

Group Briefing

May 2016

MiFID II: timing update, organisational requirements, operating conditions and defined terms

TIMING UPDATE

In our [February 2016 Client Briefing](#), we confirmed that the European Commission had signalled its intention to extend the application date for MiFID II by one year to 3 January 2018.

The status of the proposed extension (which will take the form of both a directive and a regulation) is as follows:

- » the proposals are currently scheduled to be considered by the European Parliament between 6 and 9 June 2016; and
- » the ECB issued an [opinion](#) on 29 April 2016:
 - » suggesting that the transposition deadline for Member States also be deferred by 1 year for consistency purposes; and
 - » noting that the 1 year delay would not affect the timeline for adopting the required Level 2 measures.

NEW COMMISSION DELEGATED REGULATION

On 25 April 2016, the European Commission adopted a [Delegated Regulation](#) (together with 4 Annexes) setting out organisational requirements and operating conditions for investment firms and clarifying the scope of various

defined terms under MiFID II.

Rules: The Delegated Regulation sets out rules across the following areas:

- » **Organisational requirements for investment firms**
 - » Procedures in relation to compliance, risk management, internal audit, the responsibility of senior management, complaints handling, remuneration, personal transactions, outsourcing and conflicts of interest.
 - » Underwriting and placing services, and the production and dissemination of investment research and marketing communications.
- » **Conduct of business obligations in the provision of investment services**
 - » The provision of fair, clear and non-misleading information when providing investment services or ancillary services to clients.
 - » Information that must be provided to clients and potential clients in relation to categorisation, the investment firm itself and its services, financial instruments, safeguarding client financial

instruments or client funds, cost and associated charges.

- » New requirements regarding the provision of information about investment advice, the provision of investment advice on an independent basis, and how suitability and appropriateness are assessed.
- » When financial instruments will be treated as non-complex.
- » The content of written agreements with retail and professional clients.
- » Client reporting, including statements of client financial instruments and funds.
- » Best execution and execution policies.
- » Client order handling.
- » Criteria for treating clients as eligible counterparties.
- » Recording-keeping obligations, including new rules regarding the recording of telephone conversations and electronic communications.
- » **SME growth markets**
 - » Criteria that an issuer must meet

to qualify as an SME¹.

- » Conditions with which a multilateral trading facility (MTF) must comply if it wants to be registered as an SME growth market.
- » **Trading venues**
 - » What could constitute significant damage to investors' interests and the orderly functioning of the market.
 - » Circumstances where one can assume that:
 - » behaviour prohibited under the new market abuse regime has taken place; or
 - » significant infringements of the rules of a trading venue, disorderly trading conditions or system disruptions have occurred.
- » **Other**
 - » Position reporting in commodity derivatives, and data provision by data reporting service providers.

Definitions: The Delegated Regulation clarifies some key definitions and terms including:

- » **Investment services**
 - » When an investment service will be deemed to have been provided in an incidental manner.
- » **Energy**
 - » The conditions under which wholesale energy products must be physically settled.

¹ An issuer whose shares have been admitted to trading for < 3 years will be deemed an SME if its market capitalisation is < €200 million based on any of the following: (a) the closing share price of the first day of trading if its shares have been admitted to trading for < 1 year; (b) the last closing share price of the first year of trading if its financial instruments have been admitted to trading for > 1 year but < 2 years; (c) the average of the last closing share prices of each of the first 2 years of trading if its financial instruments have been admitted to trading for > 2 years but < 3 years. An issuer with no equity instrument traded on any trading venue shall be deemed an SME if, according to its last annual or consolidated accounts, it meets at least 2 of the following 3 criteria: an average number of employees during the financial year of < 250, a total balance sheet ≤ €43,000,000 and an annual net turnover ≤ €50,000,000.

- » What constitutes an energy derivative contract for each of oil, coal and wholesale energy products.

» **Derivative contracts**

- » When a contract that is not a spot contract and is not for commercial purposes will be considered as having the characteristics of other derivative financial instruments.
- » In respect of the contracts listed at Section C(10) of Annex I to the MiFID II Directive², when other types of derivative contract might be subject to that section.
- » When a derivative contract relating to a currency will not be a financial instrument.

» **Investment advice**

- » A confirmation that a recommendation will not be regarded as a personal recommendation if issued exclusively to the public.

» **Money market instruments**

- » The conditions that treasury bills, certificates of deposit, commercial paper and similar instruments must meet to be considered money market instruments.

» **Systematic internalisers**

- » The criteria that must be met for an investment firm to be considered a systematic internaliser for shares, depositary receipts, exchange-traded funds, certificates, bonds, structured finance products, derivatives and emission allowances.

² Options, futures, swaps, forward rate agreements and any other derivative contracts relating to climatic variables, freight rates or inflation rates or other official economic statistics that must be settled in cash or may be settled in cash at the option of one of the parties other than by reason of default or other termination event, as well as any other derivative contracts relating to assets, rights, obligations, indices and measures not otherwise mentioned in Section C(10), which have the characteristics of other derivative financial instruments, having regard to whether, inter alia, they are traded on a regulated market, organised trading facility or MTF.

» **Other**

- » Algorithmic trading and algorithmic trading techniques.
- » Direct electronic access.

NEXT STEPS

The Delegated Regulation is now being considered by the EU Council and European Parliament. If neither objects, it will be published in the Official Journal and apply from the date that the MiFID II Directive applies.

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