



Proposal for MiFID review. November 2011.

The proposal for amending the 2004/39/CE Directive (onward MiFID) and the proposal for Regulation (MiFIR) have been submitted by the EC to the Council and to the Parliament of the EU on the 20th of October. The MiFID review constitutes a part of the integral reforms within the UE to achieve a safer, sounder more transparent and more responsible financial system according to the G 20 commitments to tackle the, up to now, less regulated and more opaque parts of the financial system (OTC instruments and derivatives).

The changes introduced aim, according to the recommendations from the *De Larosière* Group and the conclusions of the ECOFIN Council, to minimise –as the Recital 45 includes– the discretions available to Member States that were a common thread for the a development of a level playing field for Member States and market participants. The proposal also seeks to improve supervision, reduce costs for market participants, improve conditions of access and enhance the global competitiveness of the EU financial industry. The most remarkable items of the MiFID review are:

Level-playing field

The different trading venues –regulated markets, Multilateral Trading Facilities (MTF), and the new category of trading platform the Organised Trading Facilities (OTF)- have identical organisational, pre and post transparency, and supervision requirements. In all three venues the operator of the platform is neutral although the operator of a OTF has a degree of discretion over how a transaction will be executed so that they perform a service to clients which is qualitatively (if not functionally different form the services provided by regulated markets and MTFs to their members and participants; it is necessary, to ensure the OTF operator’s neutrality, to prohibit the trading against his own proprietary capital. The systematic internalisation is not a trading venue and is subject to specific pre-trade transparency and access requirements; any trading on own account by investment firms with clients, including other investment firms, is considered over-the-counter.

Extension of MiFID scope to products and services.

The proposal extends the MiFID scope to other products and services; concretely, emission allowances are considered as financial instruments and the definition of “executing client orders” is extended to include the selling –not necessarily attached to advise or other financial service- of financial instrument issued by a credit institution or and investment firm at the moment of their issuance. The Recital 26 establishes that it is appropriate to include also the structured deposits, in line with the future Regulation of PRIPs (Packaged Retail Investment Products).

Revision of MiFID exemptions.

The proposal limits the exemptions more clearly to activities which are not financial or ancillary services defined in MiFID, but primarily proprietary or commercial in nature. The dealing on own account is excluded from being considered investment service unless they are market makers, members or participants in a regulated market or MTF or they execute clients orders. Persons who deal on own account as ancillary activity to their main non-financial business should not be covered according to Recital 14 of the proposal.

Upgrades to the market structure framework.

The proposal creates a new market category (Organised Trading Facilities (OTF)) whose request for authorisation shall include a detailed explanation why the system does not correspond to and cannot operate as either a regulated market, MTF or systematic internaliser. The MIR refers to the so-called crossing networks (systems operated by investment firms which mainly internally match client orders) as one of the venues captured under this new category.

The OTFs have strong organisational requirements, identical transparency rules and upgrade key requirements to enhance greater competition and cross-border trading. Recital 12 says that OTFs should be able to determine and restrict access based inter alia on the role and obligations which their operators have in relation to their clients, and Recital 13 adds that an OTF is any system or facility in which multiple third parties buying and selling interests interact in the system.

Pre and post trade transparency requirements (and its waivers excluding orders that are large in scale compared with normal market size) are not contained in the MiFID but in the MiFIR.

Improvements to corporate governance.

It is proposed to strengthen the requirements for directors (both executive and non-executive): particularly, members of the boards and directors should possess the sufficient knowledge and skills and comprehend the risk associated with the activity of the firm in order to ensure the firm is managed in a sound and prudent way in the interests of investors and market integrity. Also, the proposal seeks the balance in the composition of the management bodies.

Enhanced organisational requirements to safeguard the efficient functioning and integrity of markets.

The proposal considers the algorithmic trading, the direct electronic access and the high frequency trading and the firms involved (including those offering market access to other high frequency traders) and brings all of them into MiFID; they should have appropriate organisational safeguards. The High Frequency Traders should report on-going buy and sell orders in the trading venues where they operate nevertheless market conditions. The venues should adopt appropriate risk controls (for example, circuit breakers) to mitigate disorderly trading and ensure the resiliency of their platforms and also assist the oversight and monitoring of such activities by competent authorities.

Enhancement of the investor protection framework.

The proposal, in investment advice, enlarges the disclosure of information to clients (sources of information and on-going assessment of the suitability of the financial instruments recommended) and, in investment advice and portfolio management services, restrains investment firms to accept incentives by third parties (inducements); clarifies the conditions under which the execution of orders and/or reception and transmission of client orders on certain non-complex instruments does not require the assessment of suitability from the clients; addresses the future development of guidelines on cross-selling practices; and describe how firms and their agents should handle funds and instruments belonging to their clients.

Heightened protections in the provision of investment services to non-retail clients.

It is proposed that local authorities and municipalities could be treated as professional clients if they ask for and comply with the requirements provided, and that the principle of acting honestly, fairly and professionally and the obligation to be fair, clear and not misleading should apply irrespective of client categorization, including eligible counterparties. .

New requirements for trading venues.

The proposal introduces a requirement to publish annual data on execution quality (such as the number of orders cancelled prior to execution or the speed of execution). Also, Member States shall require investment firms to summarize and make public on an annual basis, for each class of financial instruments, the top five execution venues where they executed client orders in the preceding year.

It is proposed that Trading venues on which commodity derivative contracts are traded adopt appropriate limits or alternative arrangements to ensure the orderly functioning of the market and settlement conditions for physically delivered commodities, and provide systematic, granular and standardised information on positions by different types of financial and commercial traders to regulators (including the category and identity of the end-client) and market participants (including only aggregate positions of categories of end-clients).

An improved regimen for SME markets.

It is proposed to create a new subcategory of markets known as SME growth markets. An operator of such a market (which are usually operated as MTFs) could elect to have the MTF also registered as an SME growth market if it meets certain conditions. The registration should help lead to common regulatory standards for such markets which would take in to account the needs of issuers and investors and the investor protection in these markets.

Increased and more efficient data consolidation.

The proposal aims to diminish the difficult access to transactions executed in different trading venues and improve the data quality and consistency. There are different data reporting services: the Approved Publication Arrangement (APA), through which the firms make public the information as close to real time as is technically possible, on a reasonable commercial basis; the Consolidated Tape Providers (CTPs), to make public the consolidated information into a continuous electronic data stream as close to real time as is technically possible on a reasonable commercial basis; and the Approved Reportings Mechanisms (ARMs), to report the information no later than the close of the following working day.

Heightened Powers over derivative-positions for competent authorities.

It is proposed that the competent authorities are bestowed with explicit powers to demand information from any person regarding the positions held in the derivative instruments (regarding the size and purpose of a position and any assets or liabilities in the underlying market), and to limit by introducing non-discriminatory limits on positions or the number of contracts per underlying which any given class of persons can enter into over specified of time, when necessary to ensure the integrity and orderly functioning of the affected markets.

Effective sanctions.

The appropriate administrative sanctions will be applied to breaches of MiFID to those natural or legal persons and to investment firms responsible for a breach and they should be published. The maximum level of administrative pecuniary sanctions laid down in national legislation should exceed the benefits derive from the breach and the criteria taken into account when determining the type and level of the sanction to be applied in a particular case should include at least the criteria set out in the Directive (benefits derived from the violation or losses cause to third parties, cooperative behaviour of the responsible person). Investment firms should put in place appropriate mechanism to encourage reporting of breaches.

If you want to read the whole documentation please do click on: http://ec.europa.eu/internal_market/securities/isd/mifid_en.htm

