
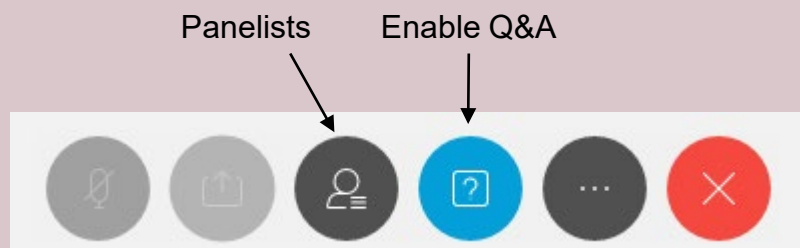


# Housekeeping

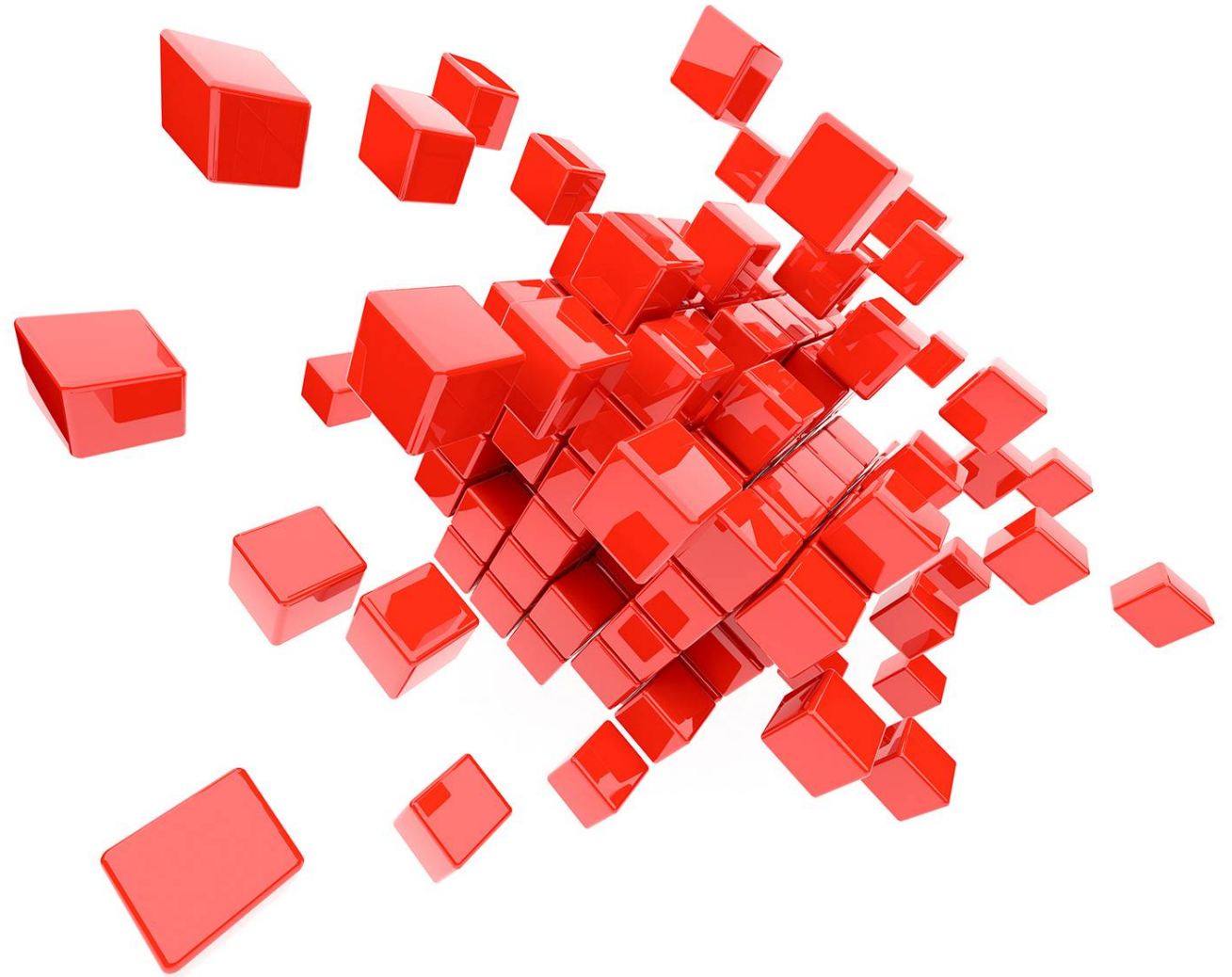
- On joining the session your microphone will be muted and your video will be turned off
- You will not be able to enable your video or un-mute your microphone during the session
- To activate the Q&A function click  the Q&A box will appear on the right hand panel
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## Fog in Channel: the MiFIR edition

Bob Penn, Damian Carolan | 23 July 2020



# What we are going to discuss today

## 1. An update from Europe

## 2. Onshoring MiFIR – what does it mean for firms?

- Background
- Process – key stages in MiFIR onshoring, and how they affect implementation
- Application – issues for EU firms
- Main substantive requirements
  - Transparency
  - STO
  - DTO
  - Transaction reporting

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*Some good news from  
the EU... and some bad*

# Clearing obligation: EU gives ground

Getting ready for changes - Communication on readiness at the end of the transition period between the European Union and the United Kingdom (9 July)

Obligation	Current EU rule	Impact of onshoring and third country status (of the UK under EU law, and <i>vice versa</i> )	Implications for markets
<b>Clearing</b>	EMIR prohibits CCPs from providing clearing services unless authorised in the EU or recognised. Recognition requires equivalence.	Following Brexit, the UK will have its own version of EMIR. At present the EU regime does not recognise the UK as equivalent.	Absent recognition of the UK CCPs, EU market participants will be unable to be members of the UK CCPs.

*... in the short term and in order to address the possible risks to financial stability, the Commission is considering the adoption of a **time-limited equivalence decision** for the United Kingdom... Such a time-limited decision would allow EU-based CCPs to develop further their capacity to clear relevant trades in the short and medium term and EU clearing members to take and implement the necessary steps, including by reducing their systemic exposure to UK market infrastructures.*

# Equivalence in other areas – not such a good story

*“With regard to the latter areas, the Commission **will not adopt an equivalence decision in the short or medium term.**”*

Affected financial services areas

**MIFIR - Art. 33(2) - DTO**; Art. 38(3) - Access for third-country trading venues and CCPs; Art. 47(1) - Investment firms providing investment services to EU professional clients and eligible counterparties

MiFID II - Art. 25(4)[a] - Regulated markets for the purposes of easier distribution in the EU of certain financial instruments

MAR - Art. 6(6) - Exemption for climate policy activities

SSR - Art. 17(2) - Exemption for market making activities

Prospectus Regulation - Art. 29(3) - Prospectus rules

Further stakeholder notice **Withdrawal of the United Kingdom and EU rules in the field of markets in financial instruments (13 July)**

*Key messages*

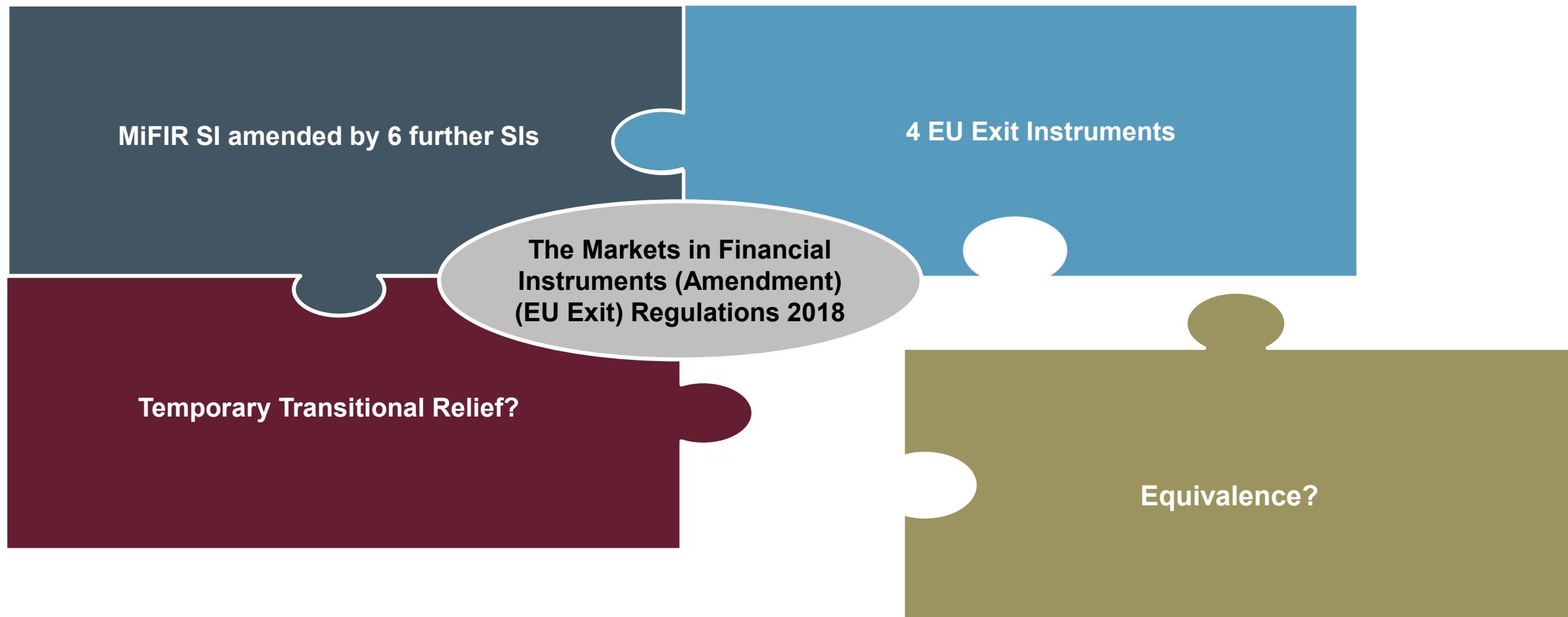
- *Tell your clients what’s going to happen at IPCD*
- *Prepare for no equivalence*

*“All stakeholders thus have to be informed and ready for a scenario where shares and derivatives subject to the EU trading obligations can no longer be traded in the UK trading venues.”*

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# *Onshored MiFIR - Background*

# UK MiFIR

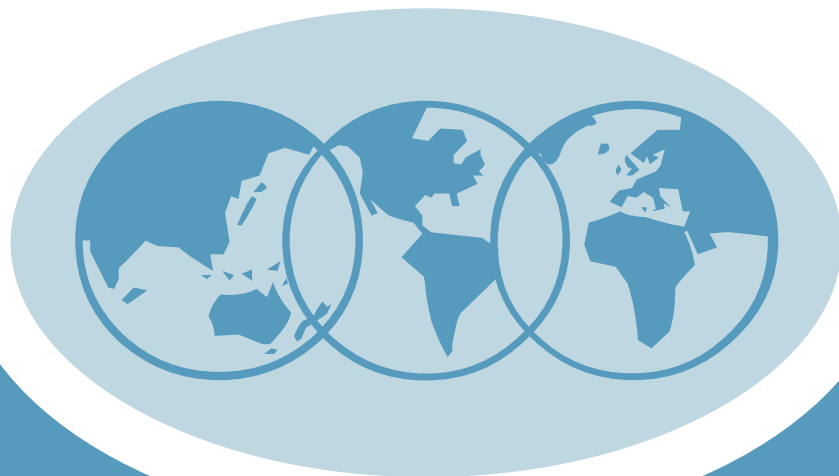




# Legislation amended by the SI

EU Legislation	UK Legislation
Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 ( <b>MiFIR</b> )	Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017 (SI 2017/701) (the <b>MiFI regulations</b> )
Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive (the <b>MiFID Org Regulation</b> )	The Data Reporting Services Regulations 2017 (SI 2017/699) (the <b>DRS regulations</b> )
Commission Delegated Regulation (EU) 2017/567 of 18 May 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regard to definitions, transparency, portfolio compression and supervisory measures on product intervention and positions (the <b>MiFIR Delegated Regulation</b> )	Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (the <b>RAO</b> )

# Scope of MiFID II regime – becoming third countries



The MiFID SI generally provides that EU states are treated as third countries.

However, there are certain **exceptions** “to help provide for a smooth transition for market participants by maintaining existing outcomes as far as possible”

## Exceptions

1. EEA emission allowances will continue to be a financial instrument.
2. Energy forwards that must be physically settled and are traded on OTFs in the EU will continue to be excluded from the definition of financial instruments.

*NB EU firms only: EU MiFID will change in scope to include energy forwards which are physically settled and traded on UK OTFs as financial instruments.*

# Temporary Transitional Powers relevant to MiFIR

## Main FCA Transitional Direction (Part 3 of Main FCA Transitional Direction)

- “*only applies in the cases set out in the Annexes...*”
- “*... where as a result of the operation of an exit instrument, a relevant obligation... applies to a person differently... the obligation is modified so that a person does not breach it if they comply with the obligation as it applied immediately before [IPCD]...*” (3.1D)
- Annex A: para 24:
  - Preserves post-trade reporting waterfall under Art 20/21 MiFIR
  - Stands still changes to Chapters II and II of MiFID II Organisational Requirements Regulation (organisational requirements; operating conditions) (but not for TP firms)

## FCA TP Transitional Direction (Part 5 of Main FCA Transitional Direction)






- “*does not apply to TP firms for the purposes of the Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018 or technical standards previously deriving from MiFID or MiFIR*” (5.5D (1))

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*Application – issues for  
EU firms*






# How does MiFIR apply to EU firms? What the law says... and FCA appears to think

Requirement	Application in TPR			Application post-TPR	
	Branch	Services		Branch	Services
Pre-trade transparency	Unclear how substituted compliance works	Unclear whether FCA intends to apply globally		Scope?	
Post-trade transparency	Unclear how substituted compliance works			Scope?	
Share trading obligation		Unclear whether FCA intends to apply globally		Scope?	
Derivatives trading obligation		Unclear whether FCA intends to apply globally		FCA considers the DTO applies to branches! Scope?	
Transaction reporting				Scope?	
Supply of reference data					

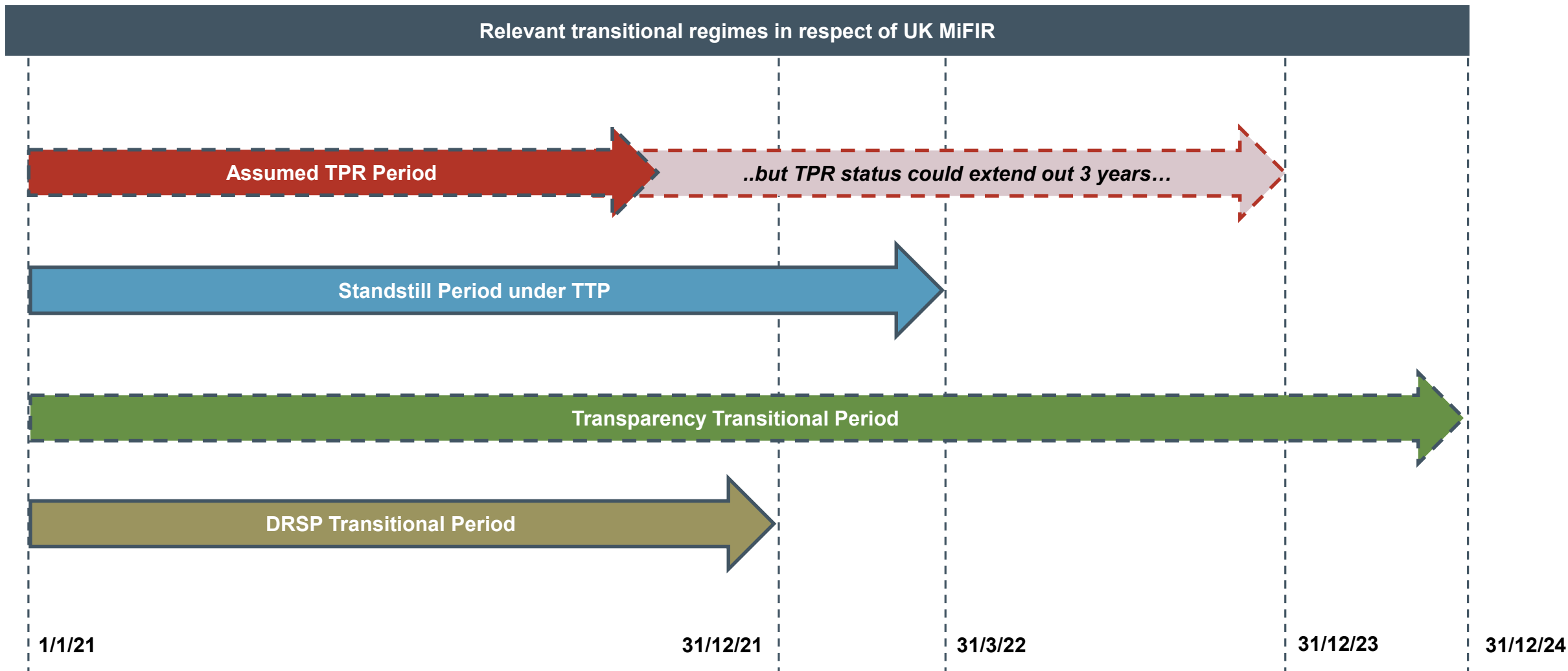
Key		
	Obligation applies	 Obligation does not apply
	Obligation strictly applies to worldwide activities	
	Obligation applies; substituted compliance available	 Obligation applies to worldwide activities; substituted compliance available

# How does MiFIR apply to EU firms? What the law says... (2)

Requirement	Application in TPR			Application post-TPR	
	Branch	Services		Branch	Services
Record keeping		Unclear whether FCA intends to apply globally			
Portfolio compression		Unclear whether FCA intends to apply globally			
Submission to clearing		Unclear whether FCA intends to apply globally			
Indirect clearing		Unclear whether FCA intends to apply globally			

Key	
 Obligation applies	 Obligation does not apply
 Obligation applies; substituted compliance available	 Obligation strictly applies to worldwide activities
 Obligation strictly applies to worldwide activities; substituted compliance available	

# Planning difficulties until you have a date to exit TPR



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# *Transparency*



# Transparency – principles underpinning SI

Base case – only UK data and transactions now important

Existing waivers now no longer appropriate – new calculations required

SI builds in broad scope for FCA temporary powers (for up to 4 years) to amend operation of transparency regime

FCA can suspend transparency requirements in respect of certain instruments

FCA can amend transparency calibrations and direct the application of the double volume cap mechanism

FCA can determine the ‘relevant area’ for transparency calculations to also include EU 27 jurisdictions

# Equity transparency

## What changes?

**TOTV:** scope of transparency requirements change from EU TOTV to UK TOTV

**Data reference systems:** EU FIRDS/FITRs to be superseded by UK FIRDS/FITRS

**SI status and calculations change:** (a) dealings on EU venues becomes OTC for purposes of the UK SI regime; (b) criteria for determining SI status are set by reference to the frequency and volume of transactions in a “relevant area” rather than the EU

**Liquidity determination:** FCA to calculate liquidity determinations under RTS 2 and publish; until it does so, follow last EU calculation (NB that liquidity determinations affect SIs’ quoting obligations.)

**Standard market size:** FCA to publish SMS determinations for certain instruments. (For static calculations, FCA’s determination of liquidity will also be relevant.)

**Double Volume Cap:** FCA power to vary DVC

**Post-trade transparency:** reporting via UK APA (subject to DRSP transitional regime) required. Reporting fields will change

**Post-trade transparency reporting waterfall:** will change (subject to transitional relief)

**Suspension power:** FCA may suspend pre- and post-trade transparency

## TP firms

**Application:** Technically, requirements apply to TP firms’ global activities and to third country branches’ UK branch activities. FCA appears to expect branch-level compliance though.

**Substituted compliance:** available where TP firm “complies with a requirement in [EU MiFIR] as it has effect in EU law in relation to the services it provides in the UK” and “the EEA requirement has equivalent effect”

-Does that exempt all dual TOTV instruments? Just those where a firm is also an SI under EU MiFIR?

## Third country firms

**Scope:** branch level application – what activities attract the SI requirements? Marketing, trading, booking?

**Publication:** will a separate MIC code be needed?

## Next steps

Connect to UK FIRDS/FITRS

Assess revised (or new) SI status; build reporting



# Non-equity transparency

## What changes?

**TOTV:** scope of transparency requirements change from EU TOTV to UK TOTV; some changes in instruments' classification

**Data reference systems:** EU FIRDS/FITRs to be superseded by UK FIRDS/FITRS

**SI status and calculations change:** (a) dealings on EU venues becomes OTC for purposes of the UK SI regime; (b) criteria for determining SI status are set out in the amended MiFID Org Reg, which considers the frequency and volume of transactions in a "relevant area" rather than the EU

**Liquidity determination:** FCA to calculate liquidity determinations under RTS 1 and publish; until it does so, follow last EU calculation/assume illiquid. (NB that liquidity determinations affect SIs' quoting obligations.)

**SSTI determinations:** FCA to publish SSTI determinations for certain instruments. (For static calculations, FCA's determination of liquidity will also be relevant.)

**Post-trade transparency:** reporting via UK APA (subject to DRSP transitional regime) required. Reporting fields will change.

**Post-trade transparency reporting waterfall:** will change (subject to transitional relief)

**Suspension power:** FCA may suspend pre- and post-trade transparency

## TP firms

As above

## Third country firms

As above

## Next steps

As above

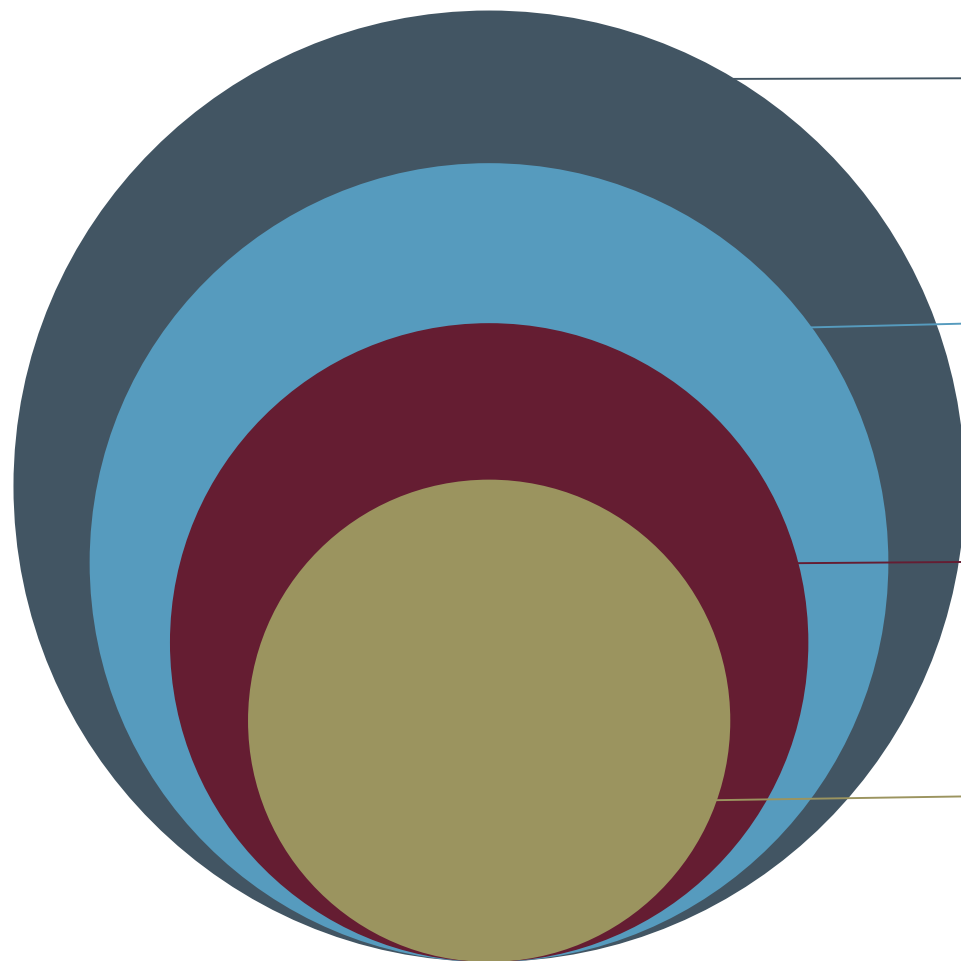


# Implications for EU (and third country) firms

- Are UK branches of EU and third country firms subject to the SI obligations?
- If so, on a branch or whole firm basis?
- What activities are covered?

Obligation	Intepretative issue(s)	TP firms	Third country firms
<b>SI status</b>	How does a foreign firm determine whether it is an SI, and on what basis?	TP firms are strictly subject to pre-trade transparency with respect to their worldwide activities. (MiFIR Art 2A). FCA appears to believe that it applies only on a branch basis, but has not issued any formal guidance.	SI obligations apply on a branch basis under GEN 2.2.22A. FCA has not issued any formal guidance.
<b>Substituted compliance</b>	How should substituted compliance work for TP firms – to all dual TOTV instruments, for just those for which they are SIs in the EU?	Substituted compliance applies where EU <i>requirement “has equivalent effect to a requirement in this Regulation as it applies in the United Kingdom”</i> . FCA has not issued any guidance.	N/A
<b>Quality of execution reporting</b>	On what basis does a firm publish execution quality data under RTS27/28 – on a branch or whole firm basis?	COBS11.2C(1) and MAR 6.3A(1) each applies on a branch basis only, as do the RTS. No substituted compliance available (GEN 2.2.29). FCA has not issued any guidance.	COBS11.2C(1) and MAR 6.3A(1) each applies on a branch basis only, as do the RTS. FCA has not issued any guidance.

# Transparency – to do list



✓ identify channels of communication used to meet transparency publication requirements

✓ connect to UK FIRDS/FITRS

✓ assess status  
✓ monitor suspensions, changes to waivers, thresholds  
✓ update SI policies

✓ TPR Firms must distinguish between UK TOTV instruments eligible for substituted compliance, where relevant

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*Share and derivatives  
trading obligations*

# Equivalence : derivatives trading obligation and share trading obligation

DTO and STO are now the most prominent equivalence issues given the threat that they pose to existing cross-Channel activity.

Obligation	Current EU rule	Impact of onshoring and third country status (of the UK under EU law, and vice versa)	Implications for markets
<b>Derivatives Trading Obligation (DTO)</b>	The DTO requires financial counterparties (FCs) or non-financial counterparties meeting the clearing threshold (NFC+s) to trade in classes of derivatives that are subject to the DTO (currently certain interest rate derivatives and index CDS) on (1) an EEA trading venue or (2) a recognised non-EU trading venue.	Following Brexit, the UK will have its own DTO. At present neither regime recognises the venues of the other.	Absent recognition, EU27 FCs and NFC+s will be unable to deal with UK FCs and NFC+s in in-scope derivatives unless they trade on a US or Singaporean venue.
<b>Share Trading Obligation (STO)</b>	The STO requires EU banks and investment firms to trade in shares issued by EU companies which are listed in the EU on (1) an EU systematic internaliser; (2) an EU trading venue; or (3) a recognised non-EU trading venue.	Following Brexit, the UK will have its own STO. At present neither regime recognises the venues of the other.	Absent recognition, this will split liquidity in dual traded shares subject to both the EU and UK STO. This will also have the effect of limiting liquidity more generally.

# EU Share Trading Obligation – some light at the end of the tunnel?

## ESMA MiFID II/MiFIR Review Report on 16 July 2020

### Notes MiFIR applies to all shares available for trading on at least one EU trading venue without

- taking liquidity into account
- differentiating between EU and non-EU shares

### Acknowledges challenges in practice regarding

- non-EU shares
- main pool of liquidity in a third country
- in particular, when this third country is not covered by an equivalence decision

### Approach to date relies on EU ISIN to limit effects

### ESMA recommendation to amend Art 23 MiFIR

- Continue to rely on EU ISIN as a proxy for main pool of liquidity in the EU
- But trading also permitted in “EU shares” on a third-country trading venue where transactions are executed in the third-country domestic currency





# Implications for EU (and third country) firms

- Are UK branches of EU (and third country) firms subject to the UK STO and DTO?
- If so what trades are covered?

Obligation	Intepretative issue(s)	TP firms	Third country firms
<b>Derivatives Trading Obligation (DTO)</b>	<p>Article 28 (DTO) applies to FCs and NFC+s when they conclude transactions in in-scope derivatives.</p> <p>Is a TP firm an FC/NFC+ for this purpose?</p> <p>Nexus: if it does apply, what does “shall conclude” mean with respect to a branch?</p>	<p>TP firms are strictly subject to the UK DTO with respect to their worldwide activities. (MiFIR Art 2A). FCA appears to believe that it applies only on a branch basis.</p> <p>There is no guidance on the ambit of “conclude”.</p>	<p>FCA appears to believe that the DTO applies on a branch basis under GEN 2.2.22A.</p> <p>There is no guidance on the ambit of “conclude”.</p>
<b>Share Trading Obligation (STO)</b>	<p>The STO applies to a firm when it “undertakes” a trade in relevant shares.</p>	<p>TP firms are strictly subject to the UK STO with respect to their worldwide activities. (MiFIR Art 2A). FCA appears to believe that it applies only on a branch basis.</p> <p>There is no guidance on the ambit of “undertake”.</p>	<p>STO applies on a branch basis under GEN 2.2.22A.</p> <p>There is no guidance on the ambit of “undertake”.</p>

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# *Transaction reporting*

# Transaction reporting



UK firms and UK branches of foreign firms will be required to report transactions in instruments which are traded on UK or EU venues

UK venue operators will be required to report reference data for instruments that are trading on UK venues, and to report non-reportable transactions of EU investment firms

# Implications for EU (and third country) firms

What transactions are covered?

Obligation	Intepretative issue(s)	TP firms	Third country firms
<b>Transaction reporting</b>	<p>Article 26 (transaction reporting) applies where an investment firm “executes” a transaction in financial instruments.</p> <p>Nexus: what does “execute” mean with respect to a branch?</p>	<p>“Execute” has no statutory definition and is not subject of guidance. Informally FCA appears to be taking a wide view based on reporting fields.</p>	<p>As TP firms?</p>

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# *Resources*

# Resources



Allen & Overy Brexit toolkit

[Allen & Overy Brexit Law – Financial Services](#)

Brexit SI tracker

Regulators' publications  
– TPR  
– BTS/Rule set changes

Equivalence table

A&O Brexit Briefings

# Questions?

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