

Markets in Financial Instruments Directive II and Markets in Financial Instruments Regulations

(MiFID II and MiFIR)

EU Member States

Austria	Belgium	Bulgaria	Croatia	Cyprus	Czech Republic
Denmark	Estonia	Finland	France	Germany	Greece
Hungary	Ireland	Italy	Latvia	Lithuania	Luxembourg
Malta	Netherlands	Poland	Portugal	Romania	Slovakia
Slovenia	Spain	Sweden	United Kingdom		

Candidate Countries

- Albania
- Iceland
- Montenegro
- Serbia
- The former Yugoslav Republic of Macedonia
- Turkey

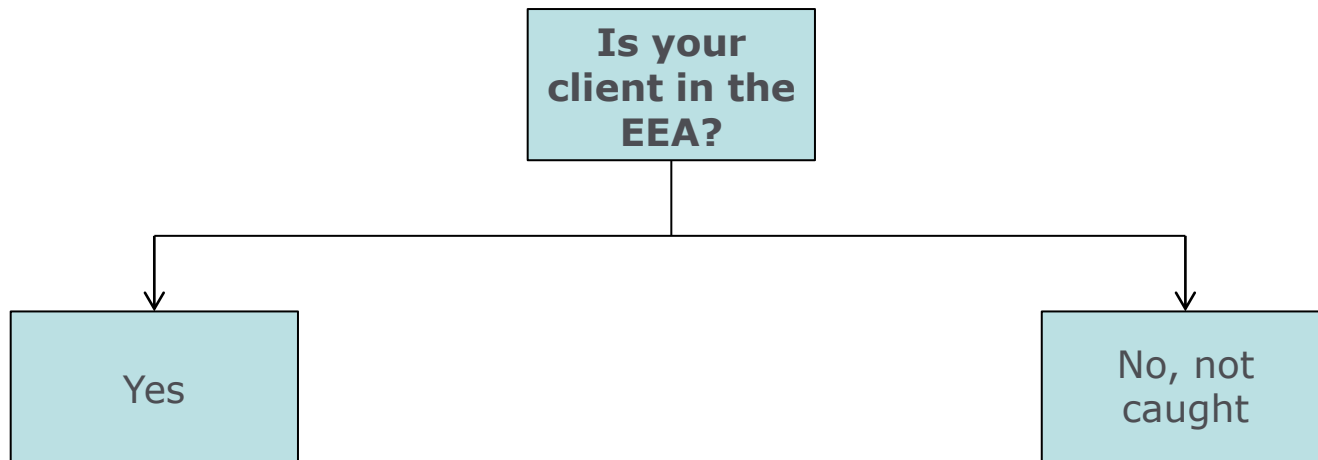
Today is designed to do two things

1. Inform you to the extent you are not already familiar with MiFID II and MiFIR; and
2. To begin a conversation about what, if anything, Guernsey should do to respond to this latest regulatory intrusion from Europe.

Questions we need to consider today

1. Do you, and therefore does Guernsey, have business caught by MiFID II?
2. Is the business caught by MiFID II sufficiently material for you and, on a larger scale, Guernsey, to respond?
3. What should the extent of the response to MiFID II be? I.e. what scale of response is appropriate.
4. Are there opportunities for you or Guernsey arising from MiFID II?

Third Country Firms – are you caught? Quick and dirty analysis



Somewhere between 60% and 80% of Guernsey's finance industry services EEA clients

**Are you providing
investment services or
activities?**

Yes

No, not
caught

Investment services and activities

1. Reception and transmission of orders in relation to one or more financial instruments;
2. Execution of orders on behalf of clients;
3. Dealing on own account;
4. Portfolio management;
5. Investment advice;
6. Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis;
7. Placing of financial instruments without a firm commitment basis;
8. Operation of an MTF;
9. Operation of an OTF.

Are you eligible for any exemptions?

Selected Exemptions

1. Own exclusive initiative – i.e. “it wasn’t me guv”, the client came to us.

Where a third-country firm solicits clients or potential clients in the Union or promotes or advertises investment services or activities together with ancillary services in the Union, it should not be deemed as a service provided at the own exclusive initiative of the client.

Note: it does not require that the actual client was solicited, promoted or advertised to. On a strict reading, any business development activity carried out in the EU would disqualify a business from this exemption. The Level 2 Rules may clarify this.

Are you eligible for any exemptions?

Selected Exemptions continued

2. Persons providing investment services ...to the customers or suppliers of their main business...provided that this is an ancillary activity to their main business.

What is ancillary will be determined at both an individual and group level.

3. Collective investment undertakings and pension funds... and the depositaries and managers of such undertakings.

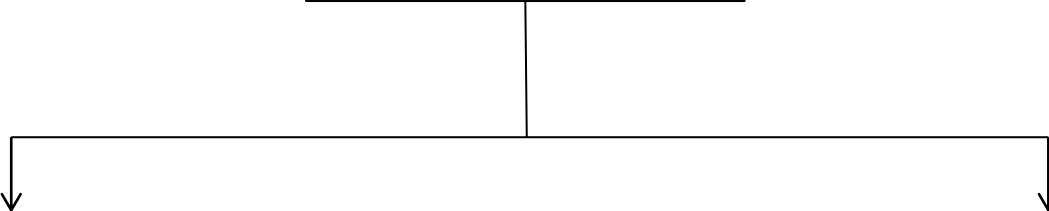
There is no definition of collective investment undertaking.

Are you eligible for any exemptions?

Selected Exemptions continued

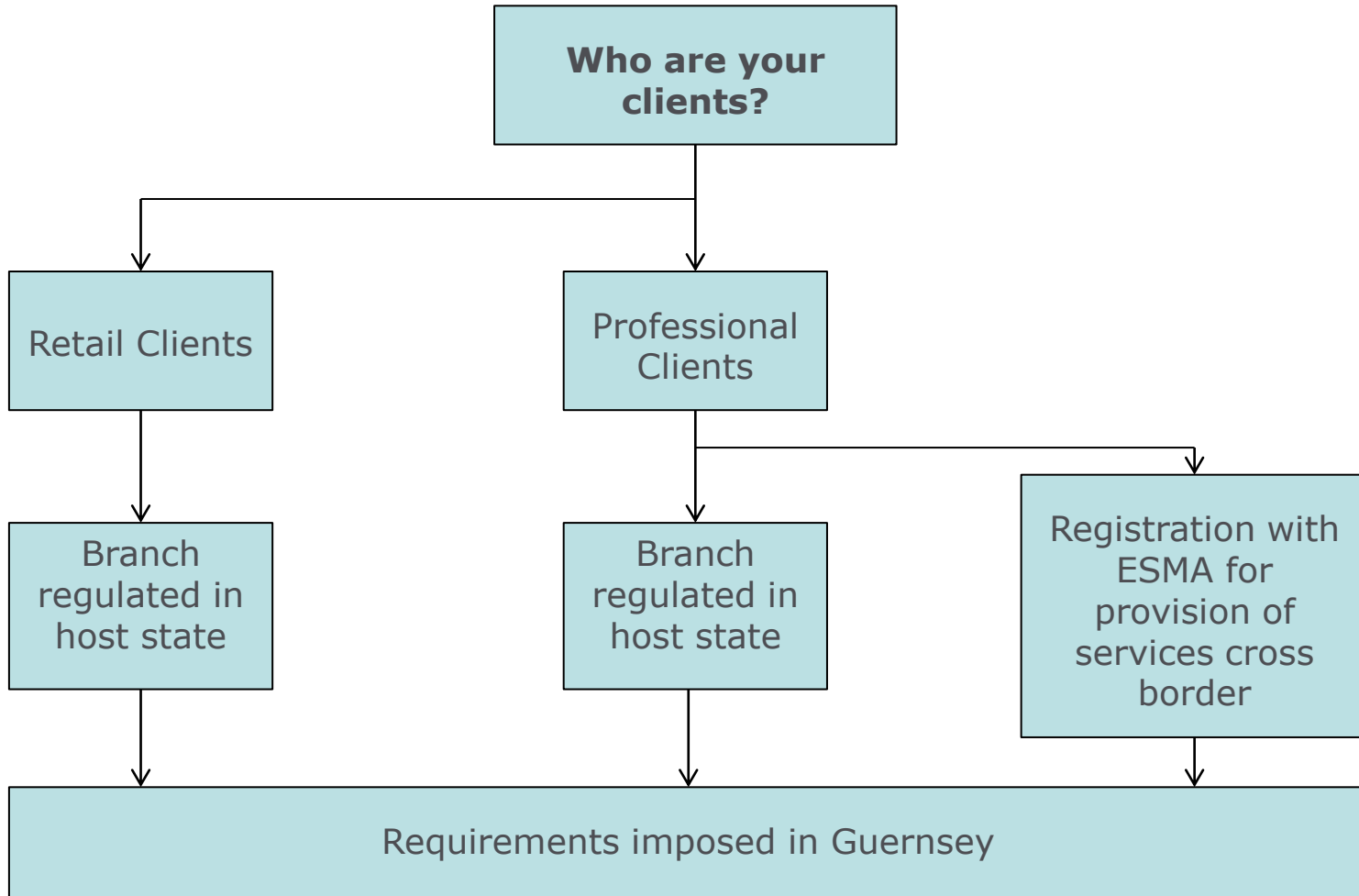
4. Insurance undertakings or undertakings carrying out the reinsurance and retrocession activities referred to in Directive 2009/138/EC when carrying out the activities referred to in that Directive;
5. Persons providing investment services exclusively for their parent undertakings, for their subsidiaries or for other subsidiaries of their parent undertakings;
6. Persons providing an investment service where that service is provided in an incidental manner in the course of a professional activity and that activity is regulated by legal or regulatory provisions or a code of ethics governing the profession which do not exclude the provision of that service;
7. Persons providing investment advice in the course of providing another professional activity not covered by this Directive provided that the provision of such advice is not specifically remunerated.

Are you eligible for any exemptions?



Yes. Not caught but depending upon exemption there may still be requirements imposed upon you

No



MIFID/MIFIR

A Guernsey Primer

MIFID/MIFIR

MIFID:

Directive transposed into national law – minimum harmonisation
Covers 'retail' clients

MIFIR:

Regulation, imposed at EU level – maximum harmonisation
Eligible counterparties and 'professional' investors

MIFID Scope

- Applies to investment firms, market operators, data reporting services providers and third country firms providing investment services or performing investment activities through the establishment of a branch in the EU.

Establishes requirements in relation to:

- Authorization and operating conditions (AOC) for investment firms
- **Provision of investment services or activities from third country firms through a branch**
- AOC for regulated markets, data service providers
- Supervision, co-operation and enforcement by competent authorities.

Much of MIFID also applies to authorized credit institutions providing investment services.

Exemptions

Various including:

- Insurers and reinsurance (when carrying out activities covered by Solvency II)
- Collective investment undertakings (not defined)
- Pensions funds (not defined)
- Person providing an investment service where that service is provided in an incidental manner and that activity is regulated by legal or regulatory provisions or a code of ethics governing the profession which do not exclude the provision of that service.
- Persons providing investment advice in the course of providing another professional activity not covered by the Directive provided that the provision of such advice is not specifically remunerated.

MIFIR Scope

Uniform requirements in relation to

- Disclosure of trade data to public
- Reporting of transactions to competent authorities
- Trading of derivatives on organised venues
- Non-discriminatory access to clearing and access to trading in benchmarks
- Product intervention power of competition authorities, ESMA and EGA and powers of ESMA on position management controls and position limits
- **Provision of investment services or activities by third country firms following an applicable equivalence decision by the Commission with or without branch.**

Key issues

- 1 What/who's in scope?
- 2 What's it entail?

Investment services and activities

- Reception and transmission of orders
- Execution of orders on behalf of a client
- Dealing on own account
- **Portfolio Management**
- **Investment advice**
- Underwriting of financial instruments and/or placing on a firm commitment basis
- Placing of financial instruments without a firm commitment
- Operation of an MTF or OTF (multilateral or organized trading facility).

MIFIR – eligible counterparties & professional investors

Professional investors

Entities which are authorized or regulated:

- Credit institutions
- Investment firms
- Other authorized or regulated financial institutions
- Insurance companies
- Collective investment schemes and management companies of such schemes.
- Pension schemes and management companies of such schemes.
- Commodity and commodity derivatives dealers
- Local
- Other institutional investors.

MIFIR – eligible counterparties & professional investors

Elected Professional investors

Criteria for those who can choose (subject to their being proper process for assessing their suitability) to be treated as professionals are local authorities (and a few others) plus individuals who meet two of the following three criteria:

- Already have carried out 10 transactions of significant size per quarter over the previous year
- Have more than half a million euros in their portfolio
- Have worked in financial services for over a year and should have knowledge of the specific products or services sold.

Branches

- A branch must comply with MIFID (as enacted by that member state) articles 16-20, 23, 24,25,27, 28(1), 30,31,32 and **Articles 3-26 of MIFIR**.
- Directive articles cover investment services generally, importantly articles 24,25, which covers **client principles, information and suitability of products**,
- Regulation articles cover pricing, pre and post trade transparency rules for market participants.
- Branches must also hold adequate capital (MIFID wording is vague ‘sufficient and initial capital is at the free disposal of the branch’) and their home jurisdictions must:
 - conform to FATF standards,
 - have Competent Authority agreements in place for the exchange of information,
 - have tax information exchange agreements in place in line the OECD Model Tax Convention on Income and Capital (ie TIEAs presently)
 - and there needs to be an investor compensation scheme in place that is ‘authorized or recognized’ by the EU investor protection directive – ie an EU standard scheme.
- In short for branches, EU levels of capital at branch and GSY needs to introduce EU style investor protection scheme.

MIFIR Equivalence

NB equivalence is required at jurisdictional and firm level – processes undetermined as yet but:

Article 47 of MIFIR states:

*'The legal and supervisory arrangements of that third country ensure that firms authorized in that third country comply with legally binding **prudential and business conduct requirements which have equivalent effect to the requirements set out in this Regulation, in Directive 2013/36/EU (ie Prudential Requirements Directive) and in Directive ../.../EU* (ie MIFID)** and in the implementing measures adopted under this Regulation and under those directives and that the legal framework of that third country provides for an effective equivalent system for the recognition of investment firms authorized under third country legal arrangements.'*

MIFIR Equivalence

Article 47 adds:

'The prudential and business conduct framework of a third country may be considered to have equivalent effect where that framework fulfills all the following conditions.

- 1) *Firms providing investment services and activities in that third country are subject to authorization and effective supervision and enforcement on an ongoing basis.*
- 2) *Firms providing investment services and activities in that third country are subject to sufficient capital requirements **and appropriate requirements applicable to shareholders and members of their management body.***
- 3) *Firms providing investment services and activities in that third country **are subject to adequate organizational requirement in the area of internal control functions.***
- 4) *Firms providing investment services and activities are subject to **appropriate conduct of business rules;***
- 5) *It ensures market transparency and integrity by preventing market abuse in the form of insider dealing and market manipulation.*

For example....

MIFID Article 9 (3)

'Member States shall ensure that the management body of an investment firm defines, oversees and is accountable for the implementation of the governance arrangements that ensure effective and prudential management of the investment firm including the segregation of duties in the investment firm and the prevention of conflicts of interest , and in a manner that promote s the integrity of the market and the interest of the clients.'

\$64m questions

- Narrow or wide interpretation of investment services?
- Do we need a MIFIR equivalent regime?
- What's an equivalent outcome?
- Can a bifurcated be taken?

Known unknowns

1. What equivalence looks like - ie costs of equivalence
2. Degree to which market access on MIFID/MIFIR's terms is required across sectors/firms
3. Economic case for / against equivalence

2014

MiFID II/MiFIR adopted by European Parliament on 15 April 2014 and by the Council on 13 May 2014.

Entered into force on 2 July 2014.

MiFID II/MiFIR empowers ESMA to propose regulatory technical standards and implementing technical standards. Furthermore, the European Commission requests ESMA to provide technical advice for the adoption of Commission delegated acts.

November 2014: GFSC discussion paper on 'Revision of Laws'.

7 & 8 July ESMA Open hearings in Paris.

May to August 2014 ESMA Public Consultation Paper (Technical Advice for Delegated Acts) ended 1 August 2014.

May to August 2014 ESMA publishes a Discussion Paper to gather input from stakeholders on the proposed regulatory technical standards and implementing technical standards, ended 1 August.

November to December 2014: GFSC engagement with key stakeholders.

December 2014 Final Technical Advice from ESMA for Delegated Acts.

December 2014 to March 2015 ESMA Public Consultation (following responses received on Discussion Paper) on Regulatory technical standards and implementing standards.

2015

February 2015: GFSC consultation paper on 'Revision of Laws' published.

June 2015 Final Regulatory technical standards submitted to the European Commission (12 months after entry into force of MiFID II)

December 2015 Final Implementing technical standards (18 months after entry into force of MiFID II)

Followed by Policy letter to States towards end of 2015.

2016

Law drafted by Law Officers for States approved with anticipated Royal Assent by the end of 2016.

June 2016 EU Members have are required to implement MiFID II in their national legislations within 24 months after the entry into force of MiFID II

2017

January 2017 MiFID II/MiFIR will apply within 30 months after the entry into force of MiFID II