of the view that the proposed one-size fits all approach regarding tick sizes regime is not appropriate. We believe that the figure of 15,000 is in relation to the proposed definition of liquid market (i.e. a share is amongst other criteria considered as liquid if it has more than 250 trades a day) far too high and needs therefore adjustments. We also suggest that ESMA evaluates in its annual review if the five liquidity classes, i.e. the brackets are still valid.

Q131. Do you agree with the definition of the "corporate action"? Please provide reasons for your answer.

No, Deutsches Aktieninstitut does not agree. We believe that dividends should be added. To ensure that missing corporate actions could be considered at a later stage a non-exhaustive list is more appropriate.

Ancillary activity

Q168. Do you agree with the approach suggested by ESMA in relation to the overall application of the thresholds? If you do not agree please provide reasons.

For the comments of Deutsches Aktieninstitut on the overall approach please refer to our answers to Q169 to Q.182.

Q169. Do you agree with ESMA's approach to include non-EU activities with regard to the scope of the main business?

Yes, Deutsches Aktieninstitut agrees.

Q170. Do you consider the revised method of calculation for the first test (i.e. capital employed for ancillary activity relative to capital employed for main business) as being appropriate? Please provide reasons if you do not agree with the revised approach.

It is important to state that many non-financial companies, irrespective of size, use commodity derivatives in order to safeguard their planning processes and to unbundle these from fluctuations in commodity prices. Many of them are also required to hold emission allowances due to the respective EU legislation.

The notion to employ capital for parts (or even portfolios) of the treasury business is a matter of the financial world as it mainly relates to the context of own fund requirements for banks, insurers etc. (CRD VI / CRR, Solvency II). To apply the "capital employed approach" is also feasible for non-financial companies active in commodity trading (often from the energy or agriculture sector) as these companies tend to have separated trading entities with a respective allocation of capital. This holds not true for the broad real economy that is not familiar with the approach to employ capital for certain treasury activities like hedging or intra-group transactions. Hence, even the theoretical employment of capital to such activities would be a significant additional administrative burden that does not serve any operative purpose for them.

Therefore, Deutsches Aktieninstitut welcomes that ESMA proposes a "de minimis exemption". For the details of this exemption, please refer to our answer in Q180.

Q171. With regard to trading activity undertaken by a MiFID licensed subsidiary of the group, do you agree that this activity should be deducted from the ancillary activity (i.e. the numerator)?

Yes, Deutsches Aktieninstitut agrees.

Q172. ESMA suggests that in relation to the ancillary activity (numerator) the calculation should be done on the basis of the group rather than on the basis of the person. What are the advantages or disadvantages in relation to this approach? Do you think that it would be preferable to do the calculation on the basis of the person? Please provide reasons. (Please note that altering the suggested approach may also have an impact on the threshold suggested further below).

We believe that the calculation in relation to the ancillary activity (numerator) should be done at person level as this is clearly in line with the level-1-text. This would also adequately mirror the licensing regime set out in Art. 2(1)(j) MiFID II which explicitly applies to persons.

Furthermore, as outlined in our answers to Q173, Q179 and Q180 the proposed thresholds are already extremely low. This situation would be aggravated if companies should calculate the thresholds on group level.

Most importantly, the consequences of exceeding the thresholds would affect all persons within the group and not only those persons involved in investment services/activities at disproportionate levels, triggering consequences (i.e. EMIR, CRD) for all of them, although the individual persons' activities remain clearly under the thresholds. This might lead to the paradox situation that although none of the entities within a group breaches the thresholds they all have to apply for a MiFID licence as the entire group has exceeded the thresholds.

Nevertheless, if ESMA maintains the proposal to consider the calculation on group level, it is necessary that the RTS provide more details for the practical application of the calculation process. For example, what are the steps required in case none of the entities within a group breaches the threshold levels, but altogether the level is crossed? How the national competent authority will approach activities carried out until one or more entities within the group will receive a license?

Q173. Do you consider that a threshold of 5% in relation to the first test is appropriate? Please provide reasons and alternative proposals if you do not agree.

No, Deutsches Aktieninstitut does not agree.

Although ESMA adjusted the procedure to calculate the "capital employed" threshold the proposed 5% is a much too drastically decrease compared to the 50% originally proposed in the discussion paper.

ESMA justifies the low thresholds by arguing that instruments used to hedge commercial activities are not considered as ancillary activity. Although this holds true for risk-mitigating derivatives ESMA should also be aware that – so far – emission allowances are not regarded as privileged transactions, irrespective whether they are hold for regulatory purposes or not (see also our answer to Q181). In order to comply with respective regulatory requirements emission allowances are a widespread instrument used by the real economy. Furthermore, investment services, other than dealing on own account, in commodity derivatives or emission allowances or derivatives thereof to the customers or suppliers of their main business are not covered by the definition "privileged transactions" as well. The latter services include inter alia the delivery of commodities for clients of the main business at cost prices. Obviously, in these cases no trading purpose is involved.

To conclude, positions in emission allowances or the investment services mentioned above – although not involving any trading purpose – bear the risk for the real economy to exceed the thresholds. Nevertheless, so far it is difficult to assess whether the level of the thresholds proposed by ESMA reflect this risk adequately.

Last but not least, we fear that due to this very low threshold major participants stemming especially of the utility sector will – instead of applying for a MiFID-licence – leave the markets. The consequence would be a negative impact on liquidity that will in turn increase bid/offer spreads and hence prices for the respective instruments to the detriment of end-users.

Therefore, ESMA should refrain from setting the thresholds on a too low level without providing a sound analysis regarding the impact on markets as a whole. The "high level cost-benefit-analysis" released in December 2014 remains silent on this issue.

Unless there is no quantitative analysis available and to avoid unintended consequences ESMA should set the thresholds on an appropriate level, i.e. 20% to 25%. These thresholds should be reviewed in a timely manner, e.g. in 2017 based on the data gathered by then.

Q174. Do you agree with ESMA's intention to use an accounting capital measure?

Yes, Deutsches Aktieninstitut agrees.

Q176. Do you agree with the proposal to use the gross notional value of contracts? Please provide reasons if you do not agree.

Yes, Deutsches Aktieninstitut agrees.

Q177. Do you agree that the calculation in relation to the size of the trading activity (numerator) should be done on the basis of the group rather than on the basis of the person? (Please note that that altering the suggested approach may also have an impact on the threshold suggested further below)

We believe that the calculation in relation to the ancillary activity (numerator) should be done at person level as this is clearly in line with the level-1-text. This would also adequately mirror the licensing regime set out in Art. 2(1)(j) MiFID II which explicitly applies to persons.

Furthermore, as outlined in our answers to Q173, Q179 and Q180 the proposed thresholds are already extremely low. This situation would be aggravated if companies should calculate the thresholds on group level.

Most importantly, the consequences of exceeding the thresholds would affect all persons within the group and not only those persons involved in investment services/activities at disproportionate levels, triggering consequences (i.e. EMIR, CRD) for all of them, although the individual persons' activities remain clearly under the thresholds. This might lead to the paradox situation that although none of the entities within a group breaches the thresholds they all have to apply for a MiFID licence as the entire group has exceeded the thresholds.

Nevertheless, if ESMA maintains the proposal to consider the calculation on group level, it is necessary that the RTS provide more details for the practical application of the calculation process. For example, what are the steps required in case none of the entities within a group breaches the threshold levels, but altogether the level is crossed? How the national competent authority will approach activities carried out until one or more entities within the group will receive a license?

Finally, we want to reiterate our concern that the data for the calculation of the overall market trading activity has to be made available centrally by ESMA or the competent authorities (see our answer to Q179).

Q178. Do you agree with the introduction of a separate asset class for commodities referred to in Section C 10 of Annex I and subsuming freight under this new asset class?

Deutsches Aktieninstitut does not agree as ESMA rightly states that freight is ancillary to other commodity businesses and should therefore not be considered as a separate asset class. Nevertheless, it would be appropriate to have freight as part of the commodity in question, i.e. gas infrastructure within the asset class "gas", electricity transmission within the asset class "power", etc. instead of including freight in the "other commodities" asset class.

In addition, ESMA should be aware that the creation of the category "other derivatives" (including C10 commodities) generates uncertainty because it remains undefined what should be included in such a category and what is the market size of such category. This will result in very difficult practical considerations for the calculation of the thresholds for the ancillary activity test. This example also demonstrates that ESMA should conduct a thorough analysis on a sound database before setting the thresholds (see our answers to Q173, Q179 and Q180).

Q179. Do you agree with the threshold of 0.5% proposed by ESMA for all asset classes? If you do not agree please provide reasons and alternative proposals.

No, Deutsches Aktieninstitut does not agree.

The threshold is very low and arbitrarily chosen. As already stated in our answer to Q173 we want to reiterate that emission allowances and investment services, other than dealing on own account, in commodity derivatives or emission allowances or derivatives thereof to the customers or suppliers of their main business are not covered by the definition "privileged transaction". It is therefore incorrect if ESMA states that the thresholds will not concern companies using derivatives for risk-mitigating purposes. To assess the impact of these activities not regarded as "privileged transactions" on the level of the trading threshold is impossible so far as there is no aggregated data for the overall market trading activity available.

Again, to avoid unintended consequences for the companies of the real economy, the liquidity of the market and the pricing/availability of the respective instruments ESMA should provide a sound analysis of the impact of this threshold on the market of the instruments in question.

Unless there is no impact analysis available, ESMA should set the thresholds on an appropriate level, i.e. at least around 15%. After experiences with these thresholds have been made ESMA should adequately adjust them within a review process e.g. starting in 2017.

Last but not least, it is unclear if ESMA intends to provide data especially regarding the calculation of the overall market activity. The latter is necessary, as market participants do not have access to trade repositories to calculate the respective figures. Therefore, ESMA or the national supervisory authorities should provide the figures regarding the overall market activity in the respective asset classes as these bodies have access to the data collected on trade repository level. Otherwise, the calculation of the market activity thresholds is not possible.

Q180. Do you think that the introduction of a de minimis threshold on the basis of a limited scope as described above is useful?

Yes, Deutsches Aktieninstitut agrees that this exemption is very helpful and should be preserved. To allocate capital for certain activities or transactions is a notion only common for financial institutions complying e.g. with capital/own fund requirements, or commodity firms with separate trading entities. However, this is not the case for most other non-financial companies. The MiFID requirement to allocate capital for certain activities would cause an additional administrative burden which is not justified especially for companies far away from exceeding the thresholds (as they are using derivatives almost exclusively for risk mitigating purposes and provided that emission allowances hold for regulatory purposes are acknowledged as privileged transactions as well). The de minimis exemption is also covered by the level-1-text as Art. 2(4) only states that ESMA "***may*** determine that the capital employed […]", which is not excluding alternative solutions.

Nevertheless, we think that ESMA should increase the threshold to 5% at the beginning combined with a review in a timely manner (e.g. in 2017).

Q181. Do you agree with the conclusions drawn by ESMA in relation to the privileged transactions?

No, we do not agree. It is frequently stated by ESMA that those companies using risk-mitigating instruments solely are not at risk to exceed the thresholds for the ancillary activity test.

Unfortunately, this is not correct as emission allowances hold for regulatory purposes (especially due to the requirements of the European Emission Allowances System) are not acknowledged as privileged transactions so far. These emission allowances are obviously not for trading purposes but for compliance with respective regulations. Consequently, these instruments should also be included as "privileged transactions". There is also not the danger that this exemption creates a loophole for trading activities as emission allowances hold to comply with regulatory re-

quirements can be easily identified as they are considered as “own use” instruments or accounted under “non-current assets: intangible assets” in accordance with existing accounting rules.

Q182. Do you agree with ESMA’s conclusions in relation to the period for the calculation of the thresholds? Do you agree with the calculation approach in the initial period suggested by ESMA? If you do not agree, please provide reasons and alternative proposals.

As mentioned in the answers of Deutsches Aktieninstitut to Q173, Q179 and Q180 the thresholds for capital employed, for the market share and the de minimis exemption should be increased on an appropriate level. These thresholds should be reviewed in a timely manner, e.g. in 2017.

Position limit regime

Q183. Do you have any comments on the proposed framework of the methodology for calculating position limits?

Due consideration must be given to the netting treatment of OTC contracts to ensure that in calculating the net position of an entity that entity is able to net OTC instruments which are closely correlated to on-venue contracts. This is critical from an end-user perspective, as financial institutions should be able to continue to provide efficient risk-mitigating derivatives.

Although risk-mitigating derivatives used by non-financial companies are exempted from the position limits regime this exemption would be rendered useless if their financial counterparties could not provide the respective instruments due to position limits set too strict. It is common practice that financial counterparties offset the OTC derivative exposure provided to their non-financial clients with exchange traded benchmarks (e.g. gas oil futures) as the OTC derivatives are closely correlated to the futures. In addition, this dynamic allows financial institutions to aggregate bespoke interests in a diverse client base resulting in a highly correlated centralised pool of liquidity that provides an efficient source of hedging instruments for non-financial companies.

ESMA must ensure that financial entities can continue to offer risk-mitigating derivatives for non-financial companies under the newly introduced position limit regime. In the absence of a “pass through hedge exemption”, it is crucial that these correlated OTC instruments continue to operate as legitimate offsets to the futures exposure assumed by financial institutions to deliver this source of liquidity to non-

financial companies. However, these OTC derivatives should not be regarded as economically equivalent to venue traded instruments.

Accordingly, ESMA should clarify that exposures to risk-mitigating OTC derivatives agreed by financial institutions and non-financial companies can be taken into account in determining the net position under the limit regime notwithstanding such contracts do not constitute economic equivalent OTC contracts. While we in principle agree with ESMA's view to keep the scope of "economic equivalence" narrow (please refer to our answer to Q204), we are clearly concerned that end-users could not make use of their exemptions for hedging transactions in practice because financial institutions would not offer them due to their own position limits.

Q200. Do you agree with the proposed draft RTS regarding risk reducing positions?

No, Deutsches Aktieninstitut does not agree. Although we welcome the aim of ESMA to refer to the definition "risk-reducing" already available under EMIR the treatment of macro, proxy and portfolio hedging is not clear. These hedging instruments are acknowledged as "risk-mitigating" under EMIR and should be treated as such under the position limits regime according to MiFID II as well.

On the one hand, ESMA notes that there is a clarification in the EMIR Q&A on what constitutes macro, proxy or portfolio hedging (see OTC Q10(c)). We think the latter is a clear statement for the intention of ESMA to follow the hedging definition already available under EMIR and detailed by the respective Q&A.

On the other hand, ESMA questions the applicability of macro hedging regarding the position limit regime as it deleted the term "directly or through closely correlated instruments" stemming from the EMIR hedging definition in Art. 1 para.1 of the respective draft technical standards (s. RTS 30 on p. 395). Please compare Art. 10 of Commission Delegated Regulation (EU) No 149/2013: "An OTC derivative contract shall be objectively measurable as reducing risks directly relating to the commercial activity […] of the non-financial counterparty or of that group, when, by itself or in combination with other derivative contracts, ***directly or through closely correlated instruments,*** it meets one of the following criteria […]".

Therefore, in order to bring the hedging exemption under the position limit regime unambiguously in line with the hedging definition under EMIR the term "directly or through closely correlated instruments" should be introduced in Art. 1 para. 1 of draft RTS 30.

Q204. Do you agree with the proposed draft RTS regarding the criteria for determining whether a contract is an economically equivalent OTC contract?

Deutsches Aktieninstitut agrees with ESMA's view to keep the criteria narrow. We would however ask ESMA to allow more flexibility in the position limit regime with regard to the netting possibilities, as outlined in our answers to Q183. We are otherwise concerned that shortcomings in the position limits regime would negatively affect the availability of hedging instruments for non-financial end-users.

Q208. Do you agree with the proposed draft RTS regarding the procedure for the application for exemption from the Article 57 position limits regime?

No, Deutsches Aktieninstitut does not agree. The proposed notification process for the hedging exemption is too complex and does not reflect risk management practice. The proposal of ESMA could be read as a requirement for companies to wait up to 30 days until each single transaction is acknowledged as "risk mitigating by the competent authorities. This would be not appropriate, as it is inconceivable to delay hedging decisions for longer periods. Besides that, filing individual transaction applications seems inefficient given the significant number of deals some corporates need to transact due to their operative needs. Therefore, in the interest of both market participants and competent authorities the notification process for the hedging exemption should be designed much leaner, and in an aggregated form (e.g. weekly or monthly summary).

One possible solution: Reference could be made to reports provided by the relevant EMIR trade repositories which already include the information given by the company whether the derivative in question is for risk-mitigating purposes or not. This report could be flagged and directly submitted by the trade repository to the competent authority. Hence, a separate notification for applying with the hedging exemption under the position limit regime would be superfluous.

Positon Reporting

Q212. What other reporting arrangements should ESMA consider specifying to facilitate position reporting arrangements?

To avoid double reporting under Art. 58 MiFID II already existing reporting arrangements should be utilised as far as possible.

According to EMIR, commodity derivatives and derivatives on emission allowances (recently according to the respective definition under MiFID I and in future under MiFID II) have to be reported to trade repositories. For these instruments the venue operator should be allowed to tap the information already available in the

trade repositories. This information is sufficient to calculate and update the respective positions of every end client in the respective derivative instruments.

Data for the positions in emission allowances is available as well: In Germany the German Emissions Trading Authority (see http://www.dehst.de/EN/Home/home_node.html) collects data according to the emission allowances and the positions each company holds in these instruments. These sources should be used for position reporting as well.

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