GETTING READY FOR THE IMPLEMENTATION OF MIFID II/MIFIR

Prospectus of ECMI Events

If you are interested in participating in these events series, please do not hesitate to contact **Dr Apostolos Thomadakis** (Researcher, European Capital Markets Institute) by email at: apostolos.thomadakis@ceps.eu or by phone: +32 (0)2 229 39 14.

The European Capital Markets Institute (ECMI) invites industry representatives, policymakers, investor associations, academics and other interested stakeholders to take part in a series of special events on the topic of MiFID II/MiFIR to discuss the readiness of market players and the supervisory community to comply with the provisions set out in new legislative framework.

BACKGROUND

The implementation of the Markets in Financial Instruments Directive (recast) (MiFID II) and the Markets in Financial Instruments Regulation (MiFIR) is expected to cause a big bang in markets next year. Ever since the economic crisis, calls for more transparency have grown louder, and constraints on investment providers increased, resulting in a radical upgrade of the MiFID of 2004, which now covers the basic principles of market organisation and rules governing market participants.

The main novelties compared to the 2004 version are the addition of a trading facility, the Organised Trading Facilities (OTFs), the rules on algorithmic trading, the licensing of data publication arrangements and the regulation of trading in commodity markets. In addition, MiFID II, in combination with EMIR (European Market Infrastructure Regulation), sets the framework to trade sufficiently liquid standardised OTC derivatives, further to the Pittsburgh G-20 conclusions.

It is expected that MiFID II will transform financial markets in Europe and this will affect every part of the securities trading value chain, from trade execution and investor protection to reporting and settlement. The impact will be both direct, by stipulating new market participant practices, and indirect, by changing the economics of securities trading (through increased automation and transparency) and, in turn, changing the business models of many market participants. New data publication rules will also be imposed and new players will enter parts of the value chain.

AGENDA

Three public panel debates will be organised at CEPS in Brussels, with high level speakers who are regulators, policymakers, industry representatives, investors or academics, and keen to engage audiences in discussion. Registration will open at least four weeks before each of the events on:

1. Pre- and post-transparency for non-equity markets
2. Data publication arrangements, consolidation and reporting
3. Investor protection provisions

Based on these discussions and drawing on its own independent research, CEPS-ECMI staff will draft a summary report for publication on the CEPS/ECMI websites and distribute it to a wide audience.

TIMELINE

Transparency – April 2017

Under the current MiFID I, transparency requirements are limited to equities admitted to trading on regulated markets (RMs). However, MiFID II proposes to substantially expand the scope of the transparency to cover financial instruments traded not only to RMs, but also to multilateral trading facilities (MTFs), organised trading facilities (OTFs), and Systemic Internalisers (SIs). This includes shares; depositary receipts; exchange traded funds; certificates and similar instruments (equity-like instruments); bonds; structured finance products; emission allowances and traded derivatives (non-equity instruments).

Arguably, the new transparency requirements are some of the most challenging and significant with respect to market structure. In particular, the obligation to report publicly in real time pre-trade actionable indications of interest (IOIs) or firm prices presents a number of challenges. While both the buy- and sell-side need to publish quotes and trades, thought also needs to be given to how this new transparency will change market behaviours and how the new data can be used.

Bond trading is mostly conducted over the counter and so far has relied on banks acting as dealers, maintaining an inventory of bonds to trade bilaterally with investors. This market structure highlights the lack of a steady flow of multiple third-party buyers and sellers. Investors have therefore come to rely on dealers for immediacy. But the market structure is also partly a function of the lack of information about prices and market conditions faced by investors. This is a key issue that MiFID II seeks to address via a pre- and post-trade transparency framework for all non-equity financial instruments, including bonds.

The asymmetry of information between investors and dealers in bond markets offers some protection for liquidity providers by shielding their positions from opportunistic traders. In other words, there is a trade-off between the transparency needs of investors and the provision of liquidity by banks and other market makers. Balancing these competing interests is a complex and delicate exercise, and goes to the heart of the challenge faced by ESMA.

New trade reporting rules risk reducing debt-issuer liquidity across the EU, potentially exacerbating the fragility of EU bond markets. MiFID II mandates the public disclosure of pre-trade quotes prices and indications of interest, unless liquidity falls below a certain threshold, as well as post-trade transaction data. In an open, executable 'firm-quote' environment, it is possible for market-makers to widen quotes or pull out of the market altogether.

- How will the new rules be implemented, and how will they impact market structure? Will greater transparency undermine liquidity?
- How will the calibration of transparency requirements for different types of trading systems work?
- Can we achieve operation simplicity and accuracy at the same time?
- How can consistent applications across all jurisdictions be ensured?
- What are the advantages and disadvantages to using an SI over a broker crossing network (BCN)?
- Will the buy-side enjoy the same support and liquidity under the SI regime as they do with BCNs?

Data – June 2017

Data is a major regulatory change under MiFID II and will play a crucial role in understanding firms' trading strategies. Data reporting and management – such as data capture, storage, breadth, reporting accuracy and publication – are among the most problematic areas for buy-siders implementing MiFID II-compliant systems. One of the reasons for the delay in the implementation of MiFID II is data collection and the ability to report information.

While the number of data fields required in the transaction reports was 23 under MiFID I, this is expected to increase to more than 80 under MiFID II (with only 13 of the 23 existing fields remaining unchanged). This is because many more details are required to identify the client and there are completely new requirements to identify the originator of the decision to trade and those executing it.

Companies must also demonstrate effective oversight and control of the policies and procedures that govern all communications. For example, there is a requirement to supply regulators with communications associated with a specific trade and being able to reconstruct the history of trade cycle events. Furthermore, companies must make records available to clients for a retention period of five years and for up to seven years for regulators. Therefore, the need for secure data storage has never been greater, especially when jurisdictional limitations need to be considered. Some jurisdictions may enforce confidentiality rules and restrict information-sharing among parties, while others may not.

In an effort to collect data in an efficient and harmonised manner, a new data collection infrastructure, the Financial Instruments Reference Data System (FIRDS), is being developed by the ESMA in conjunction with NCAs. FIRDS will cover a wide range of financial instruments brought into the scope of MiFID II, which will link data feeds between ESMA, NCAs and trading venues across the Union.

- What are the operational challenges that the additional levels of granularity impose?
- Can trade/transaction reporting platforms report across multiple sources of data in real-time?
- How can the provenance of information be tracked through a reporting regime?
- Can we support on-demand audit and investigative requests for access to complete history data on transactions, customer records, reports, computational results?
- How to demonstrate end-to-end provenance and governance on data along the reporting hierarchy with proven processes that validate sources, relationships and temporal affinity?
- Where do we stand and what has been the progress with FIRDS to date?

Investor protection – September 2017

Regarding provisions on investment advice, MiFID II takes a firmer line on conflicts of interest, inducements and cross-selling practices in the financial sector. Although the rules, in embryonic form, were already part of the 2004 directive, they have been spelled out more clearly, brought into level 1, and substantially upgraded and broadened in MiFID II. The main novelty is the requirement for investment firms to inform clients whether or not investment advice is provided on an independent basis (i.e. paid by the user), and to ban all payments from third parties, apart from certain 'minor non-monetary benefits' that are 'capable of enhancing the quality of service' (Art. 24), if advice is included. This should ensure that clients are not sold inappropriate products, and that limited inducements benefit the client.

The provisions on investment advice are largely based on the UK's retail distribution review (RDR), which came into effect at the end of 2012. It was designed to restore trust in financial advice and applies to advisers, to banks and to other providers of financial products. In an EU context, however, this is opening Pandora's Box, as it concerns services and products that are covered by a diversity of providers, firms or intermediaries, for a very diverse market with diverse practices, following different pieces of regulation and often with different supervisors in charge. Furthermore, it raises the question of how investment research is differentiated from advice.

To avoid conflicts of interest, the new rules require that firms can only pay for research from their own resources, or need to create a research payment account, which can only be funded through a research charge to clients. The total research charged to clients cannot exceed the budget of the research payment account.

- How will the unbundling of research/trading costs impact the model of investment banks and asset managers?
- Will the prohibition of commission payments enable more business for passive funds and robo-advisors?
- What are the risks and benefits related to different types of financial advice (independent and non-independent, face-to-face versus automated advice)?
- Are there any barriers to innovation and technological advances that could prevent the emergence of new distribution models?
- How clear is the identification of whether or not a particular problem is a PRIIP (exposure to reference values)?
- What is the scope of retail investors, and what are the quantitative and qualitative tests that can opt up 'retail' investors to 'professional' investor status?

PARTNERSHIP

ECMI is an independent think tank that undertakes research and contributes to policy debates on capital markets in Europe. It is managed by CEPS, one of the most authoritative think tanks operating in Europe. ECMI also offers interested stakeholders the opportunity **TO BECOME A SPONSORING PARTNER** for this series of events on MiFID II/MiFIR. The sponsorship would allow partners to have a greater expert presence and corporate visibility at the events(s). The benefits and sponsorship options are outlined in the application form at the end of this prospectus.

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More information about ECMI at: **http://www.eurocapitalmarkets.org/**

SPONSORSHIP FORM

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Sponsoring options (+21% VAT; payment via invoice)

☐ **1 event (EUR 2,500)**	**1 panellist, 1 free delegate, logo on event materials and event webpage**
☐ **3 events (EUR 6,000)**	**1 panellist/event, 3 free delegates/event, logo on event materials and event webpage**

Please indicate your preference. Depending on availability and compatibility with the programme, we will confirm the sponsorship and the event participation.

- ☐ Transparency – April 2017
- ☐ Data – June 2017
- ☐ Investor protection – September 2017
- ☐ All three events

Please indicate the name and position of the person who would potentially participate as panellist:

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Please return the form by email to Maarja Kuusik at maarja.kuusik@ceps.eu.
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Informing policy on European capital markets