



European Securities and  
Markets Authority

## **Reply form for the Consultation Paper on the Guidelines on the calibration, publication and re- porting of trading halts**





## Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the ESMA Discussion Paper on the Guidelines on specific notions under MiFID II related to the management body of market operators and data reporting services providers, 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\_GTH\_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\_GTH\_NAMEOFCOMPANY\_NAMEOFDOCUMENT.

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

ESMA\_MiFID\_GTH\_ESMA\_REPLYFORM or

ESMA\_MiFID\_GTH\_ESMA\_ANEX1

### ***Deadline***

Responses must reach us by **06 December 2016**.

All contributions should be submitted online at [www.esma.europa.eu](http://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](http://www.esma.europa.eu) under the heading 'Legal notice'.

## Introduction

**Please make your introductory comments below, if any:**

< ESMA\_COMMENT\_MIFID\_GTH\_0>

Deutsche Börse Group (DBG) welcomes ESMA's efforts to further enhance market stability in the EU and to implement the provisions to temporarily halt or constrain trading as foreseen in Article 48.5 MiFID II. With our comments we hope to contribute to these ends, and in particular, we would like to raise legislators' and regulators' attention to the following issues.

The legislators clearly differentiate between the requirements set out in Article 48.5 MiFID II and we fully support this differentiation and would like to highlight our recommendations and concerns for the two aspects accordingly. **Therefore, DBG at this introductory stage clearly rejects ESMA's proposed categorisation by which volatility interruptions are subsumed to trading halts and thus become subject to the same provisions.**

When designing Article 48 MiFID II, legislators rightly acknowledged the fundamentally distinct logic of trading halts and volatility interruptions and thus, clearly differentiated between the ability to temporarily halt or constrain trading: during trading halts, the execution of trades as well as the determination of new prices are suspended; in contrast, volatility interruptions are designed and implemented to protect price discovery in a specific order book during times of local liquidity imbalances by making use of a switch to auction trading mode in order to ensure information equality amongst market participants. We therefore propose to consider the distinction between different circuit breaker mechanisms as described by the World Federation of Exchanges (WFE) in a recent study.<sup>1</sup> By treating volatility interruptions and trading halts similarly, both concepts are jeopardised in a detrimental manner.

We explicitly welcome ESMA's intention not to propose an alignment between the trigger parameters of the different correlated instruments. We consider this notion to be fully in line with the objectives of Article 48.5 MiFID II, which does not provide for such a coordination of parameters. In our view, regulated markets applying the provisions of Article 48.5 MiFID II through volatility interruptions fully comply with the underlying objectives of the Directive by improving price continuity and ensuring price quality.

This being said, we would like to further explain our concerns regarding the feasibility of the proposed market-wide coordination for the case of volatility interruptions as they are operated on the markets of Deutsche Börse Group. In particular, **we strongly disagree with ESMA's proposal that trading venues must be able to halt or constrain trading in case of significant price moves on related markets**, even if there is no obligation to actually halt or constrain trading due to trading activity on other markets (see paragraph 34, page 13). First, it imposes large technical efforts to trigger a volatility interruption based on trading activity on a different market. Volatility interruptions are designed to react to price jumps in real time and they usually last for only a few minutes. Second, we do not see the benefits of such an external trigger. If prices of two related instruments are correlated and it is therefore likely that a volatility event on one market follows a volatility event in another market, the safeguards operated by each market will still ensure that effectively both markets change to a volatility interruption (or a trading halt). If in turn the prices are independent or the anomaly was incidental and limited to one trading venue only (local liquidity imbalance), it is also not justifiable to have volatility interruptions on both markets. Rather, any market-wide coordination of volatility interruptions would ignore this locally restricted liquidity situation but introduce a distortion of the functioning of the price discovery process across markets. Third, while the start of the volatility auction phase is just a technical burden to coordinate, the reopening of markets, which, to be consistent, needs also to be coordinated, will impose the problem of which market "leads" all related markets and still adheres to all given time settings for the respective safeguards in the different markets. Forth, there would be a need for a detailed list of markets and their relation based on instrument level to ensure that all related instruments and markets act in concert. ESMA would have to decide which instruments are correlated and which ones are not.

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<sup>1</sup> World Federation of Exchanges, Circuit Breakers – A survey among International Trading Venues, 2016 (study conducted in collaboration with the e-Finance Lab, Goethe University Frankfurt) available at <https://www.world-exchanges.org/home/index.php/files/18/Studies%20-%20Reports/356/WFE%20Survey%20on%20Circuit%20Breakers.pdf>

Besides, it is unclear how NCAs would process the information and on which basis a trading suspension would be triggered on their side under the envisaged coordination process proposed by ESMA. We assume that the intended purpose of a market-wide response by the NCAs could be to prevent volatility events on other related markets even before the safeguards on these markets are triggered. Such a prevention would require very short reaction times, potentially within microseconds for some financial instruments. This implies that such market-wide coordination processes do not allow for human intervention at all. As ESMA points out, NCAs will most likely exercise their power to suspend potentially affected instruments from trading in such a situation, which would in effect lead to a situation where a volatility interruption in one market triggers trading suspensions in (all) other markets, without sufficient time for a careful consideration of adequacy. We consider that the envisaged coordination process based on the concatenation of parameters and trigger events is not compatible with NCAs mandate to evaluate and to decide on any coordination of measures as foreseen by the Directive.

**Overall, we suggest that trading venues shall only avail of mechanisms and processes to be able to trigger volatility interruptions based on trading activity on other markets at their own discretion. Trading venues shall therefore also not be obliged to monitor trading activity on other markets. We also strongly recommend that ESMA dismisses the envisaged market-wide response coordination process for volatility interruptions completely.**

Trading venues avail of a number of safeguard mechanisms; their discretion should not be limited by overly strict regulatory prescriptions when it comes to the functional design, application and interplay of these measures. These safety mechanisms and other safeguards operated by trading venues have proven their positive contribution to market stability during highly volatile and stressed market phases, for example in the aftermath of the UK Brexit vote. Against this background, we question ESMA's notion of a "lack of instruments or mechanisms at a panEuropean level [...] to address any potential global volatility event" (see paragraph 36, p. 13f). **We currently do not see the need for any amendments to the current safety architecture; rather, we consider it a more suitable way towards enhancing the quality and effectiveness of any volatility-mitigating measures to monitor trading venues' adherence to common quality standards and to ensure compliance and equivalence across Europe.** Trading venues as well as national competent authorities are granted discretion when it comes to the design and functionality of mechanisms to protect the price discovery process and to avoid significant disruptions to the orderliness of trading. Thus, the diversity of safety measures is a clearly intended policy decision by European legislators. |

< ESMA\_COMMENT\_MIFID\_GTH\_0>

**Q1. Would you consider these factors discussed above to be useful? Could you identify any additional element to be factored in?**

<ESMA\_QUESTION\_MIFID\_GTH\_1>

In general, we recommend that besides the calibration of the parameters of trading halts, **market operators should be able to maintain adaptability in regards to trading halts for certain instruments and certain trading modes** where such measures would prove being unjustified or even detrimental to the efficient market functioning.

- First, a meaningful interplay of mechanisms to manage volatility (volatility interruptions, pre-trade price checks, trading suspensions, and matching principles that prevent large price jumps) can only be guaranteed if market operators have the necessary degrees of freedom to decide if and how to apply them.
- Second, there are certain market models and trading phases where volatility interruptions are not meaningful, for example opening auctions and markets where specialists provide quotes and the order book is therefore safeguarded by expert intervention.
- Finally, market operators have established business practices to effectively prevent erratic price changes; “flash crashes” are addressed by applying volatility interruptions on the most liquid financial instruments only. The parametrization and application of volatility interruptions on illiquid or non-linear (e.g. options) products neither provide benefit to nor address these instruments correctly. As price continuity and price ranges are highly dependent on time of trading activity, volatility interruptions are best applied to instruments that have this interplay of characteristics, which illiquid instruments are lacking.

Based on this premise, we largely share ESMA’s view and consider most of the factors that ESMA proposes to take into account for the parameterization as meaningful. Various factors are already appropriately reflected in the calibration of the trigger parameters for Deutsche Börse Group’s safety mechanisms.

**While many of the factors are meaningful, we would strongly advise though not to mandate the use of all parameters in tandem, as some of them might be misleading or highly correlated and therefore redundant.**

Among the factors enumerated, we would like to increase awareness that the observation of order imbalances should be removed from the list of relevant factors. Indeed, if there is a structural overhang in either direction, it is likely the case that market expectations / valuations change for a fundamental reason and trading should not be constrained in order to allow for efficient processing of information. Where a situation of an unbalanced order book contributes to excess volatility and disorderly trading conditions, the imbalance must stem from uninformed or erroneous trading activity. If at all, this can only be distinguished in hindsight and therefore order imbalances are not a suitable factor for preventive means to manage volatility.

Similarly, we advise not to include external reference data (e.g. from correlated instruments) to detect abnormal volatility in a specific financial instrument. If both, the instrument in question and the correlated instrument display strong price movements at the same time, it is likely that the source of the volatility is an external economic factor that moves the market. On the other hand, if a price jump is only observed in the correlated instrument, it is not justified that trading in the instrument in question is also halted.

**Overall, we recommend for the final guidelines that the factors, apart from the ones we would not support as described above, could be generally mentioned as part of a potential tool set.** We would ask ESMA to abstain from providing prescriptive examples as formulated in the proposed guidelines, as some are misleading or have limited applicability for certain instrument types. |

<ESMA\_QUESTION\_MIFID\_GTH\_1>

- Q2. Do you consider that the Guidelines regarding calibration of volatility parameters should also apply to mechanisms to reject erroneous orders (i.e. order price / volume collars) and that ESMA should propose Guidelines on this issue at its own initiative?**

<ESMA\_QUESTION\_MIFID\_GTH\_2>

We strongly recommend that ESMA does not propose additional guidelines on the calibration of other pre-trade checks. ESMA does not avail of the legal mandate to develop such additional guidelines for the calibration of pre-trade checks, and we would also like to emphasize that according to Article 48.13 MiFID II, ESMA's mandate to develop guidelines on the appropriate calibration applies to trading halts only and therefore does not cover volatility interruptions. Neither the Directive itself nor the implementing measures on Level 2 do assign the task to ESMA to develop respective measures for mechanisms to constrain trading. Following our argumentation in the introductory comments regarding the distinction between measures to halt trading and to constrain trading, trigger parameters for volatility interruptions should not fall into the scope of ESMA's mandate. In addition, only for trading halts, trading venues are obliged to report the parameters of calibration to the National Competent Authority (and to ESMA in a subsequent step).

The Directive clearly distinguishes between mechanisms where ESMA is given an active task to calibrate parameters, e.g. trading halts, and those mechanisms where legislators deliberately decided to abstain from doing so. For trading venues that apply a range of safeguarding mechanisms to ensure orderly exchange trading, efficient price discovery and prevention of excess volatility (volatility interruptions, pre-trade price checks, trading suspensions, maximum quote spreads, market order matching range etc.), it is crucial to have the necessary degrees of freedom regarding the application and parameterization of these mechanisms in order to ensure a meaningful and effective interplay. |

<ESMA\_QUESTION\_MIFID\_GTH\_2>

- Q3. Is there any other aspect which should be considered in these Guidelines so as to prevent market-wide volatility events given the current structure of European markets?**

<ESMA\_QUESTION\_MIFID\_GTH\_3>

Deutsche Börse Group does not see a need for additional regulations on mechanisms to prevent market-wide volatility. The established individual trading venues' safeguards are sufficient and have proven their effectiveness more than once in the past. |

<ESMA\_QUESTION\_MIFID\_GTH\_3>

- Q4. Do you consider that the proposed order and trade feed reporting standard for trading status will contribute to facilitate a correct identification of trading halts across Europe? Do you foresee any drawback on it?**

<ESMA\_QUESTION\_MIFID\_GTH\_4>

We generally agree with ESMA that the market should be informed immediately and precisely in the event of a trading halt. However, we do not see any additional value in the standardization of the instrument status as proposed by ESMA, given the structural differences between mechanisms to manage volatility applied on different markets and our above mentioned general concerns regarding the blurred distinctions between trading halts and volatility interruptions. In addition, such a standardization would omit all market specifics and therefore blur the already implemented handling on trading participants' side. |

<ESMA\_QUESTION\_MIFID\_GTH\_4>

- Q5. Would you prefer a further degree of granularity in the information provided as described in the text under paragraphs 46 and 47? Please elaborate in case you consider necessary further granularity but you disagree with the proposed approach.**

<ESMA\_QUESTION\_MIFID\_GTH\_5>

We understand that a certain level of granularity is useful, but the provided information should be relevant for market participants. We agree that the distinction between volatility interruptions occurring during continuous trading and auctions is informative, as well as the switch from volatility interruption to extended volatility interruption.

However, we do not see the purpose of counting how often the volatility interruption has been extended, since the trading status of the instrument is factually unchanged in case of an extension and this information does not provide any useful information for the participants in relation to the actual liquidity situation within the respective order book.

For volatility interruptions, extension processes do not systematically exist, and the process can differ from asset class to asset class. Therefore, the index proposed in paragraphs 47 iii) and iv) would not always be applicable and it should also not be forced to have extensions. Not every market uses such extensions. |

<ESMA\_QUESTION\_MIFID\_GTH\_5>

**Q6. Is the code proposed above (i.e. “VH”) appropriate, or should another code be used? Please elaborate in case you consider that another code should be used.**

<ESMA\_QUESTION\_MIFID\_GTH\_6>

We would like to make ESMA aware of the fact that Deutsche Börse Group, as well as numerous other market operators, use the industry standard FIX protocol to communicate market data (including the current trading states of the financial instruments tradable on the respective markets) in our systems and to trading participants. For example, in case of a volatility interruption, a FIX message in a numerical format (namely “208” in this case) is disseminated and it is only translated on the recipient’s side. We recommend to carefully weigh up the costs and benefits of a potential change of an already established industry standard. |

<ESMA\_QUESTION\_MIFID\_GTH\_6>

**Q7. Do you agree with the reporting template proposed?**

<ESMA\_QUESTION\_MIFID\_GTH\_7>

ESMA proposes that the annual report shall contain all parameters used on January 1 of the respective year. We suggest to refer to the first trading day of the year instead, which is usually not January 1 (i.e. a public holiday in many jurisdictions). |

<ESMA\_QUESTION\_MIFID\_GTH\_7>

**Q8. Are there any other items that should be included in the template?**

<ESMA\_QUESTION\_MIFID\_GTH\_8>

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<ESMA\_QUESTION\_MIFID\_GTH\_8>

**Q9. Please provide any views with respect to the costs and benefits identified in the relevant annex.**

<ESMA\_QUESTION\_MIFID\_GTH\_9>

TYPE YOUR TEXT HERE |

<ESMA\_QUESTION\_MIFID\_GTH\_9>