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Non-EU investment firms' access to EU investors under MiFID 2

Background

The recast Markets in Financial Instruments Directive (**MiFID 2**), along with its accompanying Regulation (**MiFIR**), were published in the Official Journal of the EU in June. The new legislation is currently expected to come into effect in January 2017.

The main new developments outlined in this client briefing can be loosely summarised in the following terms: non-EU (**third country**) firms are to be given greater, harmonised access to certain kinds of EU-based professional investors in exchange for meeting certain specified EU regulatory standards; these enhanced access provisions should be broadly reciprocal, so that EU firms should be able to benefit from similar access to third country markets.

This briefing looks at the cross-border aspects of the MiFID 2 package, and in particular, the regime whereby third country firms are permitted to deal with EU-based investors without the establishment of a physical presence in the relevant EU country.

The proposals in brief

Under the new regime, firms from outside the EU will be able to provide cross-border MiFID investment services and activities to customers and counterparties in the EU in the four main circumstances outlined below.

First, third country firms which are authorised in their home countries will be able to provide cross-border investment services and activities to eligible counterparties and "*per se*"[1] professional clients where the Commission has made an "equivalence decision" regarding the legal and supervisory arrangements in the firm's home country **and** the firm has been registered with the European Securities and Markets Authority (**ESMA**). National regulators from third countries must also enter into cooperation agreements with ESMA. The ESMA registration process may take up to several months. Certain other procedural requirements and disclosures must be complied with[2], but, once met, member states may not impose additional local requirements and the third country firm will be entitled to provide investment services to eligible counterparties and *per se* professional clients throughout the EU.

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1 A "*per se*" professional customer includes investment firms, credit institutions, large corporates meeting certain threshold criteria and national or regional governments. Any customer which would ordinarily fall to be regarded as a retail customer but which "opts up" to professional status is an "elective" professional client and not a "*per se*" professional.

2 For example, third country firms must offer to submit disputes regarding services provided to EU investors to the jurisdiction of a court or tribunal in the EU; make specified investor disclosures; and provide information regarding themselves to ESMA.

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Secondly, member states may require non-EU firms to establish an authorised branch in their member state to access retail or elective professional clients. Where such branch authorisation is obtained, the firm will be able to provide investment services in the member state in which it is authorised and the branch may provide cross border services in other member states to *per se* professional clients and eligible counterparties where the Commission has made an equivalence decision regarding the home country's legal and supervisory framework. Certain other requirements must be met.

Thirdly, cross-border investment services and activities may be provided by third country firms to retail clients, professional clients or eligible counterparties without the need to comply with the detailed MiFID 2 requirements if the service or activity is provided at the "*own exclusive initiative*" of the client or counterparty. This exemption is to be narrowly construed and the legislation specifically prohibits the marketing of new categories of investment product or service to investors under this exemption.

Lastly, a third country firm may provide cross-border investment services and activities to eligible counterparties and *per se* professional clients for a transitional three year period after the adoption of an equivalence decision by the Commission or in the absence (or withdrawal) of such a decision. In those cases, services and activities must be conducted, to the extent permitted by, and in accordance with, local rules.

What should non-EU firms do?

Now

At present, the issue is "on the horizon", rather than something firms need to take active steps in relation to, since non-EU firms should be able to continue to conduct activities in the EU to the extent permitted by, and in accordance with, local rules until at least 2020. However, changes to local rules as a result of MiFID 2 or otherwise, should be monitored in the meantime.

Next year

ESMA is required to submit draft regulatory technical standards (RTS) relating to the information which third country firms should supply to it in connection with registrations, to the Commission by July 2015. At that point, non-EU firms may wish to begin to consider what the information requirements are, whether equivalence decisions are in train in relation to their particular jurisdictions, and what the firm's strategy is for accessing European markets. Any additional liability to investors, disclosure requirements and accountability to regulators flowing from falling within the ESMA registration regime would need to be assessed and balanced against the firm's business model and likely future engagement with investors in Europe.

The Longer Term

Firms which have only occasional contact with European investors may wish to consider whether to limit their business activities in Europe to non-MiFID activities and services or whether to provide services only in response to a client's "own exclusive initiative". Firms which decide to register with ESMA when MiFID 2 is implemented should be aware of the time-frame involved.

Non-EU firms' compliance manuals and staff training will need to be updated to reflect the new rules as and when they become effective and as equivalence decisions or ESMA registrations are made. Internal resource will need to be identified and deployed so as to ensure effective oversight, compliance and handling of the new ESMA framework.