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Van: [redacted]@baml.com]
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CC: [redacted]
Onderwerp: Bank of America Merrill Lynch - MiFID position paper
Bijlagen: BofAML key points on European Commission Proposal for MiFIR_MiFID 2.pdf

Beste [redacted]

Om een bijdrage te leveren aan de huidige discussie aangaande de MiFID review, heb ik onze position paper bij deze mail gevoegd. Je zult hierin de prioriteiten (op pagina 1-2 hebben we ze opgesomd) van BoAML vinden en een korte uitleg.

Wij zouden graag eens met jou (en/of je collega's op Financien) van gedachten wisselen, maar aangezien dit dossier (nog) geen prioriteit lijkt te zijn voor de Denen, hoor ik graag van je wanneer je denkt dat we dit het beste kunnen doen.

Fijn weekend!

Mvg,

[redacted]

Government Affairs

Bank of America Merrill Lynch

Square de Meeus 38/40
B-1000 Brussels
Belgium

[redacted]

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Bank of America Merrill Lynch

6th February 2012

Bank of America Merrill Lynch ("BofAML") key points on the the European Commission Proposal for MIFIR/MIFID 2 published 20 October 2011 (the "Proposal")

Bank of America is one of the world's largest financial institutions, serving individual consumers, small and middle-market businesses and large corporations with a full range of banking, investing, asset management and other financial and risk-management products and services. Following the merger with Merrill Lynch on 1 January 2009, Bank of America Merrill Lynch became the largest brokerage in the world and now serves clients and customers in more than 100 countries.

The company is a long-established participant in the European markets, with a presence since 1922. The company employs over 15,000 people in Europe, the Middle East and Africa (EMEA), and has offices in Bahrain, Belgium, France, Germany, Greece, Ireland, Israel, Italy, Lebanon, Luxembourg, Monaco, the Netherlands, Russia, Saudi Arabia, South Africa, Spain, Switzerland, Turkey, the UAE and the United Kingdom.

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Bank of America Merrill Lynch (BofAML) is supportive of the MiFID's aims of contributing to more integrated and liquid financial markets and the establishment of a single rulebook for EU financial markets, in particular, aspects that allow for a reduction of costs for market participants and the improvement of conditions of access into the EU financial markets, as well as for the delivery of better services for investors. We are also very supportive of the aims of this Proposal in adapting existing regulation to recent developments and innovation in both technology and financial products. Finally, we agree with the MiFID's aims of not being overly prescriptive as to where trades are executed and permitting flexibility and choice for investors as to where and how they wish to execute trades.

We comment, below, where various provisions require particular focus so as to not conflict with these aims. Areas of particular interest to BofAML, discussed briefly in this paper are:

- Amendments to market structures in MiFID 2: we comment on provisions for Organised Trading Facility (OTF) operators' provision of principal capital and the definition of Over the Counter (OTC) trading and how this interacts with the Systematic Internaliser (SI) framework
- [redacted]
- Enhanced organizational requirements to safeguard the efficient functioning and integrity of the markets under MiFID 2: we discuss the proposed liquidity requirements for algorithmic market participants
- [redacted]
- Increased and more efficient data consolidation under MiFID 2: in particular, we support the proposals to enhance cost efficiency in the provision of European data, and the introduction of a consolidated post-trade tape for European equities
- [redacted]
- [redacted]
- Commodities: we comment on the provisions for position reporting, position limits, and emissions as financial products

Bank of America, N.A.
2 King Edward Street, London EC1A 1HQ
Registered branch in England at 2 King Edward Street, London EC1A 1HQ, United Kingdom no. FC 2984
Authorised and regulated by the Financial Services Authority
V.A.T. Registration no. GB 245 1224 93. London Telex: 888412/3
Incorporated in U.S.A. with Limited Liability. Chartered under U.S. law by the office of the Comptroller of Currency. Charter no. 13044
Head office: 101 S. Tryon Street, Charlotte, North Carolina, U.S.A.

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- Third Country Regimes under MiFID 2 and MiFIR: we support the proposals for access for third country firms and request clarification on certain provisions such as counterparty type definitions and access to services in third country firms
- Finally, we make a general comment on the need for global harmonization with similar proposals being implemented in other jurisdictions, in particular in the United States

1. Upgrades to the market infrastructure framework under MiFID 2

We support the Commission's view that the MiFID framework should be amended so as to include cash equity broker crossing systems within the framework of regulated venues. Such systems currently provide valuable services to clients. In addition, we support the allowance of an OTF operator to apply discretion as to the OTF's participants.

OTFs and principal capital

With respect to Cash Equities, the proposals to prohibit execution against an OTF operator's principal capital (see Article 20 of MiFID 2) will imply a significant change to the operating model of the current broker crossing networks (which will become OTF markets), to the detriment of investor activity and the provision of liquidity. To facilitate client business, brokers often execute OTC trades with clients, using principal capital, and hedge the resulting positions also using their principal capital. Prohibiting such hedging activities of client-driven business within OTFs will limit the extent to which investors can take advantage of the liquidity and spreads available in the broker's crossing network / OTF. The net effect will be to increase the cost of providing capital to clients, and to limit clients' execution choices.

In addition, in the derivatives markets, which typically operate on the request for quote model where the terms of the proposed trade are specifically requested by the client, and are, in many cases, not standard sized, liquid, quoted contracts, the limitation on use of an OTF operators' capital could mean clients' requests will go un-filled and dealers materially reduce their facilitation of risk management for clients.

Restricting OTF trading to a pure agency capacity will severely limit the amount of activity in OTFs, impact the timeliness of execution, restrict the broad range of products currently offered on these platforms, and generally impact the provision of risk capital and pricing for clients.

The proposed conduct of business rules relating to conflict of interests management, the obligation to execute orders on terms most favourable to the client, and order handling provisions included in Articles 27 and 28 MiFID 2 can be used effectively, for OTF operators, to resolve any conflict of interests that may arise between OTF operators and clients, as an alternative to a restriction on use of proprietary capital.

OTC trading and SIs

In order to ensure that firms may offer, through a combination of OTF and SI regimes, the full range of services that clients currently value in broker crossing networks and in order to ensure that appropriate transparency regimes are established, it will be important to clarify - in addition to the points we discuss on the use of the operator's principal capital - the distinctions between trading through an OTF, trading through an SI, and trading OTC.

The current proposals raise uncertainty in relation to the treatment of hybrid and voice broking systems, particularly in respect of Derivatives (e.g. Article 24, MiFIR), which become more important at times of market stress and in the handling of particularly large or bespoke sized transactions for clients. There are specific transparency requirements for SIs; further clarity as to what constitutes OTC trading through an SI and what is allowed to be done via the "traditional" OTC trading method, will be key to determining how the specific transparency requirements apply and to retain key risk management functions provided by dealers and requested by clients, notably the handling of large-sized transactions (see the relevant definitions in Article 2 and also Articles 19 and 20 of MiFIR). In addition, we believe it is important to clarify that a firm may be a SI in relation to specific instruments only, given this term refers to the entity and not the trading platform (as is the case for the OTF definition), in order to maintain client choice.

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3. **Enhanced organizational requirements to safeguard the efficient functioning and integrity of the markets under MIFID 2**

Algorithmic trading

We agree with the Commission that any proposals must "adequately deal with the potential threats for the orderly functioning of markets arising from algorithmic and high-frequency trading" and believe that existing tools employed by trading venues such as circuit breakers, coupled with appropriate provisions on market abuse within the Market Abuse Directive and Regulation achieve this. We welcome Article 17 of MiFID 2 in this regard.

However, we believe that the additional requirements for algorithmic market participants to provide liquidity on a "regular and ongoing basis.......at all times, regardless of market conditions" contained in Article 17(3) of MiFID 2 will detract from the aims of promoting robust, stable markets and the provision of liquidity. The requirement to provide ongoing liquidity is in tension with general considerations of risk management. Furthermore, the requirement as stated contrasts with market making regimes that have developed organically in the European markets to give incentives to market makers to compensate for their liquidity commitments; without such 'quid pro quo' there is significant potential for firms such as High Frequency Traders (HFT) to materially reduce their market presence. Given that HFT currently provides approximately 40% of pan-European Equity liquidity[1], and given the positive effect such liquidity has had in terms of narrowing spreads for all market participants, the perceived benefits of the proposals must be weighed against the detrimental consequences which may result. These consequences would include traders being able to commit only to substantially wider spreads, or exiting the markets altogether – whether temporarily or permanently. As a final point, we do not believe that execution-focused algorithms (such as volume-weighted average price algorithms), offered on a widespread basis to numerous institutional clients by many broker dealers,

[1] Data source from TABB Group - figure based on notional value traded YTD 2011

are indeed compatible with posting two-sided quotes since designed solely to buy or sell as required rather than to make markets.

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Equity market transparency requirements

In relation to the equity markets, we welcome the proposals in Article 4 of MiFIR for review and harmonisation of pre-trade transparency waivers across Member States and the current emphasis on the "large-in-scale" waiver in particular. We point to the other types of waivers available currently; one waiver frequently used in the cash equities market is the "reference price" waiver. It would be important for MiFIR to acknowledge both the "large in scale waiver" but also the other pre-trade waivers which are currently used by the market.

5. Market data and data consolidation (Title V of MiFID 2)

We support the Commission's intention for data providers to make market data available at lower cost and with more consumer choice (eg pursuant to unbundling). We would emphasise the importance of establishing consistent standards within such data, and we think it would be useful for the Commission to mandate this.

In relation to the equities markets, we support the proposal to introduce a high quality and complete consolidated tape for European post-trade data, and we agree that this will be best achieved via a combination of competition amongst providers and regulatory oversight to ensure appropriate and consistent quality standards and availability of underlying data from APAs at reasonable cost. We support the proposals to focus this process initially in relation to equities and equity-like products given the clear need to improve the status quo in these markets, and the more significant challenges in appropriately tailoring any extension to a broader product set.

Bank of America Merrill Lynch

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8. Commodities

Position reporting

We are not supportive of the public disclosure of disaggregated position data in the commodities markets as we believe this may lead to increased, rather than reduced, market volatility. Hence we are encouraged by the provision for aggregated weekly disclosure only of position data contained in Article 60 of MiFID 2 which is consistent with disclosure in the US markets.

Position limits

We welcome the Commission's recognition and inclusion of alternative arrangements with regard to position limits. We feel position management is an effective tool for managing the orderliness of markets and have concerns that the imposition of position limits may result in unintended consequences that damage the markets in the form of reduced liquidity and increased volatility.

Emissions as financial products

With regard to the classification of EU emission allowances as financial products, we welcome the Commission's efforts in reducing fraudulent practice in relation to the Emission Trading Scheme. However, in defining emissions as
financial products MiFID 2 should not impose regulation on compliance buyers/participants who in the normal course of their business do not carry out any regulated activity.

9. Access for third country firms

We welcome the proposals for third country firms to be able to benefit from a European "passport". This will have a significant beneficial impact in the establishment of a harmonised regime for the access of third country firms to the European markets and vice versa, helping to create a level playing field and reducing the costs and risks associated with the management of European business. Consumers and investors will benefit from the competition this regime will encourage as it will bring opportunities to EU financial institutions arising from reciprocity. Of particular importance will be the practical implementation of the requirements for equivalence and reciprocity of third country regimes. The success of implementation of these provisions will depend on the definition of the requirements for equivalence and reciprocity – we believe they should focus on a core set of principles, or a minimum standards threshold. Where there is a risk of unintended consequences developing, such as the prevention (temporary or otherwise) of third country firms not governed by equivalent and reciprocal regimes from participating in the European markets, the provisions by which European firms may request services from firms in non-equivalent third countries at their own exclusive initiative (i.e. on a reverse solicitation basis) (see Article 36(4) of MiFIR) will be instrumental. We encourage the legislators to focus sufficient attention on ensuring that this is an effective route for accessing such services as it may be critical to firms' operations in many third countries which do not satisfy the requirements for equivalence and reciprocity. We also encourage legislators to focus on the establishment of a harmonized definition of reverse solicitation as part of the level 2 rule making process. We also await clarity on reference to Professional counterparties.

10. Global harmonisation

It is clear that a number of the proposals mirror and overlap with similar proposals being implemented in other jurisdictions and particularly in the US. Where appropriate, we would urge the applicable regulators to coordinate on a global basis in order to implement complementary and consistent requirements and standards in order to avoid duplication and conflicting requirements. For example, in relation to the transparency and reporting requirements proposed to apply to derivatives, it will be important that any such requirements are consistent with those being implemented in the US under the Dodd-Frank Wall Street Reform and Consumer Protection Act in order to avoid fragmentation of information, potential double counting of cross border transactions and unnecessary inconvenience and expense to market participants should they become subject to two overlapping but inconsistent reporting regimes. In relation to proposals for electronic platform trading of derivatives, we would again urge the regulators to coordinate in relation to cross border transactions to avoid the counterparties becoming subject to potentially conflicting requirements to trade on two different venues in respect of a single transaction. It is important for reasons of market efficiency both in trading and data collection that serious efforts are made by regulators to recognise the equivalence of trading venues and data repositories outside their territories.

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