

Financial institutions  
Energy  
Infrastructure, mining and commodities  
Transport  
Technology and innovation  
Life sciences and healthcare

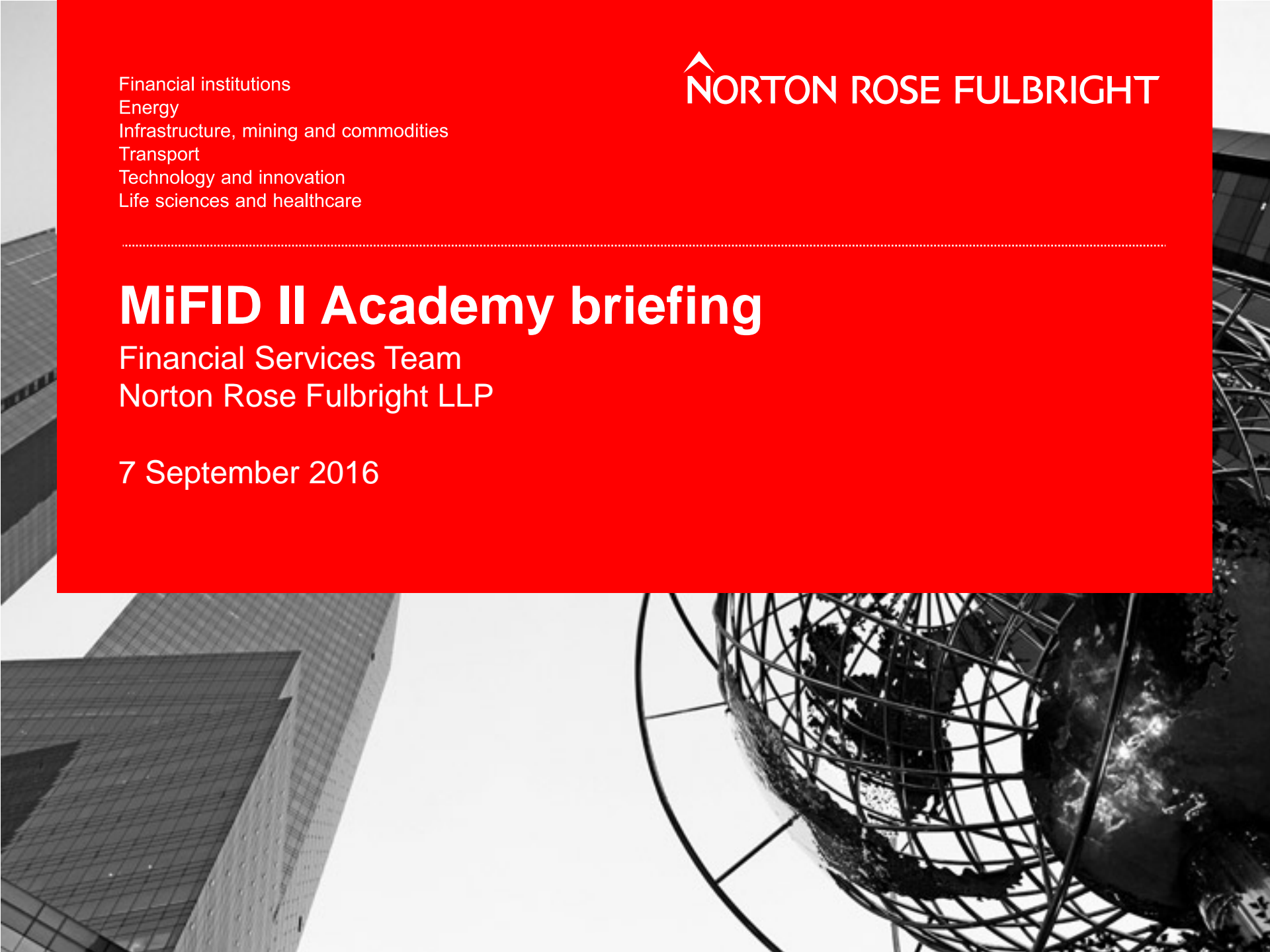
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 **NORTON ROSE FULBRIGHT**

# **MiFID II Academy briefing**

Financial Services Team  
Norton Rose Fulbright LLP

7 September 2016



# Programme

In today's MiFID II Academy 40 minute briefing, we will cover:

Update on MiFID II and MiFIR



Territoriality



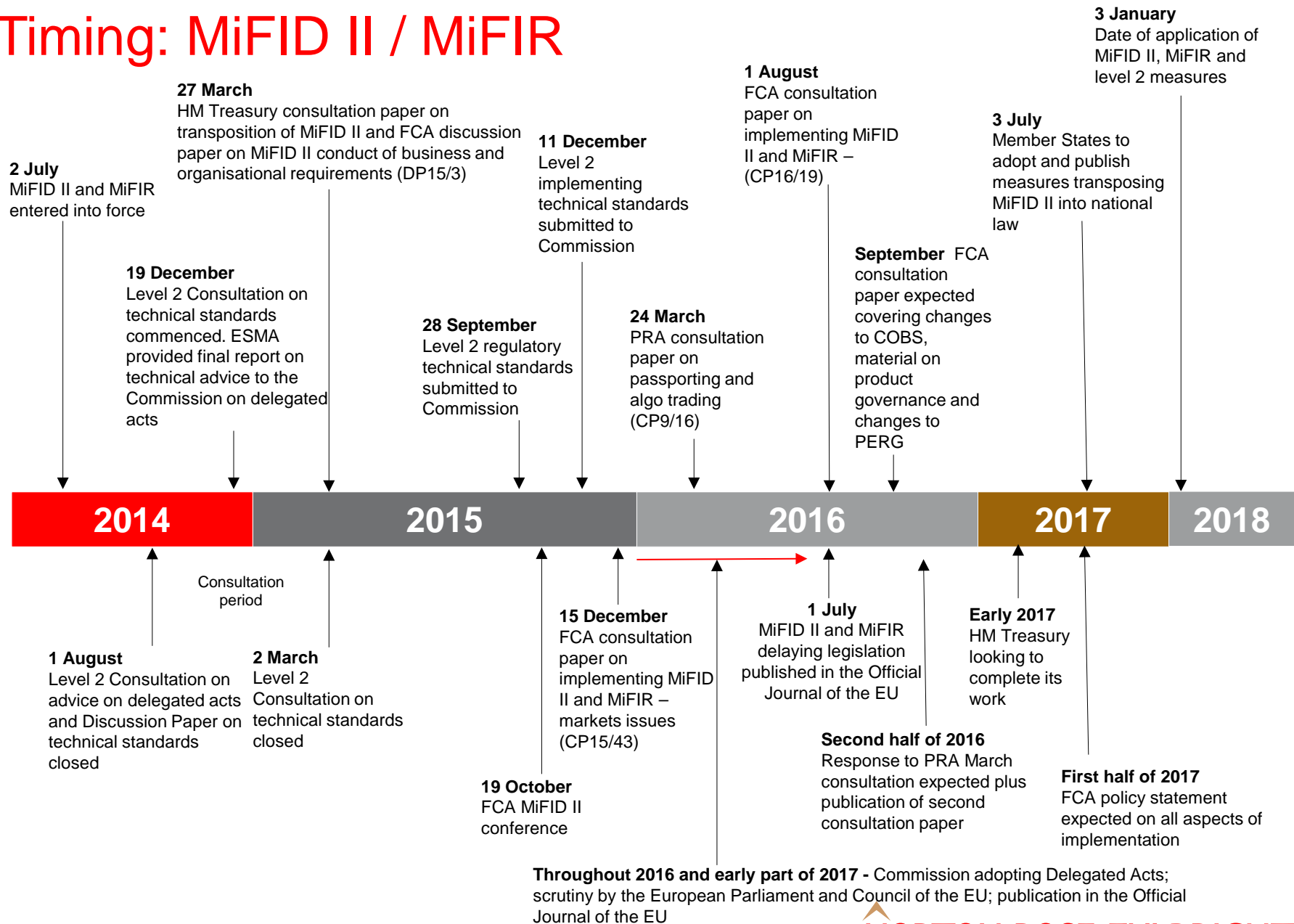
Thoughts on key themes



Project tools

# Update on MiFID II

# Timing: MiFID II / MiFIR



# Timings

## Revised dates

- 3 July 2017: Member States to adopt and publish measures transposing MiFID II into national law
- 3 January 2018: Date of application of MiFID II, MiFIR and level 2 measures
- FCA statement of 24 June 2016 said: “Firms must continue to abide by their obligations under UK law, including those derived from EU law and continue with implementation plans for legislation that is still to come into effect”
- FCA stated in the consultation that MiFID II is in the category of legislation that is still to come into effect “so both firms and we need to continue with implementation plans”
- MAR provisions referring to MiFID II concepts (OTFs, SME growth markets, emission allowances or auctioned products) will not apply until 3 January 2018
- Again, the concepts and rules as set out in MiFID I should be used until 3 January 2018

## Secondary legislation

- All RTS is now adopted by the Commission save RTS 20 and RTS 21 on commodity derivatives
- RTS 2 on non-equities transparency regime remains subject to Parliament and Council scrutiny until 14 October
- No RTS have been published in the Official Journal despite most having passed the scrutiny period
- Most ITS awaits formal adoption by the Commission but ITS on MTFs and OTFs has been published in the Official Journal
- Both Delegated Directive and Delegated Regulation are awaiting publication in the Official Journal

# Level 2: Update on implementing legislation

Technical standards under Directive 2004/39/EC (MiFID I), Directive 2014/65/EU (MiFID II) and Regulation (EU) No 600/2014 (MiFIR)

(last updated: 28/07/2016)

|       | RTS/ITS  | Legal Basis  | Adoption by the European Commission | Acts as adopted by the Commission English version | Acts as adopted by the Commission German version | Acts as adopted by the Commission French version | End of EP/Council scrutiny | Published in the Official Journal |
|-------|--|--|-------------------------------------|---|--|--|----------------------------|-----------------------------------|
| RTS 1 | Transparency requirements for trading venues and investment firms in respect of shares, depository receipts, exchange-traded funds, certificates and other similar financial instruments | MiFIR Articles 4(6), 7(2), 14(7), 20(3), 22(4) and 23(3) | 14/07/2016<br>C(2016) 4390          | <a href="#">RTS 1 in English</a>                  | <a href="#">RTS 1 in German</a>                  | <a href="#">RTS 1 in French</a>                  | 16/08/2016                 |                                   |
|       |  |  |                                     | <a href="#">Annex to RTS 1 in English</a>         | <a href="#">Annex to RTS 1 in German</a>         | <a href="#">Annex to RTS 1 in French</a>         |                            |                                   |
| RTS 2 | Transparency requirements for trading venues and investment firms in respect of bonds, structured finance products, emission allowances and derivatives                                  | MiFIR Articles 1(8), 9(5), 11(4), 21(5) and 22(4)        | 14/07/2016<br>C(2016) 4301          | <a href="#">RTS 2 in English</a>                  | <a href="#">RTS 2 in German</a>                  | <a href="#">RTS 2 in French</a>                  | 16/08/2016                 |                                   |
|       |  |  |                                     | <a href="#">Annex to RTS 2 in English</a>         | <a href="#">Annex to RTS 2 in German</a>         | <a href="#">Annex to RTS 2 in French</a>         |                            |                                   |
| RTS 3 | The volume cap mechanism and the provision of information for the purposes of transparency and other calculations  | MiFIR Articles 5(9) and 22(4)                            | 13/06/2016<br>C(2016) 2711          | <a href="#">RTS 3 in English</a>                  | <a href="#">RTS 3 in German</a>                  | <a href="#">RTS 3 in French</a>                  | 13/07/2016                 |                                   |
|       |  |  |                                     | <a href="#">Annex to RTS 3 in English</a>         | <a href="#">Annex to RTS 3 in German</a>         | <a href="#">Annex to RTS 3 in French</a>         |                            |                                   |
| RTS 4 | Criteria for determining whether derivatives subject to the clearing obligation should be subject to the trading obligation  | MiFIR Article 32(6)                                      | 26/05/2016<br>C(2016) 2710          | <a href="#">RTS 4 in English</a>                  | <a href="#">RTS 4 in German</a>                  | <a href="#">RTS 4 in French</a>                  | 27/08/2016                 |                                   |
| RTS 5 | Direct, substantial and foreseeable effect of derivative contracts within the Union  | MiFIR Article 28(5)                                      | 13/06/2016<br>C(2016) 3544          | <a href="#">RTS 5 in English</a>                  | <a href="#">RTS 5 in German</a>                  | <a href="#">RTS 5 in French</a>                  | 13/07/2016                 |                                   |
| RTS 6 | Specifying the organisational requirements of investment firms engaged in algorithmic trading  | MiFID Article 17(7)(a) and (d)                           | 19/07/2016<br>C(2016) 4478          | <a href="#">RTS 6 in English</a>                  | <a href="#">RTS 6 in German</a>                  | <a href="#">RTS 6 in French</a>                  | 19/08/2016                 |                                   |
|       |  |  |                                     | <a href="#">Annex to RTS 6 in English</a>         | <a href="#">Annex to RTS 6 in German</a>         | <a href="#">Annex to RTS 6 in French</a>         |                            |                                   |
| RTS 7 | Specifying organisational requirements of facilities trading venues allowances and derivatives   | MiFID Article 48(12)(a),(c) and (g)                      | 14/07/2016<br>C(2016) 4387          | <a href="#">RTS 7 in English</a>                  | <a href="#">RTS 7 in German</a>                  | <a href="#">RTS 7 in French</a>                  | 16/08/2016                 |                                   |
|       |  |  |                                     | <a href="#">Annex to RTS 7 in English</a>         | <a href="#">Annex to RTS 7 in German</a>         | <a href="#">Annex to RTS 7 in French</a>         |                            |                                   |

# Level 3: Work has begun

In differing stages across various standing committees

## Investor protection and intermediaries

- Initial release of Q&A and guidelines for consultation on product governance expected in September
- Around 27 Q&As will include coverage on topics such as best execution, suitability, appropriateness, taping, investment advice on an independent basis

## Transaction reporting

- Date of consultation on guidelines cannot be confirmed until the relevant RTS have been approved
- Expectation that the consultation will be at least another 3 months away

## Commodity Derivatives Task Force

- Working on Q&A but timeline unknown given that the relevant RTS have not yet been finalised
- Task Force is said to be working on interpretation and practical questions on ancillary activity and position limits regime

## Secondary Markets Standing Committee

- Consultation on guidelines on trading halts and management bodies expected in September
- Consultation on guidelines on double volume cap expected in September
- Q&A and potentially guidelines expected after September covering a wide range of issues including on multilateral systems, market making, and double volume cap
- Questions on territorial application of transparency to non-EU branches of EU investment firms thought to be under consideration

# The UK papers: A quick recap

HM Treasury consultation on transposition of MiFID II

- Covers third countries, data reporting services, position limits and reporting, unauthorised persons, structured deposits, power to remove board members, OTFs and binary options; draft SIs found in Annexes
- UK Government not currently minded to exercise the discretion to apply the regime specified in Article 39 MiFID II

FCA discussion paper on conduct of business and organisational requirements (DP15/3)

- Discusses the implications of certain MiFID II conduct of business and organisational requirements for firms primarily contained within Articles 24 and 25

FCA consultation paper on implementing MiFID II and MiFIR – markets issues (CP15/43)

- Consults on issues concerning the regulation of secondary trading of financial instruments
- Appendix II contains draft MiFID II Handbook Guide that will sit alongside the Handbook changes
- Notes that MiFIR and RTS and ITS are directly applicable so it is not consulting on certain issues including the double volume cap mechanism to restrict the 'dark' trading of equity and equity-like financial instruments

PRA consultation paper on passporting and algo trading (CP9/16)

- Covers passporting, algorithmic trading and DEA
- Includes the statement that a firm's existing MiFID passport will remain valid and unchanged but firms need to assess whether they wish to include the new activities and/or investment types of MiFID II
- Proposal for a new Algorithmic Trading Part of the PRA Rulebook; proposals closely mirror those in FCA consultation but there are subtle differences due to the regulators' different statutory objectives

Upcoming policy developments

Autumn 2016, the FCA will release the third Consultation Paper on MiFID II implementation  
First half of 2017, there will be a Policy Statement to *Consultation Paper 15/43: MiFID II implementation*  
Early 2017, there will be a Policy Statement to *Consultation Paper 16/19: MiFID II implementation*  
The PRA intends to publish a further CP in due course to cover other areas of MiFID II

FCA consultation paper on MiFID II implementation (CP16/19)

See next slides



# Latest FCA MiFID II consultation paper: Highlights

## Timing

- Consultation closes 28 October 2016
- A third FCA consultation paper is expected in September 2016 and will include proposed changes to COBS, material on product governance and some further changes to PERG
- FCA policy statement covering all aspects of implementation expected in the first half 2017

## Branches of non-EEA firms

- EU law requires that third country branches are treated no more favourably than EU firms
- FCA applies same conduct rules to third-country branches as to UK firms and EEA branches
- However, it applies organisational requirements on a modular basis:
  - conduct focused requirements - rules
  - prudential focus - either switched off or applied as guidance so third country branches can either follow or demonstrate compliance by following home state requirements
- FCA proposes similar approach for new (e.g. product governance) and upgraded (e.g. conflicts of interest) conduct and organisational requirements in MiFID II

## Article 3 firms

- Article 3 firms must be subject to at least analogous requirements for a range of authorisation, conduct of business and organisational requirements
- FSA applied similar requirements to those in MiFID I to Article 3 firms so the UK already complies in significant respects
- Further information in next FCA CP

# Latest FCA MiFID II consultation paper: Highlights

## Commodity derivatives

- Firms, whether authorised or not, trading commodity derivatives will need to configure their trading activities so that they comply with position limits
- Requirements will be partly transposed in legislation
- MAR 10 will provide:
  - guidance on some aspects of the legislation (e.g. when FCA will consider granting an exemption to a non-financial firm)
  - rules on position management for MTFs and OTFs (REC covers regulated markets)
  - rules on position reporting for investment firms and third country branches
- FCA will set position limits in 2017

## CASS

- Intelligent copy out of new MiFID II requirements – all new requirements will apply to all designated investment business including non-MiFID business
- Professional clients of non-MiFID firms will still be able to opt out
- Where CASS already covers a requirement, FCA will maintain existing wording with tweaks
- FCA will maintain super-equivalent provisions relating to prime brokerage, third party custody arrangements, terminating aTTCA and unclaimed assets

# Latest FCA MiFID II consultation paper: Highlights

## SYSC

- Complex application explained in Navigation Guide for SYSC
- Requirements in directive are set out in SYSC and requirements in implementing regulation are signposted
- Extends application of organisational requirements in implementing regulation to all of a UK MiFID (common platform) firm's designated business
- Extends general organisational requirements to all of an Article 3 firm's designated investment business by rules and guidance
- PRA authorised firms are also subject to PRA's general organisational requirements

## Remuneration

- New SYSC 19F on remuneration and performance management of sales staff
- Currently limited to common platform firms, Article 3 MiFID II firms and branches of third country firms (only in relation to activities carried on from an establishment in the UK)

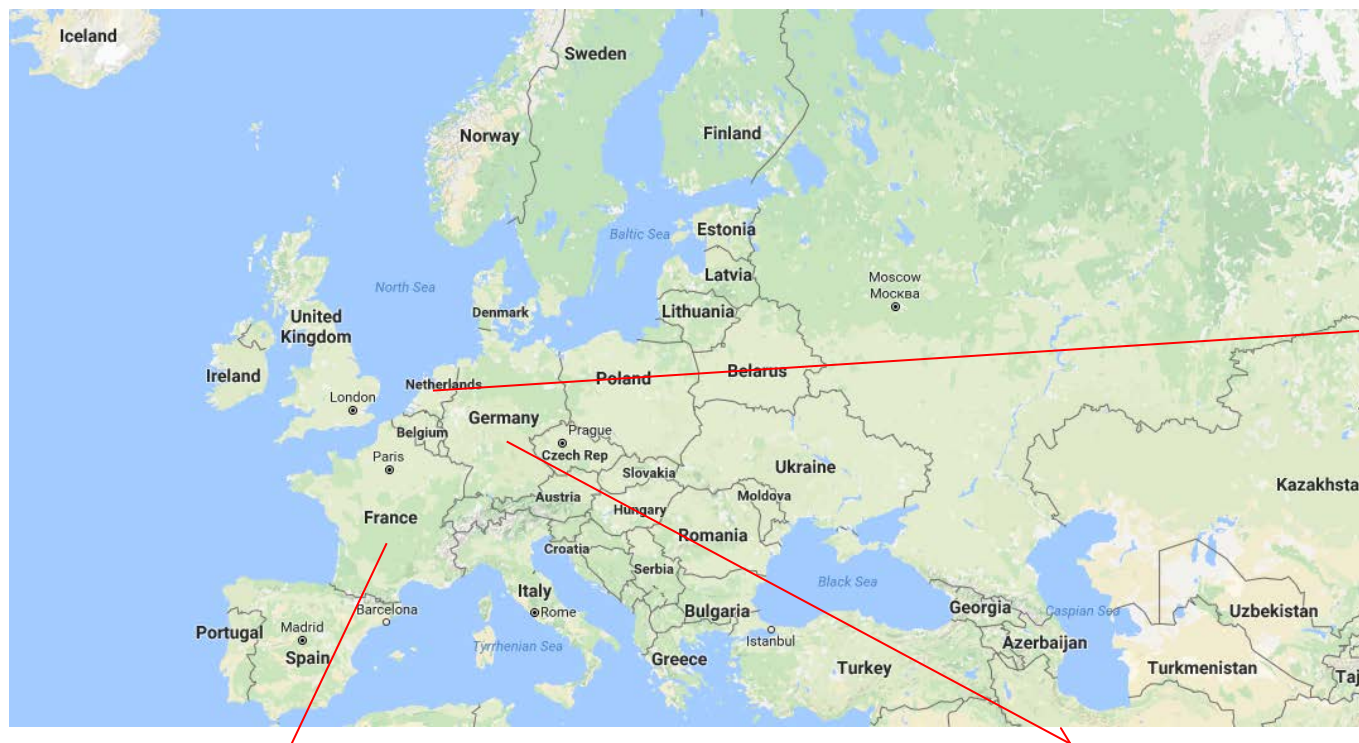
## Whistleblowing

- New SYSC 18.6 transposing MiFID II requirements and signposting requirements in other EU legislation

## Complaints handling

- New DISP 1.1A for handling MiFID complaints containing MiFID II requirements and those from other EU legislation
- MiFID II requirements apply to retail clients, professional clients and eligible counterparties
- Record keeping and reporting of complaints will apply in relation to all client types (for ECPs in relation to ECP business)
- FOS jurisdiction extended so that it can consider complaints about advice on or sales of structured deposits

# Current position in other jurisdictions



- July 2016: The Netherlands Authority for the Financial Markets has decided to build a new system for MiFIR transaction reports in cooperation with the Danish, Finnish, Norwegian and Swedish regulators.

- April 2016: Autorite des Marches Financiers (AMF) published MiFID II transposition guide for asset management companies. The AMF has covered all the key topics of the directive for asset management companies, including product governance, independent investment advice, fees and best execution.

- January 2016: The German Federal Ministry of Finance (BMF) published a revised draft of the German Financial Market Amendment Act following the delay in MiFID II implementation.
- The BMF stated that MiFID II will be subject to and implemented through a further second German Financial Market Amendment Act at a later time.

# Territoriality

# Characteristic performance: the EU view

## MiFID/MiFID II

- Important to remember that single market directives were a reaction to the lack of realisation of the four freedoms, in particular the right to provide services in another member state
- The freedom to provide investment services and activities and the right to establish a branch can be found in articles 31 and 32 of MiFID – in reality the precautionary approach is to serve a cross border services notice when in doubt

## Commission interpretative communication: Freedom to provide services and the interests of the general good in the Second Banking Directive

- Very little assistance on these fundamental territorial issues in MiFID II: guidance on similar issues is old:
- Only activities carried on within the territory of another Member State should be the subject of prior notification
- In order to determine where an activity was carried on, the place of provision of what may be termed the “characteristic performance” of the service, e.g. the essential supply for which payment is due must be determined

The Commission has not produced an interpretative communication for MiFID. It is arguable that the principles in the communication on the Second Banking Directive can be applied to MiFID investment services and activities on the basis that Chapter II of Title II of MiFID (operating conditions for investment firms) also applies to the investment services and activities of firms operating under the Banking Consolidation Directive, which is now repealed and replaced by the CRD IV

Communications made by the Commission have the status of guidance and are not binding on the national courts of EEA states

Communications do not necessarily represent the views taken by all EEA states: currently differing approaches



# Characteristic performance: the UK view

FCA and PRA are of the opinion that UK firms that are credit institutions and MiFID investment firms should apply the 'characteristic performance test' when considering whether prior notification is required for services business

Firms should note that other EEA states may take a different view and apply a solicitation test

In the case of a UK firm conducting portfolio management this means looking at where the investment decisions and management are actually carried on in order to determine where the service is undertaken

Where a credit institution or MiFID investment firm: (1) intends to send a member of staff or a temporarily authorised intermediary to the territory of another EEA state on a temporary basis to provide financial services; or (2) provides advice, of the type that requires notification under either MiFID or the Banking Consolidation Directive, to customers in another EEA state, the firm should make a prior notification under the freedom to provide services

The key distinction in relation to temporary activities is whether a firm should make its notification under the freedom of establishment in a Host state or whether it should notify under the freedom to provide services into a Host state

**SUP  
Appendix  
3**



# The basics of the MiFID II / MiFIR third country regime

Article 39 MiFID II sets out certain conditions for a Member State's authorisation of a branch, which apply where a Member State chooses to require third country firms to establish a local branch in order to provide investment services or perform investment activities with or without any ancillary services to retail and/or elective professional clients in its territory

FCA consulting on not implementing Article 39 MiFID II

Article 46(1) MiFIR sets out a requirement for certain third country firms to register with ESMA. Subject to an equivalence assessment being undertaken by the Commission, Article 46(1) MiFIR provides that a third country firm may provide investment services or perform investment activities with or without any ancillary services to ECPs and per se professional clients established in the EU without the establishment of a branch where it is registered in the register of third country firms kept by ESMA



# Unpacking the issues for firms

A number of hot topics on the ESMA registration process:

- Will ESMA adopt the literal equivalence approach or the EMIR style policy equivalence plus top up?
- The comparison of capital requirements is particularly sensitive as some non-EU countries have a different and lighter approach



There is a genuine debate about when a cross border service is being provided in the markets space but in reality any dealing with an EU counterparty will bite

Pre-equivalence - will current domestic regimes continue to permit access? HM Treasury has indicated that the overseas persons exclusion will continue to apply

Post equivalence - can a third country firm operate an MTF or OTF and what does this mean for the concept of trading venue and equivalent third country markets?

Note that the regime applies even to performing investment activities with EU professional clients and eligible counterparties

# A word on Brexit: Inward and outward business

Lack of guidance from MiFID/MiFIR texts is key

Level 3 ESMA Q&A could play a key role here

For UK firms, the first question is when they are providing a cross border service into an EEA member states

The second question is whether the Article 46 MiFIR equivalence regime will work: reciprocity is the key to the “small deal” mechanics working

The third question is whether in the absence of UK equivalence UK firms can create a marketing or “blocker” entity in the EU for EU client business

All of this is irrespective of the “big deal” being done or not on Brexit

For inwardly passporting firms doing services or operating from a branch all will depend on the UK attitude: current noises are positive

# Thoughts on key themes

# OTFs: The state of play

Continuing uncertainties on scope of OTF: No Level 2 on definition so all eyes are on the Level 3 Q&A

Why have one?

- An eligible venue for mandatory traded derivatives
- Drive to create an OTF for C6 trades, e.g. those which must be physically settled in energy products: These are carved out from financial instrument definition and so from the threshold calculation for NFCs

Proposed new PERG answer on multilateral system

# OTFs: What are they?

**OTF:** "a *multilateral system...* in which *multiple third-party buying and selling interests* in bonds, structured finance products, emission allowances or derivatives are able to *interact in the system* in a way that *results in a contract* in accordance with Title II of MiFID II"

## Markets facing requirements

- Non-discrimination and transparency
- Conflicts management
- Monitoring compliance with the rules and orderly trading
- Market surveillance
- System resilience and tick sizes
- Position reporting

## Client facing obligations

- Clients' best interests
- Appropriate information requirements
- Suitability and appropriateness
- Best execution
- Prompt and fair execution of orders
- Publication of limit orders in shares

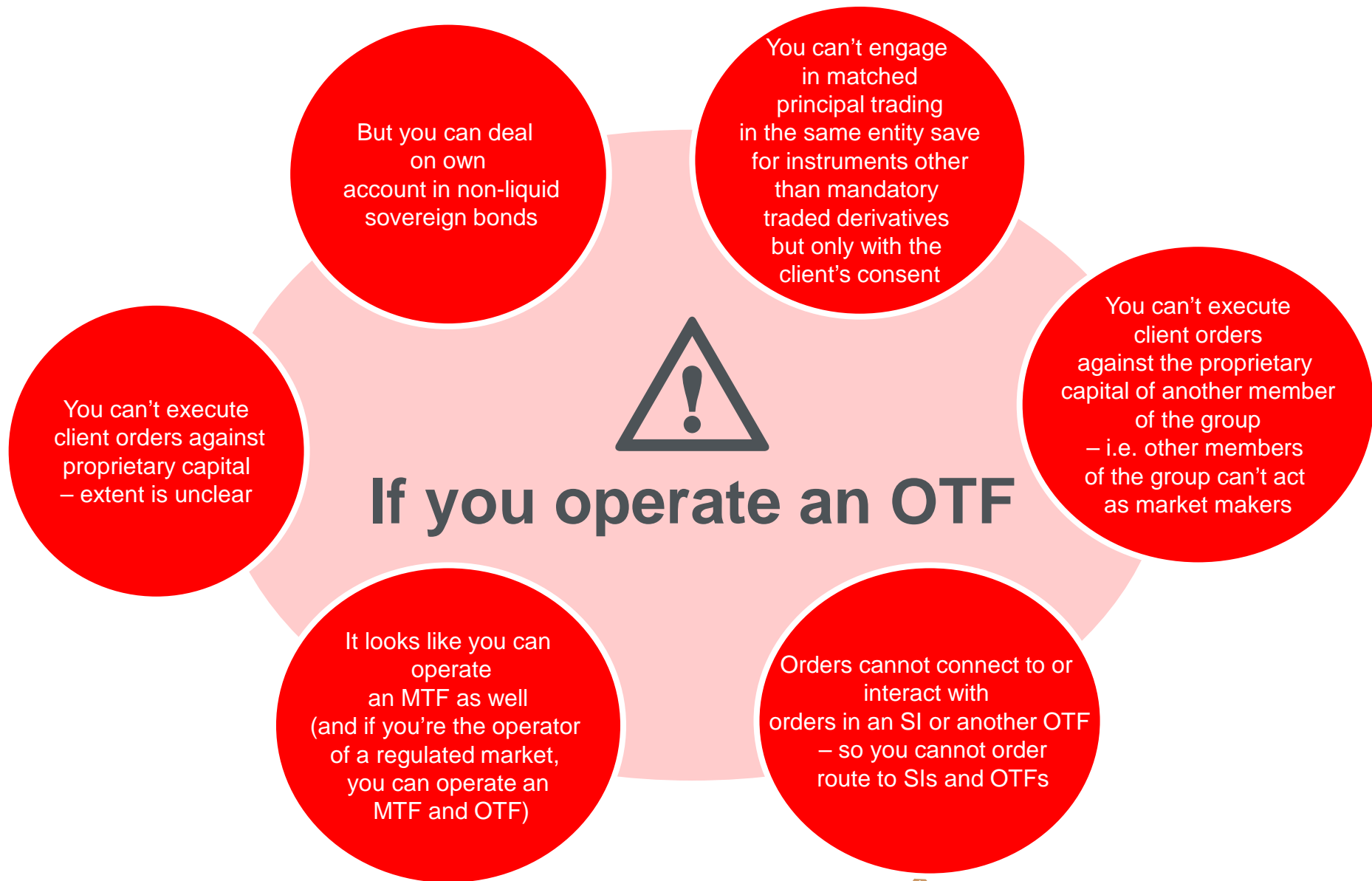
## Other differences from MTFs

- Only for non-equities
- Must exercise discretion by deciding to place or retract orders on the OTF and / or deciding not to match an order with other available orders at a given point in time
- May facilitate negotiation between clients
- Not subject to mandatory CCP clearing – will FCA allow a bit more flexibility?

## Questions without answers (yet)

- Who might become an OTF?
- What will OTF rules look like?
- How much discretion will clients accept?

# Structural considerations



# Wholesale Conduct – managing the product lifecycle

- Clarity around target market
- Alignment between product and customer need
- Risks to customers considered and understood
- Product properly approved
- Conflicts managed
- Management reporting on outcomes

- Marketed in line with research and design principles
- Promotion strategy suitable for target market
- Materials clear on cost and risk as well as benefits
- Materials considered in light of end user

Design/Govern

Market

Review

Distribute

- Periodic post launch reviews – event and time driven
- Review of distribution results
- Periodic reports to management
- Ongoing reporting to customers
- Open dialogue between manufacturer and distributor

- Distribution strategy appropriate for market
- Distributors clear on product terms and risks
- Ensure that distributors have key information
- Ensure incentivisation does not compromise outcomes

# Product Governance – control factors

Robust governance for manufacturers through the product lifecycle is key

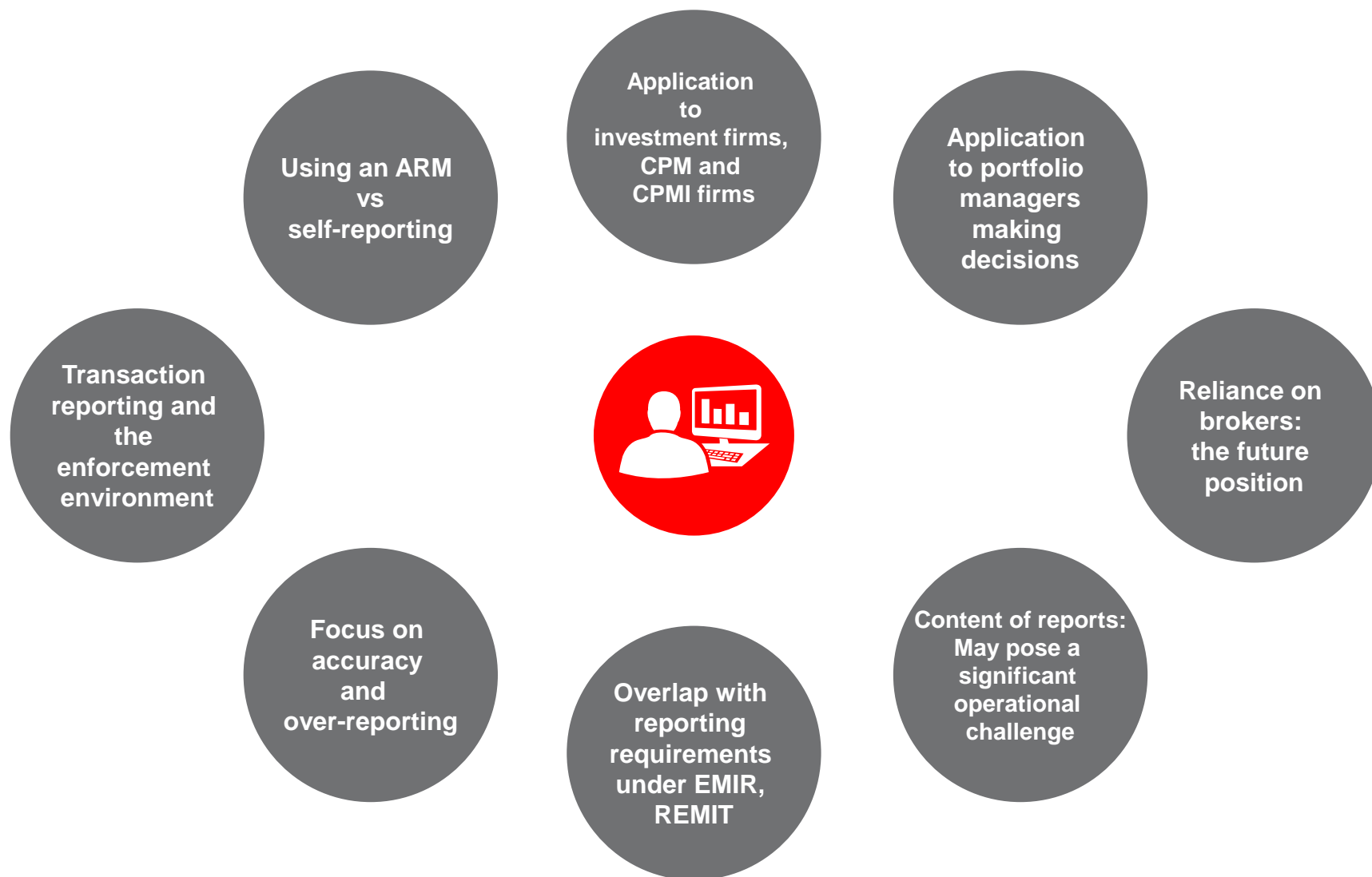
- Full involvement of product, compliance and management in product oversight
- Accountability for product management and oversight clearly defined
- Documented product approval process, embedded into organisational policies and procedures
- Effectively trained product teams
- Documented reviews at each stage of product development, always aligned with customer demographic and design principles
- Ongoing reviews of product performance and underlying product construction
- Proper dissemination of information to distributors, assuring that the distributors understand the product
- Assuring the suitability of distributors and channel when considering the product and customers
- Ongoing oversight of distributor performance
- Product review process that accounts for product risk and changes to:
  - the environment;
  - the customer base; and/or
  - the structure of the instruments.



# Transaction reporting for investment firms

|  |  |
|--|--|
| <p><b>Which trades?</b></p>              | <ul style="list-style-type: none"> <li>• Investment firms that execute transactions in financial instruments:             <ul style="list-style-type: none"> <li>- that are admitted to trading or traded on a trading venue or for which a request has been made</li> <li>- where the underlying is a financial instrument traded on a trading venue</li> <li>- where the underlying is an index or basket of financial instruments traded on a trading venue</li> </ul> </li> </ul>  |
| <p><b>Transactions and execution</b></p> | <ul style="list-style-type: none"> <li>• Transaction means an acquisition or disposal subject to various exceptions</li> <li>• Execute means certain activities that results in a transaction including discretionary investment decisions</li> <li>• A firm that transmits orders (including those generated by portfolio managers) doesn't need to report if it provides certain information within its order</li> </ul>   |
| <p><b>Which information?</b></p>         | <ul style="list-style-type: none"> <li>• <b>65 fields</b> – though some will not be required in certain cases</li> <li>• New fields include client ID, IDs of person or committee that make decision to trade and algo responsible for decision and execution</li> <li>• Legal entities to be identified by LEI codes, simplified concatenation for individuals</li> <li>• Codes for algos and committees must be unique, consistent and persistent</li> <li>• Various new designations – e.g. waivers, short sales</li> </ul> |
| <p><b>How?</b></p>                       | <ul style="list-style-type: none"> <li>• Firms can report themselves or through an ARM or in some cases trading venue – they must take reasonable steps to ensure compliance where they don't report themselves and remain responsible</li> <li>• Trading venues will report trades executed by firms <b>not subject to</b> reporting obligation</li> </ul>  |
| <p><b>To whom and by when?</b></p>       | <ul style="list-style-type: none"> <li>• Home competent authority of firm, even where a branch executes the transaction (unless a branch of a non-EEA firm)</li> <li>• As quickly as possible and <b>no later than end of next working day</b></li> </ul>  |
| <p><b>Link to EMIR?</b></p>              | <ul style="list-style-type: none"> <li>• Transactions reported to a trade repository under EMIR count provided:             <ul style="list-style-type: none"> <li>- that trade repository is also an ARM</li> <li>- the report contains all the required details</li> <li>- trade repository transmits information to competent authority</li> </ul> </li> </ul>  |

# Transaction reporting: some key angles for the buy-side



# Transaction reporting: 'exemption' for transmitting firms?

Firms transmitting orders received from clients, or resulting from discretionary management decisions, may be able to rely on third parties to submit transaction reports on their behalf, provided certain criteria are met

Transmitting asset managers would need to send to the receiving broker a number of specified details for the trade

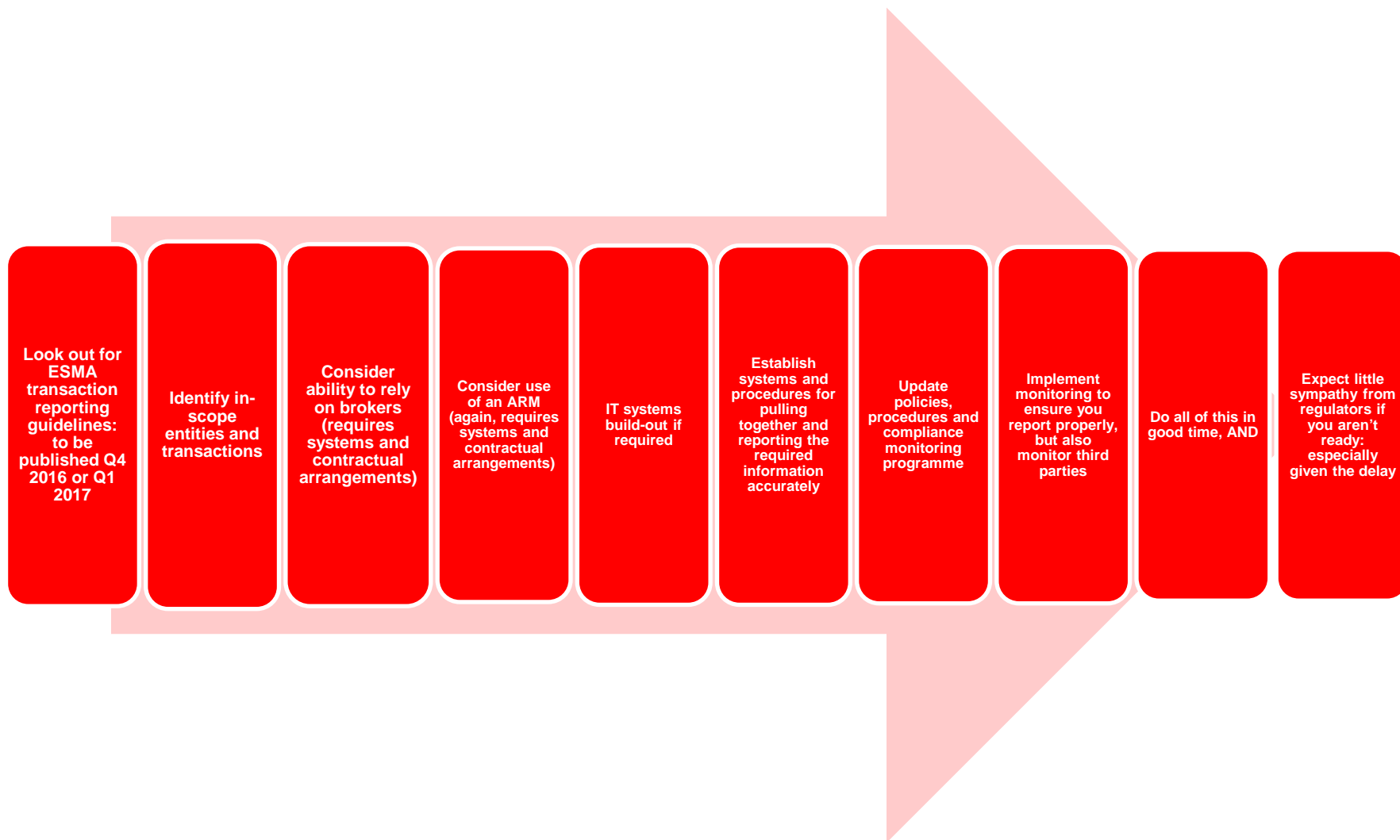
Transmitting asset managers would need to have a written agreement in place with their receiving broker covering a number of specified matters

Circumstances in which the 'exemption' would not apply (e.g., where non-EU brokers are used)

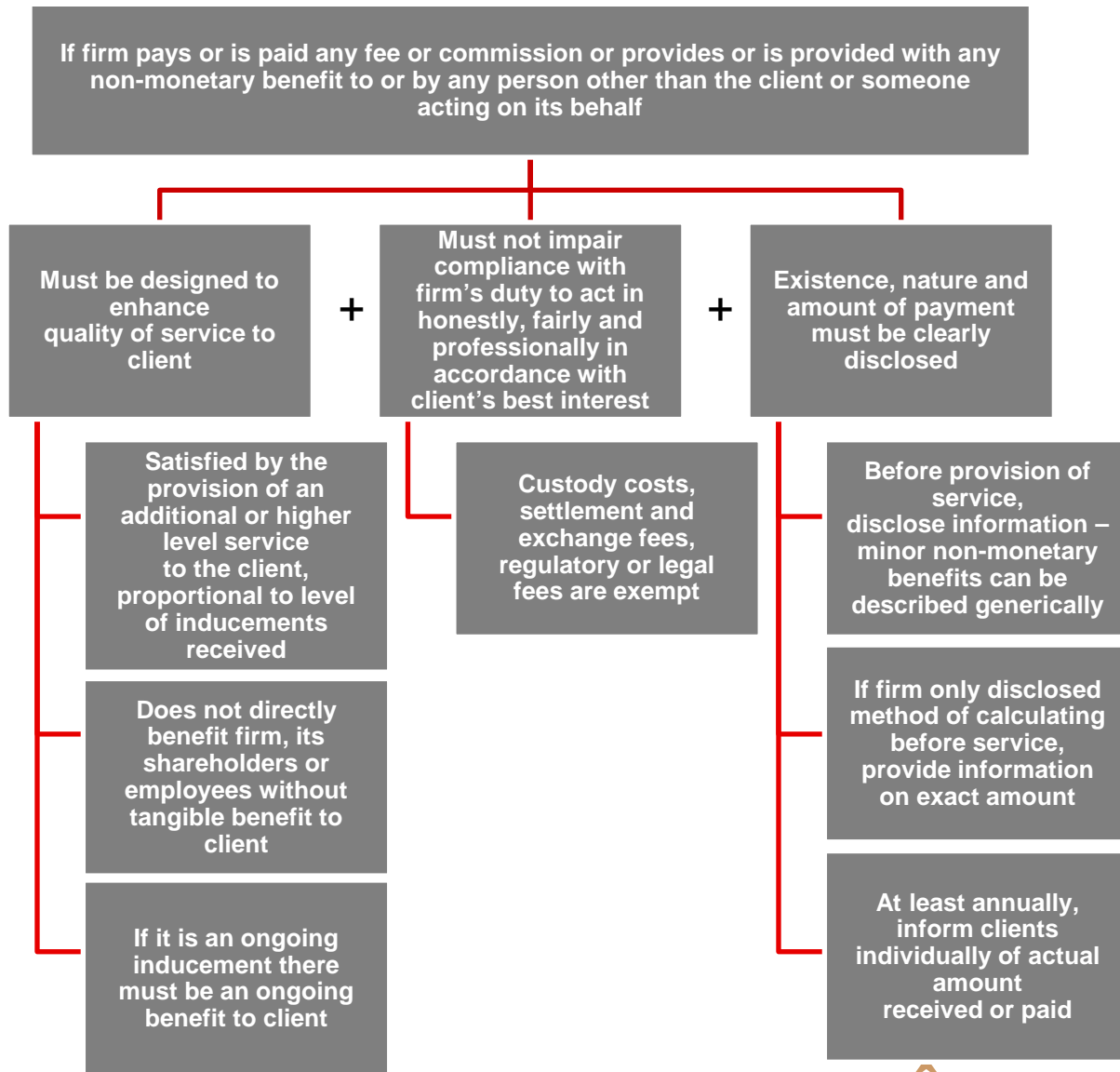
Applicability in the context of DMA

Requirement to verify completeness, accuracy and timeliness of reports made by third parties

# Transaction reporting: key items for the 'to do' list



# Inducements generally: a recap



# Inducements for investment advice and portfolio management

- Cannot accept and keep any third party payments other than acceptable minor non-monetary benefits
- Must be reasonable and proportionate and of a scale that is unlikely to influence firm's behaviour to detriment of clients' interests
- Must disclose before providing service

- Return to clients fees, commissions and monetary benefits ASAP after receipt
- Policy to ensure that amounts are allocated and transferred
- Inform clients through periodic statements

## **Acceptable minor non-monetary benefits:**

- (a) Information or documentation relating to products or services which is generic in nature or personalised
- (b) Issuer commissioned/paid third party new issuance material provided relationship disclosed and made available at the same time to other investment firms or general public
- (c) Participation in conferences, seminars and other training events
- (d) Hospitality of a reasonable de minimis value
- (e) Other minor non-monetary benefits which a Member State deems capable of enhancing the quality of service and are of a scale and nature that are unlikely to impair compliance with duty to act in client's best interest

# Purchase of research: MiFID II

Purchase of research is not prohibited if firm pays through:

**Own resources**

**OR**

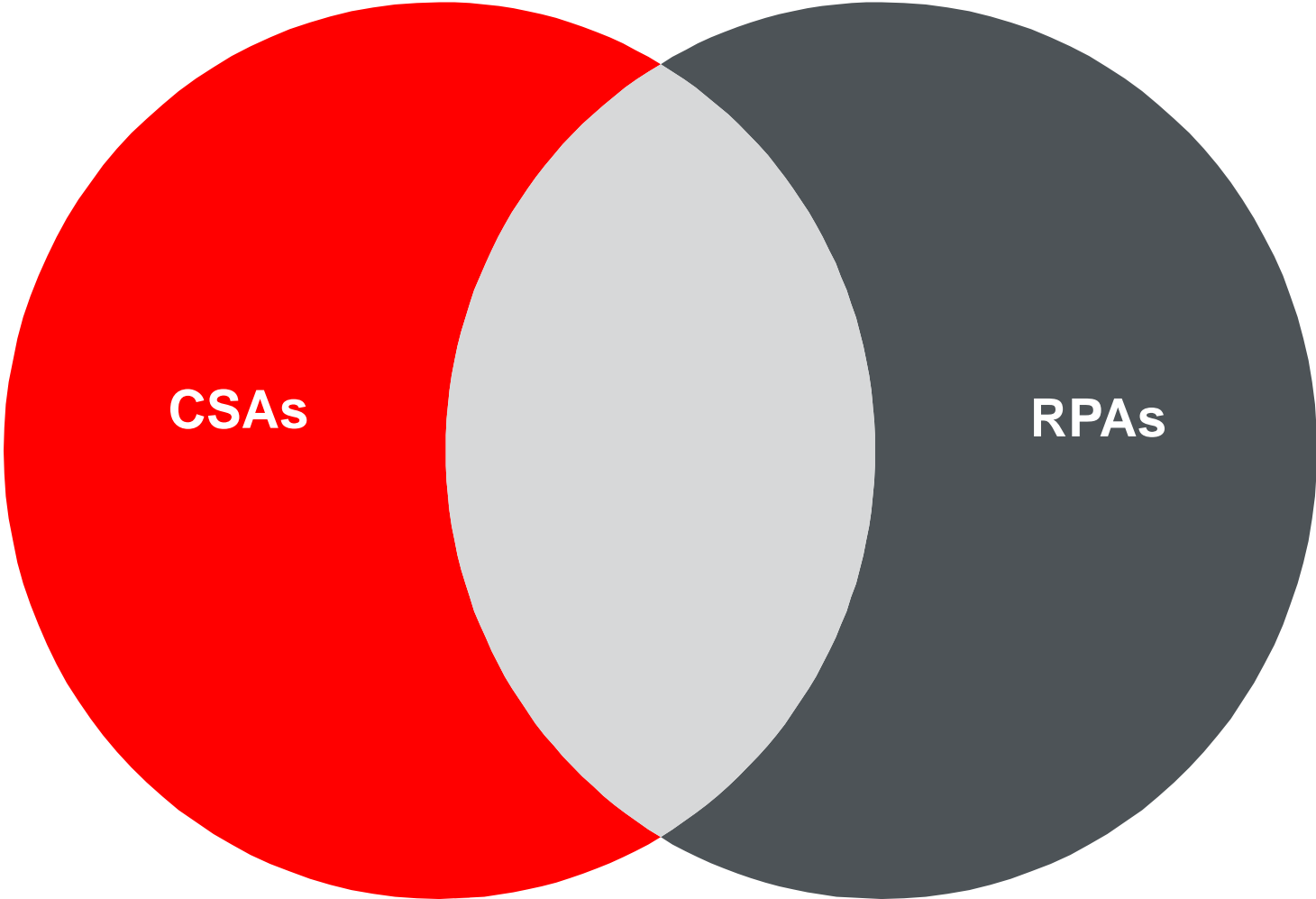
**Research payment account provided:**

- The account is funded by a specific research charge to client
- Set and regularly assess a research budget
- Firm is responsible for research payment account
- Firm regularly assesses quality of research against robust quality criteria set out in a policy
- Firms assesses its ability to contribute to better investment decisions
- Before providing service, tell clients of budgeted amount and charge and agree research charge and frequency in terms and conditions
- Provide annual information on total costs incurred by client for research
- If required by client or competent authority, provide further information
- All operational arrangements must identify research charge separately
- Tell clients about any increase in advance
- Any surplus at end of period must be rebated or offset against research budget for following period
- Allocation of budget is subject to appropriate controls and senior management oversight
- Cannot use to fund internal research
- Firm providing execution services must identify separate charges that only identify execution costs

**Why is this relevant?**

- **Where does it leave the CSA model?**
- **How do you make a research payment account work?**
- **Client money account implications**
- **Shutting off nil value service agreement**

# The future of the CSA model?





# Our tools on your MiFID implementation project

# MiFID II Gap analysis straw man

| NORTON ROSE FULBRIGHT                 |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
|---------------------------------------|---|---|---|---|-------------------------------|-------------------------------------|-------------------------------------|------------------------------|---|--|---|--|
| MIFID I/MIFIR: Gap Analysis Straw Man |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
| BEST EXECUTION                        |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
| SCOPE                                 |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
|                                       | Applicable to all <u>investment firms</u> with establishment in the EEA and to branches in the EEA of non-EEA entities which execute orders on behalf of others.  |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
| GOAL                                  |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
|                                       | An <u>investment firm</u> must take all sufficient steps to obtain, when executing orders, the best possible result for its client, taking into account a range of factors.<br><br>The aim was to enhance best execution rules for retail clients. However, this has not resulted in major changes to these requirements. A secondary aim was an improvement in investor protection and efficiency of the best execution assessment by increasing the transparency of relevant policies and procedures. |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
| MIFID II                              |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
| Client Classification                 |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
| Article Number MIFID II / MIFIR       | Legislative Provision (Level 1)   | Article / Page Number ESMA TA (including references to MIFID I Implementation Directive / Draft RTS   | Related ESMA Technical Advice / Draft RTS (Level 2) | Guidelines by ESMA, EBA etc (Level 3)   | Applicable to retail clients? | Applicable to professional clients? | Applicable to eligible counterpart? | Type of financial instrument | Baseline Requirement (Legal)  | Guidance on Baseline Requirement (Legal) | What is new in MIFID II / MIFIR compared to MIFID I?  | UK Implementation (Legal) (Reference and Comments) |
| I. BEST EXECUTION REQUIREMENT         |   |   |   |   |                               |                                     |                                     |                              |   |  |   |  |
| 1                                     | MIFID2.01 First subparagraph  | Member States shall require that investment firms take all sufficient steps to obtain, when executing orders, the best possible result for their clients taking into account price, costs, speed, likelihood of execution and settlement, size, where or any other consideration relevant to the execution of the order.  | TA, p.117, paragraph 1                              | ESMA confirmed that Articles 44 to 46 of the MiFID Imp Dir should apply as amended (see below).   |                               |                                     |                                     | All                          | Firms must take all sufficient steps to obtain the best possible result for clients when executing orders, taking into account the following factors:<br>a) Price;<br>b) Costs;<br>c) Speed;<br>d) Likelihood of execution and settlement;<br>e) Size;<br>f) Nature; and<br>g) Any other consideration relevant to the execution of the order.<br><br>The relative importance of these factors is determined by the Criteria set out below.   |  | This is an existing requirement under MIFID I, however the fact of taking 'all reasonable steps' has been replaced with 'all sufficient steps' but it is not clarified how these are different. |  |
| 2                                     |   | Member States shall ensure that, when executing client orders, investment firms take into account the following criteria for determining the relative importance of the factors referred to in Article 2(1) of Directive 2004/39/EC:<br>(a) the characteristics of the client, including the categorization of the client as retail or professional;<br>(b) the characteristics of the client order;<br>(c) the characteristics of financial instruments that are the subject of that order;<br>(d) the characteristics of the execution venue to which that order can be directed.<br><br>For the purposes of this Article and Article 46, 'execution venue' means a regulated market, an MTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing.<br><br>ESMA recommended that the definition of execution venue be amended to take into account the activities of OTFs in the definition of a trading venue. | MIFID/IMP/DIR.44.01                                 | Member States shall ensure that, when executing client orders, investment firms take into account the following criteria for determining the relative importance of the factors referred to in Article 2(1) of Directive 2004/39/EC:<br>(a) the characteristics of the client, including the categorization of the client as retail or professional;<br>(b) the characteristics of the client order;<br>(c) the characteristics of financial instruments that are the subject of that order;<br>(d) the characteristics of the execution venue to which that order can be directed.<br><br>For the purposes of this Article and Article 46, 'execution venue' means a regulated market, an MTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing.<br><br>ESMA recommended that the definition of execution venue be amended to take into account the activities of OTFs in the definition of a trading venue. |                               |                                     |                                     | All                          | <b>Criteria</b><br>When executing client orders, the following is the criteria for determining the relative importance of the factors above:<br>(a) the characteristics of the client, including the categorization of the client as retail or professional;<br>(b) the characteristics of the client order;<br>(c) the characteristics of financial instruments that are the subject of that order;<br>(d) the characteristics of the execution venue to which that order can be directed.<br><br>For the purposes of this Article and Article 46, 'execution venue' means a regulated market, an MTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing.<br><br>ESMA recommended that the definition of execution venue be amended to take into account the addition of OTFs in the definition of a trading venue. |  | This is an existing requirement under MIFID I, but the situation of execution venue is new.   |  |



## Financial services: *Regulation tomorrow*

Tracks financial services regulatory developments and provides insight and commentary

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### United Kingdom (and EU regulation)

## Commission publishes MiFIR RTS for the reporting of transactions to NCAs



By **Hannah Meakin and Mark Chalmers** on August 23, 2016  
Posted in **Italy, Regulation and compliance, Regulation and compliance, Regulation and compliance, The Netherlands, United Kingdom**

Article 26(9) of the Markets in Financial Instruments Regulation empowers the European Securities and Markets Authority (**ESMA**) to develop draft regulatory technical standards (**RTS**) which specify further the rules applicable to reporting transactions to member state competent authorities (**NCAs**) by investment firms.

ESMA issued a consultation paper on 19 December 2014 and the consultation closed on 2 March 2015. ESMA submitted draft RTS to the European Commission (**Commission**) in July 2015. The draft RTS that were consulted on and those submitted to the Commission did not contain an explicit reference to the exclusion of collateral transfers from the meaning of transaction. However, feedback to an earlier ESMA discussion paper indicated support for an explicit reference which resulted in ESMA writing to the Commission in April to request the explicit exclusion of transfer of collateral from transaction reporting.

### About

Our blog, *Financial services: Regulation tomorrow* offers a convenient resource for those keeping track of the evolving and increasingly complex global financial services regulatory environment. It reports on financial services regulatory developments and provides insights and commentary across Africa, Asia, Australia, Canada, Europe and the United States. We cover a broad range of financial services regulatory topics including banking and capital adequacy regulation, clearing and settlement, anti-money laundering, insurance, regulation and compliance retail and wholesale conduct and securities regulation.

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# MiFID II Academy upcoming webinars

- Research, payment accounts and commission sharing agreements (15 September 2016)
- Update on MiFID II across Europe (29 September 2016)
- Markets for the buy-side (13 October 2016)
- Wholesale conduct (27 October 2016)
- Market structures (10 November 2016)

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Pegasus and Regulation tomorrow



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## Pegasus

### Preparing for MiFID II



MiFID II and MiFIR (together 'MiFID II') will underpin the provision of investment services across and into Europe, both in terms of how trading is carried on and how firms organise and conduct themselves. They will affect both the wholesale and retail sides of the industry, in relation to both securities and derivatives. Nor should MiFID II be seen as solely European, as its effect will be far reaching and influence all firms dependent on the European client base.

Recently legislation delaying the implementation of MiFID II to 3 January 2018 was published in the Official Journal of the EU. Despite the delay, firms need to continue to press ahead with their implementation work. There is still a lot to do to be ready in time for the new implementation date. In addition, the UK's referendum vote to leave the EU should not be taken as a sign for firms to stop their work as it is expected that MiFID II will be implemented before the UK concludes its exit negotiation. The FCA's statement on the EU referendum result stated: "Firms must continue to abide by their obligations under UK law, including those derived from EU law and continue with implementation plans for legislation that is still to come into effect."

### We are committed to helping firms keep on top of MiFID II

Pegasus is our dedicated online resource housing all our MiFID II know-how and links to other resources clients will need for any MiFID II project.

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Trading venues and  
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infrastructure

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algorithmic trading  
obligations

Impact on  
commodities and  
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Transparency,  
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Pegasus is our dedicated online resource housing all our MiFID II know-how and links to other resources clients will need for any MiFID II project.

Our materials are strategically grouped under the core topic headings below so that information is readily accessible.



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Pegasus - Our guide to MiFID II

Re:insurance - Our guide to reform affecting the insurance industry

Phoenix - Our guide to UK regulatory reform

The UK Corporate Governance Portal - access to the latest corporate

# Investor protection

Protecting the interests of customers is a cornerstone of European financial regulation, and in these pages, we set out our key materials on the core investor protection provisions of MiFID II.



Investor protection (conduct of business)



Impact of MiFID II on EU conduct of business regime



MiFID II Academy slides



40 minute briefing slides



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The logo consists of a stylized, upward-pointing chevron shape in a gold color, positioned above the first letter of the text.

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