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Commission Delegated Regulation (EU) 2017/578 of 13 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards specifying the requirements on market making agreements and schemes (Text with EEA relevance)

COMMISSION DELEGATED REGULATION (EU) 2017/578

of 13 June 2016

supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards specifying the requirements on market making agreements and schemes

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU[(1)], and in particular Article 17(7)(a), (b) and (c) and Article 48(12)(a) and (f) thereof,

Whereas:

(1) Two main goals should be attained in specifying the market making obligations of algorithmic traders pursuing market making strategies and the related obligations of trading venues. First, an element of predictability to the apparent liquidity in the order book should be introduced by establishing contractual obligations for investment firms pursuing market making strategies. Second, the presence of those firms in the market should be incentivised, particularly during stressed market conditions.

(2) The provisions in this Regulation are closely linked, since they deal with a set of related obligations for investment firms engaged in algorithmic trading pursuing market making strategies and for trading venues where those market making strategies may take place. To ensure coherence between those provisions, which should enter into force at the same time, and to facilitate a comprehensive view of and a compact access to them by persons subject to those obligations, including investors that are non-Union residents, it is desirable to include those provisions in a single Regulation.

(3) This regulation should apply not only to regulated markets but also to multilateral trading facilities and organised trading facilities as required by Article 18(5) of Directive 2014/65/EU.

(4) Market making strategies may relate to one or more financial instruments and one or more trading venues. However, in certain cases, it may not be possible for a trading venue to monitor strategies involving more than one trading venue or instrument. In those cases, trading venues should be able, in accordance with the nature, scale and

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complexity of their business, to monitor market making strategies pursued on their own venue, and therefore should restrict corresponding market making agreements and schemes to those situations only.

(5) All members or participants engaged in algorithmic trading pursuing a market making strategy on a trading venue which allows for or enables algorithmic trading should enter into a market making agreement with the operator of that trading venue. Incentives under a market making scheme should, however, only be required for certain instruments traded under a continuous auction order book trading system. Nothing should prevent trading venues from establishing any other type of incentives at their own initiative for other financial instruments or trading systems.

(6) Cases where there is no mandatory requirement for trading venues to set out a market making scheme taking into account the nature and scale of the trading on those trading venues should be clearly identified. To this end, it is appropriate to identify financial instruments and trading systems that increase the risk of high volatility and for which it is crucial that the provision of liquidity is incentivised, in order to ensure orderly and efficient functioning of markets. In this respect, this Regulation should take into account that when certain liquid instruments are algorithmically traded in continuous auction order book trading systems there is a greater risk of overreaction to external events which can exacerbate market volatility.

(7) Trading venues for which it is considered appropriate to have market making schemes in place in accordance with this Regulation should be required to review their existing agreements to ensure that the provisions of those agreements concerning algorithmic traders pursuing a market making strategy comply with this Regulation.

(8) The market making scheme may incentivise investment firms having signed a market making agreement to perform their obligations under normal trading conditions, but should provide incentives for firms effectively contributing to liquidity provision under stressed market conditions. Therefore, there should be a scheme of incentives to limit a sudden and large-scale withdrawal of liquidity under stressed market conditions. In order to avoid divergent application of this obligation, it is important that trading venues communicate the existence of stressed market conditions to all parties to the market making scheme. Exceptional circumstances should be determined exhaustively and therefore do not include any regular or pre-planned information events that may affect the fair value of a financial instrument due to changes in the perception of market risk, whether occurring during or outside trading hours.

(9) Members, participants or clients having signed a market making agreement have to meet a minimum set of requirements in terms of presence, size and spread in all cases. However, the members, participants or clients meeting those minimum requirements only under normal trading conditions may not necessarily access any type of incentive. Trading venues may establish market making schemes which only reward members, participants or clients meeting more stringent parameters in terms of presence, size and spread. The market making schemes put in place by trading venues should therefore clearly indicate the conditions for accessing incentives and should take into account

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the effective contribution to the liquidity in the trading venue measured in terms of presence, size and spread by the participants in the schemes.

(10) In order to prevent divergent application of this Regulation and to ensure fair and non-discriminatory implementation of market making schemes, it is crucial that all members of, participants in and clients of a trading venue are informed in a coordinated manner of the occurrence of exceptional circumstances. It is therefore necessary to specify the communication obligations of the trading venues in such exceptional circumstances.

(11) For reasons of consistency and in order to ensure the smooth functioning of the financial markets, it is necessary that the provisions laid down in this Regulation and the related national provisions transposing Directive 2014/65/EU apply from the same date.

(12) This Regulation is based on the draft regulatory technical standards submitted by the European Securities and Markets Authority to the Commission.

(13) The European Securities and Markets Authority has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Securities and Markets Stakeholder Group established by Article 37 of Regulation (EU) No 1095/2010 of the European Parliament and of the Council[(2)],

HAS ADOPTED THIS REGULATION:

Article 1

Obligation for investment firms to enter into a market making agreement

1 Investment firms shall enter into a market making agreement regarding the financial instrument or instruments in which they pursue a market making strategy with the trading venue or venues at which this strategy takes place where, during half of the trading days over a one month period, in execution of the market making strategy, they:

a post firm, simultaneous two-way quotes of comparable size and competitive prices

b deal on their own account in at least one financial instrument on one trading venue for at least 50 % of the daily trading hours of continuous trading at the respective trading venue, excluding opening and closing auctions.

2 For the purposes of paragraph 1:

a a quote shall be deemed to be a firm quote where it includes orders and quotes that under the rules of a trading venue can be matched against an opposite order or quote;

b quotes shall be deemed simultaneous two-way quotes if they are posted in such a way that both the bid and the ask-price are present in the order book at the same time;

c two quotes shall be deemed of comparable size when their sizes do not diverge by more than 50 % from each other;

d quotes shall be deemed to have competitive prices where they are posted at or within the maximum bid-ask range set by the trading venue and imposed upon every investment firm that has signed a market making agreement with that trading venue.

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Article 2

Content of market making agreements

1 The content of a binding written agreement referred to in Article 17(3)(b) and Article 48(2) of Directive 2014/65/EU shall include at least:

a the financial instrument or instruments covered by the agreement;

b the minimum obligations to be met by the investment firm in terms of presence, size and spread that shall require at least posting firm, simultaneous two-way quotes of comparable size and competitive prices in at least one financial instrument on the trading venue for at least 50 % of daily trading hours of during which continuous trading takes place excluding opening and closing auctions and calculated for each trading day;

c where appropriate, the terms of the applicable market making scheme;

d the obligations of the investment firm in relation to the resumption of trading after volatility interruptions;

e the surveillance, compliance and audit obligations of the investment firm enabling it to monitor its market making activity;

f the obligation to flag firm quotes submitted to the trading venue under the market making agreement in order to distinguish those quotes from other order flows;

g the obligation to maintain records of firm quotes and transactions relating to the market making activities of the investment firm, which are clearly distinguished from other trading activities and to make those records available to the trading venue and the competent authority upon request.

2 Trading venues shall continuously monitor the effective compliance of the relevant investment firms with the market making agreements.

Article 3

Exceptional circumstances

The obligation for investment firms to provide liquidity on a regular and predictable basis laid down in Article 17(3)(a) of Directive 2014/65/EU shall not apply in any of the following exceptional circumstances:

(a) a situation of extreme volatility triggering volatility mechanisms for the majority of financial instruments or underlyings of financial instruments traded on a trading segment within the trading venue in relation to which the obligation to sign a market making agreement applies;

(b) war, industrial action, civil unrest or cyber sabotage;

(c) disorderly trading conditions where the maintenance of fair, orderly and transparent execution of trades is compromised, and evidence of any of the following is provided:

(i) the performance of the trading venue's system being significantly affected by delays and interruptions;

(ii) multiple erroneous orders or transactions;

(iii) the capacity of a trading venue to provide services becoming insufficient;