

## **Review of the Markets in Financial Instruments Directive**

### **Questionnaire on MiFID/MiFIR 2 by Markus Ferber MEP**

The questionnaire takes as its starting point the Commission's proposals for MiFID/MiFIR 2 of 20 October 2011 (COM(2011)0652 and COM(2011)0656).

All interested stakeholders are invited to complete the questionnaire. You are invited to answer the following questions and to provide any detailed comments on specific Articles in the table below. Responses which are not provided in this format may not be reviewed.

Respondents to this questionnaire should be aware that responses may be published.

Please send your answers to [econ-secretariat@europarl.europa.eu](mailto:econ-secretariat@europarl.europa.eu) **by 13 January 2012.**

Name of the person/organisation responding to the questionnaire	<b>Financial Services Authority</b>
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<b>Theme</b>	<b>Question</b>	<b>Answers</b>
Scope	1) Are the exemptions proposed in Directive Articles 2 and 3	The changes to Article 2 are designed to: (i) bring high-frequency trading firms who are direct members of markets inside the scope of the directive; and, (ii) narrow the scope of

	<p>appropriate? Are there ways in which more could be done to exempt corporate end users?</p>	<p>trading in commodity derivatives that falls outside of regulation. We support the objectives of the Commission and the proposed changes on high-frequency trading firms but have concerns about the detail of what is proposed in relation to commodities.</p> <p>The changes proposed by the Commission mean that end users of commodities would fall inside the scope of the directive if their trading in commodity derivatives was not judged to be ‘ancillary’ to their main business. The Commission has set out some useful factors to be taken into account when making this judgement, however, without knowledge of how the criteria to determine ancillary will be set at level 2 it is not possible to reach a conclusion on the extent to which the changes will bring corporate end users within the scope of MiFID.</p> <p>It also needs to be understood that the breadth of the exemption for commodities firms is potentially affected by the definition of financial instruments. The broader the scope of the definition of financial instruments the more financial services activity end users will be carrying out. Here there is a particular concern about the Commission’s proposed change to C(6) of Annex I to include physically-settled contracts traded on OTFs. This risks bringing into the scope of financial services regulation many commercial, physically-settled contracts.</p> <p>The UK has regulated activity in commodity derivatives markets since the late 1980s. The scope of regulation for firms dealing on own account in commodity derivatives is not set by reference to whether or not the activity is ‘ancillary’ or not. In the UK end users dealing on own account in commodity derivatives can remain exempt if their counterparties are credit institutions/investment firms or other end users where the transaction has been arranged by a credit institution/investment firm. As a result end users either set up a regulated entity to arrange transactions on their behalf or their transactions are arranged by existing credit institutions/investment firms.</p> <p>Wherever the boundary is finally set one of the most significant potential costs of</p>
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		<p>regulation for specialist commodity derivatives firms is their capital requirement. Currently they are exempt from key aspects of the Capital Requirements Directive (CRD) but this exemption expires at the end of 2014. It will be important for the Commission to ensure that a thorough review of the options for an appropriate prudential regime for these firms is conducted and that whatever option is chosen an adequate time is given to firms to adapt to the regime. We would encourage the Parliament to support this review and that it should take place in a timely manner.</p> <p>We believe there continues to be a case for an optional exemption under Article 3. The overwhelming majority of firms in the UK falling under this exemption have opted to stay out of the directive because they are small firms who do not have any interest in providing services in other Member States. They are already subject to conduct rules which are very similar to those imposed on firms conducting the same business who are authorised under the directive in order to provide consistent consumer protection.</p> <p>The Commission is proposing to change the scope of the Article 3 exemption. Firms who receive and transmit orders in relation to the narrow list of instruments covered in the article but who do not provide investment advice would require authorisation under the Commission's proposals. We do not believe that this change is proportionate. Most of the firms affected (of whom there might be 30 to 40 in the UK) are small firms and it will simply encourage them to apply for an unnecessary permission to provide investment advice to remain outside the directive.</p>
	<p>2) Is it appropriate to include emission allowances and structured deposits and have they been included in an appropriate way?</p>	<p><u>Structured deposits</u></p> <p>The FSA agrees with the proposals to extend certain MiFID requirements to cover the sale of structured deposits, to ensure consumers get a consistent level of protection regardless of the legal form of the products they buy.</p> <p>However, it will also be important for the MiFID II proposals to be customised to reflect the nature of structured deposits. As the products are deposits, the Directive will need to reflect, for example, their coverage by the Deposit Guarantee Schemes Directive</p>

		<p>(DGSD) for compensation purposes, rather than the Investor Compensation Scheme Directive.</p> <p><u>Emission allowances</u></p> <p>We understand that emissions allowances have been brought within MiFID in response to various problems with spot market trading in recent years. These problems included most prominently the theft of allowances from national registries and VAT carousel fraud perpetrated through the emission trading scheme. It is debateable whether the application of financial services regulation addresses either of these problems and we note that action had already been taken by member states and the Commission to address these issues, where the introduction of the Registry Regulation and of a common EU platform for emissions allowances and of zero rating for VAT have gone a long way to mitigating these risks.</p> <p>Application of financial services regulation to the spot market does have the potential benefit of covering trading in these allowances with the provisions of the Market Abuse Regulation and therefore to hopefully deter market manipulation. We have however not been made aware of any significant manipulation or attempted manipulation of this market. We believe this is due to the market's size and the consequent difficulty for any would-be manipulation of cornering physical supply of allowances.</p> <p>We are not aware of any in depth cost benefit analysis by the Commission to justify its decision to classify allowances as financial instruments. It may though lead to significant costs for participants who are not currently regulated, although the number of these is not known and is uncertain because of the review of MiFID exemptions. These costs include costs of compliance as well as potential greater costs, including capital, of prudential regulation when the CRD is reviewed.</p> <p>We suggest that the physical market spot allowances could alternatively be added to the</p>
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		REMIT regime, because they are intrinsically linked to the physical market trading of gas and power and are therefore natural companions. In any case we note that a suitable alternative could be to give this jurisdiction to physical market regulators, as has been done in France.
	3) Are any further adjustments needed to reflect the inclusion of custody and safekeeping as a core service?	No.
	4) Is it appropriate to regulate third country access to EU markets and, if so, what principles should be followed and what precedents should inform the approach and why?	<p>Yes – the current MiFID framework governing the access of third country firms to EU markets (current Recital 28) has worked well in practice. Third country firms authorised to provide services and perform activities through a branch in a Member State do not have passporting rights and cannot be afforded more favourable treatment than branches of investment firms having their head office in the EU. Given the way the current regime has worked it is therefore unclear why wholesale reform is required.</p> <p><b>Impact</b></p> <p>Without prejudice to the position of principle stated above, detailed comments highlighting our concerns with the proposals – together with remedial suggestions that we view as necessary to conceive of an appropriate harmonised EU framework – are provided against the specific articles in this table (<b>see articles 41-46 MiFID and articles 36-39 MiFIR</b>).</p> <p>We wish nonetheless to make the following overarching points:</p> <ul style="list-style-type: none"> <li>• The scope of access restrictions coupled with the firm deadline for the restrictions to come into effect would significantly curtail the ability of third-country firms to do business in the EU and is also potentially very damaging to EU investors and firms.</li> <li>• <b>Reciprocity</b> should not be a condition for access as it will undermine the</li> </ul>

		<p>effectiveness of the proposed regime (see response to question 29).</p> <ul style="list-style-type: none"> <li>Any <b>equivalence assessment</b> should be outcomes-based (vs. a detailed line-by-line assessment of the third country's regulatory framework as currently drafted). It is not clear, how many jurisdictions will be able to jump the equivalence hurdle and with a firm four year deadline for the new restrictions come into effect – coupled with the inevitable resourcing constraints that the Commission will face in practice – the suggested arrangements are simply unworkable.</li> <li><b>Professional clients</b> should be subject to the same regime as eligible counterparties. By mandating the provision of all investment services to professional clients to take place through the establishment of a branch in the EU, the Commission's proposals will negatively impact the competitiveness of the EU's international financial centres without improving investor protection.</li> </ul>
Corporate governance	5) What changes, if any, are needed to the new requirements on corporate governance for investment firms and trading venues in Directive Articles 9 and 48 and for data service providers in Directive Article 65 to ensure that they are proportionate and effective, and why?	<p>We want to see strengthened corporate governance of investment firms. However, we want to ensure that corporate governance proposals are proportionate and work for firms of all sizes. The FSA has concerns that the material in the proposal, particularly when supplemented by technical standards, could be too prescriptive and restrictive particularly for small firms providing limited services. There is also an issue of ensuring consistency with CRD IV (at the moment the proposals are largely the same, though the MiFID deadline for BTS is 2014 while the deadline for BTS under CRD IV is 2015).</p> <p>In Article 9 of the proposed text there is the option for competent authorities to allow a person to hold additional directorships beyond the limits set out. Competent authorities should also have the discretion to limit an individual to fewer directorships, in order to achieve the general aim set out in Article 9 1. (a) that members of the management body shall commit sufficient time to perform their functions in the investment firm.</p>
Organisation of markets	6) Is the Organised Trading Facility category appropriately defined and	We welcome the proposal to introduce a new category of trading venue to cover both broker crossing systems and venues suitable for the trading of derivatives subject to the

and trading	differentiated from other trading venues and from systematic internalisers in the proposal? If not, what changes are needed and why?	<p>G20 obligation.</p> <p>In broad terms, we consider that the OTF category is appropriately defined and, in particular, would include venues that bring together buying and selling interests through the use of discretion by the platform operator (while excluding facilities in which no genuine trade execution or arranging takes place). This approach will ensure that facilities such as the voice and hybrid trade execution services of inter-dealer brokers, which perform a critical role in providing trading opportunities in less liquid non-equity markets, are brought within the scope of trading venue regulation. This would represent a significant tightening of regulatory standards for such platforms.</p> <p>However, we have some concerns over the requirements for an OTF:</p> <p>Article 20 of MiFID would prohibit the operator of an OTF from executing client orders against its proprietary capital within the OTF, where it offered own account dealing services. This prohibition would extend to the execution of orders by way of a matched principal service. The resultant loss of liquidity support to such systems by dealers, particularly in the context of less liquid non-equity instruments (such as bonds) could have a significantly adverse effect on the efficiency of the market. The stated objective of the dealing restriction (namely, the maintenance of operator neutrality) can be achieved in a different way, for example through a venue-specific requirement for the operator to apply conflicts management procedures (as is being proposed by MiFID for the operation of a MTF). In any event, we do not consider that it is appropriate to treat the execution of client orders on a matched principal basis as dealing on own account, as this would serve to deprive end users of services where the platform operator stands between the buyer and the seller, enabling counterparty risk to be managed.</p> <p>We also note that, according to its recitals, MiFIR intends that the new on-venue pre-trade transparency regime for non-equity instruments should be calibrated “...for different types of trading, including order-book and quote-driven systems as well as</p>
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	<p>7) How should OTC trading be defined? Will the proposals, including the new OTF category, lead to the channelling of trades which are currently OTC onto organised</p>	<p>There is no need to have a specific definition of OTC trading, but it should be considered to be all trading that is not undertaken on one of the trading venue types defined under MiFID. In addition, it will be critical for Level 2 measures to set out a clear and objective framework for the assessment of when an own account dealing activity is conducted on an “organised, systematic and frequent” basis, in non-equity</p>

	<p>venues and, if so, which type of venue?</p>	<p>instruments, such as to create a clear boundary between a SI activity in a given product and OTC activity.</p> <p>OTC trading should differentiate transactions conducted between financial counterparties from those conducted by non-financial counterparties for commercial reasons. The OTC definition should preserve non-financial counterparty access to OTC contracts used to mitigate commercial risk.</p> <p>Yes, the proposals will lead to the channelling of trades which are currently OTC onto organised venues. However, it is difficult to assess the likely distribution of business, assuming the current proposals are carried forward, in light of some of the uncertainties regarding the requirements for OTFs. If the issues arising from the own account dealing restriction and the non-equity transparency regime are addressed, MiFIR should increase investor protection by bringing a portion of the OTC onto organised venues, authorised and regulated as OTFs. If operating effectively, the derivatives trading obligation should ensure that standardised and sufficiently liquid derivatives trade on organised venues, while preserving the possibility of OTC execution of non-standardised or less liquid products relied upon by end investors to mitigate commercial risk.</p>
	<p>8) How appropriately do the specific requirements related to algorithmic trading, direct electronic access and co-location in Directive Articles 17, 19, 20 and 51 address the risks involved?</p>	<p>The FSA strongly agrees that systemic risk to markets should be effectively managed. We welcome the Commission's focus on algorithmic trading, particularly the aspects of the text dealing with systems and controls. We agree it is right that high frequency trading (HFT) firms need to be authorised if they are accessing markets as direct members. This acknowledges the potential risks that automated trading presents to market orderliness, and the need for greater regulatory visibility into their activities.</p> <p>However, the definition of <i>algorithmic trading</i> in the recast MiFID (see Article 4(2)(30)), that is used in Article 17, goes beyond high frequency algorithmic trading and effectively captures any trading activity where a computer is responsible for generating the relevant orders. Critically, <i>HFT is not the same thing as algorithmic trading</i>; instead</p>

		<p>HFT is a subset of algorithmic trading that uses high speed computer algorithms to generate and execute trading decisions, for the purpose of generating a return on proprietary capital. This distinction has not been recognised in the MiFID II proposals and that is an important omission.</p> <p>The current Article 17 will capture a very wide spectrum of firms even though they are not partaking in HFT. Firms would need to ensure that their algorithms operate continuously during the trading hours of the venue(s) to which they send orders and ensure that the algorithm posts firm quotes at competitive prices to provide ongoing liquidity. Whilst we recognise that the proposal is motivated by a rational concern that, in times of market crisis, algorithmic systems are likely to withdraw liquidity from the market; the corollary of such a provision is that participants' risk management may be wholly compromised. Further, the provision will be hard to implement in practice as there would be numerous proprietary trading firms whose trading strategies do not involve 2-sided passive liquidity provision and whose entire business models could become unviable. The knock on effect may be a reduction in liquidity across affected markets.</p> <p>The UK authorities have given considerable attention to whether HFT presents risks to markets. In the UK the Government has commissioned a research project, involving leading international academics, looking into the impact of computerised trading on financial markets.</p> <p>Initial findings from this project suggest that liquidity has improved, transaction costs are lower, and market efficiency has not been harmed by computerised trading in regular market conditions. The project has found no direct evidence that HFT has increased volatility.</p> <p>There is other evidence to suggest that HFT has brought positive externalities such as:</p> <ul style="list-style-type: none"> <li>• improved immediacy of execution;</li> <li>• reduced spreads;</li> </ul>
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	<p>9) How appropriately do the requirements on resilience, contingency arrangements and business continuity arrangements in Directive Articles 18, 19, 20 and 51 address the risks involved?</p>	<p>The FSA broadly supports the proposals, under Article 51, that seek to ensure that systems are suitably resilient and include appropriate risk controls, such as preventing systems from sending erroneous instructions. However, there are various elements of Article 51 that would benefit from further refinement. It would be very difficult to set out a market-wide order to trade ratio and there could be a number of adverse consequences of seeking to do so, such as wider spreads. If the intention of a maximum ratio is to protect platform’s systems this could be achieved with a “throttling” requirement as provided for in Article 51(3).</p> <p>Article 51 includes a proposal, under 51(7)(c), that the Commission will set out conditions under which trading is to be suspended across the EU's trading venues. The FSA supports trading venues implementing risk controls, such as circuit breakers or</p>

		<p>limit up/down measures and this has been a longstanding focus of the FSA's supervisory approach. However, the FSA does not support harmonised circuit breakers across the EU as venues need the flexibility to design their own controls (which may include so-called "limit up/limit down" structures) to satisfy the overall objective of having mechanisms in place to control or limit the risk of disorderly trading. Additionally, whether all venues should halt trading, in a single stock or across the market, depends on the underlying reason that triggers the suspension. For example, if one venue is not operational due to system problems this is not a compelling reason for all other venues to have to suspend trading.</p>
	<p>10) How appropriate are the requirements for investment firms to keep records of all trades on own account as well as for execution of client orders, and why?</p>	<p>We believe it is appropriate to require investment firms to keep records of all trades on own account as well as for the execution of client orders.</p> <p>We support the principle that investment firms have to keep orderly records for their business and, in particular, relevant data related to transactions undertaken either on own account or as an agent. The records must be sufficient to enable any Competent Authority (CA) to monitor the firm's compliance with the reporting requirements. Moreover, records should be retained in order for the relevant CA to be able to access them readily and to reconstitute each key stage of processing of each transaction as this is very important for any market abuse investigations and subsequent enforcement actions. As far as the retention period is concerned, we believe records should be retained for as long as is relevant for the purposes for which they are kept, and the proposed period of five years seems to be reasonable and appropriate.</p>
	<p>11) What is your view of the requirement in Title V of the Regulation for specified derivatives to be traded on organised venues and are there any adjustments needed to make the requirement</p>	<p>We fully support the G20 commitment to bring all standardised and sufficiently liquid OTC derivatives to exchanges or electronic trading platforms, as part of the package of measures to increase transparency, combat market abuse and reduce systemic risk. However, securing these outcomes is dependent on an appropriate regulatory framework that applies a suitably flexible definition of an organised venue, in line with IOSCO recommendations, and is based upon a rigorous process for assessing whether a given</p>

	practical to apply?	<p>product exhibits the necessary level of liquidity.</p> <p>In that context, we believe that MiFIR should be amended to incorporate a clearer set of criteria for the assessment of sufficient liquidity by ESMA, in order to ensure that the derivatives trading obligation will not apply to less liquid products, or disrupt access to OTC markets for end users which rely on bespoke instruments to mitigate commercial risk. We consider that the following criteria for determining the liquidity criteria should be included:</p> <ul style="list-style-type: none"> <li>• whether the volume of trading in a product on multilateral venues, relative to total volumes, is sufficiently high to support a conclusion that such trading methods are viable;</li> <li>• whether the ratio of market participants to traded products/contracts in a given product market is sufficiently high to support a conclusion that there is an active pool of willing buyers and sellers; and</li> <li>• the need to ensure that imposing the trade obligation will not result in a widening of bid/offer spreads.</li> </ul> <p>In addition, we consider that trading of derivatives subject to the trade obligation should be permitted on single dealer platforms (platforms operated by a single bank, which commits its own capital to offer two-way quotes to clients), regulated under MiFIR as systematic internalisers. Single dealer platforms are increasingly significant in non-equity asset classes and account for up to 15% of dealing in interest rate swaps. A single dealer has an incentive to invest in its platform, to offer the best client experience, and therefore will often provide richer functionality than a multi-dealer platform. A trading landscape for sufficiently liquid derivatives which included a mix of single and multi dealer platforms would therefore provide greater choice to market participants while potentially enabling a broader range of instruments to be brought within the scope of organised trading, thereby potentially serving to reduce systemic risk. In addition, the</p>
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		disclosed counterparty model of a single dealer platform means that the dealer has a reputational incentive to stand behind its quotes and hence may offer greater liquidity resilience during periods of market stress. The introduction of the non-equity SI regime provides a mechanism to attach requirements to a systematic internaliser which are consistent with the principles of organised trading established by IOSCO in its 'Report on Trading' (February 2011), as proposed by MiFIR (for example, in the area of pre-trade transparency). We consider that there is no material difference between the ability of a single dealer and multi dealer platform to deliver the outcomes envisaged by the G20.
	12) Will SME gain a better access to capital market through the introduction of an MTF SME growth market as foreseen in Article 35 of the Directive?	<p>We believe that the provision of a SME Growth Market designation is the right approach to the concern of prohibitive regulatory burden on SMEs and we are supportive of this proposal.</p> <p>The proposal suggests that labelling these markets as SME Growth Markets will increase visibility and therefore investment and we agree that it certainly would be clearer for investors and issuers. We would suggest, though, that consideration might be given to what incentives or benefits there are for analysts and investors to ensure that capital flows to these markets. We would also note that market operators will need to see benefits to them as well as the issuers who are admitted to their markets in order to request the designation. It may be important in this case that "majority" (paragraph 3(a)) is clarified and it may be useful to do this in Level 1 rather than in Level 2.</p>
	13) Are the provisions on non-discriminatory access to market infrastructure and to benchmarks in Title VI sufficient to provide for effective competition between providers?	The grounds on which access may be refused are broad (volumes and users) and could be exploited to block access unfairly or for inappropriate reasons (such as competitive drivers). The grounds on which a CCP/Venue can refuse access should be limited to circumstances where an undue risk to the CCP/Venue is posed: provision can always be made for disproportionate start-up costs to be borne by the member.

	<p>If not, what else is needed and why? Do the proposals fit appropriately with EMIR?</p>	<p>EMIR contains analogous provisions in respect of OTC derivatives transactions.</p>
	<p>14) What is your view of the powers to impose position limits, alternative arrangements with equivalent effect or manage positions in relation to commodity derivatives or the underlying commodity? Are there any changes which could make the requirements easier to apply or less onerous in practice? Are there alternative approaches to protecting producers and consumers which could be considered as well or instead?</p>	<p>We welcome powers being given to competent authorities to intervene in traders' positions since manipulation of commodities markets, where physical delivery of the commodity is required, has been shown to be most likely to occur from a participant amassing a large position which enables it to control or exert pressure on the physical deliverable supply to the detriment of other users. We do not think this should apply to cash settled markets as the same risk does not arise, it being practically impossible to corner the supply of cash. Keeping these powers as broad as possible - and keeping the position setting powers closer to the markets - ensures that position management arrangements can be implemented which are appropriate to the nature of the individual commodity markets. The entity best placed to set well judged limits is that which is closest to the market, i.e. the market operator with supervision from a competent authority and with ESMA playing a co-ordinating role. We question what information the Commission will use to set limits effectively since MiFID does not provide for information flow on markets to the Commission. We would be concerned where these powers were restricted or narrowed and necessitated a "one size fits all" approach to position management as this would lead to market inefficiencies, and ultimately higher costs to consumers.</p> <p>We would caution against the powers being used to try to reduce liquidity in markets by targeting particular classes of participants. This could damage market functioning and lead to less efficient price discovery and greater volatility. Financial participants provide valuable liquidity to markets by providing counterparties to hedgers' trades where there might not necessarily be a corresponding hedgers to match the trade (i.e. every buyer needs a corresponding seller and vice versa). Further, financial participants act as market makers and provide additional capital to markets, freeing up capital lines and making it easier for hedging participants to manage the risk arising from their physical market operations. A hedger only market would be unlikely to function well since there would</p>

		be insufficient liquidity.
Investor protection	15) Are the new requirements in Directive Article 24 on independent advice and on portfolio management sufficient to protect investors from conflicts of interest in the provision of such services?	<p>The FSA supports this overall aim of this proposal to tackle the potential for commissions to bias recommendations (or decisions to trade). Under the UK Retail Distribution Review (RDR), we have sought to tackle this problem by making firms that give advice set their own charges and banning commissions set by product providers. While firms providing investment advice will describe their services as either 'independent' or 'restricted', this will not affect how they can be paid.</p> <p>The Commission proposes restrictions on inducements for independent advice. The issue here is that this approach could lead to distortion in some markets and confusion for consumers, as many financial advisers may simply discard the label 'independent' in order to continue receiving inducements from product providers. In order to avoid such distortion in some markets, and tackle the risk of bias and conflicts of interest, a possible solution could be to ban the receipt of third party payments for all firms that give investment advice. This would aim to ensure that investment firms are not influenced at all in their product selection and recommendation by the reward that they receive from product providers.</p> <p>But while wholesale financial markets are increasingly international in design and outlook, national specificities remain in retail markets (for example, the instruments purchased, types of firms selling investments and services offered differ greatly between MSs). While we need to ensure that commission payments do not bias advice, different Member States' regulators are likely to need some margin of flexibility under MiFID II to deal with these conflicts in different ways. In the UK, we have been able to make rules banning product providers from offering commissions to firms that recommend their products, without jeopardising access to advice (partly because investors can arrange for fees to be deducted from their investments if they do not wish, or are unable, to pay for them separately).</p>

	<p>16) How appropriate is the proposal in Directive Article 25 on which products are complex and which are non-complex products, and why?</p>	<p>We support the Commission's plans to tighten up the standards that determine when a product can be considered non-complex.</p> <p>The new proposals introduce greater controls on execution only services (where a firm such as a stockbroker buys and sells at the customer's request with no advice). Fewer products will automatically be classified as 'non-complex', meaning that firms may have to conduct an appropriateness test when selling these products without advice (this involves the firm collecting information from the client to determine whether he or she has the knowledge and experience to understand the risks involved in the transaction or service).</p> <p>The proposal will increase protection for investors who are being loaned money to buy an investment or who are buying products that incorporate structures that are difficult to understand. One point we would make, however, is that (as noted in response to Question 2), it will be important to make sure that the rules are amended to explain whether structured deposits are non-complex.</p> <p>As far as the new proposals for the treatment of UCITS are concerned, we can appreciate the rationale for reviewing the issues that certain types of UCITS structure pose – particularly those that are structured. However, UCITS are regulated collective investment schemes with carefully developed EU regulation designed to ensure that they are products which are appropriate for retail investor, providing high levels of investor protection. Certain inefficiencies in the UCITS regime were recently addressed in a recast of the UCITS directive (commonly referred to as UCITS IV) and the Commission has indicated that it will begin work on UCITS V during Q1 2012. It would seem sensible to address any concerns about the inclusion of overly risky or complex products in the UCITS regime through UCITS V, rather than through revision of MiFID.</p>
	<p>17) What, if any, changes are needed to the scope of the best execution</p>	<p>There is no need to change the scope of the best execution provisions in MiFID. The existing rule appropriately distinguishes between the needs of retail and professional</p>

	<p>requirements in Directive Article 27 or to the supporting requirements on execution quality to ensure that best execution is achieved for clients without undue cost?</p>	<p>clients and properly takes into account the fact that the quality of execution can depend on factors other than just the price achieved. However, this framework needs to be applied more vigorously by competent authorities in their supervisory work, co-ordinating through ESMA to discuss issues of interpretation and methods of supervision. More effective supervision will be aided by the proposals in MiFIR for greater pre-trade transparency and enhancements to post-trade transparency.</p> <p>The Commission's proposal includes a change in the scope of the best execution rule. Article 17 (6) of MiFIR applies best execution to investment firms when providing quotes. Currently, based on a letter the Commission sent to CESR and which was published in CESR's 2007 Q&amp;A on Best Execution, firms providing quotes are only subject to best execution when a client relies on them in relation to some aspect of execution quality such as price. When a client is not relying on a firm providing quotes to act on its behalf in relation to some aspect of execution quality then it makes sense that the best execution obligation does not apply.</p> <p>We do not believe that, as proposed in Article 27 (2), it is appropriate to require execution venues to produce data on at least an annual basis on execution quality based on a template drawn up by ESMA. It would be better, as suggested by CESR in its advice to the Commission, to put a clearer obligation on investment firms executing orders to obtain data as part of their annual review of their execution policies. They would then demand data from the venues, or via data vendors, that were attuned to their needs (which may differ from firm to firm depending on the sorts of orders they execute) as the users of the data.</p>
	<p>18) Are the protections available to eligible counterparties, professional clients and retail clients appropriately differentiated?</p>	<p>It remains appropriate to have three different categories of client in MiFID because of the significant differences in terms of resources and levels of sophistication between clients. We also believe that, as the Commission proposes, the existing boundaries between the three categories should be left largely unchanged given the flexibility that professionals and eligible counterparties have to seek a higher level of protection.</p>

		<p>However, we agree with the Commission that it is appropriate to clarify the standards that apply to dealings with eligible counterparties and to ensure that eligible counterparties get adequate information about services and financial instruments.</p>
	<p>19) Are any adjustments needed to the powers in the Regulation on product intervention to ensure appropriate protection of investors and market integrity without unduly damaging financial markets?</p>	<p>We believe that banning products in order to protect retail customers should be an option available to CAs in certain prescribed circumstances, but it should be undertaken with great caution and only in response to specific problems to avoid damaging the competitiveness of the market and consumers' interests.</p> <p>While some market failures may be common across the EU, in many cases they will be specific to the particular characteristics of national markets. The proposed approach seems as balanced as we could expect, allowing both national action and co-ordinated EU responses.</p> <p>We note that there are some areas where the text could be updated to improve consumer protection:</p> <p>Article 31(3)(b) states that the power can only be used where it does not create the risk of regulatory arbitrage. Where the power is being used on a PRIP and it is possible to structure the product as an insurance-based PRIP, regulatory arbitrage is a real possibility. The product intervention power needs to be duplicated in the IMD in order to allow the power to be used for consumer protection purposes.</p> <p>Article 31(6) requires ESMA to review product restrictions regularly and at least every three months. When the power is used for consumer protection purposes it may well be necessary to intervene for long periods of time or even permanently. For instance, if a product is inappropriate for retail customers at one time, it is likely to be inappropriate for customers permanently. It should be possible for ESMA to set longer review periods (perhaps annually) where the power is used for consumer protection purposes.</p>

		<p>Article 32(3) requires CAs to notify other CAs one month in advance before introducing national product intervention rules. This is a significant fetter on use of the power and will prevent action being taken on an emergency basis. If consumer detriment is already occurring, the month delay would lead to more consumers suffering. We would prefer no requirement to pre-notify other CAs. Or, at most, the notification period should be one week.</p> <p>Both articles 31 and 32 should include a power to set rules on what happens if contracts are sold in contravention of product intervention rules after they have come into force. If a firm ignores the rules and sells the product anyway, the rules should allow ESMA or the CA (where the action is solely at national level) to specify what redress or compensation is owed and that the contract is automatically void. This new power is included in the proposed amendments to the UK's national legislation.</p>
Transparency	20) Are any adjustments needed to the pre-trade transparency requirements for shares, depositary receipts, ETFs, certificates and similar in Regulation Articles 3, 4 and 13 to make them workable in practice? If so what changes are needed and why?	In regard to the obligation for investment firms to make public quotes, we support the requirement for systematic internalisers to provide a two-way quotation and the criteria for determining the minimum quote size.
	21) Are any changes needed to the pre-trade transparency requirements in Regulation Articles 7, 8, 17 for all organised trading venues for bonds, structured products, emission allowances and derivatives to ensure they are appropriate to the different instruments? Which instruments are	<p>We believe that MiFIR should be amended to clarify that delegated acts giving effect to the on-venue pre-trade transparency regime should be calibrated for each type of trading model that could operate as a regulated market, MTF or OTF. In particular, such calibration should distinguish between the following types of system or facility:</p> <ul style="list-style-type: none"> <li>• order driven systems;</li> <li>• quote driven systems where market makers provide continuous two-way quotes;</li> <li>• periodic auction systems;</li> <li>• request for quote (RFQ) systems, where liquidity providers provide a quote in</li> </ul>

	<p>the highest priority for the introduction of pre-trade transparency requirements and why?</p>	<ul style="list-style-type: none"> <li>• response to a request by a market participant;</li> <li>• voice-based systems, where the operator arranges trades between participants through voice negotiation; and</li> <li>• hybrid systems composed of two or more of the above functionalities, or where the price formation process is of a different nature</li> </ul> <p>This would be consistent with the approach adopted under Article 17 of the existing MiFID Implementing Regulation.</p> <p>In addition, the calibration should recognise, and allow for, the fact that certain of these systems (specifically, RFQ and voice-based systems) do not operate on a basis of continuous firm orders or quotes (but indicative prices).</p> <p>Additionally, we believe that requiring systematic internalisers to publish firm quotes in bonds and derivatives would have a detrimental impact on liquidity by increasing the risk that dealers face when quoting. The precise impact on liquidity provision is difficult to assess, given a number of uncertainties in the MiFIR text. In particular, as a minimum, MiFIR should be amended to clarify that the size below which the quote of a systematic internaliser is firm to other clients is a retail size (calibrated for each class of instrument), and the limits on access which a systematic internaliser is permitted to apply by means of its commercial policy.</p> <p>The SI regime would also, on the face of MiFIR, apply to instruments traded on OTFs and not cleared by a CCP. Requiring a SI to trade at a price quoted to one client with other clients in non-cleared instruments would impair proper risk management, as the price would incorporate the level of counterparty risk associated with the particular client. In the absence of a central database of OTF-traded instruments (which is not currently provided for and would likely be impractical to maintain), it is unclear how a dealer would be able to verify whether or not a particular instrument was within the</p>
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		<p>scope of SI quote obligations.</p> <p>Finally, in order to align in a consistent and coherent manner the SI regime in non-equities with the SI regime in equities, we suggest that the firm quote obligation should apply to liquid instruments only. As stated in Recital 12, those financial instruments traded purely OTC which are deemed particularly illiquid should be outside the scope of the transparency obligations. ESMA should determine the threshold beyond which bonds, SFPs, emission allowance units and derivatives shall be considered as being liquid. Derivatives subject to the trading obligation under article 26 of MiFIR should be considered as being liquid.</p>
	<p>22) Are the pre-trade transparency requirements in Regulation Articles 7, 8 and 17 for trading venues for bonds, structured products, emission allowances and derivatives appropriate? How can there be appropriate calibration for each instrument? Will these proposals ensure the correct level of transparency?</p>	<p>We strongly consider that pre-trade transparency should be tailored to both particular class (and sub-class) of instrument and the type of trading (i.e. order book, quote-driven, auction, RFQ, voice and hybrid), in accordance with the intention set out at Recital 14 of MiFIR.</p> <p>We consider this should be achieved by requiring ESMA, as part of its work on calibration, to differentiate between each trading model potentially falling to be regulated as a Regulated Market, MTF or OTF (see the list provided in our response to question 21). Further, the detailed requirements should recognise that unduly rigid, equity-like requirements (for example, requiring continuous streaming of firm orders or quotes) are not compatible with certain trade execution methods. Voice broking facilities and request for quote systems, which provide the critical ability to discover liquidity and negotiate trade terms in less liquid instruments, function on the basis of broadcasting indicative prices. The pre-trade transparency requirements such systems should be required to meet as trading venues should allow for the distribution of indicative pricing information.</p> <p>In addition, to facilitate the level of granularity we believe is necessary, we suggest a phased approach, per product market, to the introduction of pre-trade transparency</p>

		<p>requirements. This will ensure sufficient time for ESMA to develop a set of properly tailored regimes, focused on the individual characteristics of each product market.</p> <p>Further, we believe that thought should be given to the possibility of a power for competent authorities to temporarily suspend pre-trade transparency requirements, in particular sets of products, in the event of severe market stress (evidenced by a substantial or sustained decline in liquidity relative to usual levels of liquidity in a given product). Such a power would ensure that pre-trade requirements, designed to operate in normal market conditions, do not exacerbate the market impacts of a period of market stress.</p>
	<p>23) Are the envisaged waivers from pre-trade transparency requirements for trading venues appropriate and why?</p>	<p>As currently drafted, the viability of MiFIR's on-venue transparency requirements depends on the nature of the waivers made available under Article 8. However, MiFIR does not provide sufficient detail for the design of the delegated acts that will be critical in setting the scope of those waivers.</p> <p>We believe that the conditions under which pre-trade transparency disclosure may be waived should be expanded, in order to ensure that delegated acts are set by reference to clear criteria contained in the framework regulation. For example, to evaluate the liquidity profile of a financial instrument, we suggest that the ratio of market participants to traded products/contracts in a given market should be taken into account. Additionally, the potential for a widening of bid-offer spreads in respect of the financial instrument should also be included.</p> <p>In addition, we consider that thought should be given to a provision that would allow a competent authority to temporarily suspend the on-venue pre-trade transparency obligation in a particular set of products, where such products experience a material decline in liquidity (relative to usual levels of liquidity) that may be associated with stressed market conditions. In effect, such a provision would operate as a "safety valve" where a concern arose that transparency requirements designed to function in normal</p>

		<p>market conditions were exacerbating the market impacts of a particular period of stress. We would advocate specific and objective criteria for the design of such a “dynamic liquidity threshold”.</p> <p>We believe that the proposed timeframe for processing pre-trade transparency waivers by ESMA is excessive and could put the investment firms operating MTFs and OTFs at a competitive disadvantage, while also potentially stifling innovation. We recommend that ESMA reviews the pre-trade transparency waiver application within 2 months with immediate effect thereafter. This timeframe would be consistent with the already existing ESMA process to assess pre-trade transparency waivers.</p>
	<p>24) What is your view on the data service provider provisions (Articles 61 - 68 in MiFID), Consolidated Tape Provider (CTPs), Approved Reporting Mechanism (ARMs), Authorised Publication Authorities (APAs)?</p>	<p>We are very supportive of the Approved Publication Arrangement (APA) regime and believe that this will improve the quality and consistency of post-trade transparency information. Additionally, the regime will assist with the consolidation of trade data and begin to address the fragmentation of transparency information. This will be further enhanced with the introduction of Consolidated Tape Providers (CTPs), giving market participants the opportunity to access information from a single point, thereby increasing confidence and price discovery. We support the Commission's proposal of Option C as the preferred method for delivering the tape.</p> <p>As a general point on these provisions, there is a risk here that data reporting services may withdraw their authorisation and leave the market suddenly without giving sufficient notice to the competent authority or the firms that rely on their services. For example, if an ARM decides to withdraw its authorisation, enough time would have to be given to the firms who rely on this ARM for them to find an alternative and allow them to continue complying with their transaction reporting<sup>1</sup> obligations. This sort of</p>

<sup>1</sup> Transaction reports contain certain mandatory information on transactions entered into by firms, and are sent to and used by regulators to detect and investigate suspected instances of market abuse

		<p>situation could also arise for those firms who submit trade reports<sup>2</sup> to APAs and market participants who receive a consolidated tape from a CTP. A requirement could be added for data reporting service providers to give sufficient notice before withdrawing the service.</p> <p>Also it would seem desirable to extend the sanctioning regime at Article 75 to include data reporting service providers that breach their duties under Title V as this might have an important impact on transparency requirements.</p>
	<p>25) What changes if any are needed to the post-trade transparency requirements by trading venues and investment firms to ensure that market participants can access timely, reliable information at reasonable cost, and that competent authorities receive the right data?</p>	<p>We believe that the new regime on data reporting services as discussed above provides a significant improvement on the current situation. We also welcome the provisions requiring the unbundling of trade data. The obligation to provide pre- and post-trade data separately should improve the access to post-trade information. This should also reduce the costs for some users by enabling them to choose whether to purchase pre-trade data or post-trade data. We also welcome further clarification of what constitutes a reasonable commercial basis. This should help ensuring that a fairly-priced consolidated data solution is delivered to markets participants.</p> <p>In terms of non-equities, we support the extension of a post-trade transparency regime to this area provided the right balance is struck between transparency and liquidity. Trading models for most of non-equity instruments are fundamentally different from equities by relying heavily on the provision of capital by intermediaries. . Transparency requirements will need to be calibrated for non-equity products, derivatives and structured finance products at a sufficient level of granularity to reflect the wide diversity of liquidity both between and within asset classes.</p> <p>We would suggest that the Level 1 Regulation should contain provisions which specify that transparency will be appropriately calibrated in Level 2, which will suitably take</p>

<sup>2</sup> Trade reports also contain information on transactions that are entered into by firms, but these will contain less specific information than transaction reports and are for the purposes of market transparency, meaning that other market participants will be able to see the trade reports to assist with things such as price formation

		into account the differences in non-equity products and market structures. This should be included within the Level 1 text, consolidating the existing Recital 14 that already acknowledges this issue.
Horizontal issues	26) How could better use be made of the European Supervisory Authorities, including the Joint Committee, in developing and implementing MiFID/MiFIR 2?	<p>It is important to note that the ESAs will need sufficient time to develop level 2 measures, as experience with the Short Selling Regulation and European Market Infrastructure Regulation has shown.</p> <p><i>Investor protection and regulatory arbitrage</i></p> <p>The FSA welcomes close co-ordination on issues of cross-sector importance between ESMA, EIOPA and EBA. We also welcome the creation of a Joint Committee and the exchange of information between all three authorities.</p> <p>It is important to attain consistent application of policy decision on cross-cutting issues such as corporate governance and sanctions where there are similar provisions e.g. MiFID and CRD IV.</p> <p>Specifically, and as mentioned in response to question 2, the FSA welcomes the proposed inclusion of structured deposits within MiFID's scope, as part of the drive for greater consistency in selling practices for competing Packaged Retail Investment Products (PRIPs). At the same time, we remain concerned about the need for consistency of selling standards across those PRIPs that are covered by MiFID and those that are covered by the recast Insurance Mediation Directive. The FSA supports delivering consistent investor protection regardless of the legal form of products. As a result, we believe that it is important that coordination occurs between ESMA, EBA and EIOPA in the Joint Committee, to support consumer protection and reduce the scope for regulatory arbitrage.</p> <p><i>Markets issues</i></p>

		<p>ESMA is uniquely placed to provide advice and support on legislation debated by Council and Parliament, including measures relating to integrity, transparency, efficiency and orderly functioning of securities markets and measuring aimed at enhancing financial consumer protection. In particular, ESMA can bring to bear its experience and in-depth knowledge of securities market and provide support in the design of new measures, analysis of impact of proposed measures as well as possible alternatives. Given the scope and breadth of MiFID/MiFIR, we believe that it would be desirable to engage with ESMA at an early stage, especially in areas requiring detailed technical work such as the calibration of the transparency regime. In our view, it would also be desirable if ESAs/joint committee considered the interaction between different pieces of EU legislation and its impact on securities markets.</p>
	<p>27) Are any changes needed to the proposal to ensure that competent authorities can supervise the requirements effectively, efficiently and proportionately?</p>	<p>At this stage, it is difficult to know whether competent authorities will be able to supervise the requirements effectively, efficiently and proportionately because the level 1 text is relatively high level. This will come down to what the detail looks like at level 2.</p> <p>However, some specific areas that we have identified are as follows:</p> <p>Article 32(3) of the Regulation requires CAs to notify other CAs one month in advance before introducing national product intervention rules. This is a significant constraint on effective use of the power and will prevent action being taken on an emergency basis. If consumer detriment is already occurring, the month-delay would cause more consumers to suffer. We would prefer no requirement to pre-notify other CAs. Or, at most, the notification period should be one week.</p> <p>Articles 32 of the Regulation should include a power to set rules on what happens if contracts are sold in contravention of product intervention rules after they have come into force. If a firm ignores the rules and sells the product anyway, the rules should allow the CA to specify what redress or compensation is owed and that the contract is</p>

		<p>automatically void. This new power is included in proposed amendments to the UK's national legislation</p> <p>Article 36.2 (b) – clarification required to cross-reference use of tied agents to Article 37, ensuring Tied Agents are notified under a freedom of establishment. This will apply to both credit institutions as well as investment firms.</p> <p>Article 37 - use of Tied Agents established in a member State outside the home Member State of the investment firm. Clarity is sought to confirm that where no branch is established in the host Member State the agents will operate in, details of the Tied Agents will still need to be notified under a Freedom of Establishment, in accordance with Article 37.2. This will apply to both investment firms and credit institutions.</p> <p>Article 44.1 – clarity is sought regarding the scope of passporting rights to be enjoyed by 3<sup>rd</sup> Country firms. Is this limited to rights under the freedom of services?</p>
	<p>28) What are the key interactions with other EU financial services legislation that need to be considered in developing MiFID/MiFIR 2?</p>	<p>A number of provisions cut across Directives, for example there are provisions on sanctions and corporate governance in both CRD IV and MiFID (although each has a different implementation timescale). Third country proposals form part of MiFID/MiFIR, the AIFMD and EMIR. The MiFIR transaction reporting requirements have been extended to mirror the scope of MAR and the retail focused conduct of business provisions are relevant for PRIIP initiative.</p> <p><b>Packaged Retail Investment Products (PRIIPs) and Insurance Mediation Directive (IMD)</b> - The Commission's PRIIPs initiative seeks to create a level playing field in terms of the requirements for competing retail investment products such as collective investment schemes, structured products (including structured deposits), insurance-based investments (e.g. unit-linked and with profits policies) and derivatives. It has proposed applying consistent standards across the market by:</p> <ul style="list-style-type: none"> <li>- requiring the delivery of a Key Investor Information-style product disclosure</li> </ul>

		<p>document, using the one developed for UCITS (the Key Investor Information Document, “KIID”) as the benchmark for all PRIIPs; and</p> <ul style="list-style-type: none"> <li>- taking MiFID requirements as the benchmark for consistent selling practices and applying them across the PRIIPs market more widely – through the reviews of MiFID and of the Insurance Mediation Directive (IMD).</li> </ul> <p>For selling practices, we understand that the Commission prefers the approach of updating MiFID and IMD rather than dealing with all PRIIPs under a single measure. If this parallel MiFID II and IMD II route is chosen, inconsistent standards could result and consumer protection could be compromised. A horizontal approach applying broad standards across a range of different types of products through one set of rules (instead of through two different instruments) would probably be the most successful model in order to achieve greater consistency in regulation between different industry sectors. This sort of approach is already been attempted for structured deposits, which are to be included in MiFID II.</p> <p><b>EMIR</b> - Mandatory clearing of derivatives is covered to a degree by both EMIR and MIFIR: OTC derivative products may be determined subject to a clearing obligation under EMIR, and MIFIR should ensure that those products that are made subject to such an obligation will continue to be so subject if trading later moves to a regulated market within the scope of MIFIR.</p> <p><b>CRD IV</b> – The current MiFID article 12 requires that ‘<i>Member States shall ensure that the competent authorities do not grant authorisation unless the investment firm has sufficient initial capital in accordance with the requirements of Directive 93/6/EEC (original capital adequacy directive) having regard to the nature of the investment service or activity in question.</i>’ This same requirement appears in MiFID II as Article 15</p>
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		<p>but the reference to directive 93/6/EEC has been replaced by a reference to 2006/49/EC (capital adequacy of investment firms and credit institutions (recast) (CAD)). The CAD sets out the capital and professional indemnity insurance requirements for investment firms which are dependent upon the investment business that the firm undertakes.</p> <p>It seems appropriate to substitute the current proposed MiFID II Article 15 reference to 2006/49/EC with an appropriate reference to CRD IV (which comprises a directive and a regulation) when the latter is agreed. The draft text in MiFID II Article 15 refers to the initial capital requirements of the CAD. However, the CAD also specifies that a minimum amount of own funds should also be maintained and the MiFID II text would be clearer if it also referred to that.</p> <p>In addition, MiFID Article 3 requires that a firm exempted from the scope of MiFID must be subject to requirements that are at least analogous to certain requirements in the directive, including Article 21 which requires the firm to comply at all times with the conditions for initial authorisation established in Chapter 1 of the directive. It is not clear whether the intention is that firms exempt under Article 3 should be subject to capital requirements that are at least analogous to those in the CAD.</p> <p><b>Solvency II</b> – The MiFIR changes to non-equity transparency, when considered along with the impact from Solvency II, may well have implications that affect member states macro-economies and so affect jobs and growth in the EU.</p> <p>We foresee insurance companies will have to hold more capital under Solvency II. As a result, their capital would be more expensive (and scarcer). Generally insurers buy and hold bonds, whilst dealers trade them. As a result of capital being more expensive, dealers will be less willing to risk their capital dealing bonds. With less capital being invested in bonds, and risk/return being a primary consideration, SME financing may be significantly damaged. In turn, if SMEs cannot get adequate funding this will negatively impact EU Member States ability to generate jobs and economic growth.</p>
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		<p><b>Transparency Directive</b> – The TD focuses on those issuers with securities admitted to trading on regulated markets and therefore any changes to the requirements of regulated markets could potentially impact whether issuers are required to comply with aspects of the TD. However, there is little within MIFID or MIFIR that directly impacts on the TD.</p> <p>The implementation of Article 35 (SME Growth Markets) could be a tangential matter for the TD as it effectively creates a second tier of ‘regulated market’ but at the moment it is not clear that there is any intention that issuers on such markets would come within scope of the TD, rather they would come within scope of the competent authority for a tailored set of requirements. However, it could be possible that any Level 2 requirements impose obligations within the TD on these issuers.</p> <p><b>Central Securities Depositories Legislation</b> – Based on the Commission’s consultation document, the CSD Legislation is expected to have a section on access and interoperability between CSDs and other market infrastructure/investment firms. The MiFID legislative proposals mention settlement systems and access across a few sections, namely Recital 71 and Articles 39, 40, 57. It will be important to ensure that there is some kind of consistency between the two pieces of legislation. Issues such as how access and interoperability will be achieved, how the grounds for refusing access will be achieved or how competent authorities could oppose access and interoperability will need to be considered.</p> <p><b>MAD/MAR</b> – MiFID2/MiFIR are determinative of the scope of MAR as Article 2 of the proposals states that the Regulation applies, inter alia, to financial instruments admitted to trading on regulated markets (or which a application for admission has been made), financial instruments traded on a MTF or an OTF and behaviour in relation to such financial instruments. This affects both the prohibitions on insider dealing and market manipulation in chapter 2 of MAR and the disclosure requirements in chapter 3.</p>
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		<p>Financial instruments, regulated markets, MTFs and OTFs for the purposes of MAR are as defined in MiFIR. Additionally, issuers of financial instruments admitted to trading on SME growth markets, as defined in new MiFID, are exempt from the obligation to draw up insider lists. Regarding powers of competent authorities (CAs), both MAR and MiFID introduce new restrictions (see MAR article 17(2)(f)) preventing CAs from obtaining the content of communications from investment firms. This restriction would be hugely damaging to enforcement action and involve enormous cost to industry (in terms of the lost costs installing equipment for recording telephone calls) and is something the UK will oppose very strongly. It should be noted that the sanctions provisions in chapter 5 of MAR follow a “horizontal template” that is common to MiFID and a number of other legislative proposals. Finally, the regime in MAR relies heavily on the transaction reporting regime imposed by MiFIR/MiFID.</p> <p><b>REMIT</b> – REMIT establishes a market abuse regime for the physical power and gas markets in the EU. It requires cooperation and information sharing between the competent financial authority, the national (energy) regulatory authority and ACER. In order to inform the monitoring and investigation functions required under REMIT, data about orders and transactions will need to be collected. There is likely to be overlap in the information useful to investigations under both MAR and REMIT, and REMIT also carves out reporting obligations where the information has already been provided to competent financial authorities, therefore, it will be important to try to align the information requirements for transaction reports under MiFID. This will facilitate better information sharing between regulators, and will reduce compliance costs for firms.</p> <p>There is also some uncertainty about the scope of the two market abuse regimes (REMIT and MAR2), therefore it would be useful if the definition of financial instrument (in addition to MAR2) can provide more clarity on this boundary.</p>
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		<p><b>Prospectus Directive</b> – In October 2011 ESMA published the first phase of its technical advice to the Commission in relation to the directive amending the PD<sup>3</sup>. This included a statement that although outside the Commission’s mandate for providing the technical advice, a proportionate disclosure regime for unlisted SMEs might be created via the Commission’s revisions to MiFID. This could provide a separate primary market regulatory framework for SMEs to help meet the Commission’s policy objective of creating more favourable disclosure regimes for SMEs.</p> <p><b>Short Selling Regulation</b> – The Short Selling Regulation (hereafter “The Regulation”) makes certain references to MiFID and in some instances relies on MiFID concepts and definitions. Regarding the latter, the scope of the Regulation is defined with reference to MiFID, stating that it applies to derivatives of financial instruments and debt instruments referred to in Annex C of MiFID<sup>4</sup> (see Articles 1(1)(a) and (b)). Definition-wise, the Regulation also relies on the MiFID definitions for various terms, such as ‘financial instrument’, ‘MTF’, ‘regulated market’, ‘investment firm’, ‘local firm’, ‘home member state’, ‘relevant competent authority’ etc.<sup>5</sup> For the purposes of the Regulation ‘relevant competent authority’ is the competent authority of the most relevant market in terms of liquidity as per MiFID.</p> <p>Article 23, which gives CAs power to temporarily restrict short selling where there is a significant fall in price, also relies on the MiFID implementing Regulation for what a significant fall in price in the case of a liquid share would be (a 10% or more fall in price)<sup>6</sup>. Liquid share is defined in MiFID (A22) as a share admitted to trading on a regulated market with a free float not less than EUR 500 million and either 1) the</p>
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<sup>3</sup> Paragraph 324; ESMA/2011/323; Final report – ESMA’s technical advice on possible delegated acts concerning the Prospectus Directive as amended by the Directive 20010/73/EU; 4 October 2011

<sup>4</sup> These are contained in Annex 1 Section C points (4) to (10) of MiFID.

<sup>5</sup> Other references are made to the Regulation (EC) No 1287/2006 implementing MiFID for the definitions of ‘trading day’ and ‘turnover’.

<sup>6</sup> Article 23.5

		<p>average number of transactions in the share is not less than 500 or b) the average daily turnover for the share is not less than EUR 2 million. ESMA, is developing Level 2 standards as to what thresholds should apply to non-liquid shares and other financial instruments.</p> <p>The Regulation, like MiFID provides an exemption for market makers from the restrictions imposed by the regulation but uses a different definition than MiFID. Under the Regulation, ‘market making activities’ means activities done in any of the following capacities i) by posting simultaneous two way quotes with the result of providing liquidity on a regular basis to the market, ii) as part of usual business by fulfilling client orders or iii) for hedging purposes.</p> <p>Lastly, in terms of scope for review the recitals make reference to considerations that MiFID should perhaps address, namely other investor protection measures such as position limits and restrictions on products (recital 28) and whether investment firms should include short sale reports to CAs as additional information (recital 13).</p>
	29) Which, if any, interactions with similar requirements in major jurisdictions outside the EU need to be borne in mind and why?	<p>The MiFID/MiFIR third country access proposals potentially engage the regulatory regimes of every third country whose firms wish to do business with the EU. Indeed, the key feature of the new regime is the introduction of a preliminary equivalence and reciprocity assessment by the Commission. This involves a determination that:</p> <ul style="list-style-type: none"> <li>• The third country’s regulatory framework has an equivalent effect to the EU’s financial services regulatory framework; and</li> <li>• The third country provides reciprocal access for EEA firms to its markets.</li> </ul> <p>However, in our view it is not realistic to expect third countries to accept or replicate a regime based on blanket equivalence and reciprocity. As noted elsewhere, the proposed equivalence assessment appears to require a wide ranging and fairly detailed line-by-line assessment of a third country’s regulatory framework. It is unrealistic to expect third</p>

		<p>countries to meet such standards even in instances where their domestic regimes are based on common comparable laws and standards. The reality is that even in highly-regulated G-20 jurisdictions it will not be possible to ensure equivalence in every area on this basis. And the same may apply in the reverse, as there are likely to be areas where EU requirements will fall short of their G-20 counterparts. As for reciprocity, seeking to impose it unilaterally will undermine the effectiveness of the proposed regime. From a practical standpoint, the structure of a third country's regulatory architecture and the nature of the powers given to its regulatory bodies may mean that it is simply not possible to grant the EU the blanket access that it seeks. It may also be incompatible with the EU's international trade commitments (i.e. GATS) and may lead to retaliation between trading partners at a time when greater cooperation and regulatory convergence is desirable.</p> <p>The MiFIR proposal to require standardised and sufficiently liquid derivatives to trade only on venues possessing the characteristics of an "organised venue" is intended to implement a global G20 commitment<sup>7</sup>. Consequently, a range of international financial centres are considering the appropriate steps to give effect to this commitment. In formulating EU rules to move trading of suitable OTC derivatives to organised venues, it is important to take into account the approaches taken (or proposed) in the range of other financial centres with developed or developing markets in such instruments.</p>
	30) Is the sanctions regime foreseen in Articles 73-78 of the Directive effective, proportionate and dissuasive?	<p>We support the Directive's aims to set some minimum common standards at the EU level on sanctions with competent authorities continuing to administer the sanctions regime. As the appropriate action in a particular case will depend on the unique facts of that case we consider that minimum harmonisation is the right approach with competent authorities retaining discretion over how they exercise enforcement powers and sanctions. It is also important that Member States retain the power to impose criminal</p>

<sup>7</sup> Statement No. 13, *Leaders' Statement: The Pittsburgh Summit* (September 24 – 25, 2009), available at [http://www.g20.org/Documents/pittsburgh\\_summit\\_leaders\\_statement\\_250909.pdf](http://www.g20.org/Documents/pittsburgh_summit_leaders_statement_250909.pdf)

		<p>sanctions where appropriate for breaches of the Directive or the Regulation.</p> <p>As to the degree of harmonisation, providing a list of breaches in Article 75 is unnecessary and has a number of inadvertent consequences even if the list is intended to be non-exhaustive. Firstly, it fails to list all breaches and so conveys the impression that other breaches are not important or are less important. It also restricts taking action for certain breaches to cases where there are “repeated” breaches of an obligation. Clearly there are cases where a single breach can have significant repercussions and should be able to be sanctioned.</p> <p>There is a need to clarify certain elements of the drafting to ensure that the proposed regime is effective, proportionate and dissuasive. By way of example the sanctions regime does not extend to all regulated entities in some instances. It would seem desirable to extend the sanctioning regime at Article 75 to include data reporting service providers that breach their duties under Title V.</p> <p>We are supportive of a general requirement to publish sanctions and the discretion for competent authorities to take account of the impact of publication. However, we have some concerns that the proposed obligation at Article 74 to publish <u>any</u> measure or sanction as this would potentially include all supervisory measures which is unnecessarily wide and will be impractical to operate in practice.</p> <p>The proposals envisage publishing on an anonymous basis where publication would cause disproportionate damage to the parties involved. We believe there is a need to introduce a higher threshold of “exceptional cases” to ensure publication of sanctions except in very rare circumstances. Where this higher threshold is met (the expectation of severe damage to the individual) the discretion <u>not to publish</u> should also be afforded to competent authorities.</p> <p>We support the introduction of the provisions on whistle blowing at Article 77 but</p>
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		<p>consider that the requirement should apply to both potential and actual breaches.</p> <p>We are concerned that the new limitation introduced in Article 71.1(d) on obtaining telephone and data traffic records from investment firms is too restrictive and will hamper the ability of regulators to supervise firms. In particular, the prohibition on accessing the content of such records makes no sense given the requirements in Article 16(7).</p>
	<p>31) Is there an appropriate balance between Level 1 and Level 2 measures within MIFID/MIFIR 2?</p>	<p>Both MiFID and MiFIR have a large number of delegated acts (c. 18 sets) and binding technical standards (c. 14 sets).</p> <p>While the actual rules governing use of delegated acts are unclear, they are required under the treaty to effect only “non-essential” elements of legislation. However, in certain areas delegated acts are being proposed for measures that appear quite fundamental. For example, delegated acts will seemingly determine the future viability of the voice broking industry.</p> <p>Similarly, binding technical standards are proposed for various matters that seem more than merely technical. For example ESMA will determine whether contracts for difference (CFDs) are subject to the derivatives trading obligation. And ESMA will decide on whether interest rate swaps need to be traded on multilateral venues – this much power could in theory give ESMA the option to effect a major change in market structure: e.g. to drive all interest rate swaps onto multilateral venues.</p> <p>We believe that there should be greater detail at level 1, particularly in the following areas:</p> <ul style="list-style-type: none"> <li>- the grounds for refusing CCP/Venue access should be defined at level 1;</li> <li>- the PTT waiver on grounds of liquidity;</li> <li>- the assessment of sufficient liquidity by ESMA in the context of the derivatives trade obligation;</li> <li>- the size specific to the instrument for when the quote of an SI is firm;</li> </ul>

		<ul style="list-style-type: none"> <li>- Reference data provided by trading venues regarding transaction reporting (please see comments under Article 23 of the draft Regulation below); and</li> <li>- MiFID, Article 35 (3)a – it may be important that ‘majority’ is clarified at level 1 (please see answer to question 12).</li> </ul>
<b>Detailed comments on specific articles of the draft Directive</b>		
<b>Article number</b>	<b>Comments</b>	
Recitals		
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16	<p>We introduced a rule on recording conversations and electronic communications which took effect in March 2009 (it has subsequently been extended to cover mobile phones). The retention period under our rule is six months rather than 3 years. We chose this length of retention period based on an effort to balance the costs and benefits of the rule. The principal use we make of</p>	

	<p>recordings is in market abuse cases. In relation to market abuse most potentially suspicious behaviour comes to light within six months of it taking place. In circumstances where we are uncertain whether recordings will be of use we can request that investment firms hold the records for longer than six months to enable us to do further work to determine whether the recordings will be of interest. We would therefore recommend that the retention period in Article 16 (7) is reduced to six months.</p> <p>Our recording rules do not include provisions dealing with access to the recordings by clients. This is a matter we leave to be dealt with by broader privacy and data protection legislation, which includes implementation of relevant EU legislation, which we believe provides a more appropriate framework for dealing with this issue. We do not believe that the provision dealing with access in the second paragraph of Article 16 (7) is therefore necessary.</p>
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19	We think that paragraph 3 on arrangements to identify clearly and manage the potential adverse consequences of a conflict of interest applies equally well to OTF operators.
20	Please see our answer to question 6. We are concerned about the negative consequences of requiring that operators of an OTF cannot execute client orders against their own proprietary capital, and believe that the objective of operator neutrality can be achieved by a conflicts management provision, similar to that in article 19 for MTFs.
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24	Paragraph 7 deals with ‘cross selling’. We are supportive of efforts to ensure that clients do not end up with products they do not need. But we think that the provision as it stands is too opaque. It includes a requirement for firms to inform clients whether products can be bought separately and, if so, to provide separate information on costs and charges. ESMA is then required to produce cross-selling guidelines but only a general indication is given of what these should cover. In our view it would be preferable if the Directive text could be clearer on what it is intended that the ESMA guidelines should cover. This was not an issue that was discussed in the consultation paper on MiFID.
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30	<p>We support the introduction in paragraph 1 of this article of a framework for firms' relationship with eligible counterparties. The standards articulated are vital to underpinning a properly functioning market. We also believe that it is appropriate to apply some information provisions to firms' relationship with eligible counterparties, albeit that we believe that they will have to be carefully calibrated at level 2 to ensure that eligible counterparties receive usable information rather than information whose only purpose is to discharge a regulatory obligation.</p>
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32	<p>We do not think that the operator of an MTF should be given the authority to demand market-wide suspension in the case of 'non-disclosure of information about the issuer or financial instrument'.</p> <p>In order to make a decision on whether to demand a market-wide suspension in this case, the decision-maker must have appropriate expertise, a view of the whole EU market and contact with the issuer. If there is a rumour that an issuer has not disclosed some financial information, for example, then a competent authority with access to the issuer will be able to verify whether the rumour is true before demanding a suspension. A MTF, without this direct link, may well act on the rumour and demand a suspension triggering suspension in the instrument across the EU. This could cause significant and unnecessary disruption to the market.</p> <p>Finally, it is worth noting that in the recent work of its MiFID Article 41 Task Force, ESMA looked at issues surrounding the notification of trading suspensions. One issue that was considered was the idea of giving the primary market a role in triggering market-wide suspensions, but this was rejected by ESMA.</p>
33	<p>We support this provision, and think that the provisions for RMs and MTFs should be aligned with this proposal.</p>
34	<p><b>Article 34 (1):</b> We are concerned that investment firms, MTFs and OTFs share sensitive information about abusive behaviour of their member firms.</p> <p>In theory a venue could be placed in the odd position of having to report suspicious trading about a trader to the employer of that trader in its capacity as a venue operator. Moreover, the proposal raises the potential for ongoing market abuse investigations by regulators to be compromised.</p>

	We believe reporting should be done to the regulator (as already required in Articles 31 and 56 of MiFID) rather than to other platforms and the national regulator should decide whether it is appropriate for the information to be disseminated to other trading platforms.
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36	We support the proposed changes in this article and the following article which seek to clarify certain aspects relating to firms conducting cross-border business or opening a branch in another Member State. There are two areas in which we believe additional clarification would be helpful. First, in both articles there is insufficient clarity in the references to tied agents (it needs to be clearer in Article 36 that the references are to tied agents established in a firm's home Member State whilst in Article 37 they are to tied agents established in a host Member State). Second, CESR recommended in its advice to the Commission that the language on a situation where a firm has no presence in another Member State other than through tied agents (the language at the end of Article 37 (2) needs to be clarified to ensure better supervision of tied agents.
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41	<p><b>Para 1 (c)</b> – The basic content of the cooperation arrangements are to be determined by ESMA (see art.44(2)(a)). In line with the approach adopted under the AIFMD, it is crucial to ensure that the detail of the agreements is consistent with broadly accepted non-discriminatory international standards developed by IOSCO in respect of the cooperation arrangements put in place between regulators.</p> <p><b>Para 2 – Status of Professional Clients</b></p> <p>As drafted, professional clients would be precluded from receiving investment services or entering into transactions with third country firms on a cross-border basis via the ESMA registration regime under Title VIII of MiFIR ('Provision of services without a branch by third country firms'). By mandating the provision of all investment services to professional clients to take place through the establishment of a physical branch presence in the EU, the Commission's proposals will undermine existing EU sectoral legislation (see below); and negatively impact existing business models, market practices and the viability and competitiveness of the EU's international financial centres (London, Paris, Frankfurt, Dublin, Luxemburg, Amsterdam etc.) that will be key engines of the future growth of the Single Market.</p>

***Suggestion – Broaden the proposed MiFIR regime for cross-border business to allow third country firms to provide cross-border services to ‘per se’ professional clients (i.e. within the meaning of MiFID Annex II (I)).***

**Potential Overlap between MiFID/AIFMD Third Country Regimes**

The interaction between the MIFID/MIFIR third country proposals and the AIFMD in circumstances where an AIFM is using the services of a third country portfolio manager or a third country custodian needs to be clarified. Managers of funds in the EU (whether UCITS, AIFMs or other types of funds) will often need to invest outside the EU and therefore need to use the services of third country firms. Such services will include the use of portfolio management services and safekeeping and administration services in a wide variety of third countries. The MiFID/MIFIR third country regimes would on their face seem to apply to these relationships. This could have a significant practical impact on the ability of EU funds to invest in third countries and use third country services (notwithstanding the limited ability given by the non-solicitation exclusion).

**1) Portfolio Management**

The purpose of the MiFID/MiFIR third country provisions is to harmonise the requirements for the provision of services by third country firms in the EU. But for example the relationship between an AIFM and a third country portfolio manager is already specifically regulated by the requirements in the AIFMD (article 20 AIFMD). Therefore there seems to be an overlap and inconsistency between the specific AIFMD regime for AIFMs and third country portfolio managers and the general MiFID/MIFIR third country provisions.

**2) Custodianship Arrangements**

In similar vein, acting as a custodian in a third country for a person in the EU may also trigger the third country requirements in MIFIR relating to the provision of services by third countries in the Union. Our view of the exemption under article 2.1(h) of MiFID is that it applies to the manager/operator of the fund itself and not to a person to whom management of assets of the fund is delegated. Likewise, that it only applies to the depositary of the fund and not to persons acting as custodians of the assets for the depositary.

Moreover, under both scenario 1) and scenario 2) described above, the third country firm would be:

- classified as a per se professional within the meaning of MiFID Annex II (I); and
- providing a service on a cross-border basis into the EU that is not covered within the scope of the MiFIR third country

	<p>regime (i.e. portfolio management or safekeeping).</p> <p>Therefore, as only Eligible Counterparties can provide services from a third country on a cross-border basis (covering the narrow range of activities covered in article 30(2) MiFID 2 – which does not include portfolio management or safekeeping and administration) into the EU, unless these firms could avail themselves of the narrow ‘non-solicitation’ exemption, they would effectively be precluded from providing such services as branching does not make any sense in this context and would be patently unworkable in practice. As a result this could create significant practical difficulties for many EU funds that use third country firms and invest in third countries.</p> <p>Further, there appears to create a direct conflict between AIFMD delegation provisions and the third country provisions in MiFID/MiFIR. It is also worth noting that it is not clear for other fund managers that there is any analogous position to that in the AIFMD regarding delegation to third party portfolio managers – so there may be broader issues in relation to other sectoral directives.</p> <p><b><i>Suggestion – the interaction between MiFID/MiFIR third country provisions and the specific delegation provisions under the AIFMD and other sectoral directives should be clarified through the inclusion of express statement that the latter should override the former in the event of a conflict (by virtue of the fact that they are part of a targeted framework of rules governing a specific sectoral regime).</i></b></p> <p><b>Para 3 – Equivalence</b></p> <p>As drafted, the text uses fairly strict equivalence language in setting out the conditions for assessing third country regulatory frameworks. The equivalence assessment appears to require a detailed line-by-line assessment of the 3rd Country’s regulatory framework. A strict equivalence regime is impossible where a third country regime has specific features tailored to the needs of its domestic market. More broadly, bearing in mind that many third country regimes (e.g. the US, Australia, Canada) may employ differing regulatory approaches to address identical risks and achieve common regulatory outcomes (investor protection, financial stability, market integrity), it will often be unrealistic and impractical to expect such jurisdictions to meet the proposed strict standards of equivalence even where their domestic regime is predicated upon common or comparable laws and standards. Any move towards common standards should be based on internationally accepted non-discriminatory standards and benchmarks developed by IOSCO.</p> <p><b><i>Suggestion – Any equivalence requirement should be explicitly outcomes-based using internationally accepted non-discriminatory standards (e.g. IOSCO) as benchmarks This should be made clear in both in the operative provisions and the</i></b></p>
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	<p><i>recitals.</i></p> <p><b>Para 3 – Reciprocity</b></p> <p>A requirement for reciprocity will undermine the effectiveness of the proposed regime. The <i>legal vires</i> of the Commission in seeking to exert extraterritorial jurisdiction is unclear and breaches its international trade commitments under the GATS agreement. At a time when trading partners should be encouraging cross-border trade in services and working towards greater co-operation and regulatory convergence, requiring reciprocal access to third country markets on the basis of strict equivalence may lead to the ‘Balkanisation’ of international financial markets based on ‘tit-for-tat’ retaliation.</p> <p><b><i>Suggestion – Remove all references to reciprocity.</i></b></p>
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43	<p><b>Para 2</b> – The text currently exempts branches of third country firms from compliance with Article 28(2) of the recast directive (MiFID 2). There seems to be no clear justification for this.</p>
44	<p><b>Para 2</b> – In line with the approach adopted under the AIFMD, the ESMA implementing measures on co-operation arrangements with third country authorities should be based on existing recognised international standards using IOSCO standards as the relevant benchmarks.</p>
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53	<p>We do not think that an RM should be given the authority to demand market-wide suspension in the case of ‘non-disclosure of information about the issuer or financial instrument’.</p> <p>In order to make a decision on whether to demand a market-wide suspension in this case, the decision-maker must have appropriate expertise, a view of the whole EU market and contact with the issuer. If there is a rumour that an issuer has not disclosed some</p>

	<p>financial information, for example, then a competent authority with access to the issuer will be able to verify whether the rumour is true before demanding a suspension. A RM, without this direct link, may well act on the rumour and demand a suspension triggering suspension in the instrument across the EU. This could cause significant and unnecessary disruption to the market.</p> <p>Finally, it is worth noting that in the recent MiFID Article 41 Task Force, ESMA looked at issues surrounding the notification of trading suspensions. One issue that was considered was the idea of giving the primary market a role in triggering market-wide suspensions, but this was rejected by ESMA.</p>
54	Please see the comment in relation to article 34 above.
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59	We refer to our answer to Question 14 above.
60	<p>We welcome the introduction of mandatory position reporting for commodity derivative contracts. Information on positions in commodity markets is vital for managing their orderly operation and exercising the position authorities envisages in art. 59.</p> <p>A practical concern however relates to the proposed frequency of information provision, i.e. in “real time”. This indicates positions should be subject to continuous reporting which is not practical, probably technically infeasible and would certainly be high costs. We suggest that daily reporting of positions is sufficiently frequent to enable market operators to accurately judge how to use their market intervention powers.</p> <p>It is also of great value to the market investigator/ enforcer when analysing course of conduct for potential manipulation. Further, making aggregated disclosure of this information to the market will provide valuable additional to the market, although it is important that the safeguard to protect the identities of participants in markets where the number of participants is relatively low.</p>
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64	Please see answer to question 24.

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71	<p>Article 71 2(a) provides for competent authorities to have a power to access any document in any form whatsoever which would be relevant for the performance of their supervisory duties and to receive a copy of it. We consider that such access should extend to where it is relevant to the exercise of competent authorities' "functions".</p> <p>Article 71 2(d) gives competent authorities the power to "require existing telephone and existing data traffic records held by investment firms where a reasonable suspicion exists that such records related to the subject-matter of the inspection may be relevant to prove a breach by the investment firm of its obligations under this Directive; these records shall however not concern the content of the communication to which they relate". Whilst we are content that telephone and existing data traffic records can only be requested by a competent authority on a reasonably held suspicion of a breach of MiFID (the text should also refer to breaches of MiFIR), we are concerned that the prohibition preventing competent authorities from accessing the content of such records will significantly compromise the effectiveness of their supervisory and investigative work. It is essential that competent authorities continue to be able to access content with respect to firms that they are responsible for supervising and taking enforcement action against. This sentence also appears to introduce a major discrepancy with Article 16 which provides that investment firms must record telephone conversations or electronic communications for transactions and keep them for a period of 3 years. The stated purpose of this is to enable competent authorities to monitor compliance with the requirements under the Directive and in particular to ascertain that the investment firm has complied with all obligations with respect to clients or potential clients.</p>
72	<p>Article 72(1) deals with the remedies to be made available to competent authorities. It must make clear that this is intended to be minimum harmonising giving competent authorities the ability to exercise remedies in addition to those listed in the article.</p>
73	<p>Article 73(2) provides that Member States shall ensure that where obligations apply to investment firms and market operators, in</p>

	<p>case of a breach, administrative sanctions and measures can be applied to the members of the investment firms' and market operators' management body, and any other natural or legal persons who, under national law, are responsible for a violation. We welcome the move to hold individuals responsible but consider that further thought is required as to the scope of persons subject to the sanctioning regime (addressees) and consider that Member States should retain discretion as to which individuals may be held responsible.</p> <p>It is not clear why the sanctions regime applies only in respect of breaches of obligations placed on investment firms and market operators when there are others to whom requirements in the directive apply, e.g. credit institutions, data reporting service providers. This reinforces our concerns on further thought being given to the scope of addressees so as to ensure that the sanctions regime is effective, proportionate and dissuasive.</p>
74	<p>We are supportive of a general requirement to publish sanctions and the discretion of the competent authority to take account of the impact of publication as proposed. However, we have some concerns that the proposed obligation at Article 74 to publish <u>any</u> measure or sanction will potentially include all supervisory measures which is unnecessarily wide and will be impractical to operate in practice. There was no like concern with a reference to “any measure” in MiFID 1 as the reference is read in the context of a discretionary power to publish measures.</p> <p>As currently drafted the Article permits publication on an anonymous basis where publication would cause disproportionate damage to the parties involved. We believe there is a need to introduce a higher threshold of “exceptional cases” is needed to ensure publication of sanctions except in very rare circumstances. Where this higher threshold is met (the expectation of severe damage to the individual) the discretion not to publish should also be afforded to competent authorities</p>
75	<p>Article 75(1) specifies precise breaches in respect of which sanctioning powers listed under Article 75(2) must be made available to competent authorities. We are concerned that specifying precise breaches is unnecessary and has created a number of mistakes (for examples it omits various breaches and incorrectly describes others). It also upsets the institutional balance provided for under the Treaties and in particular Article 288 TFEU which leaves to the Member State the choice of the form and the method of implementing the directive provisions. It is not clear whether the list is exhaustive or non-exhaustive but, even it is intended to be non-exhaustive listing out breaches in this manner also gives the impression that other breaches are not relevant or are less relevant.</p> <p>Certain of the listed breaches (e.g. those listed in (l) (n) (s) and (t)) contemplate sanctions only in the event of repeated failings.</p>

	<p>Technically one particular breach may in given circumstances warrant the imposition of a measure or sanction and it is therefore unnecessary to stipulate repeated failings to trigger the application of the sanctions regime.</p> <p>Article 75(2): We support the list of sanctioning powers to be made available to competent authorities. These should be clearly expressed as minimum harmonising allowing competent authorities to have other sanctioning powers in addition to those referred to in paragraph 2 and that they may impose higher levels of sanctions than those established in that paragraph. Further such powers should be without prejudice to Member States' ability to impose sanctions and without prejudice to the powers made available to competent authorities under Article 72 or the measures and sanctions that competent authorities may take under Article 73.</p> <p>In our view there is nothing that prevents the minimum sanctioning powers being extended to all breaches rather than being restricted to those that are listed in Article 75(1).</p>
76	<p>Article 76(1) provides that Member States shall ensure that when determining the type of administrative sanctions or measures and the level of administrative pecuniary sanctions, the competent authorities shall take into account all relevant circumstances, including those listed. We agree that the list of circumstance should be non- exhaustive but we also consider that not all the listed circumstances will be relevant to every case and need only be taken into account where it is appropriate to do so.</p> <p>Article 76(2) provides for ESMA guidelines on types of administrative measures and sanctions and level of administrative pecuniary sanctions. This is technically unnecessary as ESMA has the power to make guidelines under the ESMA Regulation if necessary.</p>
77	<p>Article 77(1) provides that Member States shall ensure that competent authorities establish effective mechanisms to encourage reporting of breaches of the provisions of MiFIR and of national provisions implementing this Directive to competent authorities. This provision needs to cover actual and potential breaches. This is something that has been recognised in the proposed Market Abuse Regulation. The same comment applies to Article 77(2).</p>
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81	The wording in the last line of Article 81(1) should be changed backed to its original form as the changes appear to now

	inadvertently prevent disclosure of information to third countries for criminal cases i.e. revert to “without prejudice to cases covered by criminal law or the other provisions of this Directive”. Mutual assistance between EU Authorities and third country authorities in criminal cases is clearly an important issue.
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83	We oppose the requirement for mandatory Regulatory Technical Standards in this Article given that discretionary Regulatory Technical Standards were only recently agreed to in Omnibus I. It follows that provision for Technical Standards to be submitted to the Commission by a specified date should be deleted
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85	Again mandatory Technical Standards should be replaced with discretionary Technical Standards as per the recently agreed Omnibus 1.
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87	We do not consider that the grounds for refusal to act on a request for cooperation in original paragraph (a) should be deleted i.e. where it may affect the sovereignty, security or public policy of the State addressed. This is a legitimate basis for refusing a request.
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99	<b>Para 1</b> – The proposed third country transitional arrangements are inadequate and risk fundamentally destabilising the functioning of financial markets. Member States should be able to retain national regime for third country firms without an inflexible deadline, at least until the Commission has made a decision on equivalence in relation to a particular country. It is also not clear why the transitional provisions have not been extended to third country firms who have not previously done business in the EU, including

	new firms. <i>Suggestion – Member States should be able to retain national regime for third country firms without an inflexible deadline, at least until the Commission has made a decision on equivalence in relation to a particular country.</i>
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<b>Detailed comments on specific articles of the draft Regulation</b>	
<b>Article number</b>	<b>Comments</b>
Recitals	<p>(16) The criteria for the identification of an SI activity in non-equity instruments will need to include a clear framework for assessing whether, in a given non-equity instrument, bilateral trading with clients is undertaken on an “organised, systematic and frequent” basis in order to enable market participants to establish to which requirements their activities are subject.</p> <p>(17) The recital should specify that a business relationship characterised by dealings above retail size in non-equity instruments is not intended to fall within the pre-trade transparency regime.</p> <p>(20) The recital should be clear that it is recognised that the OTC market in customised derivatives contracts serves a critical economic function in allowing end users to mitigate commercial risk, and that accordingly the trading procedure should also aim to preserve access to such contracts which by their nature are not appropriate for multilateral trading.</p> <p>(23) We strongly support the Commission’s moves to increase competition in derivatives by addressing trading and clearing access arrangements.</p> <p>(25) For consistency with draft MiFID, the recitals should also refer to ‘Alternative Arrangements’.</p> <p>(31) The proposal that only OTC derivatives mandated for clearing in EMIR should be subject to clearing obligation leaves a large loophole in the EU’s implementation of the G20 commitment. OTC derivatives that move onto regulated markets via industry initiative rather than through the EMIR clearing obligation will escape the clearing obligation, and may therefore remain uncleared (there are derivatives RMs in the EU that do not require full clearing). To meet the letter and the spirit of the G20 commitment MiFIR should subject all derivative products on regulated markets to the clearing obligation provided it is appropriate to do so (based on the criteria set out in EMIR).</p>
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3	<p>There does not appear to be a definition of “admitted to trading” in the regulation text. We assume therefore this is intended to refer to “admitted to trading <u>on a regulated market</u>” which is a generally understood concept.</p> <p>It is not clear what is meant by “traded on an OTF”. Does this mean traded once? Or does it need to be regularly traded? It seems unrealistic and impossible to expect market operators to be aware of or to monitor every instrument that is traded on every OTF in the EU. It also does not seem appropriate to apply transparency obligations to an instrument just because it is once traded on an OTF somewhere. Therefore as drafted this seems unworkable.</p>
4	<p>6 months is a long period for a business to wait for a waiver application. A period of two months for ESMA’s review with immediate effect thereafter would seem more reasonable and would be consistent with ESMA’s existing process for the assessment of pre-trade transparency waivers.</p>
5	<p>There does not appear to be a definition of ‘other similar financial instruments’ and it is therefore not clear which other instruments this will apply to.</p>
6	<p>We assume the intention is to provide for competent authorities to be able to authorise not just regulated markets but also MTFs and/or OTFs to defer publication.</p> <p>Recital 14 refers to the need for transparency requirements to be calibrated for different types of instruments, and this needs to be reflected in the substantive provision.</p>
7	<p>It is not clear how the requirement to “make public prices and the depth of trading interest at those prices for orders or quotes advertised through their systems...” would work with inter-dealer voice systems. Nor is it entirely clear what the impact would be on RFQ platforms.</p> <p>It is important that this be resolved at Level 1, given the fundamental importance of inter-dealer systems for bond and derivative markets.</p> <p>To this end further consideration should be given to introducing further Level 2 measures to develop a calibrated pre-trade transparency regime for voice broking, hybrid and RFQ OTFs, that recognises that such systems do not operate on the basis of continuous or firm orders or quotes (but rather indicative prices).</p>

8	<p>6 months is a long period for a business to wait for a waiver application. A period of two months for ESMA's review with immediate effect thereafter would seem more reasonable and would be consistent with ESMA's existing process for the assessment of pre-trade transparency waivers.</p> <p>Paragraph 5 would appear to be redundant. It appears to have been copied from Article 4 but as no previous waivers have been granted in non-equity markets, it is not clear this provision serves any purpose.</p>
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17	<p>The scope of the provision in paragraph 3 is extremely wide including instruments traded on an OTF and not cleared by a CCP. For those instruments, the obligation to make a price quoted to one client available to all clients could impair proper risk management, since prices will incorporate the level of counterparty risk associated with the specific client. The impact of this requirement will depend critically on the decision at level 2 determining the "size specific to the instrument". We believe consideration should be given to specifying in the Level 1 text that this size is envisaged to be retail size.</p> <p>Paragraph 6 - As the Commission recognised in ESC-07-2007 (reprinted in CESR 07-320) there will be circumstances when a person who agrees to deal against a quote provided by an investment firm is not relying on the firm to protect their interests in relation to the transaction. This often happens where professional clients request quotes from several dealers before deciding to whom to pass their orders. In these limited circumstances the dealer should not be seen as executing an order <i>on behalf of a client</i> and the best execution obligation should not apply.</p>
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20	Imposing post-trade transparency on highly bespoke derivatives that are reported to trade repositories but not traded on a regulated

	venue nor clearing-eligible would deliver little benefit to investors in terms of best execution as it is likely that only the contracting parties will have a genuine interest in the pricing of many of the instruments captured by the provision.
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22	<p><b>Article 22 (2):</b> We fully support the Commission proposal for trading platforms to keep at the disposal of competent authorities order book data; this is extremely useful information for surveillance and market abuse investigations.</p> <p>We would like to see further clarity as to the circumstances in which a competent authority can make a request to a venue. A useful suggestion would be for some parameters to be set at Level 2.</p> <p>In addition, the Commission indicated during the first council working group that the reference in this article should be to Articles 23(1) and 23(3).</p>
23	<p><b>Article 23 (2):</b> We welcome the Commission proposal of extending the scope of transaction reports to other instruments that can also be subject to market abuse.</p> <p>For ease of understanding the transaction reporting scope could be defined ‘positively’ (instead of negatively). This would be consistent with recital 29. For instance, this article could refer to instruments “which are admitted to trading on a regulated market or traded on an MTF or on an OTF”.</p> <p>A practical concern, however, relates to the proposed inclusion in scope of instruments which are “likely to have an effect”. This category of instruments will potentially capture instruments which are primarily traded outside the EEA and instruments that do not necessarily pose a risk for market abuse (such as inflation swaps, interest rate swaps, some debt-based instruments).</p> <p>For the above reasons, we believe that it would be appropriate to give a role to ESMA to develop binding technical standards to define the instruments that would be subject to transaction reporting obligations. We would therefore suggest this to be flagged in the Level 1 text (in Article 23(8) of the Commission proposal).</p> <p><b>Article 23 (4):</b> Under Article 23(1) of the Commission proposal, investment firms which execute transactions in financial instruments shall report details of such transactions to the competent authority.</p>

We agree that investment firms that ‘only’ transmit orders and also transmit the identity of the client (in accordance with paragraph 3) can be exempted from transaction reporting obligations. However, we cannot fully understand how it is possible for an investment firm to simply receive and transmit orders to an executing broker without also transmitting the identity of the client. Otherwise, how can the executing broker pass the resulting stock to the client? The executing broker will only be able to transfer ownership to the intermediary firm. This would make the intermediary firm party to the execution rather than ‘only’ receiving and transmitting the order. As the intermediary has executed a transaction (has taken ownership from the executing broker), it would have to transaction report as well.

This article could be simplified in order to clarify when exactly the investment firm can be exempted from transaction reporting.

**Article 23 (6):** We agree that double reporting for investment firms should be avoided.

We wonder whether trade-matching or reporting systems including trade repositories have to become ARMs in order to transmit the transaction reports to the competent authorities. It would be useful to understand what the effect of ‘may’ in the text might be. We believe it is important for trade repositories to comply with the ARM regime (see Article 68 of MiFID- Commission proposal) in order for the competent authority to be satisfied that trade repositories have the adequate policies and arrangements in place to report the information required under Article 23.

In addition, in order to be consistent with recital 29, it would be worth clarifying in the last sentence of this paragraph, that the transaction reporting obligation on the investment firm shall be considered to be complied with when the transactions have been reported to a trade repository **and are transmitted to the competent authority by the trade repository.**

**Article 23 (7):** The home/host rule for reporting by branches (article 23(7) of the proposed MiFIR and article 37(8) of the proposed MiFID) has raised a number of difficulties for branches as under these articles they might end up reporting the same transaction to two different member states.

Article 37(8) of MiFID, when applied to transaction reporting, requires that all transactions executed by branches where **the service is provided** within the territory of the host Member State, shall be reported to the host Member State competent authority, whereas

other transactions executed by branches shall be reported to the home Member State competent authority. This implies that branches have potentially to report its transactions to two different Competent Authorities: 1) the host member competent authority when the branch **provides a service** within the host member states and 2) the home competent authority in all other cases.

In its Level 3 Guidelines on MiFID transaction reporting, CESR tried to find a way to avoid branches reporting their transactions to two competent authorities. Therefore, CESR guidelines, allow **all** transactions executed by branches to be reported to the host Member State competent authority.

The main issue faced by branches with this approach is that there is no clear definition of what constitutes a **“service provided within the host territory”**. Firms question whether it relates to the office that books a trade, the office that has the relationship with the client or the office that commits the firm to the trade. In addition, Member States may have different and conflicting definitions, which may potentially result in the branch reporting the same transaction to two competent authorities.

In order to overcome this difficulty as well as to provide some clarification in this area, it would be worth granting ESMA the power to draft regulatory technical standards in this field. We would recommend this to be flagged in the Level 1 text (in Article 23(8) of the Commission proposal).

**Article 23 (8):** ESMA powers could be extended to include the following in order to ensure stronger harmonisation of transaction reporting requirements:

- A definition of what constitutes a transaction for the purpose of this article.
- The relevant financial instruments covered by Article 23(2) (please see our comments related to the proposed scope above).
- Transaction reporting obligations of branches of investment firms (see comment below – Additional comment- for explanation).

**Additional comment: Reference data**

	<p>In order for competent authorities to be able to make sense of the transaction reports submitted to them under Article 23 (3), it is crucial for trading platforms (RM, MTFs and OTFs) to provide competent authorities with appropriate reference data. Article 11 of the implementing Directive 2004/39/EC states that ‘regulated market shall submit identifying reference data on each financial instrument admitted to trading in an electronic and standardised format to its home competent authority’.</p> <p>Currently, all competent authorities collect reference data from the regulated markets that they supervise and transmit it to ESMA (on a daily basis). ESMA consolidates this information and disseminates back to all CAs. The reference data received from ESMA is then used to validate against the transaction reports; improving the quality of the data as inaccurate transaction reports would be rejected. Collecting accurate reference data is therefore crucial for competent authorities’ ability to monitor the market effectively and consequently enables them to meet their MiFID obligations.</p> <p>The FSA has been collecting reference data since MiFID I, and our experience has taught us that collecting reference data from regulated markets can be sometimes very challenging. Our lack of power against trading platforms in this area does not allow us or any other competent authority to enforce them to comply with their reference data requirements. This issue will be amplified with the introduction of new categories of trading venues (i.e., MTFs and OTFs).</p> <p>These issues can have detrimental impact on data quality if they are not addressed. We believe it would be useful to include a provision in the Level 1 text stating trading venues’ obligations with regards to providing appropriate reference data. The Level 1 text should ensure that 1) the new trading venues i.e. MTFs and the OTFs are also captured under this provision and 2) competent authorities shall be able to take disciplinary actions if trading venues do not comply with their obligation to supply accurate and complete reference data. In addition, the Level 1 text should also ensure that the standards of the reference data as well as the format and the timing of providing the data are defined by ESMA through technical standards.</p>
24	<p>This provision appears to effectively preclude the use of electronic “single dealer platforms” for the trading of G20 derivatives. Some 5-15% of interest rate swaps are estimated to trade on these venues which are highly valued by end users, and are able to deliver the regulatory outcomes envisaged by the G20. We do not believe the rationale for excluding them has been adequately explained.</p>

	We believe SI should be added as an eligible venue for the trading of G20 derivatives. As commented elsewhere, the prohibition at Article 20 of the Directive (on OTF operators trading against their own capital in their OTF) should also be removed, so as to allow derivatives market participants to access an additional source of liquidity in OTFs.
25	<p>The current draft of MIFIR only applies a clearing obligation to derivatives that were previously traded OTC and that were subject to a clearing obligation under EMIR. However, in keeping with the G20 commitment of reducing risk in the global derivatives market, we recommend that all derivatives are subject to the clearing obligation. This will also serve to ensure that a clearing obligation cannot be circumvented by taking an OTC product to exchange.</p> <p>Virtually all derivatives currently traded on regulated markets are effectively cleared in any case</p>
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28	<p>The basis on which a CCP or trading venue may refuse access should be restrictive and decisions should be subject to scrutiny by the competent authority.</p> <p>The initial text proposal includes 'volumes of transactions' and 'users' as a basis for refusing access, which could be interpreted broadly and potentially used to block access unfairly.</p> <p>Art 28(3) provides CCPs with 3 months to facilitate access for trading venues. We feel that this timeline is too long, given that the CCP simply needs to grant access to the trading venue in question: the functionality should already be in place. We would suggest that it should be a matter of days or weeks.</p> <p>We would further support the inclusion of a requirement to notify ESMA of a refusal to grant access -under both 28 and 29 – to provide an extra point of scrutiny over access refusal.</p>
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30	The current draft of MIFIR provides for CCPs and trading venues to be granted non-discriminatory access to licence benchmarks by the entity holding the proprietary rights. This is needed to allow CCPs to be able to use reference benchmarks underlying OTC transactions which are necessary in order to be able to clear certain derivative contracts.
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36	<p><b>Para 1 – Absence of Requirements relating to Markets</b></p> <p>The explanatory text to the proposals states that the third country provisions create a harmonised framework for granting access to EU markets for firms and market operators based in third countries. However, the scope of application of the proposals in relation to third country market operators is unclear. There are indeed:</p> <ul style="list-style-type: none"> <li>• No mention of market operators in the provisions or articles relevant to trading venues;</li> <li>• No specific provisions governing remote access to third country market infrastructure by EU firms (or conversely access to EU market infrastructure by third country firms);</li> <li>• No equivalence criteria relating to the recognition of third country market infrastructure; and</li> <li>• It is not clear a firm registered with ESMA under article 36 of MiFIR could become a member of an EU trading venue without otherwise being authorised in the EU.</li> </ul> <p>Moreover, the Commission proposals appear to reverse the current position in relation to passporting by venues. For a third-country firm to require authorisation then they have to be undertaking activities outside their state of incorporation. But currently under MiFID, if an EU investment firm remotely accesses an MTF outside its home member state it is the MTF operator who has to make a passporting notification under article 31 of MiFID and not the investment firm. Likewise in the UK we allow third-country venues to admit remote members based in the UK under our Recognised Overseas Investment Exchange regime. UK firms accessing ROIEs are treated as doing business in the UK and are not required to be authorised by the home member state of the ROIE.</p> <p><b>Para 1 – Status of Professional Clients</b></p> <p>As drafted, professional clients would be precluded from receiving investment services or entering into transactions with third country firms on a cross-border basis via the ESMA registration regime under Title VIII of MiFIR (‘Provision of services without a branch by third country firms’).</p> <p>In our view <i>per se</i> professional clients (namely those professional clients referred to Annex II, Section I (I) of MiFID) should be</p>

subject to the same regime as Eligible Counterparties (ECPs). Third country firms that wish to be able to provide services or activities to eligible counterparties and *per se* professional clients across the Union should be able to do so, if they register with ESMA and (among other things) an equivalence assessment has been carried out by the Commission in relation to the regulatory and supervisory framework of the third country.

EU firms rely on third country firms and markets on a daily basis for their funding and investment needs. Many EU banks, investment firms and asset managers wish to access international markets by dealing with non-EU firms, including in a broad variety of emerging markets, and for a range of services going beyond the limited range of services covered by Article 30 MiFID 2. It is therefore not realistic to rely on the passive provision of services to allow such business, when in practice in many cases it is impossible in wholesale markets to identify which party took the initiative.

***Suggestion – Broaden the proposed regime for cross-border business to allow third country firms to provide cross-border services to per se professional clients.***

#### **Para 4 – ‘Non-solicitation Exemption’**

The scope of the ‘non-solicitation’ exemption needs to be re-drawn:

1. Given the scope of access restrictions applicable to professional clients, it is unrealistic to expect firms and their clients to rely on the narrowness of the proposed ‘non-solicitation’ exemption to address the wide range of interactions and communications which take place across international markets (this issue is of particular concern for EU international financial centres where banks, investment firms and asset managers in those centres need access to non-EU firms around the world in order to provide a full range of services to their EU and non-EU clients).
2. Many investment services and activities are provided in the context of continuing relationships between the firm and the client. It would unduly limit the access of EU investors and counterparties to the services provided by third country firms if third country firms were, for example, effectively prohibited from providing information and research to their existing clients.

***Suggestion – It should be made clear that the exemption is intended to apply at the relationship level and not on a transaction-by-transaction basis.***

3. In addition, in some cases, the services will be provided wholly outside the EU (e.g. where the client receives services while

	<p>travelling outside the EU).</p> <p><b><i>Suggestion – It should be made clear in the relevant recitals of MiFID and MiFIR that such services fall outside the perimeter of the directive and the regulation.</i></b></p> <p>4. Moreover, third-country firms should also be exempt from the requirement for authorisation in their dealings with firms authorised under directives in the EU or clients whose dealings are intermediated through investment firms. In many cases, an authorised EU firm will be mediating the transaction concerned, e.g. where an EU client is instructing an EU firm to act as its agent to execute transactions on a third country market through a third country firm. In these circumstances the indirect provision of services to the EU client should not be regarded as taking place in the EU. The burden should be on regulated EU firms to determine the level of protection that they need and the quality of the counterparties with which they deal whilst ensuring that their clients are provided with the full scope of EU regulatory protections. Also the huge range of non-EU counterparties that might require registration simply because they deal with EU eligible counterparties of this kind will make the task of national supervisors very difficult.</p> <p><b><i>Suggestion – In these circumstances, the indirect provision of services to the EU client should not be regarded as taking place in the EU and an express statement to this effect should be included in the MiFID/MiFIR recitals</i></b></p> <p>5. Finally, the exemption itself needs to be replicated in the operative provisions of the re-cast Directive. Indeed, although Recital 74 of the recast directive (and recital 36 MIFIR) clearly states that “<i>the provision of this directive should not affect the possibility for persons established in the Union to receive investment services by a third country firm at their own exclusive initiative</i>”, only article 37(4) of MIFIR expressly spells the exemption out in its operative provisions.</p> <p><b><i>Suggestion – replicate the exemption in the operative provisions of MiFID 2 to ensure consistency.</i></b></p>
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45	<b>Para 1</b> – The proposed third country transitional arrangements are inadequate and risk fundamentally destabilising the functioning of financial markets. Member States should be able to retain national regime for third country firms without an inflexible deadline, at least until the Commission has made a decision on equivalence in relation to a particular country. It is also not clear why the transitional provisions have not been extended to third country firms who have not previously done business in the EU, including new firms.
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