10 March 2022

FIA EPTA response to the European Banking Association (EBA) Consultation Paper on the Draft Regulatory Technical Standards on the specific liquidity measurement for investment firms under Article 42(6) of Directive (EU) 2019/2034

Introduction:

The European Principal Traders Association (FIA EPTA) welcomes the opportunity to respond to the EBA Consultation Paper on the Draft Regulatory Technical Standards on the specific liquidity measurement for investment firms under Article 42(6) of Directive (EU) 2019/2034.

FIA EPTA represents 26 independent European Principal Trading Firms (PTFs) which deal on own account, using their own money for their own risk, to provide liquidity and immediate risk transfer in exchange-traded and centrally-cleared markets for a wide range of financial instruments, including shares, options, futures, bonds and ETFs. FIA EPTA's members are based in the Czech Republic, Germany, Ireland, The Netherlands, and the UK.

Our members are independent market makers and providers of liquidity and risk transfer on trading venues and to end-investors across Europe. Market making and liquidity provision (also referred to as principal trading or dealing on own account) is a distinct activity that is undertaken by non-systemic investment firms rather than banks, in a highly dispersed and varied ecosystem of independent Principal Trading Firms. These firms operate in an innovative and competitive fashion leading to a vibrant, dynamic and diverse ecosystem which massively reduces interconnectedness and increases substitutability. This fundamentally reduces systemic risk whilst improving market quality and lowering costs for retail and institutional investors alike.

We would welcome the opportunity to provide further background to the EBA on the issues raised in our response.

Question 1: Where respondents are of the view that the draft RTS should define other elements of liquidity risk, comments are most helpful when they clearly describe the alternative elements of liquidity risk that competent authorities may use to assess whether liquidity risk is adequately covered by Part Five of IFR.

FIA EPTA would like to clarify that the concept of a liquidity mismatch between liquid assets and liquidity requirements, which is common for specific (asset management) business models like pension funds or investment funds, does not really apply to a market making model with a trading book and taking place in a CCP cleared environment or being governed by netting agreements.

Taking the example of an investment fund, we understand that there may be instances of a structural mismatch between the dealing frequency of units in these funds and the underlying assets in which the fund invests. Such a liquidity mismatch makes redemption requests harder to meet which could ultimately lead to the temporary suspension of dealings in the fund.

By contrast, typical trading books held by market makers who deal on own account, are very different. For example, where a market making firm holds derivatives positions, these are typically traded under an ISDA Master Netting Agreement or Master Clearing Agreement that creates a single contract where transactions can offset each other. All trades are, therefore, aggregated and replaced with a single net amount. That does mean that derivatives positions are managed on a portfolio basis.

Derivatives are also carried at fair value (mark-to-market) and collateral is posted daily with the General Clearing Member (GCM) on a net basis.

Funding requirements resulting from margin calls from the GCM are therefore calculated on a net basis. Therefore, assets in a market making firm's trading books do not represent resources to creditors and derivatives payables do not represent claims. Instead, the net amount would be a net payable or a net receivable and only margin requirement on the net portfolio would represent a funding requirement.

Based on the above considerations, we would suggest to the EBA to rephrase Article 1(4)(b) as follows:

> *(b) take into account the available historical data on liquidity mismatches between liquid assets and liquidity requirements, the historical trends in liquidity and the observed material variations of liquid assets and liquidity requirements for a period of time over which, according to the competent authority, sufficient information is available.* ***<u>The Competent Authority shall also take into account, when relevant, the existence of netting agreements and risk mitigation mechanisms used by a General Clearing Member, Prime Broker and/or Central Counterparty and to which the investment firm is subject.</u>***