

Update to the Joint Banca d'Italia/Consob Communication of 5 June 2013 regarding the application of the ESMA Guidelines on the exemption for market making activities and primary market operations under Regulation (EU) 236/2012 on short selling and certain aspects of Credit Default Swaps.

Exemption for market making activities conducted outside a trading venue.

The ESMA Guidelines of 1 February 2013 ⁽¹⁾ on the exemption for market making activities and primary market operations under Regulation (EU) 236/2012 on short selling and certain aspects of credit default swaps (hereinafter the 'ESMA Guidelines' or 'Guidelines') define, *inter alia*, the requirements that must be met in order to benefit from the exemption provided for in Article 17 of Regulation (EU) 236/2012 (hereinafter 'Regulation') for market making activities in shares, sovereign bonds and financial instruments linked to shares and sovereign bonds.

Entities benefitting from the above-mentioned exemption are not subject to: (i) the restrictions on uncovered short sales of shares and sovereign debt; (ii) the ban on entering into uncovered sovereign credit default swap positions; (iii) the reporting and disclosure obligations regarding net short positions in shares; and (iv) the reporting obligation regarding net short positions in sovereign debt.

In particular, the Guidelines require that the exemption provided for in Article 17 of the Regulation (hereinafter 'exemption') be applied to only market making activities carried out in financial instruments that are, jointly:

1. included in the list of financial instruments to be considered for the calculation of net short positions; such list includes financial instruments whose underlying financial instruments are shares or sovereign debt, such as derivatives, financial indices and depositary receipts (the 'product scope' requirement); and
2. traded on a trading venue, provided that the market maker is a direct member of that trading venue and carries out, at least in part, the market making activity on that trading venue (the 'trading venue membership' requirement).

¹ ESMA 2013/158: 'Guidelines on the exemption for market making activities and primary market operations under Regulation (EU) 236/2012 of the European Parliament and the Council on short selling and certain aspects of credit default swaps'.

The interpretation of the Regulation given by the ESMA Guidelines, specifically the trading venue membership requirement, prevents entities which carry out market making activities entirely outside a trading venue from benefitting from the exemption.

The Guidelines have been applied in Italy since June 2013, as indicated in the joint Banca d'Italia/Consob communication of 5 June 2013.

However, seven years after the Regulation entered into force, there is still no harmonisation across Europe with regard to the exemption for market making activities, as national competent authorities of the main countries of the Union do not entirely comply with the ESMA Guidelines. In particular, the national competent authorities of the United Kingdom, Germany, France and, recently, Spain, allow the use of the exemption for market making activities which do not comply with the abovementioned trading venue membership requirement.

Moreover, as came to light following the peer review carried out by ESMA in 2015 ⁽²⁾, a few national competent authorities that formally declared their compliance with the Guidelines have adopted a supervisory approach which partly differs from the Guidelines.

ESMA itself, during the periodic review of the Regulation, proposed to the European Commission in its technical advice of 21 December 2017³ that the Regulation be amended to clarify that market makers should not be required to comply with the trading venue membership requirement in order to benefit from the exemption. Nonetheless, the process for amending the Regulation has yet to begin and, consequently, its completion will take quite time.

Therefore, taking into account the fact that the ESMA Guidelines are currently applied, in their entirety, in only a minority of Member States, and considering the position taken by ESMA in its technical advice, and having regard to the fact that the application of the Guidelines by the Italian competent authorities exposes Italian entities to an unlevel playing field compared with other European entities, Banca d'Italia and Consob have decided to cease the application of the Guidelines with specific regard to the trading venue membership requirement.

Thus, market makers subject the supervision of Banca d'Italia and Consob will be able to benefit from the exemption for market making activities in shares, sovereign bonds and financial instruments linked to shares and sovereign bonds, even when such market making activities are carried out entirely outside a trading venue.

This expands the scope of market making activities which can benefit from the exemption.

As a consequence, to give an example, market making activities in financial instruments traded over-the-counter only, like sovereign credit default swaps and equity contracts for difference, will be able to benefit from the exemption.

This Communication has been notified to ESMA and applies after its publication on the Banca d'Italia and Consob websites.

² ESMA/2015/1791: 'Peer Review Report Compliance with SSR as regards Market Making activities'.

³ ESMA70-145-386: 'Technical Advice on the evaluation of certain elements of the Short Selling Regulation'.

Rome, 4 November 2019.

FOR BANCA D'ITALIA

The Governor

Ignazio Visco

FOR CONSOB

The Chairman

Paolo Savona