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From:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
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To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union

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Subject:	COMMISSION DELEGATED REGULATION (EU) .../... of 8.6.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the annual publication by investment firms of information on the identity of execution venues and on the quality of execution

Delegations will find attached document C(2016) 3337 final.

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COMMISSION DELEGATED REGULATION (EU) .../...

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supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the annual publication by investment firms of information on the identity of execution venues and on the quality of execution

(Text with EEA relevance)

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE DELEGATED ACT

Directive 2014/65/EU in financial instruments (MiFID II) requires investment firms who execute client orders to summarise and make public on an annual basis, for each class of financial instruments the top five execution venues in terms of trading volumes where they executed client orders in the preceding year and information on the quality of execution obtained.

Article 27(10)(b) of MiFID II empowers the Commission to adopt, following submission of a draft regulatory technical standard by the European Securities and Markets Authority (ESMA), a delegated Regulation further specifying the content and the format of information on the top five execution venues and on the quality of execution.

The draft regulatory technical standards were submitted to the Commission on 28 September 2015. In accordance with Article 10(1) of Regulation No (EU) 1095/2010 establishing ESMA, the Commission shall decide within three months of receipt of the draft standards whether to endorse them. The Commission may also endorse the draft standards in part only, or with amendments, where the Union's interests so require, having regard to the specific procedure laid down in those Articles.

2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT

In accordance with Article 10 of the Regulation (EU) 1095/2010 ESMA has carried out a public consultation on the draft regulatory technical standards¹. The consultation paper was published on 19 December 2014 on ESMA website and the consultation closed on 2 March 2015. In addition, ESMA sought the views of the Securities and Markets Stakeholder Group (MSG) established in accordance with Article 37 of the ESMA Regulation. The MSG chose not to provide advice on these issues due to the technical nature of the standards.

Together with the draft technical standards, and in accordance with the third subparagraph of Article 10(1) of Regulation (EU) No 1095/2010, the ESMA has submitted its impact assessment, including the analysis of costs and benefits related to the draft technical standards. This analysis is available at http://www.esma.europa.eu/system/files/2015-esma-1464_annex_ii_-_cba_-_draft_rts_and_its_on_mifid_ii_and_mifir.pdf.

3. LEGAL ELEMENTS OF THE DELEGATED ACT

This Delegated Regulation specifies the content and the format of information on the top five execution venues in terms of trading volumes where they executed client orders in the preceding year and on the quality of execution to be published by

¹ ESMA/2014/1570. The ESMA Consultation Paper (CP) on MiFID/MiFIR technical standards was published on 19 December 2014. The consultation period closed on 2 March 2015.

investment firms. This is essential to improve clients' understanding and scrutiny over the execution quality. Article 1 sets out the subject matter. This Regulation lays down rules on the content and the format of information to be published by investment firms on an annual basis in relation to client orders executed on trading venues, systematic internalisers, market makers or other liquidity providers or entities that perform a similar function to those performed by any of the foregoing in a third country.

Article 2 contains definitions of the terms 'passive order', 'aggressive order' and 'directed order' for the purposes of this Regulation.

Article 3 lays down the content of the information on the top five execution venues and the quality of execution. Investment firms are required to publish information on the top five execution venues for each class of financial instruments. Specifically, the firms must publish information about the volume and number of orders executed on each execution venue so that investors may be able to form an opinion as to the flow of client orders from the firm to execution venues. To prevent potentially market-sensitive disclosures on the volume of business of the investment firms, the execution volume and the number of executed orders should be expressed as percentage of the total volumes and the total number of orders executed for each class of financial instruments.

Given the differences in how firms obtain the best possible result for retail clients as compared to professional clients, the information on the top five execution venues must be provided distinctly for retail and professional clients. Further, due to the specific nature of securities financing transactions, firms executing these transactions should make public the top five execution venues in a separate report.

Investment firms are also required to publish an assessment of execution quality obtained on all execution venues used by the firm. In particular, investment firms must publish for each class of financial instruments a summary of the analysis and conclusions they draw from the detailed monitoring of the quality of execution obtained on the execution venues. This information will allow investors to assess the quality of execution and will help them to assess the effectiveness of the monitoring of execution policies carried out by investment firms.

Article 4 lays down rules for the format and publication of the information required under this Regulation.

Investment firms are required to publish the information on the top five execution venues on their websites, by filling out relevant templates. The summary of the analysis and conclusions investment firms draw from their detailed monitoring of the quality of execution venues shall be published by investment firms on their websites in an electronic format.

COMMISSION DELEGATED REGULATION (EU) .../...

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supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the annual publication by investment firms of information on the identity of execution venues and on the quality of execution

(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 on markets in financial instruments and amending Directive 2004/92/EC and Directive 2011/61/EU², and in particular point (b) of the first subparagraph of Article 27(10),

Whereas:

- (1) It is essential to enable the public and investors to evaluate the quality of an investment firm's execution practices and to identify the top five execution venues in terms of trading volumes where investment firms executed client orders in the preceding year. In order to make meaningful comparisons and analyse the choice of top five execution venues it is necessary that information is published by investment firms specifically in respect of each class of financial instruments. In order to be able to fully evaluate the order flow of client orders to execution venues, investors and the public should be able to clearly identify if the investment firm itself was one of the top five execution venues for each class of financial instrument.
- (2) In order to fully assess the extent of the quality of execution being obtained on execution venues used by investment firms to execute client orders, including execution venues in third countries, it is appropriate that investment firms publish information required under this Regulation in relation to trading venues, market makers or other liquidity providers or any entity that performs a similar function in a third country to the functions performed by any of the foregoing.
- (3) In order to provide precise and comparable information, it is necessary to set out classes of financial instruments based on their characteristics relevant for publication purposes. A class of financial instruments should be narrow enough to reveal differences in order execution behaviour between classes but at the same time broad enough to ensure that the reporting obligation on investment firms is proportionate. Given the breadth of the equity class of financial instruments, it is appropriate to

² OJ L 173, 12.6.2014, p. 349.

divide this class into subclasses based on liquidity. As liquidity is an essential factor governing execution behaviours and as execution venues are often competing to attract flows of the most frequently traded stocks, it is appropriate that equity instruments are classified according to their liquidity as determined under the tick size regime as set out in Directive 2014/65/EU of the European Parliament and the Council.

- (4) When publishing the identity of the top five execution venues on which they execute client orders it is appropriate for investment firms to publish information on the volume and number of orders executed on each execution venue, so that investors may be able to form an opinion as to the flow of client orders from the firm to execution venue. Where, for one or several classes of financial instruments, an investment firm only executes a very small number of orders, information on the top five execution venues would not be very meaningful nor representative of order execution arrangements. It is therefore appropriate to require investment firms to clearly indicate the classes of financial instruments for which they execute a very small number of orders.
- (5) To prevent potentially market sensitive disclosures on the volume of business being conducted by the investment firm, the volume of execution and the number of executed orders should be expressed as a percentage of the investment firm's total execution volumes and total number of executed orders in that class of financial instrument, respectively, rather than as absolute values.
- (6) It is appropriate to require investment firms to publish information which is relevant to their order execution behaviour. To ensure that investment firms are not held accountable for order execution decisions for which they are not responsible, it is appropriate for investment firms to disclose the percentage of orders executed on each of the top five execution venues where the choice of execution venue has been specified by clients.
- (7) There are several factors which may potentially influence the order execution behaviour of investment firms such as close links between investment firms and execution venues. Given the potential materiality of these factors it is appropriate to require analysis of such factors in assessing the quality of execution obtained on all execution venues.
- (8) The different order types can be an important factor in explaining how and why investment firms execute orders on a given execution venue. It may also impact the way an investment firm will set its execution strategies, including programming of smart order routers to meet the specific objectives of those orders. It is therefore appropriate that a distinction between the different categories of order types be clearly marked in the report.
- (9) In order to properly analyse information it is important that users are in a position to differentiate between execution venues used for professional client orders and execution venues used for retail client orders, given the notable differences in how investment firms obtain the best possible result for retail clients as compared to professional clients, namely that investment firms must predominantly assess the factors of price and cost when executing orders from retail clients. Therefore it is appropriate that information on the top five execution venues be provided separately

for retail clients and for professional clients respectively, permitting a qualitative assessment to be made of the order flow to such venues.

- (10) In order to comply with the legal obligation of best execution, investment firms, when applying the criteria for best execution for professional clients, will typically not use the same execution venues for securities financing transactions (SFTs) and other transactions. This is because the SFTs are used as a source of funding subject to a commitment that the borrower will return equivalent securities on a future date and the terms of SFTs are typically defined bilaterally between the counterparties ahead of the execution. Therefore, the choice of execution venues for SFTs is more limited than in the case of other transactions, given that it depends on the particular terms defined in advance between the counterparties and on whether there is a specific demand on those execution venues for the financial instruments involved. It is therefore appropriate that investment firms summarise and make public the top five execution venues in terms of trading volumes where they executed SFTs in a separate report so that that a qualitative assessment can be made of the order flow to such venues. Due to the specific nature of SFTs, and given that their large size would likely distort the more representative set of client transactions (namely, those not involving SFTs), it is also necessary to exclude them from the tables concerning the top five execution venues on which investment firms execute other client orders
- (11) It is appropriate that investment firms should publish an assessment of quality of execution obtained on all venues used by the firm. This information will provide a clear picture of the execution strategies and tools used to assess the quality of execution obtained on those venues. This information will also allow investors to assess the effectiveness of the monitoring carried out by investment firms in relation to those execution venues.
- (12) In specifically assessing the quality of execution obtained on all execution venues in relation to cost, it is appropriate that an investment firm also performs an analysis of the arrangements it has with these venues in relation to payments made or received and to discounts, rebates or non-monetary benefits received. Such an assessment should also allow the public to consider how such arrangements impact the costs faced by the investor and how they comply with Article 27(2) of Directive 2004/65/EC.
- (13) It is also appropriate to determine the scope of such publication and its essential features, including the use that investment firms make of the data on execution quality available from execution venues under Commission Delegated Regulation (EU) .../...³
- (14) Information on identity of execution venues and on the quality of execution should be published annually and should refer to order execution behaviour for each class of financial instruments in order to capture relevant changes within the preceding calendar year.

³ Commission Delegated Regulation (EU) .../.. supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards concerning the data to be published by execution venues on the quality of execution of transactions (OJ L.. – to be inserted before publication)

- (15) Investment firms should not be prevented from adopting an additional level of reporting which is more granular, provided that in such case the additional report complements and does not replace what is required under this Regulation.
- (16) 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.
- (17) This Regulation is based on the draft regulatory technical standards submitted by the European Securities and Markets Authority (ESMA) to the Commission.
- (18) ESMA 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 Council⁴,

HAS ADOPTED THIS REGULATION:

Article 1
Subject matter

This Regulation lays down rules on the content and the format of information to be published by investment firms on an annual basis in relation to client orders executed on trading venues, systematic internalisers, market makers or other liquidity providers or entities that perform a similar function to those performed by any of the foregoing in a third country.

Article 2
Definitions

- (a) ‘Passive order’ means an order entered into the order book that provided liquidity;
- (b) ‘Aggressive order’ means an order entered into the order book that took liquidity;
- (c) ‘Directed order’ means an order where a specific execution venue was specified by the client prior to the execution of the order.

Article 3
Information on the top five execution venues and quality of execution obtained

1. Investment firms shall publish the top five execution venues in terms of trading volumes for all executed client orders per class of financial instruments referred to in Annex I. Information regarding retail clients shall be published in the format set out

⁴ Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

in Table 1 of Annex II and information regarding professional clients shall be published in the format set out in Table 2 of Annex II. The publication shall exclude orders in Securities Financing Transactions (SFTs) and shall contain the following information:

- (a) class of financial instruments;
- (b) venue name and identifier;
- (c) volume of client orders executed on that execution venue expressed as a percentage of total executed volume;
- (d) number of client orders executed on that execution venue expressed as a percentage of total executed orders;
- (e) percentage of the executed orders referred to in point (d) that were passive and aggressive orders;
- (f) percentage of orders referred to in point (d) that were directed orders;
- (g) confirmation of whether it has executed an average of less than one trade per business day in the previous year in that class of financial instruments.

2. Investment firms shall publish the top five execution venues in terms of trading volumes for all executed client orders in SFTs for class of financial instruments referred to in Annex I in the format set out in Table 3 of Annex II. The publication shall contain the following information:

- (a) volume of client orders executed on that execution venue expressed as a percentage of total executed volume;
- (b) number of client orders executed on that execution venue expressed as a percentage of total executed orders;
- (c) confirmation of whether the investment firm has executed an average of less than one trade per business day in the previous year in that class of financial instruments.

3. Investment firms shall publish for each class of financial instruments, a summary of the analysis and conclusions they draw from their detailed monitoring of the quality of execution obtained on the execution venues where they executed all client orders in the previous year. The information shall include:

- (a) an explanation of the relative importance the firm gave to the execution factors of price, costs, speed, likelihood of execution or any other consideration including qualitative factors when assessing the quality of execution;
- (b) a description of any close links, conflicts of interests, and common ownerships with respect to any execution venues used to execute orders;
- (c) a description of any specific arrangements with any execution venues regarding payments made or received, discounts, rebates or non-monetary benefits received;

- (d) an explanation of the factors that led to a change in the list of execution venues listed in the firm's execution policy, if such a change occurred;
- (e) an explanation of how order execution differs according to client categorisation, where the firm treats categories of clients differently and where it may affect the order execution arrangements;
- (f) an explanation of whether other criteria were given precedence over immediate price and cost when executing retail client orders and how these other criteria were instrumental in delivering the best possible result in terms of the total consideration to the client;
- (g) an explanation of how the investment firm has used any data or tools relating to the quality of execution, including any data published under Commission Delegated Regulation (EU) .../...to be inserted before publication [RTS 27];
- (h) where applicable, an explanation of how the investment firm has used output of a consolidated tape provider established under Article 65 of Directive 2014/65/EU.

Article 4

Format

Investment firms shall publish the information required in accordance with Article 3(1) and 3(2) on their websites, by filling in the templates set out in Annex II, in a machine-readable electronic format, available for downloading by the public and the information required in accordance with Article 3(3) shall be published on their websites in an electronic format available for downloading by the public.

Article 5

Entry into force and application

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

It shall apply from the date that appears first in the second subparagraph of Article 93(1) of Directive 2014/65/EU

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 8.6.2016

*For the Commission
The President
Jean-Claude JUNCKER*