

MiFID III

Regulatory Overview and Timelines

Regulation Overview

Both European Commission and UK have recently drafted several amendments to the MiFID framework that many have dubbed MiFID III. While the European Commission's proposals are still in consultation phase and changes are still expected to be made, the UK has passed two Acts/Policies which are both in the implementation phases. MiFID III is following a staggered approach, where amendments have been proposed in several policy updates. On December 12, 2023 the UK drafted its fourth set of commencement regulations made under the Financial Services and Markets Act 2023 to revoke and replace the previous MiFIR/MiFID II rules.

This white paper will summarize many of the recent proposed amendments to the MiFIR/MiFID II both in UK and EU markets.

Objectives for Updates to the MiFID Framework

In the efforts made by European Commission and FCA to update MiFIR and MiFID II rules, these regulatory bodies have generally aimed to achieve the following objectives:

- Enhancing post-trade transparency and availability of market data for more efficient pricing;
- Enhancing execution quality by lowering the costs of trading;
- Promoting greater competition, choice and access between trading venues, systematic internalisers (“SIs”), and investment firms to ensure EU/UK market infrastructures can remain internationally competitive;
- Lowering operational and compliance costs for firms for firms that have not delivered much benefit;
- Improving market resilience during market outages;
- Harmonize the rules to be consistent with other international regulations.

Regulatory Timelines

Updates to the MiFIR/ MiFID II Framework include “MiFID Quick Fix” which were aimed to be more temporary in nature in order to support economic recovery of COVID-19, as well as more recent proposed updates which are aimed to be permanent enhancements. The timelines for these amendments is as follows:

(EU) No 600/2014 (“MiFIR”) & Directive 2014/65 (“MiFIR II”)	Directive (EU) 2021/338 (“MiFID Quick Fix”)	COM(2021)727 Proposal	CP22/12 & PS23/4	Retail Investment Strategy Proposal	Financial Services & Markets Act 2023	
Final regulations drafted of MiFIR & MiFIR II to strengthen transparency and improve functioning of the financial markets.	Amendments made to MiFIR in order to support the recovery from the economic shock caused by COVID.	Amendments to EU No 600/2014 aimed at enhancing market data transparency & creating a consolidated tape	Consultation papers and policy statements drafted on improving equity secondary markets.	Proposal published by European Commission which is an omnibus directive amending existing legislation	Bill passed to create a UK regulatory framework that is better tailored to UK markets.	
May 15, 2014	Feb 16, 2021	Nov 25, 2021	Jul 5, 2022	May 3, 2023	May 24, 2023	Jun 29, 2023

Recent Amendments to the MiFID Framework for UK

Following Brexit, the UK created a new Financial Services and Markets Act 2023 to create a new regulatory framework for the UK designed specifically for the UK financial markets. This act makes transitional amendments to MiFIR and MiFID II for eventual revocation of the EU laws. In addition, FCA recently adopted consultation paper 22/12 with updates to post-trade transparency, pre-trade transparency waivers and tick size regime.

Financial Services and Markets Act 2023

Key changes to the MiFID framework include the following:

- Removing the Share Trading Obligation which stipulated that shares could only be traded on certain venues, so that firms can trade shares either (i) on a trading venue in the UK or overseas, or (ii) on an OTC basis;
- Removing the Double Volume Cap (DVC) to enable firms better choice to execute on the venue with best price. The DVC was a cap to limit the trading under the reference price waiver and the negotiated transaction waiver for liquid instruments in an equity instrument;
- Revising the definition of “Systematic Internaliser” (SI). The definition of SI was initially determined on a qualitative basis, but in 2018 the definition was amended to introduce quantitative thresholds. The latest revisions revert back to a qualitative definition and gives the FCA the power to specify how the new definition should be interpreted to keep it flexible and able to account for market evolutions;
- Removing restrictions on SIs for midpoint crossing (i.e., crossing halfway between the buying and selling prices). Initially the restrictions were limited to trading venues but were extended to SIs in 2020;
- Re-aligning the counterparties in scope of the Derivatives Trading Obligation to those in scope of the EMIR Clearing Obligation. In 2019 EMIR was amended to alter the counterparties in scope of the CO, but the DTO was not updated to reflect that change;
- Exempting additional post-trade risk reduction services from the derivative trading obligation (DTO) and gives the FCA the power to modify or suspend the DTO;
- Giving the FCA the relevant powers to update the pre-trade transparency waivers as its elements have been considered to be too restrictive;
- Simplifying the transparency regime for fixed income and derivatives by delegating responsibility for calibrating the scope and firm-facing transparency requirements to the FCA;
- Removing the requirement for position limits in commodity derivatives, and transferring the responsibility of setting position limits from the FCA to the trading venues;

Policy Statement 23/4 on Improving Equity Secondary Markets

Key changes to the MiFID framework coming into force on April 29, 2024:

- Improving the content of post-trade transparency by:
 - (i) modifying and expanding the list of transactions that are exempted from post-trade transparency because they are non-price forming,
 - (ii) achieve greater consistency and limit duplications in the use of trade identification flags,
 - (iii) changing the conditions under which investment firms are required to report trades executed OTC, to simplify and lower the cost of reporting for firms;
- Simplifying the reporting of OTC transactions for all classes of financial instruments by removing the SI status as a criterion for establishing when an investment firm is required to report transactions. In its place will be a new “designated reporter regime” whereby firms would elect to register themselves as a designated reporter.

Key changes to the MiFID framework that came into force April 28, 2023:

- Updating the reference price waivers for pre-trade transparency that requires orders and quotes to be publicly displayed before execution, by updating the definition of “the most relevant market in terms of liquidity” to enable reference prices to be derived from trading venues outside the UK;
- Removing the fixed minimum monetary threshold for reserve orders and stop orders benefiting from the “order management facility” waiver to allow trading venues to determine the minimum size thresholds according to the characteristics of their markets;
- Improving the quality of execution by removing restrictions to allow trading venues to set the minimum tick size at the level of the primary market located overseas (when that tick size is smaller).

In addition, FCA aims to enhance market resilience by establishing a task force to develop good practices for trading venues and investment firms in the event of a trading venue outage.

European Commission Proposed Amendments for EU

Two proposals have been drafted by the European Commission to propose several amendments to MiFIR and MiFID II, which are considered to be the next wave of MiFID reform in the EU. These initiatives are aimed at retail investors to enable them to access relevant, comparable, and easily understandable information so they make informed investment choices. The key changes of both of these proposals is summarized below.

COM(2021)727 Proposal For Amendments to EU No 600/2014

Key proposed changes to the MiFID framework include the following:

- Implementing an EU-wide central database (“consolidated tape”) to provide a comprehensive view of prices and volumes of equity and equity-like securities traded throughout the EU. All EU trading venues and systematic internalisers (Sis) are to provide the consolidated tape provider with market data in standardized data reports;
- Updating the scope of the Share Trading Obligation by (i) limiting it to only shares admitted to trading on an EEA regulated market, (ii) remove the exemption for trades in shares that are non-systematic, ad-hoc, or irregular and infrequent;
- Removing the open access regime for exchange traded derivatives;
- Removing potential conflicts of interest by banning payments-for-order-flow to prevent firms from forwarding client orders for execution to certain venues due to payments received;
- Shorten and harmonize publication deferrals for non-equity post-trade reports to the public;
- Making market operators and investment firms operating a trading venue to provide market data on a reasonable commercial basis in line with the Guidelines;
- Adding a licensing requirement for multilateral systems to operate;
- Re-aligning the counterparties in scope of the Derivatives Trading Obligation to those in scope of the EMIR Clearing Obligation;
- Adding sanctions for infringements of certain new provisions in MiFIR;
- Requiring SIs to publish firm quotes that are a minimum of twice the standard market size, and no longer allowing SIs to match at midpoint below twice the standard market size;
- Permanently removing the requirement for trading venues and SIs to publish best execution reports which MiFID Quick Fix had suspended;
- Looking to update transaction reporting requirements in order to achieve greater consistency between MiFID, SFTR, and EMIR which are to be defined in a future RTS.

EU Retail Investment Strategy Proposal

Key proposed changes to the MiFID framework include the following:

- Utilizing risk warnings for ‘particularly risky’ products in order to enhance the transparency of financial instruments which would be provided in electronic format;
- Further enhancing transparency with new annual statements provided by firms to clients, as well as standardized disclosure on costs, associated charges and third-party payments;
- Adopting of sound and effective internal policies on marketing communications, which are defined, approved and overseen by the firm’s management bodies;
- Developing a structured pricing process disclosing costs and charges to investors. ESMA and EIOPA are to develop benchmarks on cost and performance which firms would compare their products to before offering them to the market to ensure consumers are getting value-for-money investments;
- Extending the ban on payment of commissions (“inducements”) under MiFID II to insurance-based products;
- For firms that provide advice to clients, replacing the ‘quality enhancement’ test under MiFID II to recommend an appropriate range of financial products, including the most cost-efficient investment, and offering at least one alternative financial product so the client can compare the potential options;
- Strengthening supervisory enforcement by enhancing coordination and communication between competent authorities in order to regulate cross-border services;
- Updating the definition the definition of clients to be treated as “professional” to lower the minimum wealth threshold from EUR 500k to EUR 250k, and adding a new criterion around professional experience or education.

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