

3 November 2017

Ms Verena Ross
Executive Director
European Securities and Markets Authority
CS 60747
103 rue de Grenelle
75345 Paris Cedex 07, France

Dear Ms Ross

Legal uncertainties arising in the context of Article 4 RTS 21 – aggregation of positions and the meaning of “control”

The role of the Financial Markets Law Committee (the "FMLC" or the "Committee") is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.

The FMLC is greatly appreciative of ESMA's continuing efforts to provide market participants with feedback on the implementation of Directive 2014/65/EU on markets in financial instruments ("MiFID II") and associated legislation via its Q&A documents.¹ In a similar vein, the FMLC requests clarification as to the operation of Article 4 of Commission Delegated Regulation (EU) 2017/591 ("RTS 21")² and the manner in which positions are to be aggregated.

The approach to aggregation in the Level 1 legislation

Article 57(1) MiFID II requires that position limits:

shall be set on the basis of all positions held by a person and those held on its behalf at an aggregate group level[...]

Article 57(12)(b) then directs ESMA to develop the methods to determine when the positions of a person are to be aggregated within a group. ESMA does so through regulatory technical standards ("RTS").

The approach to aggregation in the RTS and the meaning of “control”

Pursuant to Article 4(1) of RTS 21, a parent undertaking (that is subject to Article 57(1)) determines its net position by aggregating "its own net position" with "the net positions of each of its subsidiary undertakings". The exception to this rule occurs in respect of collective investment undertakings: Article 4(2) states that, by way of derogation, the disaggregation of the net positions of a collective investment vehicle is permitted when the parent undertaking does not in any way influence the investment decision in respect of opening, holding or closing these positions.

Taken as a whole, therefore, Article 4 of RTS 21 appears to require a parent undertaking to add the net positions of all of its subsidiary undertakings—subject to the collective investment undertaking exception—irrespective of whether such parent undertaking influences the opening, holding or closing of any of the positions of its subsidiaries.

+44 (0)20 7601 4286
contact@fmlc.org

8 Lothbury
London
EC2R 7HH
www.fmlc.org

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In recital 4 of RTS 21, however, ESMA states:

It is appropriate to only provide for aggregation at the group level if a parent undertaking can control the use of positions. [emphasis added]

One interpretation of this could be that it explains the basis for carving out collective investment scheme positions held on behalf of investors, referred to at the end of the recital. Another is that this suggests that, if control were not present, then aggregation would not be required. The recital then goes on to stipulate that:

Accordingly, parent undertakings should aggregate positions held by their subsidiaries with any positions the parent entity holds directly, in addition to subsidiaries aggregating their own positions.

This second statement, following on from the first, seems to assume that a parent/subsidiary relationship is always indicative of control. It is possible, however, that within a group structure the parent undertaking would have not be able to “control the use” of the positions of a subsidiary undertaking (for example, in the case of the parent undertaking of an investment manager of segregated portfolios). It is a matter of uncertainty, therefore, as to whether under RTS 21 the word “control” is meant as a proxy for a parent/subsidiary relationship.

Further complexity as to which entities are caught in the group for aggregation is introduced if one turns to ESMA’s MiFID II/MiFIR Consultation Paper dated 19 December 2014 (the “Consultation”). Here, when describing the methods for aggregation of a person’s positions with a group (further to its mandate in Article 57(12)(b)), ESMA notes that:

For the purpose of consistency within EU legislation, reference has been made to the definitions in EU Accounting Directive 2013/34/EU regarding entities, group structures and concepts of control. [emphasis added].³

Under Article 22(1) and (2) of Directive 2013/34/EU on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings (the “Accounting Directive”),⁴ various metrics of control are presented including, for example, where a parent undertaking has a majority of the shareholders’ or members’ voting rights in a subsidiary undertaking, or where it has the right to exercise a dominant influence over a subsidiary undertaking pursuant to a contract. Under the Accounting Directive, therefore, a parent/subsidiary relationship is—in itself—not taken as indicative of control.

The Consultation goes on to state that:

A majority of respondents agreed with ESMA’s proposal to aggregate the positions in commodity derivatives that a person holds or controls. A number of respondents discussed the precise level of ownership that may, or may not, reflect control over the activity of a subsidiary undertaking. In this respect ESMA believes that the specification of a specific percentage within MIFID II framework may provide opportunities for avoidance of the rules that alignment with the concepts expressed in the Accounting Directive do not.

ESMA proposes that the commodity derivative positions of a person should be aggregated on a ‘whole’ position basis with those that are

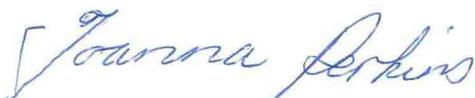
under the beneficial ownership of the position holder which means that although a firm may own a percentage of another firm it must aggregate the position in its entirety and not on a pro rata basis the position held by that firm according to the percentage of its holding. ESMA notes that this approach could lead to double counting and seeks stakeholders views on whether they consider any issues may arise from such.

Despite this discussion in the Consultation, however, direct reference to “concepts of control” or the Accounting Directive is then omitted from RTS 21.⁵

The meaning of “control” within the context of RTS 21 is, therefore, uncertain. In particular, it is unclear whether a parent undertaking is required to aggregate the positions of subsidiary undertaking where it cannot control the use of such positions, where the subsidiary is not a collective investment vehicle or the manager of a collective investment vehicle. The FMLC recommends, therefore, that ESMA provide guidance as to the meaning of “control” in this context.

I and Members of the Committee would be delighted to meet you to discuss the issues raised in this letter. Please do not hesitate to contact me to arrange such a meeting or should you require further information or assistance.

Yours sincerely,



Joanna Perkins
FMLC Chief Executive

¹ These include Q&A on MiFID II and MiFIR commodity derivatives topics, Q&A on MiFID II and MiFIR market structure topics and Q&A on MiFIR data reporting, which can be found here: https://www.esma.europa.eu/databases-library/esma-library?f%5B0%5D=im_esma_sections%3A20. ESMA has also produced helpful FAQ documents, as well as opinions and procedure papers, which are available through the same link.

² RTS 21: methodology for the calculation and the application of position limits for commodity derivatives traded on trading venues and economically equivalent OTC contracts. Commission Delegated Regulation (C(2016) 4362 final) of 1 December 2016, available at <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R0591&from=EN>.

³ ESMA Consultation Paper MiFID II/MiFIR, (ESMA 2014/1570) 19 December 2014, p.546, available at https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-1570_cp_mifid_ii.pdf.

⁴ Directive 2013/34/EU of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings (the “Accounting Directive”), available at <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32013L0034>.

⁵ Note that the definition of “control” does appear at Article 4(35)(b) MiFID II (within the definition of “close links”) and refers to Article 22(1) and (2) of the Accounting Directive.

