Deutsche Börse Group Response

to EBA/CP/2021/42

“Draft Guidelines on liquidity requirements exemption for investment firms under Article 43 (4) of Regulation (EU) 2019/2033”

published for consultation on 10 December 2021

Eschborn, 9 March 2022

A. Introduction

Deutsche Börse Group ("DBG") welcomes the opportunity to comment on the European Banking Authority's ("EBA") consultation paper "Draft Guidelines on liquidity requirements exemption for investment firms under Article 43 (4) of Regulation (EU) 2019/2033" – EBA/CP/2021/42 – issued on 10 December 2021 (in the following referred to as "Draft Guidelines").

DBG is operating in the area of financial markets along the complete chain of trading, clearing, settlement and custody for securities, derivatives and other financial instruments and as such acts as a provider of regulated financial market infrastructures.

The following three legal entities are in scope of Regulation (EU) 2019/2033 (Investment Firm Regulation – "IFR") within DBG: 360 Treasury Systems AG ("360T") is licensed as a Multilateral Trading Facility ("MTF") providing trading solutions for FX market participants and classifies as a class 2 investment firm, Eurex Securities Transactions Services GmbH ("ESTS") which classifies as a class 2 investment firm as well and is acting as a Buy-in Agent executing orders on behalf of clients and Eurex Repo GmbH ("ExR") which classifies as a class 3 investment firm and is an operator of a MTF.

As investment firms are generally exposed to different levels of liquidity risk depending on their size and nature of activities, the liquidity requirements set out in the IFR follow the proportionality principle. Consequently, investment firms which are classified as small and non-interconnected in accordance with Article 12 IFR ("class 3 investment firms") and which are not exposed to liquidity risks, can be exempted from liquidity requirements if their national competent authority grants permission (second subparagraph of Article 43 (1) IFR).

We welcome EBA's mandate arising from Article 43 (4) IFR to issue guidelines specifying the criteria which the national competent authorities may take into account when exempting investment firms that meet the conditions for qualifying as a class 3 investment firm from the liquidity requirements set out in Article 43 (1) IFR as these aim to promote a harmonised application of the assessment of exemption and, thus, counteract unequal treatment of investment firms within the European Union seeking exemption from liquidity requirements.

While we generally consider a list of investment services and activities which principally do not create liquidity risks as plausible to derive eligibility for exemption as set in paragraph 13 of the Draft Guidelines, we would like to point out that the categorical exclusion of some investment firms from the possible exemption is not in line with EBA's mandate set out in Article 43 (4) IFR. The categorical exclusion of some class 3 investment firms contradicts the intention of the legislator stated in the second subparagraph of Article 43 (1) IFR as the respective requirement generally allows any class 3 investment firm to be exempted regardless of the investment service it provides. Against this background, we consider the limitation of a possible exemption to only dedicated class 3 investment firms an exceedance of EBAs mandate stipulated in Article 43 (4) IFR.

The list of identified investment services and activities which generally do not give rise to liquidity risks is not to be considered exhaustive as it does not conversely allow to draw conclusions that any other investment service or activity, not captured on the list, necessarily creates liquidity risk and should, therefore, be excluded from any potential exemption under Article 43 (1) IFR. Having said that, we see no reason for categorically excluding operators of a MTF / an OTF. Therefore, we recommend to either consider the exemption for all investment firms – regardless of the investment service and activities provided – to be decided on a case-by-case basis as the activities of each investment firm can vary in nature, size and risk taken within the provision of a specific investment service. Alternatively, we propose to include additional investment firms in the list of eligible investment firms for exemptions as considered by EBA as Option 1b in the Draft Guidelines regarding the determination of the scope of application.

Finally, we would like to note that the relevant information which should be used by national competent authorities for assessing the possibility of exemption from liquidity requirements under Article 43 (1) IFR as outlined in section 4.4 of the Draft Guidelines, is generally clear but will most probably not be available. Class 3 investment firms are generally not required to maintain the respective information, i.e., ILAAP and ICAAP as well as winding-down plans. Therefore, we encourage EBA to continue specifying further relevant information.

This document at hand outlines our comments to Question 1 and Questions 2 in the Draft Guidelines. In absence of a dedicated questions relating to sections 4.4. and 4.5 of the Draft Guidelines, we included out comments regarding the information to be provided by investment firms for the purpose of the assessment for the exemption in our answer to Question 2.

B. Comments

Question 1: With regard to the investment services and activities eligible for the exemption listed in paragraph 13, do you consider that other services and activities should be included? If yes, please provide an explanation?

The second subparagraph of Article 43 (1) IFR empowers national competent authorities to exempt investment firms that qualify as a class 3 investment firm as set out in Article 12(1) IFR from liquidity requirements under Article 43 (1) IFR. Article 43 (4) IFR obliges EBA to issue guidelines specifying further the criteria which the competent authorities may take into account when exempting class 3 investment firms. As no investment services and activities were categorically excluded by the legislator in the second subparagraph of Article 43 (1) IFR, we understand that all investment firms that qualify as a class 3 investment firm are generally eligible for the exemption set out in the subparagraph of Article 43 (1) IFR.

In contrast to the second subparagraph of Article 43 (1) IFR, which generally allows competent authorities to exempt any investment firm qualifying as a class 3 investment firm from Article 43 (1) IFR, paragraph 13 of the Draft Guidelines states that only investment firms which provide specific investment services are "eligible for the exemption". As a consequence, (i) investment firms that operate a Multilateral Trading Facility ("MFT") as referred to in Annex I, Section A, point (8) of MiFID II, (ii) investment firms that operate an Organised Trading Facility (OTF) as referred to in Annex I, Section A, point (9) of MiFID II, (iii) investment firms which are dealing on own account as referred to in Annex I, Section A, point (3) of Directive 2014/65/EU ("MiFID II") and (iv) investment firms which carry out the underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis as referred to in Annex I, Section A, point (6) of MiFID II are being categorically excluded from the possibility to request exemption under Article 43 (1) IFR irrespective of their actually existing liquidity risks. While we do understand, that trading on own account and underwriting business or placing of financial instruments can result in liquidity risks, as the case may be, we lack understanding for a categorical exclusion, particularly of MTFs and OTFs.

We fully agree with EBAs approach, that competent authorities should take the respective investment firm's risk to its clients and the firm itself into account, when assessing an investment firm's request for exemption under Article 43 (1) IFR (s. paragraph 19 of the Draft Guidelines). Following this approach, we would like to point out that an investment firm operating a MTF generally does not give raise to liquidity risk as it only facilitates the exchange of financial instruments between multiple parties where buyers and sellers are paired to form a contract. The buyers and sellers do not constitute clients of the operator of the MTF such that the MTF is generally not exposed to default risks of the buyers or sellers. This said, it is unclear why EBA did not include investment firms operating a MTF into the list of investment firms which are eligible for exemption from Article 43 (1) IFR.

Similarly, investment firms operating an OTF generally do not give raise to liquidity risk in a manner which would justify the categorical exclusion through paragraph 13 of the Draft Guidelines.

We understand that investment firm which are dealing on own account as referred to in Annex I, Section A, point (3) MiFID II and/or carry out the underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis as referred to in Annex I, Section A, point (6) MiFID II may pose a higher liquidity risks than other investment services. Nevertheless, investment firms which offer these services have not been excluded from the scope of potential addressees of the second subparagraph of Article 43 (1) IFR and should, therefore, neither be categorically excluded via a level 2 text.

In our view, the categorical exclusion of specific investment firms as eligible for exemption from the liquidity requirements under Article 43 (1) IFR – although qualifying as a class 3 investment firm –

does not reflect the intention of the legislator and is not consistent with the general objectives of the prudential investment firm regime. Paragraph 13 of the Draft Guidelines exceeds EBAs mandate as specified in Article 43(3) IFR as it limits the right of certain class 3 investment firms to benefit from a possible exemption as well as it limits competent authorities' right to exempt any class 3 investment firm as considered appropriate and anchored in the second subparagraph of Article 43 (1) IFR. Therefore, we strongly encourage EBA to reconsider paragraph 13 of the Draft Guidelines to avoid general exemption of *any* class 3 investment firms, most notably MTFs. Instead of providing an exhaustive list of investment firms eligible for an exemption under Article 43 (1) IFR, we suggest providing guidance to competent authorities when performing a case-by-case assessment by applying the general principles of proportionality, whereas EBA might encouraged competent authorities to exercise particular caution when assessing investment firms performing services potentially relating to liquidity risk. We, therefore, suggest amending paragraph 13 of the Draft Guidelines as follows:

"*13**. In accordance with the second subparagraph of Article 43 (1) of Regulation (EU) 2019/2033 (IFR), competent authorities should consider any investment firm qualifying as small and non-interconnected as set out in Article 12 (1) IFR*** ~~*F*~~*for the exemption from the liquidity requirement under Article 43 (1)* ***IFR.*** ~~*of Regulation (EU) 2019/2033, competent authorities should only consider investment firms that provide the following limited set of investment services:*~~

~~*i) reception and transmission of orders in relation to one or more financial instruments as referred to in Annex I, Section A, point (1) of Directive 2014/65/EU;*~~

~~*ii) execution of orders on behalf of clients as referred to in Annex I, Section A, point (2) of the Directive 2014/65/EU;*~~

~~*iii) portfolio management as referred to in Annex I, Section A, point (4) of Directive 2014/65/EU;*~~

~~*iv) investment advice as referred to in Annex I, Section A, point (5) of Directive 2014/65/EU;*~~

~~*v) placing of financial instruments without a firm commitment basis as referred to in Annex I, Section A, point (7) of Directive 2014/65/EU*~~;"

Competent authorities should take into account the investment firms' size and nature of activities, such as the type of investment services as set out in Annex I, Section A of Directive (EU) 2014/65 provided by the investment firms. When assessing the requested exemption for investment firms offering investment services in accordance with Annex I, Section A, point (3) and point (6) of Directive (EU) 2014/65, competent authorities should particularly consider that liquidity risks might result from the provision of these investment services."

In any case, we urge EBA (at least) to consider the inclusion of the operation of a MTF as an investment service eligible for the exemption as listed in paragraph 13 of the draft Guidelines.

Question 2: Do you consider that the exemption based on investment firms' financial resources needs for its orderly wind down is sufficient?

We support EBAs approach to base the assessment of the exemption on the investment firms' financial resources needs for its orderly wind down. Investment firms should have sufficient liquid financial resources in the wind down phase to prevent a collapse in a disorderly manner which could cause damage to its clients and further market participants. Nevertheless, we would like to highlight, that an assessment of an investment firms' needs for liquid financial resources both under normal and stress conditions might jeopardise the new IFR's target of simplifying the prudential framework for investment firms particularly under consideration that only class 3 investment firms are allowed to request the exemption under Article 43 (1) IFR.

The burden of providing competent authorities with the relevant information for assessing eligibility of the exemption should not exceed the benefits resulting from the potential exemption.

Moreover, while we generally consider the relevant information to be provided by investment firms to competent authorities, for assessing whether an investment firm is exposed to liquidity risk, as appropriate and clear, we think that some relevant information will most probably not be available.

According to paragraph 22 of the Draft Guidelines, "competent authorities should use all relevant information, such as, where available ILAAP and ICAAP conclusions for the purpose of the assessment for exemption. We would like to highlight that most class 3 investment firms will not be able to provide this information as they are generally not required to apply the requirements for internal capital and liquid assessment as set out in Article 24 of Directive (EU) 2019/2034 (Investment firm Directive – "IFD"). Investment firms qualifying as a class 3 investment firm only apply the requirements of Article 24 IFD if explicitly requested by the competent authority and, solely, to the extent the competent authority deems it to be appropriate. This said, we recommend EBA to consider dropping ILAAP and ICAAP conclusions from the list of relevant information for the purpose of assessing exemptions.

Furthermore, EBA states that competent authorities should use the investment firm's wind down plans to assess the exemption from Article 43 (1) IFR (paragraph 22 of the Draft Guidelines). We recognise that the wind down plans of an investment firm, where available, can be considered as a relevant information in the context of assessing the exemption from liquidity requirement. However, we would like to highlight that investment firms are generally in scope of the national transposition of Directive (EU) 2014/59 (Bank Recovery and Resolution Directive – "BRRD"). According to Article 10 (1) BRRD it is the resolution authority's obligation to draw up a resolution plan (which can be understood to be the wind-down plan) for each institution that is not part of a group subject to consolidated. The same applies on a group level, where the responsibility of drawing the group resolution plan lies with the resolution authority (Article 12 (1) BRRD) as well. Although investment firms would be required to support resolution authorities in drafting those plans, investment firms will most likely not draft such plans prior to being requested to do so. Moreover, minimum own funds requirements for class 3 investment firms are at least as one quarter of their fixed overheads requirements (s. Article 11 in conjunction with Article 13 IFR), which shall already ensure properly winding down of an investment firm. Therefore, we suggest EBA to delete the "wind down plan" as a relevant information to be requested by investment firms for the assessment for exemption. Instead of requiring investment firms to provide "*any information of evidence*", we encourage EBA to continue specifying further relevant information.

Finally, we would like to note, that the used terminology in paragraph 23 referring to granting exemption in case the investment firm is "not exposed to liquidity risk" might be misleading. We recommend EBA to consider re-phrasing the wording "[…] to ensure that the respective investment firm's activities and services do not give rise to liquidity risk".

***

We are at your disposal to discuss the issues raised and proposals made if deemed useful.