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ISLA INTERNATIONAL SECURITIES LENDING ASSOCIATION

SECURITIES LENDING – MIFID2 ANALYSIS

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ISLA

The International Securities Lending Association (ISLA) is a trade association established in 1989 to represent the common interests of participants in the securities lending industry. ISLA works closely with regulators across Europe and our activities embrace markets and prudential regulatory regimes as well as investor protection. In the United Kingdom the association has representation on the Securities Lending Committee, a committee of market practitioners chaired by the Bank of England.

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A. INTRODUCTION

1. Purpose of paper

[1]With the effective replacement of MiFID1[2] by MiFID2[3] from 3 January 2018, and the introduction by MiFID2 of certain changes affecting securities lending, this paper is intended to provide a summary of the main issues affecting securities lending and current thinking to date regarding such issues, as well as a summary of the requirements under the MiFID2 regime (including MiFIR[4]) which apply to securities lending. Reference is also made to the rules[5] of the Financial Conduct Authority (the "**FCA**") which implement MiFID2 and related requirements where applicable. (This paper does not consider the requirements of SFTR[6], except as relevant for interpretation of the requirements of MiFID2.) Analysis of the implications of the UK ceasing to be a member of the EU is beyond the scope of this paper.

Certain issues are unfortunately at this stage still unclear, and much will depend on the particular approach adopted over time by the relevant regulatory authority in each EEA jurisdiction when applying the MiFID2 requirements. Moreover, each firm will need to determine the extent to which it is subject to MiFID2 requirements in the light of its own particular operational systems and contractual arrangements. However, this paper should at least assist in clarifying some aspects, and drawing attention to areas where caution is required.

Section (A) of this purpose discusses certain general issues regarding the potential application of MiFID to securities lending transactions. Section (B) provides a short summary of Section (C) which considers certain more specific issues which, if applicable, may have an impact on firms, depending on the relevant business models or processes used, except for Section (C)(10) which is a reminder of the general requirements which apply to all firms under MiFID2. Schedule 1 lists the areas where there is a specific exclusion or restriction of the application of MiFID2 requirements to securities financing transactions. Schedule 2 is a summary table outlining the requirements of MiFID2, and related legislation.

2. Terminology

2.1 Securities lending v stock lending

The terms "securities lending" and "stock lending" are interchangeable, and there is no particular significance to the use of one term rather than another. The general term used in MiFID2 is "securities financing transaction" which includes securities lending transactions, although as explained in section 5 below also includes certain other arrangements.

1. Further discussions with ISLA members regarding the practical implications of the issues discussed in this paper may be appropriate.
2. Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments
3. Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments
4. Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments.
5. As set out in FCA Policy Statement PS 17/14, published 3 July 2017.
6. Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse

2.2 Other usage

It should be noted that, depending on context, slightly different definitions may be used in legislation and regulatory requirements. For example, in the current rules of the UK Financial Conduct Authority, "stock lending" is defined to mean "the disposal of a designated investment subject to an obligation or right to reacquire the same or a similar designated investment from the same counterparty", and "stock lending activity" is defined to mean "the activity of undertaking a stock lending transaction". In contrast, under the term "securities or commodities lending" it says "see securities or commodities lending or borrowing transaction", and "securities or commodities lending or borrowing transaction" is defined to mean "(in accordance with Article 4(34) of the Banking Consolidation Directive and Article 3(1)(n) of the Capital Adequacy Directive (Definitions) and for the purposes of BIPRU) any transaction in which an undertaking or its counterparty transfers securities or commodities against appropriate collateral subject to a commitment that the borrower will return equivalent securities or commodities at some future date or when requested to do so by the transferor, that transaction being securities or commodities lending for the undertaking transferring the securities or commodities and being securities or commodities borrowing for the undertaking to which they are transferred."

Thus, as may be seen, depending on context and definition, stock lending may refer to the transfer of securities constituting the loan, or may refer to both the transfer of the loaned securities and the transfer of collateral for such loan.

3. What is Securities Lending

3.1 Structure

Although termed a "loan", a securities loan or stock loan consists of the transfer of ownership of securities from the lender to the borrower, so that the securities become the property of the borrower, subject to the agreement that securities of the same type will be transferred back to the lender by the borrower in the future[7].

The market standard terms of a securities loan or stock loan require the borrower to transfer ownership of collateral[8] to the lender, so that the collateral (which may be cash or securities) becomes the property of the lender, subject to the agreement that collateral of the same type will be transferred back to the borrower by the lender when the securities loan terminates and securities of the same type as those originally transferred are transferred back to the lender.

In a default situation, the obligation of the borrower to deliver securities of the same type as the loaned securities, and the obligation of the lender to deliver assets of the same type as the collateral, are accelerated and converted into an obligation to pay the value of the relevant assets, and such obligations are then set off against each other.

7. This is different from, for example, a custody arrangement where the recipient of the securities becomes the legal owner but holds the securities on behalf of the custody client, or a security arrangement involving transfer of securities to the secured party where the secured party receives by way of security only and (in the absence of a right of use) cannot make use of the securities except on enforcement of the security interest.
8. For the purposes of this paper, the provision of collateral by granting a security interest rather than title transfer is not considered.

3.2 Economic purpose

Although a securities loan involves a transfer of ownership of securities, the purpose of the loan is not that the borrower of the securities should become the permanent owner of such securities, because the borrower is subject to a contractual obligation to return equivalent securities[9]. Moreover, to the extent feasible, the economic benefits of the loaned securities are to be received by the lender by payment to the lender by the borrower of an amount equal to dividends or other income arising in respect of the loaned securities, inclusion of income in the form of securities as part of the loan, and the right of the lender to direct that, at termination of the loan, it receives equivalent securities respecting which corporate action rights arising before such termination have been exercised in a particular manner[10]. As a result, for many purposes it is recognised that the transfers under a securities loan should not be regarded in the same way as transfers for an ordinary sale or purchase of securities, since it is a fundamental part of the arrangement that securities of the same type will be transferred back to the lender in future.

For example, for accounting purposes, the loaned securities normally continue to be recorded on the balance sheet of the lender, although legal title has been transferred to the borrower, and in general, in a default situation, taxes and duties such as capital gains tax and stamp duty do not apply in the same way.

For similar reasons, the regulatory regime has, at least in part, recognised that there is a different between a securities loan, and a sale or other transfer of securities where all economic benefits are transferred and there is no intention to return the securities to the lender.

4. Why is MiFID2 relevant to Securities Lending

4.1 Application of MiFID2 regime

MiFID2 requirements apply to a number of activities, including "Reception and transmission of orders in relation to one or more financial instruments[11]" (there is no specific definition of this service in MiFID2, although recital 44 states that "reception and transmission of orders should also include bringing together two or more investors, thereby bringing about a transaction between those investors"), "Execution of orders on behalf of clients" (which means "acting to conclude agreements to buy or sell one or more financial instruments on behalf of clients and includes the conclusion of agreements to sell financial instruments issued by an investment firm or a credit institution at the moment of their issuance"), and "dealing on own account" (which means "trading against proprietary capital resulting in the conclusion of transactions in

9. It is important that the borrower's obligation is to return equivalent securities, rather than the same securities as originally transferred, since otherwise this suggests that full title has not been transferred to the borrower, and risks recharacterisation of the securities loan as the creation of a security interest over the relevant securities.
10. In general, it is not feasible for a borrower to agree to procure the exercise of voting rights arising in respect of loaned securities at the direction of the lender, since the borrower may not be the owner of the securities at the time the rights arise.
11. A "financial instrument" means any of the instruments specified in Annex I, Section C of the relevant Directive, which are, broadly, types of securities or derivatives, which would not normally include securities lending transactions (it is not impossible that a securities lending transaction might be created on non-standard terms which would result in its being regarded as a derivative contract, but this would be unusual).

one or more financial instruments"). MiFIR also applies to investment firms providing investment services and/or performing investment activities in various respects (although Title II (Transparency for Trading Venues, Articles 3 to 13) and Title III (Transparency for Systematic Internalisers and Investment Firms Trading OTC, Articles 14 to 23) do not apply to securities financing transactions[12]).

4.2 Transactions/orders

There is no specific definition of "transaction" or "order" for the purposes of MiFID2. Nevertheless, the definition of "execution of orders on behalf of clients" includes reference to concluding "agreements to buy or sell one or more financial instruments", the definition of "dealing on own account" includes reference to "trading" and the "conclusion of transactions in one or more financial instruments", and the term "limit order" is defined to mean "an order to buy or sell a financial instrument at its specified price limit or better and for a specified size". Moreover, MiFID2 contains provisions which exempt securities financing transactions from certain requirements applicable to conclusion of transactions or execution of orders.

As a result, it seems clear that securities loans are subject to all MiFID2 requirements regarding transactions, except to the extent that any applicable exemption applies.

Although relevant exemptions refer to securities financing transactions, a securities financing transaction is not a "transaction" in the sense generally used in MiFID2 (nor is a securities financing transaction a financial instrument for MiFID2 purposes). However, a securities loan typically involves both a transfer of loaned securities from lender to borrower, and a transfer of collateral from borrower to lender, and the assets transferred may be financial instruments. It is therefore each such transfer which is a transaction potentially subject to MiFID2 requirements[13].

4.3 Who is subject to MiFID2

An entity will (absent any relevant exclusion) be subject to MiFID2 requirements, as implemented in the UK, if it is:

- an investment firm as defined in the [14]RAO (in summary, a person whose regular occupation or business is the provision or performance of investment services and activities on a professional basis, excluding persons who due to Article 2 are outside MiFID2, and excluding persons whose home member state is an EEA state other than the UK), and
- incorporated (or otherwise established) in the UK (or for certain purposes, in another EEA jurisdiction if operating through a branch in the UK).

For this purpose, "investment services" and "investment activities" refer to the activities listed in MiFID2, Annex I, Section A, therefore a firm which only carries out activities listed in MiFID2, Annex I, Section B is not within the scope of MiFID2. However, if an

12. MiFIR, Article 1(5a)
13. It is possible that there may be unusual circumstances where there is no transfer of collateral, but in such case the transfer of loaned securities would still be within the scope of MiFID2, or, where the loaned securities are not financial instruments but the collateral assets are, the loan transfer is not within the scope of MiFID2 but the collateral transfer is.
14. The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001, SI 2001/544

entity is an investment firm as a result of activities within MiFID2, Annex I, Section A, it will be within the scope of MiFID2 in relation to any of its services or activities which fall within MiFID2, Annex I, Section B, as well as any services or activities within MiFID2, Annex I, Section A.

An entity which is not an "investment firm" but which provides services in the UK within MiFID2, Annex I, Section A or B is likely to be subject to the requirements implementing MiFID2 in the UK which apply to "equivalent third country business"[15]. (An entity which does not provide services in the UK within MiFID2, Annex I, Section A or B may nevertheless be subject to regulatory requirements implementing MiFID2 in the UK to the extent that such requirements are also applied by UK regulatory requirements to persons or activities which are not within the scope of MiFID2.)

Thus, examples of entities likely to be subject to MiFID2 requirements as implemented in the UK in the context of securities lending are:

- an entity incorporated in the UK which in the UK executes securities lending transactions as an agent, or for its own account (since it is carrying out activities listed in MiFID2, Annex I, Section A).
- an entity incorporated in an EEA jurisdiction which through a branch in the UK executes securities lending transactions as an agent, or for its own account (on the basis that certain MiFID2 requirements as implemented in the UK apply to activities provided from a UK branch of an EU entity).
- an entity incorporated in the US (or other non-EEA jurisdiction) which through a branch in the UK executes securities lending transactions as an agent, or for its own account (on the basis that MiFID2 requirements as implemented in the UK apply to activities which would be subject to MiFID2 if carried out by a MiFID investment firm).

Analysis of the requirements applicable to EEA entities operating in the UK under a MiFID2 or CRD[16] passport, or services provided by EEA entities or third country entities into the UK on a cross-border basis without an establishment in the UK, is beyond the scope of this paper.

5. MiFID1 v MiFID2

In MiFID1 and MiFID2, the term generally used is "securities financing transaction" rather than "securities lending" or "stock lending"[17], although the term "securities financing transaction" includes securities lending. The approach under MiFID1 is somewhat different from the approach in MiFID2.

15. Currently this means the business of a non-EEA investment firm carried on from an establishment in the United Kingdom that would be MiFID business if that firm were a MiFID investment firm.
16. Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms
17. Although "stock lending" is mentioned in MiFID1 Recital (26), and MiFID2 Recital (51), where it is clearly understood to mean a transfer of title to the loaned securities: "In order to protect an investor's ownership and other similar rights in respect of securities and the investor's rights in respect of funds entrusted to a firm those rights should in particular be kept distinct from those of the firm. This principle should not, however, prevent a firm from doing business in its name but on behalf of the investor, where that is required by the very nature of the transaction and the investor is in agreement, for example stock lending" (MiFID2 Recital (51), which is substantially the same as MiFID1 Recital (26)).

5.1 MiFID1

Under the MiFID1 regime, a securities financing transaction was defined in the MiFID Implementing Regulation[18] as "an instance of stock lending or stock borrowing or the lending or borrowing of other financial instruments, a repurchase or reverse repurchase transaction, or a buy-sell back or sell-buy back transaction"[19].

For the purposes of such Regulation, it was specifically stated that "a reference to a transaction is a reference only to the purchase and sale of a financial instrument" and that other than in relation to Chapter II (record-keeping), "the purchase and sale of a financial instrument does not include... securities financing transactions". The effect of this was to disapply transaction reporting requirements in the Regulation in relation to securities lending.

5.2 MiFID2

Under the MiFID2 regime, securities financing transactions are defined[20] as "transactions as defined in Article 3 point (11) of Regulation (EU) 2015/2365[21] on transparency of securities financing transactions and of reuse."

This definition is wider than the old MiFID1 definition, since it defines a "securities financing transaction" as "(a) a repurchase transaction; (b) securities or commodities lending and securities or commodities borrowing; (c) a buy-sell back transaction or sell-buy back transaction; (d) a margin lending transaction;" and provides specific definitions for each of (a) to (d). In particular:

'securities or commodities lending' or 'securities or commodities borrowing' is defined to mean "a transaction by which a counterparty transfers securities or commodities subject to a commitment that the borrower will return equivalent securities or commodities on a future date or when requested to do so by the transferor, that transaction being considered as securities or commodities lending for the counterparty transferring the securities or commodities and being considered as securities or commodities borrowing for the counterparty to which they are transferred".[22]

'repurchase transaction' is defined to mean "a transaction governed by an agreement by which a counterparty transfers securities, commodities, or guaranteed rights relating to title to securities or commodities where that guarantee is issued by a recognised exchange which holds the rights to the securities or commodities and the agreement does not allow a counterparty to transfer or pledge a particular security or commodity to more than one counterparty at a time, subject to a commitment to repurchase them, or substituted securities or commodities of the

18. Commission Regulation (EC) No 1287/2006 of 10 August 2006 implementing Directive 2004/39/EC of the European Parliament and of the Council as regards recordkeeping obligations for investment firms, transaction reporting, market transparency, admission of financial instruments to trading, and defined terms for the purposes of that Directive, applicable in full from 1 November 2007
19. Commission Regulation (EC) No 1287/2006, Art 2(10)
20. In Commission Delegated Directive (EU) 2017/593 of 7 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits, Art 1(3).
21. SFTR
22. SFTR, Article 3(7)

same description at a specified price on a future date specified, or to be specified, by the transferor, being a repurchase agreement for the counterparty selling the securities or commodities and a reverse repurchase agreement for the counterparty buying them".[23]

'buy-sell back transaction' or 'sell-buy back transaction' is defined to mean "a transaction by which a counterparty buys or sells securities, commodities, or guaranteed rights relating to title to securities or commodities, agreeing, respectively, to sell or to buy back securities, commodities or such guaranteed rights of the same description at a specified price on a future date, that transaction being a buy-sell back transaction for the counterparty buying the securities, commodities or guaranteed rights, and a sell-buy back transaction for the counterparty selling them, such buy-sell back transaction or sell-buy back transaction not being governed by a repurchase agreement or by a reverse-repurchase agreement within the meaning of point (9)".[24]

Unlike MiFID1, the MiFID2 regime does not provide a blanket exemption from transaction reporting for securities financing transactions (including securities lending). As a result, all transaction reporting requirements under the MiFID2 regime are applicable to the transfer of securities involved in a securities financing transactions, except to the extent that the MiFID2 regime provides exemptions from certain requirements. In particular, see Schedule 1 to this note.

6. Type of Securities Lending Activity

Regulatory requirements applicable to securities lending activity may affect firms in slightly different ways, depending on the nature and operational structure of the securities lending activity. For the purposes of this note, the main types of activity considered are as follows.

6.1 Agency lending

The concept of agency lending is not defined in MiFID2 or related legislation, but is generally understood to mean an arrangement where a firm enters into a securities lending transaction as agent of the entity lending securities, thereby creating a securities lending transaction between the lender and the borrower, not between the agent and the borrower.

(a) Who are the parties to the securities loan?

The securities loan is between the lending agent's principal (the lender) and the borrower which is counterparty to the loan.

Where a firm provides an agency lending service, a firm agrees with its client that the firm will from time to time, as agent of the client, enter into securities loans with third party borrowers. The firm is not party to the securities loans as principal, therefore does not have the obligations of the lender under the relevant loans, although the borrower will normally require that it has certain rights against the agent as well as the lender.

23. SFTR, Article 3(9)
24. SFTR, Article 3(8)

(b) Who is the lending agent's client?
The lender is the client to whom the lending agent is providing agency lending services.

Although the borrower as counterparty to the loan has rights against the lender under the terms of the loan, and may have certain rights against the agent, the borrower is not a client of the firm as a result of the firm providing agency lending services to the lender. (If in separate documentation (or tripartite documentation) the firm has agreed to provide to the borrower services which fall within the scope of MiFID2 or the RAO, such as custody services, the borrower would be a client of the firm in respect of those services, but this would not result in the borrower being a client of the firm in respect of the agency lending services provided by the firm to the lender.)

Whether the borrower regards the principal lender as a client will depend on the analysis of whether the counterparty is a client (see 6.4 below). Depending on the arrangements, the lending agent may be the borrower's client for regulatory purposes rather than the lender, pursuant to COBS 2.4.3R[25].

(c) Is the service execution-only?
This is unlikely, although the arrangements could in principle be structured in this way.

An agency lending arrangement could be structured on the basis that the specific details of the loan (including securities to be loaned, borrower, and amount and type of collateral to be provided) are instructed by the lender for each loan, and the firm simply acts on those instructions.

However, typically a firm will agree with its client the categories of: securities owned by the client which are available for lending: borrower to whom the client is willing to lend; and type and amount of collateral which the client wishes to receive. It is then the firm which makes the final decision as to the securities to be loaned, the borrower who is party to such loan, and the type and amount of collateral which is received, in which case the service is not execution-only.

(d) Is custody part of the agent lending service?
Custody services may be provided in addition to the agency lending services.

The firm providing agency lending services would commonly also hold as custodian for the lender the securities of the lender which are available for lending, and receive as custodian for the lender collateral assets transferred by the borrower to the lender.

The provision of custody services by the agent is not essential, as the agent firm may, rather than holding assets for the lender, rely on a mandate from the client in respect of the relevant securities accounts and/or cash accounts so that the agent is able to direct the lender's custodian to transfer or receive securities or collateral as required.

25. Under COBS 2.4.3R, where a firm is aware that a person to whom it provides services is acting as agent for a principal, the agent and not the principal is the firm's client, provided that the firm has not agreed in writing to treat the principal as its client, and the agent is itself either a firm or an overseas financial services institution, and the main purpose of the arrangements is not to avoid duties which the firm would otherwise owe to the principal.

6.2 Matched principal

In MiFID2, Article 4(1)(38), "matched principal trading" is defined to mean "a transaction where the facilitator interposes itself between the buyer and the seller to the transaction in such a way that it is never exposed to market risk throughout the execution of the transaction, with both sides executed simultaneously, and where the transaction is concluded at a price where the facilitator makes no profit or loss, other than a previously disclosed commission, fee or charge for the transaction".

In the context of securities lending transactions, where a firm enters into a securities loan as borrower and a securities loan on the same terms as lender, this will constitute matched principal trading if both securities loans transactions are executed simultaneously, and the firm makes no profit or loss, other than a previously disclosed commission, fee or charge.

(a) Who are the parties to the securities loan?

The firm will be party as borrower to a securities loan by a lending counterparty, and the firm will be party as lender to a securities loan to a borrowing counterparty.

Instead of an agency lending service, a firm may facilitate securities lending by a client by borrowing securities from the client and entering into a loan to a third party borrower on matching terms. In such case, the firm will have obligations as principal under each loan.

(b) Who is the firm's client?

Depending on how the firm documents the arrangements, the persons from whom the firm borrows securities, or the persons to whom the firm lends securities, or both, may be clients of the firm, or may only be counterparties with whom the firm enters into transactions from time to time.

(c) Is the service execution-only?

This is unlikely, although the arrangements could in principle be structured in this way.

The arrangements could be structured on the basis that the client instructs the firm of the details of each loan. Alternatively, the firm and the client may agree various parameters for loans based on which the firm makes the final decision regarding entry into each loan, in which case the service is not execution-only.

(d) Is custody part of this service?

Custody services may be provided in addition to this service.

The firm may provide custody services to the client, or may have a mandate from the client authorising the firm to instruct transfers of securities or cash to be made to or from the client's custody accounts with a third party custodian.

6.3 Borrowing/lending for own account

For the purposes of this paper, the activity of borrowing/lending for own account is considered to be where a firm borrows or lends securities solely for its own purposes, and is not borrowing or lending where the counterparty is regarded as a client (see

further discussion in 6.4 respecting the possibility of a counterparty being regarded as a client of the firm).

(a) Who are the parties to the securities loan?
The firm enters into securities loans with third parties (which may for the purposes of other services be clients of the firm) as borrower or as lender for its own account.

(b) Who is the firm's client?
On the basis that the firm enters into the securities loan solely for its own account, and not as part of a service provided to clients, the counterparties to the securities loan transactions are not clients of the firm since the firm is not providing a service to such persons. For this purpose, it is assumed that such own account transactions are not provided in the context of a client relationship, i.e. there is no indication that the counterparty "legitimately relies on the firm to protect his or her interests in relation to the pricing and other elements of the transaction – such as speed or likelihood of execution and settlement – that may be affected by the choices made by the firm when executing the order"[26]. A firm engaging in own account borrowing or lending of securities must consider carefully whether, in the particular circumstances of its arrangements, its activities may be regarded as the provision of services to clients, as further discussed in 6.4 below.

(c) Is the service execution-only?
For the reasons set out in (b), this is not a service provided to clients and the firm is not executing client orders, therefore this question is not relevant.

(d) Is custody part of this service?
The counterparties to the securities loan transactions may be custody clients of the firm, but the custody services will be separate from the firm's securities lending activities.

6.4 Particular considerations for borrowing/lending for (dealing on) own account

(a) Dealing on own account constituting client service
It is important to note that it is not impossible for own account dealing to be regarded as the provision of services regulated by MiFID2 to a client. An example in a securities lending context may be where a hedge fund client of a prime broker requests the broker to lend securities to the client from time to time to cover short positions of the client. Loans by the broker to the client may be loans from the broker's own proprietary assets, and may or may not be matched by the broker borrowing similar assets from a counterparty in the market, but in either case it would be difficult to argue that the hedge fund is not a client of the broker for the purposes of the securities loan from the broker to the hedge fund.

Where lending or borrowing by a firm on own account does constitute a client service, the firm will (in the absence of other limitations of the general requirements, for example where the client is an eligible counterparty) need to consider the extent to which it is subject to general requirements applicable to the provision of investment

26. Commission Opinion on the scope of best execution under MiFID and the implementing directive: Working Document ESC-07-2007, p.4, section 8.

services under MiFID2 to a client, including best execution obligations (see Part (C), section 1, below) publication obligations under RTS 28 (see Part (C), section 2, below), requirements applicable to a Systematic Internaliser (see Part (C), section 4 below), and requirements applicable to portfolio management (see Part (C), section 8 below), and also general requirements such as the requirements relating to conflicts of interest, and inducements (see Part (C), section 10, sub-sections 10.8 and 10.14 below).

(b) FCA TR 14/13

As referenced by the FCA in Thematic Review TR 14/13 entitled "Best execution and payment for order flow" ("**TR 14/13**"), guidance on this issue is set out in the Commission Opinion on the scope of best execution under MiFID and the implementing directive: Working Document ESC-07-2007 (the "**Commission Opinion**"). The analysis considers circumstances in which best execution requirements apply, but is of wider application, since the existence of a client relationship resulting in the firm having an obligation to comply with best execution requirements will necessarily mean there is a client relationship to which other relevant requirements apply.

(c) Commission Opinion 2007

In the Commission Opinion, the Commission states the following:

"in some cases, proprietary trades will attract the best execution obligation. The application or otherwise of best execution will depend on whether the execution of the client's order can be seen as truly done on behalf of the client. This is a question of fact in each case which ultimately depends on whether the client legitimately relies on the firm to protect his or her interests in relation to the pricing and other elements of the transaction – such as speed or likelihood of execution and settlement – that may be affected by the choices made by the firm when executing the order. The following considerations, taken together, will help to determine the answer to this question:

- whether the firm approaches (initiates the transactions with) the client or the client instigates the transaction by making an approach to the firm. In those cases where the firm approaches a retail client and suggests him to enter into a specific transaction it is more probable that the client will be relying on the firm, to protect his or her interests in relation to the pricing and other elements of the transaction.
- questions of market practice will help to determine whether it is legitimate for clients to rely on the firm. For example, in the wholesale OTC derivatives and bond markets buyers conventionally 'shop around' by approaching several dealers for a quote, and in these circumstances there is no expectation between the parties that the dealer chosen by the client will owe best execution.
- the relative levels of transparency within a market will also be relevant. For markets where clients do not have ready access to prices while investment firms do, the conclusion will be much more readily reached that they rely on the firm in relation to the pricing of the transaction.
- the information provided by the firm about its services and the terms of any agreement between the client and the investment firm will also be relevant, but not determinative of the question. The use of standard term agreements to characterise commercial relationships otherwise than in accordance with economic reality should be avoided....

These factors are likely to support the presumption that, in ordinary circumstances, a retail client legitimately relies on the firm to protect his or her interests in relation to the pricing and other parameters of the transaction. Similarly, prima facie application of these factors is likely to lead to the presumption that in the wholesale markets clients do not rely on the firm in the same way."[27]

(d) FCA views

In TR 14/13, the FCA stresses that the factors identified by the Commission "should be taken together"[28]. In addition, in TR 14/13, the FCA expresses the following views[29]:

(i) "The key concept in quote-driven markets is whether the firm is acting 'on behalf of the client' when executing its order. This focuses on the economic reality of the relationship between the firm and the client and, specifically, whether the client 'legitimately relies' on the firm to protect their interests in relation to pricing and other important elements of the transaction."

(ii) "'Legitimate reliance' is driven by reference to the categorisation of the client and to other characteristics of the transaction."

(iii) "The starting point for firms is that: retail clients do legitimately rely on the firm to protect their interests in relation to the pricing and other parameters of a transaction (with the intention that best execution is always provided to retail clients)"

(iv) "for professional clients this starting point is reversed. The assumption is that they do not rely on firms to achieve best execution."

(v) "in order to reach this conclusion, we expect firms to apply a four-fold cumulative test, published by the European Commission, (further details of which are set out in Chapter 4) which addresses: which party initiates the transaction; questions of market practice and the existence of a convention to 'shop around'; the relative levels of price transparency within a market; and the information provided by the firm and any agreement reached."

(vi) "where firms act as the counterparty to client orders, they may still be 'acting on behalf of their clients'."

(vii) "best execution would not be owed by a market maker which displayed quotes that were then accepted by a client, provided that the client was not legitimately relying on the firm to protect his or her interests in relation to the pricing and other elements of the transaction" BUT "(bearing in mind the starting point that retail clients would be legitimately relying on the firm)".

(viii) "In other situations, executing a client order against a firm's proprietary position (including a systematic internaliser), where the firm is making decisions on how the order is executed (i.e. is working the order on the client's behalf) or executing a client order by dealing as a riskless principal on behalf of the client, including cases where the client is charged a spread on the transaction, will always be cases where best execution applies."

27. Commission Opinion, p.4, section 8.
28. TR 14/13, p.44, first paragraph.
29. See TR 14/13 pp. 15, 16 and 44.

(ix) A firm cannot argue that it has no client relationship with a counterparty solely on the basis that the counterparty deals on quotes and therefore initiates the transaction; all of the Commission's factors (as set out in (c) above) must be considered by the firm.

(x) It is not sufficient to refer to the existence of a market practice or a convention to 'shop around' for different quotes; a firm must also consider whether there are circumstances that may prevent counterparties from seeking or obtaining different quotes (the FCA gives the example of "CfD providers who were entering into 'captive trades' with clients which prevented them from shopping around in order to close their open positions"

(xi) Firms must consider how price transparency affects legitimate reliance by a counterparty on the firm (the FCA specifically refers to "OTC instruments and markets where it was common practice to source additional liquidity and tighter pricing away from the electronic order book")

(xii) The FCA evidently approves of an approach where a firm assumes that a retail client is legitimately relying on the firm to deliver best execution on the basis that this is "fully in line with the Commission's conclusion that 'in ordinary circumstances a retail client legitimately relies on the firm to protect his or her interests in relation to the pricing and other parameters of the transaction.' "

(xiii) The FCA also notes that "In addition to this four-fold cumulative test, the Commission Opinion also provides a number of non-exhaustive considerations that help to determine whether or not a client is legitimately relying on a firm to protect their interests in relation to the transaction and this, whether or not a firm is acting on behalf of the client. All firms should consider these tests and the examples provided by the Commission when reviewing their own activities."

(e) In general

In general, a firm entering into transaction will need to consider whether the counterparty should be treated as client, based on the Commission's factors and the FCA's views as indicated above, or whether for other reasons the firm considers that the counterparty should be treated as a client, and then, based on the nature of the client and the relationship, the extent of the regulatory obligations to such client (for example, whether best execution obligations apply). In principle, other than where a counterparty is a type of entity which could constitute a retail client, it would seem arguable that, where there is no existing client relationship between the firm and the counterparty, it will be easier to reach a conclusion that the counterparty is not a client of the firm. Nevertheless, it is important for a firm to carry out appropriate analysis of all factors as contemplated by the FCA, and to retain evidence that it has done so.

B. EXECUTIVE SUMMARY

Part (C) of this paper considers various issues which commonly arise for consideration in the context of securities lending arrangements. In summary, these are as follows.

(1) Best execution
Best execution requirements are applicable to securities lending transactions entered into by a firm for or with clients, but will not apply where a firm is lending or borrowing securities on its own account provided that in doing so the firm is not regarded as executing client orders (see Part (A), para 6.4 above).

(2) Execution venues
Best execution reporting requirements in RTS 27 do not apply to securities financing transactions, but RTS 28 contains specific publication obligations relating to securities financing transactions constituting execution of client orders.

(3) MTF/OTF requirements
Requirements applicable to the operation of an MTF or OTF may apply to securities lending arrangements consisting of agency lending or matched principal arrangements, but are unlikely to be relevant where a firm is only lending or borrowing securities on its own account and provided that in doing so the firm is not regarded as executing client orders (see Part (A), para 6.4 above).

(4) Systematic internalisers
Requirements applicable to a systematic internaliser may apply to matched principal lending arrangements, but will not be relevant to agency lending or to a firm which is only lending or borrowing securities on its own account, provided that in doing so the firm is not regarded as executing client orders (see Part (A), para 6.4 above).

(5) Data retention
Data retention requirements will apply to securities loans executed by a firm in the context of agency lending arrangements, matched principal arrangements or where only lending or borrowing securities on its own account.

(6) Transaction reporting
Transaction reporting requirements only apply to securities lending transactions in limited circumstances.

(7) TTCA disclosures
The prohibition on receipt by a firm of title transfer collateral from a retail client will not affect agency lending services, but will apply to any matched principal transaction with a retail client, or transaction entered into by the firm for its own account with a retail client, where the retail client is required to provide collateral to the firm on a title transfer basis.

The requirement for a firm to provide risk warnings to a non-retail client when receiving title transfer collateral from such client will not apply in the context of agency lending, but will apply to any matched principal transaction with a client, or transaction entered

into by the firm for its own account with a client, where the client is required to provide collateral to the firm on a title transfer basis.

(8) Portfolio management

Securities lending services provided by a firm to a client may constitute portfolio management services, depending on the nature of the services provided by the firm to the client.

(9) Custody requirements

Various requirements apply to a custodian which enters into securities lending transactions with or for a client. Requirements to consider and document the appropriateness of the use of title transfer collateral arrangements only apply where the firm receives title transfer collateral from the client.

(10) General requirements

Various general requirements apply to a firm when providing securities lending services to clients, or lending or borrowing securities on its own account, namely (where providing services to a client) requirements relating to client reporting, client classification, conflicts, remuneration policies, client agreements, costs and charges, services disclosures, inducements, unbundling and client order handling rules, as well as certain other general requirements for firms subject to MiFID2, namely requirements relating to systems and resources, outsourcing, record keeping, telephone recording and electronic communications, and algo trading, and investment research/ marketing.

C. ISSUES ARISING FROM APPLICATION OF MIFID2/MIFIR

1. Best Execution

1.1 General

MiFID2, Article 24(1) requires all firms, when providing investment services or ancillary services to clients, to "act honestly, fairly and professionally in accordance with the best interests of its clients".

MiFID2, Article 27(1) imposes a requirement for all firms to "take all sufficient steps to obtain, when executing orders, the best possible result for clients taking into account price, costs, speed, likelihood of execution and settlement, size, nature or any other consideration relevant to the execution of the order", although "where there is a specific instruction from the client the investment firm shall execute the order following the specific instruction."

MiFID2 Level 2 Regulation, Article 64, specifies criteria for determining the relative importance of the relevant factors when executing client orders, and specifically states that a firm complies with Article 27(1) where it acts on specific instructions from the client relating to the order or any specific aspect of the order.

MiFID2 Level 2 Regulation, Article 65(1) requires a firm providing portfolio management to comply with MiFID2 Article 24(1) "when placing orders with other entities for execution that result from decisions by the investment firm to deal in financial instruments on behalf of its client".

MiFID2 Level 2 Regulation, Article 65 requires all firms, when providing the service of receipt and transmission of orders, to comply with the obligations under MiFID2 Article 24(1) to act in accordance with the best interests of their clients when transmitting client orders to other entities for execution.

1.2 Application to securities lending

There is nothing to indicate that the above requirements would not apply to securities lending transactions. In the European Commission's Q&A responses to MiFID1 questions, the Commission stated that MiFID1 Article 21 (which imposed obligations similar to MiFID2 Article 27) did "not exclude any types of orders or financial instruments from the scope of its application" and "Securities financing transactions (SFTs) should therefore fall under the obligation of best execution whenever a client of an investment firm issues an order and expects the investment firm to act on her behalf."

In addition, in the MiFID2 Level 2 Regulation: (i) Recital (99) contemplates the application of the best execution requirements to securities financing transactions, since it states "In order to comply with the legal obligation of best execution, investment firms, when applying the criteria for best execution for professional clients, will typically not use the same execution venues for securities financing transactions (SFTs) and other transactions."; (ii) Article 64(1)(b) specifically requires firms, for the purposes of MiFID2 Article 27(1), to take into account "the characteristics of the client

order, including where the order involves a securities financing transaction (SFT)";
(iii) Article 66(3)(b) requires a firm's execution policy to include "a list of the execution venues on which the firm places significant reliance in meeting its obligation to take all reasonable steps to obtain on a consistent basis the best possible result for the execution of client orders and specifying which execution venues are used for each class of financial instruments, for retail client orders, professional client orders and SFTs".

Also, in the ESMA Q&A on MiFID II and MiFIR investor protection and intermediaries topics (Last update: 10 July 2017), in the response to Question 15 (Do the RTS 27 reporting requirements apply to Securities Financing Transactions (SFTs)?), ESMA notes "ESMA wishes to make clear that, irrespective of the above clarification concerning the application of RTS 27 to SFTs, the MiFID II best execution requirements otherwise apply to investment firms when carrying out SFTs."

On this basis, it seems clear that securities financing transactions, including securities lending, executed on behalf of clients will be subject to best execution requirements, except to the extent of any specific instructions regarding the nature of the transactions.

1.3 Type of securities lending activity

(a) Agency lending

On the basis of the above, a firm entering into securities lending transactions as agent of a client will be executing orders, and will subject to the best execution requirements to the extent that the firm is not acting on specific instructions. For example, where criteria have been agreed between the firm and the client regarding securities available for lending, borrowers to whom the client's assets may be loaned, and acceptable types and amounts of collateral, the firm will not have best execution obligations in relation to the agreed criteria, but will have best execution obligations regarding the determination of the remaining variables, such as which and how many of, and when, the available securities are loaned, to which borrower, and the particular type of collateral within the agreed criteria which is accepted on behalf of the client.

To the extent that the provision by a firm of an agency lending service to a client is regarded as provision of portfolio management services to the client (see discussion in section 7 below), for the purposes of MiFID2 the firm will be regarded as providing portfolio management but not execution of orders or receipt and transmission of orders, and therefore will only be subject to the obligation to act honestly, fairly and professionally in accordance with the best interests of its clients if it places orders with other firms for execution[30].

30. This position may vary, depending on local law implementation. For example, in the UK a firm carrying out portfolio management must, if it also executes transactions or transmits orders for execution, comply with the relevant requirements applicable to such activities.

(b) Matched principal

A firm executing client orders by borrowing securities from a client and lending the securities received under the loan to a different client on a matched principal basis will be regarded as both executing orders on behalf of clients, and dealing on own account, and will be subject to the best execution requirements to the extent that the firm is not acting on specific instructions. For example, if criteria have been agreed between the firm and the client regarding securities available for lending, borrowers to whom the client's assets may be loaned, and acceptable types and amounts of collateral, the firm will not have best execution obligations in relation to the agreed criteria, but will have best execution obligations regarding the determination of the remaining variables, such as which and how many of, and when, the available securities are loaned, to which borrower, and the particular type of collateral within the agreed criteria which is accepted on behalf of the client.

(c) Borrowing/lending for own account

Where a firm borrows or lends securities for its own account, it is dealing on its own account (trading against proprietary capital resulting in the conclusion of transactions in one or more financial instruments) and therefore should not be regarded as executing client orders to which best execution requirements apply (provided that on the particular facts the counterparty does not satisfy the criteria to be regarded as a client for this purpose – see Part (A), para 6.4 above).

2. Execution venues

2.1 Relevant requirements

RTS 27[31] concerns the specific content, the format and the periodicity of the data to be published by execution venues relating to the quality of execution of transactions, and contains no specific exemption for securities financing transactions, but ESMA has stated that it considers that the best execution reporting requirements set out in RTS 27 should not apply to securities financing transactions[32].

The term "execution venue" is not defined, but Article 1 of RTS 27 states that it applies to "trading venues [this term is defined in MiFID2 to mean a regulated market, MTF or OTF], systematic internalisers, market makers, or other liquidity providers". This is similar to the definition in the MiFID2 Level 2 Regulation, Article 64(1), which states "For the purposes of this Article and Articles 65 and 66, 'execution venue' includes a regulated market, an MTF, an OTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing."

RTS 28[33] contains rules on the content and the format of information to be published by investment firms on an annual basis in relation to client orders executed on trading venues, systematic internalisers, market makers or other liquidity providers or entities that perform a similar function to those performed by any of the foregoing in a third country. The main publication obligation under Article 3(1) specifically excludes "orders in Securities Financing Transactions (SFTs)", but, in relation to securities financing transactions, Article 3(2) imposes a separate obligation regarding publication of the top five execution venues in terms of trading volumes for all executed client orders in SFTs, and Article 3(3) (requiring publication for each class of financial instruments, a summary of the analysis and conclusions they draw from their detailed monitoring of the quality of execution obtained on the execution venues where they executed all client orders in the previous year) will also apply.

31. Commission Delegated Regulation (EU) 2017/575 of 8 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards concerning the data to be published by execution venues on the quality of execution of transactions

32. ESMA Q&A on MiFID II and MiFIR investor protection and intermediaries topics: "**Question 15** [Last update: 10 July 2017] *Do the RTS 27 reporting requirements apply to Securities Financing Transactions (SFTs)?* **Answer 15** – Article 1(5)(a) of MiFIR, subsequent to amending Regulation (EU) 2016/1033 of 23 June 2016, states that SFTs are not subject to the pre and post trade transparency obligations set out in Title II and III of MiFIR. While no specific exemption was included with respect to the RTS 27 best execution reporting obligations, Recital 10 of RTS 27 refers to the need for regulatory consistency between its requirements and those on post trade transparency. In this context, ESMA considers that the best execution reporting requirements set out in RTS 27 should not apply to SFTs.

    ESMA wishes to make clear that, irrespective of the above clarification concerning the application of RTS 27 to SFTs, the MiFID II best execution requirements otherwise apply to investment firms when carrying out SFTs.

    ESMA also wishes to clarify that while RTS 27 would not apply to SFTs, this would not lead to a complete absence of execution quality reports for SFTs, as RTS 28 explicitly requires investment firms to report, inter alia, on order routing behaviours specifically with respect to SFTs and to provide a summary on the quality of execution obtained. Investment firms should also note that RTS 28 already makes specific reference to how data concerning SFTs should be published."

33. Commission Delegated Regulation (EU) 2017/576 of 8 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the annual publication by investment firms of information on the identity of execution venues and on the quality of execution

2.2 Type of securities lending activity

(a) Agency lending

A firm providing agency lending services will not be subject to RTS 27, but may be subject to RTS 28 if the loan transactions are executed on trading venues, systematic internalisers, market makers or other liquidity providers or entities that perform a similar function to those performed by any of the foregoing in a third country (a non-EEA jurisdiction).

(b) Matched principal

A firm executing client orders by borrowing securities from a client and lending the securities received under the loan to a different client on a matched principal basis will be regarded as executing orders on behalf of clients, as well as dealing on own account, but will not be subject to RTS 27, although may be subject to RTS 28 if the loan transactions are executed on trading venues, systematic internalisers, market makers or other liquidity providers or entities that perform a similar function to those performed by any of the foregoing in a third country.

Note also the amendment proposed to the Level 2 Regulation (see section 4 below) which would state that "An investment firm shall not be considered to be dealing on own account for the purposes of Article 4(1)(20) of Directive 2014/65/EU (definition of 'systematic internaliser') where that investment firm participates in matching arrangements with the objective or consequence of carrying out de facto riskless back-to-back transactions in a financial instrument outside a trading venue". If this amendment is made, it seems less likely that a firm providing lending services by executing loans for clients on a matched principal basis would be subject to RTS 28 (unless the loan transactions are executed on trading venues, market makers or other liquidity providers or similar third-country entities).

(c) Borrowing/lending for own account

Where a firm borrows or lends securities for its own account, it is dealing on its own account (trading against proprietary capital resulting in the conclusion of transactions in one or more financial instruments), and would not be subject to RTS 27, and should not be regarded as executing client orders within the scope of RTS 28 (provided that on the particular facts the counterparty does not satisfy the criteria to be regarded as a client for this purpose – see Part (A), para 6.4 above).

3. MTF/OTF analysis and organisational/trading process/ specific requirements

3.1 Specific additional requirements apply where a firm operates an MTF or OTF under MiFID2:

"**MTF**" means "a multilateral system, operated by an investment firm or a market operator, which brings together multiple third-party buying and selling interests in financial instruments – in the system and in accordance with non-discretionary rules – in a way that results in a contract in accordance with Title II of this Directive".

"**OTF**" means "a multilateral system which is not a regulated market or an MTF and in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in the system in a way that results in a contract in accordance with Title II of this Directive".

MiFID2 Article 18 (requirements include that investment firms and market operators operating an MTF or an OTF must establish transparent rules and procedures for fair and orderly trading and establish objective criteria for the efficient execution of orders, and have arrangements for the sound management of the technical operations of the facility, including the establishment of effective contingency arrangements to cope with risks of systems disruption).

MiFID2 Article 19 (requirements include that investment firms and market operators operating an MTF must establish and implement non-discretionary rules for the execution of orders in the system, and a prohibition on operators of an MTF from executing client orders against proprietary capital or engaging in matched principal trading).

MiFID2 Article 20 (requirements include that an investment firm and a market operator operating an OTF must establish arrangements preventing the execution of client orders in an OTF against the proprietary capital of the operator OTF or from any entity that is part of the same group or legal person as the operator; the operator may engage in matched principal trading if the client consents (subject to exceptions for certain derivatives); the operator must not engage in dealing on own account other than matched principal trading except with regard to sovereign debt instruments for which there is not a liquid market; execution of orders on an OTF must be carried out on a discretionary basis (discretion to be exercised only when deciding to place or retract an order on the OTF it operates, and/or when deciding not to match a specific client order with other orders available in the systems at a given time, provided it is in compliance with specific instructions received from a client and with its obligations in accordance with Article 27)).

MiFID2 Article 31 (requirements include that investment firms and market operators operating an MTF or OTF establish and maintain effective arrangements and procedures, relevant to the MTF or OTF, for the regular monitoring of the compliance by its members or participants or users with its rules, and monitor the orders sent, including cancellations and the transactions undertaken by their members or participants or users under their systems, in order to identify infringements of those rules, disorderly trading conditions, conduct that may indicate behaviour that is prohibited under Regulation (EU) No 596/2014[34] or system disruptions in relation to a financial instrument and shall deploy the resource necessary to ensure that such monitoring is effective).

MiFID2 Article 32 (requirements regarding the powers of an investment firm or a market operator operating an MTF or an OTF to suspend or remove from trading a financial instrument which no longer complies with the rules of the MTF or an OTF unless such suspension or removal would be likely to cause significant damage to the investors' interests or the orderly functioning of the market).

MiFID2 Article 38 (requirements regarding appropriate arrangements with a CCP or clearing house and a settlement system of another Member State with a view to providing for the clearing and/or settlement of some or all trades concluded by the members or participants under their systems).

Additional requirements under the Level 2 Regulation determine when suspension or removal from trading would be deemed likely to cause significant damage to the investors' interests or the orderly functioning of the market (Article 80), where significant infringement of rules, disorderly trading conditions or system disruptions in relation to financial instruments may be assumed (Article 81), and circumstances where conduct indicating behaviour prohibited under Regulation (EU) No 596/2014 may be assumed (Article 82).

3.2 Type of securities lending activity

(a) Agency lending

A firm's agency lending arrangement may, depending on how it is structured, be regarded as a system constituting an MTF if it brings together multiple third parties in a way that results in a securities lending transaction (or other contract), or an OTF if it is a system in which multiple third parties are able to interact in a way that results in a securities lending transaction (or other contract).

The analysis will depend on the detailed nature of the legal and operational structures comprising the agency lending arrangements. For example, in arrangements where the borrowers and lenders interact only with the firm under separate bilateral agreements rather than with each other, it is difficult to regard the firm as operating a multilateral system in which the parties interact with each other or which brings such parties together.

34. Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation)

(b) Matched principal

Depending on how a firm's matched principal system is structured, such system may potentially constitute an MTF if it brings together multiple third parties in a way that results in a securities lending transaction (or other contract), but the firm should ensure that this is not the case since an operator of an MTF is not permitted to engage in matched principal trading.

If a firm's matched principal system is a system in which multiple third parties are able to interact in a way that results in a securities lending transaction (or other contract), this will constitute an OTF, therefore client consent will be required to the matched principal trading.

(c) Borrowing/lending for own account

If a firm creates a system to enable it to borrow or lend on its own account, it is unclear how such system could constitute an MTF or an OTF, since to be an MTF it is necessary that the system brings together multiple third parties in a way that results in a contract, and to be an OTF it is necessary that multiple third parties interact in the system in a way that results in a contract. Moreover, an operator of an MTF is not permitted to execute client orders against proprietary capital.

4. Systematic internaliser

4.1 Meaning

MiFID2 Article 4(1)(20) defines a 'systematic internaliser' as "an investment firm which, on an organised, frequent systematic and substantial basis, deals on own account when executing client orders outside a regulated market, an MTF or an OTF without operating a multilateral system".

MiFID2 further states "The frequent and systematic basis shall be measured by the number of OTC trades in the financial instrument carried out by the investment firm on own account when executing client orders. The substantial basis shall be measured either by the size of the OTC trading carried out by the investment firm in relation to the total trading of the investment firm in a specific financial instrument or by the size of the OTC trading carried out by the investment firm in relation to the total trading in the Union in a specific financial instrument. The definition of a systematic internaliser shall apply only where the pre-set limits for a frequent and systematic basis and for a substantial basis are both crossed or where an investment firm chooses to opt-in under the systematic internaliser regime".

MiFID2 Level 2 Regulation Articles 12 to 16 provide further details regarding the circumstances in which a firm would be regarded as a systematic internaliser in respect of shares, bonds and certain other types of instrument.

MiFID2 Level 2 Regulation Recital (19) clarifies that "a systematic internaliser should not be allowed to bring together third party buying and selling interests in functionally the same way as a trading venue", and "A systematic internaliser should not consist of an internal matching system which executes client orders on a multilateral basis, an activity which requires authorisation as a multilateral trading facility (MTF). An internal matching system in this context is a system for matching client orders which results in the investment firm undertaking matched principal transactions on a regular and not occasional basis."

MiFIR Article 23(2) states "An investment firm that operates an internal matching system which executes client orders in shares, depositary receipts, ETFs, certificates and other similar financial instruments on a multilateral basis must ensure it is authorised as an MTF under Directive 2014/65/EU and comply with all relevant provisions pertaining to such authorisations."

It should be noted that an amendment has been proposed to by the European Commission to the Level 2 Regulation which will affect the definition of "systematic internaliser". The amendment would state that "An investment firm shall not be considered to be dealing on own account for the purposes of Article 4(1)(20) of Directive 2014/65/EU [the definition of systematic internaliser] where that investment firm participates in matching arrangements with the objective or consequence of carrying out de facto riskless back-to-back transactions in a financial instrument outside a trading venue".

4.2 Type of securities lending activity

(a) Agency lending

The activity of acting as systematic internaliser will not be relevant to an agency lending service, since an agent lender is not dealing on own account.

(b) Matched principal

Depending on the internal systems in place for creation of securities loans, a firm entering into loans for client on a matched principal basis might be a systematic internaliser.

The proposed amendment published by the European Commission 19/6/2017 states "An investment firm shall not be considered to be dealing on own account for the purposes of Article 4(1)(20) of Directive 2014/65/EU where that investment firm participates in matching arrangements with the objective or consequence of carrying out de facto riskless back-to-back transactions in a financial instrument outside a trading venue"[35].

Since the particular nature of the systems, operational processes and policies, and contractual terms, of each firm will vary, a firm will need to determine whether its activities would be regarded as acting as a systematic internaliser based on the specific details of its own arrangements.

(c) Borrowing/lending for own account

A firm borrowing or lending securities for its own account but not executing client orders is not within the definition of systematic internaliser (own account transactions will not constitute client orders provided that on the particular facts the counterparty does not satisfy the criteria to be regarded as a client for this purpose – see Part (A), para 6.4 above).

35. But this may mean that analysis is required as to whether the firm is instead operating an MTF or an OTF.)

5. Data Retention

5.1 General

MiFIR Article 25(1) requires firms to keep at the disposal of the relevant regulatory authority, for five years, the relevant data relating to all orders and all transactions in financial instruments which they have carried out, whether on own account or on behalf of a client. In the case of transactions carried out on behalf of clients, the records shall contain all the information and details of the identity of the client, and the information required under Directive 2005/60/EC of the European Parliament and of the Council[36].

There is no explanation of the meaning of "relevant data" in MiFIR (or in any related legislation or RTS[37]) but MiFID2 Level 2 Regulation Article 75 (made pursuant to MiFID2 Article 16(6)) requires that firms shall, immediately after receiving a client order or making a decision to deal to the extent they are applicable to the order or decision to deal in question, record and keep at the disposal of the competent authority at least the details set out in Section 2 of Annex IV. Also, MiFID2 Article 16(6) states that where the details set out in Section 2 of Annex IV are also prescribed under MiFIR Articles 25 and 26, they shall be maintained in a consistent way and according to the same standards prescribed under Articles 25 and 26 of MiFIR.

It seems reasonable to conclude that "relevant data" must refer to data required to be maintained under MiFIR or MiFID2, and therefore will include at least the details set out in MiFID2 Level 2 Regulation, Annex IV, Section 2:

Record keeping of transactions and order processing

1. name and designation of the client;
2. name and designation of any relevant person acting on behalf of the client;
3. a designation to identify the trader (Trader ID) responsible within the investment firm for the investment decision;
4. a designation to identify the Algo (Algo ID) responsible within the investment firm for the investment decision;
5. transaction reference number;
6. a designation to identify the order (Order ID);
7. the identification code of the order assigned by the trading venue upon receipt of the order;
8. a unique identification for each group of aggregated clients' orders (which will be subsequently placed as one block order on a given trading venue). This identification should indicated 'aggregated_X' with X representing the number of clients whose orders have been aggregated;

36. Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing)
37. RTS 24 (Commission Delegated Regulation (EU) 2017/580 of 24 June 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regard to regulatory technical standards for the maintenance of relevant data relating to orders in financial instruments) relates to MiFIR Article 25, but concerns only trading venue operator obligations under MiFIR Article 25(2).

9. the segment MIC code of the trading venue to which the order has been submitted;
10. the name and other designation of the person to whom the order was transmitted;
11. designation to identify the Seller & the Buyer;
12. the trading capacity;
13. a designation to identify the Trader (Trader ID) responsible for the execution;
14. a designation to identify the Algo (Algo ID) responsible for the execution;
15. B/S indicator;
16. instrument identification;
17. ultimate underlying;
18. put/Call identifier;
19. strike price;
20. up-front payment;
21. delivery type;
22. option style;
23. maturity date;
24. unit price and price notation;
25. price;
26. price multiplier;
27. currency 1;
28. currency 2;
29. remaining quantity;
30. modified quantity;
31. executed quantity; 32. the date and exact time of submission of the order or decision to deal. The exact time must be measured according to the methodology prescribed under the standards on clock synchronisation under Article 50(2) of Directive 2014/65/EU;
33. the date and exact time of any message that is transmitted to and received from the trading venue in relation to any events affecting an order. The exact time must be measured according to the methodology prescribed under Commission Delegated Regulation (EU) 2017/574;

34. the date and exact time any message that is transmitted to and received from another investment firm in relation to any events affecting an order. The exact time must be measured according to the methodology prescribed under the standards on clock synchronisation under Article 50(2) of Directive 2014/65/EU;
35. any message that is transmitted to and received from the trading venue in relation to orders placed by the investment firm;
36. any other details and conditions that was submitted to and received from another investment firm in relation with the order;
37. each placed order's sequences in order to reflect the chronology of every event affecting it, including but not limited to modifications, cancellations and execution;
38. short selling flag;
39. SSR exemption flag;
40. waiver flag.

5.2 Data retention and "actionable interests"

(a) ESMA Q&A

The ESMA Q&A on MiFIR data reporting (7 July 2017 version) which includes the following re Order Record Keeping:

"Question 1 – Are actionable indications of interest subject to the order record keeping requirements for Investment Firms and trading venues under Article 25(1) and (2) of MiFIR?

Answer 1 – Yes. An "actionable indication of interest" is defined in Article 2(1)(33) of MiFIR as "a message from one member or participant to another within a trading system in relation to available trading interest that contains all necessary information to agree on a trade". Actionable indications of interest are subject to pre-trade transparency requirements under Articles 3(1) and 8(1) of MiFIR, along with current bid and offer prices and the depth of trading interests at those prices. To ensure that relevant and sufficient data is kept at the disposal of competent authorities, paragraphs 1 and 2 of Article 25 of MiFIR set out the obligation on investment firms and trading venues to maintain records of, amongst others, the relevant data relating to these orders, including actionable indications of interest."

(b) Securities Loans

This ESMA explanation references, and the term "actionable indication of interests" is only used in, MiFIR pre-trade transparency requirements which do not apply to securities financing transactions, therefore it seems arguable that actionable indications of interest relating to securities loans should not be subject to the requirements under MiFIR Article 25(1).

5.3 Type of securities lending activity

(a) Agency lending

The data retention requirement will apply to the firm in relation to the relevant data relating to all securities loans of financial instruments which they have executed as agent of each client.

(b) Matched principal

The data retention requirement will apply to the firm in relation to the relevant data relating to all securities loans of financial instruments which they have executed on a matched principal basis.

(c) Borrowing/lending for own account

The data retention requirement will apply to the firm in relation to the relevant data relating to all securities loans of financial instruments which they have executed on their own account.

6. Transaction Reporting

6.1 General

MiFIR Article 26 requires firms which execute transactions in financial instruments to report complete and accurate details of such transactions to the relevant regulatory authority as quickly as possible, and no later than the close of the following working day, where: (a) the financial instruments are admitted to trading or traded on a trading venue (a regulated market, OTF or MTF) or for which a request for admission to trading has been made; (b) the financial instruments have underlying financial instruments traded on a trading venue; or (c) the financial instruments have an underlying index or basket composed of financial instruments traded on a trading venue.

RTS 22[38] states that for the purposes of MiFIR Article 26 (obligation to report transactions) the term "transaction" does not include securities financing transactions as defined in the SFTR, unless a member of the European System of Central Banks is counterparty to the securities financing transaction[39].

However, it should be noted that item 65 in Table 2 of RTS 22 includes the following: "Securities financing transaction indicator – 'true' shall be populated where the transaction falls within the scope of activity but is exempted from reporting under Regulation (EU) 2015/2365. 'false' otherwise."

6.2 Type of securities lending activity

(a) Agency lending

The reporting obligation under MiFIR Article 26 does not apply to securities lending transactions unless a member of the European System of Central Banks is a counterparty.

(b) Matched principal

The reporting obligation under MiFIR Article 26 does not apply to securities lending transactions unless a member of the European System of Central Banks is a counterparty.

(c) Borrowing/lending for own account

The reporting obligation under MiFIR Article 26 does not apply to securities lending transactions unless a member of the European System of Central Banks is a counterparty.

38. RTS 22 (Commission Delegated Regulation (EU) 2017/590 of 28 July 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regard to regulatory technical standards for the reporting of transactions to competent authorities), Art 2(5)(a)

39. Although generally RTS 22 applies from 3 January 2018, this limited reporting requirement respecting securities financing transactions only applies 12 months after the date of entry into force of the delegated act adopted by the Commission pursuant to SFTR, Article 4(9), i.e. the same time as when the obligations under SFTR, Article 4(1) will apply to financial counterparties referred to in SFTR Article 3(3)(a) and (b) (investment firms authorised under MiFID and credit institutions authorised in the EU), and third country entities referred to in SFTR Article 3(3)(i) which would require authorisation or registration in accordance with SFTR, Article 3(3)(a) and (b) if they were EU entities.

7. TTCA Disclosures

7.1 General

(a) MiFID2 Article 16(10) prohibits all firms from concluding "title transfer financial collateral arrangements with retail clients for the purpose of securing or covering present or future, actual or contingent or prospective obligations of clients" (this applies to all firms, not just those holding client assets).

MiFID2 does not define "title transfer financial collateral arrangement", but Recital (52) of MiFID2 refers to title transfer financial collateral arrangements as defined under Directive 2002/47/EC of the European Parliament and of the Council[40], which defines a 'title transfer financial collateral arrangement' as "an arrangement, including repurchase agreements, under which a collateral provider transfers full ownership of, or full entitlement to, financial collateral to a collateral taker for the purpose of securing or otherwise covering the performance of relevant financial obligations". The term "financial collateral" is not defined in that Directive, but under Article 1(4), "financial collateral... must consist of cash or financial instruments ".[41]

The term "title transfer collateral arrangement" or "TTCA" is used in the MiFID2 Level 2 Directive[42], but this is evidently intended to mean the same as "title transfer financial collateral arrangement" since Recital (6) of such Directive states "Article 16(10) of Directive 2014/65/EU prohibits firms from concluding title transfer collateral arrangements (TTCAs) with retail clients for the purpose of securing or covering present or future, actual or contingent or prospective obligations."

Since the MiFID2 prohibition relates to title transfer collateral arrangements with retail clients for the purpose of covering the obligations of such clients, the prohibition relates to the provision of title transfer collateral by retail clients, not the receipt of title transfer collateral by retail clients.

The above point is made clearer in the FCA rules where the term "title transfer collateral arrangement" or "TTCA" is defined slightly differently as: "(1) (in CASS 6) an arrangement by which a client transfers full ownership of a safe custody asset (or an asset which would be a safe custody asset but for the arrangement) to a firm for the purpose of securing or otherwise covering present or future, actual, contingent or prospective obligations. (2) (in CASS 7) an arrangement by which a client transfers full ownership of money to a firm for the purpose of securing or otherwise covering present or future, actual, contingent or prospective obligations."

40. The Financial Collateral Directive.

41. Although a transfer of cash does not transfer legal title to an asset as the same way as transfer of securities, cash can still be the subject of a TTCA. (Much will depend on the documentation since a payment resulting in an obligation for the recipient may, depending on the applicable terms, be characterised in various ways, such as a loan, or a bank deposit, or a title transfer collateral arrangement.)

42. Commission Delegated Directive (EU) 2017/593 of 7 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits

(b) MiFID2 Level 2 Directive, Article 6(3) requires firms "Where using title transfer collateral arrangements" to "highlight to professional clients and eligible counterparties the risks involved and the effect of any title transfer collateral arrangement on the client's financial instruments and funds." SFTR[43] Article 15(1)(a)(ii) imposes a similar requirement (the party providing collateral under a title transfer collateral arrangement must be "duly informed in writing by the receiving counterparty of the risks and consequences that may be involved in... concluding a title transfer collateral arrangement"). It is likely that compliance with the SFTR requirement will satisfy the MiFID2 requirement. This is supported by the approach of the FCA in the UK, as the amendments to the CASS rules to implement MiFID2 include the statement that "A firm may choose to combine its client communication under CASS 6.1.6DR(4)[44] with any communication made in order to comply with article 15.1(a)(ii) of the SFTR"[45].

(c) MiFID2 Level 2 Regulation Article 63 requires firms holding client financial instruments or client funds to provide a statement of client assets held on a quarterly basis, such statement to include "the extent to which any client financial instruments or client funds have been the subject of securities financing transactions"[46], and "a clear indication of the assets or funds which are subject to the rules of Directive 2014/65/EU and its implementing measures, and those that are not, such as those that are subject to Title Transfer Collateral Agreement"[47]

7.2 Effect of prohibition

(a) TTCA

A title transfer collateral arrangement is not the same as a securities lending transaction, although a title transfer collateral arrangement may form part of a securities lending transaction. The MiFID2 prohibition on taking title transfer collateral from retail clients does not prohibit securities lending transactions with retail clients, or the receipt by retail clients of title transfer collateral, but means that, from 3 January 2018, securities lending transactions and repurchase transactions with retail clients which require the retail client to provide title transfer collateral to the firm to secure redelivery or repayment obligations will not be possible.

43. Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse
44. The CASS rule which implements MiFID2 Article 6(3).
45. CASS 6.1.6EG
46. MiFID2 Level 2 Regulation Article 63(2)(b). (This requirement already applies under the MiFID1 regime, under Article 43(2) of the MiFID Implementing Directive (Commission Directive No. 2006/73/EC implementing Directive 2004/39/EC of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive)).
47. MiFID2 Level 2 Regulation Article 63(2)(d).

This is consistent with the fact that the requirements in Article 6 of the MiFID2 Level 2 Directive[48], which concern appropriate use of title transfer collateral arrangements, only contemplate title transfer collateral arrangements between a firm and its professional clients or eligible counterparties. Similarly, Recital (7) of the MiFID2 Level 2 Directive states the following: "Demonstrating a robust link between collateral transferred under a TTCA and client's liability should not preclude taking appropriate security against a client's obligation. Investment firms could thus continue to require a sufficient collateral and where appropriate, to do so by a TTCA. That obligation... should not prohibit the appropriate use of TTCAs in the context of... repos for non-retail clients." Moreover, Recital (8) of the MiFID2 Level 2 Directive states "While some securities financing transactions may require the transfer of title of clients' assets, in that context investment firms should not be able to effect arrangements prohibited under Article 16(10) of Directive 2014/65/EU", and Article 5(5) of the MiFID2 Level 2 Directive states "Member States shall ensure that investment firms do not enter into arrangements which are prohibited under Article 16(10) of Directive 2014/65/ EU."

New CASS 6.1.6R(3)(a) states that "A firm must not enter into a TTCA in respect of an asset belonging to a retail client."

It should of course be noted that the TTCA prohibition only applies to title transfer collateral arrangements with retail clients, therefore, when deciding whether the TTCA prohibition applies to the transfer of title transfer collateral by a borrower of securities, a preliminary step to will be to determine whether the borrower is a client of the firm receiving the collateral (see discussion of when a counterparty may be a client in Part (A), para 6.4, above).

(b) Retail Clients

It should be noted that the provisions of Article 5(1) to (4) MiFID2 Level 2 Directive governing the circumstances in which firms may enter into securities financing transactions in respect of custody assets are not limited to professional clients and eligible counterparties. Also, the final FCA CASS rules implementing MiFID2 could be read as contemplating securities financing transactions with retail clients because CASS 6.4.1AG states "The FCA expects firms which enter into arrangements under CASS 6.4.1R ["arrangements for securities financing transactions in respect of safe custody assets held by it on behalf of a client or [to] otherwise use such safe custody assets for its own account of the account of any other person or client of the firm"] with retail clients to only enter into securities financing transactions and not otherwise use retail clients' safe custody assets".

48. Commission Delegated Directive (EU) 2017/593 of 7 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits

The result of these provisions is that, although MiFID2 contains no prohibition on entering into securities financing transactions with retail clients, or on transferring collateral on a title transfer basis to retail clients, any collateral which is provided by retail clients under securities financing transactions (or for any other purpose) cannot be provided by such clients on a title transfer basis.

7.3 Type of securities lending activity

(a) Agency lending

The prohibition on title transfer collateral arrangements with retail clients is not directly relevant to a firm providing agency lending services, because the firm is not party to the securities loan, and does not receive collateral from the client. (In contrast, a party to a securities loan which enters into the loan with a counterparty which acts through an agent will (if not treating the agent as its client, see Part (A), para 6.1(b), above) need to determine whether the counterparty is a client, and if so whether it is a retail client and therefore subject to the TTCA prohibition (see Part (A), para 6.4 above – it should be noted that it is unlikely that a counterparty will not be viewed as a client if such counterparty is a person who would fall within the category of retail client).)

The agent lender will not be subject to the requirements to give risk warnings regarding title transfer collateral arrangements, because such requirements apply where the firm itself uses a title collateral arrangement and receives collateral from the client, but the agent lender is not party to the securities loan and does not receive collateral from the client to whom it provides the agency lending services.

Where the firm acting as agent lender is also custodian for its clients, it will need to provide to the client the relevant client assets statements, including the information regarding client assets which have been transferred under a securities financing transaction, or are subject to a title transfer collateral arrangement.

(b) Matched principal

The prohibition on title transfer collateral arrangements with retail clients means that, as regards the transactions under which the firm lends securities and therefore receives collateral, if the counterparty to such transaction is a retail client of the firm, the firm cannot receive collateral in the form of title transfer collateral from that client.

The requirements to give risk warnings regarding title transfer collateral arrangements apply where the firm uses a title collateral arrangement and receives collateral from its client, therefore will apply in relation to the transactions under which the firm lends securities and receives title transfer collateral from the counterparty and the counterparty is a client of the firm (but the SFTR risk warning must be provided even if the counterparty is not a client of the firm).

If the firm also provides custody services to the borrower or lender counterparties, it will need to provide to its client the relevant client assets statements, including the information regarding assets which have been transferred under a securities financing transaction, or are subject to a title transfer collateral arrangement.

(c) Borrowing/lending for own account

The prohibition on title transfer collateral arrangements with retail clients means that, as regards the transactions under which the firm lends securities and therefore receives collateral, if the counterparty to such transaction is a retail client of the firm, the firm cannot receive collateral in the form of title transfer collateral from that client.

The requirements to give risk warnings regarding title transfer collateral arrangements apply where the firm uses a title collateral arrangement and receives collateral from its client, therefore will apply in relation to the transactions under which the firm lends securities and receives title transfer collateral from the counterparty and the counterparty is a client of the firm (but the SFTR risk warning must be provided even if the counterparty is not a client of the firm).

If the firm also provides custody services to the counterparties, it will need to provide to its client the relevant client assets statements, including the information regarding assets which have been transferred under a securities financing transaction, or are subject to a title transfer collateral arrangement.

8. Portfolio management

8.1 General

The term 'portfolio management' is defined in MiFID2, Article 4(1)(8) to mean "managing portfolios in accordance with mandates given by clients on a discretionary client-by-client basis where such portfolios include one or more financial instruments". This is the same definition as in MiFID1, and there is nothing to indicate that it should be interpreted differently for the purposes of MiFID2.

In the European Commission Q&A for MiFID1, the Commission contemplated that securities lending activities could constitute portfolio management since it stated that "Securities lending activities will normally involve the provision of the investment service of execution of orders on behalf of clients, reception and transmission of orders and portfolio management."

8.2 Type of securities lending activity

(a) Agency lending

A firm entering into securities lending transactions as agent of a client will not be exercising any discretion if it enters into the transactions, and determines the terms of such transactions, only by complying with specific instructions from the client. The extent to which the firm has any discretion will depend on the terms agreed with the client, and in some respects how the firm's systems operate.

Since the particular nature of the systems, operational processes and policies, and contractual terms, of each firm will vary, a firm will need to determine whether its activities would be regarded as acting as portfolio management[49] based on the specific details of its own arrangements.

(b) Matched principal

A firm executing client orders by borrowing securities from a client and lending the securities received under the loan to a different client on a matched principal basis will not be exercising any discretion if it enters into the transactions, and determines the terms of such transactions, only by specific agreement with the relevant client.

Since the particular nature of the systems, operational processes and policies, and contractual terms, of each firm will vary, a firm will need to determine whether its activities would be regarded as acting as portfolio management based on the specific details of its own arrangements.

(c) Borrowing/lending for own account

Where a firm borrows or lends securities for its own account, it is dealing on its own account[50] (trading against proprietary capital resulting in the conclusion of transactions in one or more financial instruments), and therefore should not be regarded as providing a service to a client (provided that on the particular facts the counterparty does not satisfy the criteria to be regarded as a client for this purpose – see Part (A), para 6.4 above).

49. It should be noted that in the UK, the Financial Conduct Authority regards portfolio management as an investment service within the definition of distribution, therefore, if a firm's lending activities fall within portfolio management, there will be additional implications.

50. Note assumption in 6.3(b) on p.14.

9. Custody requirements

9.1 General

The requirements of MiFID2 Articles 16(8) and (9), and the more detailed requirements in the MiFID2 Level 2 Directive, Articles 2 to 8, will apply to any firm which holds financial instruments or (for most purposes, only where the firm is not a credit institution) cash for clients.

9.2 Custody requirement relevant to securities lending

Under the MiFID2 Level 2 Directive, Article 5, where a firm holds financial instruments as custodian for a client:

(a) the firm must not enter into arrangements for securities financing transactions in respect of such financial instruments, or otherwise use such financial instruments for its own account or the account of any other person or client of the firm, unless both: (i) the client has given his prior express consent to the use of the instruments on specified terms, as clearly evidenced in writing and affirmatively executed by signature or equivalent, and (ii) the use of that client's financial instruments is restricted to the specified terms to which the client consents[51].

(b) the firm must not enter into arrangements for securities financing transactions in respect of financial instruments which are held on behalf of the client in an omnibus account maintained by a third party, or otherwise use financial instruments held in such an account for its own account or for the account of any other person unless, in addition to the above conditions, either: (i) each client whose financial instruments are held together in an omnibus account must have given prior express consent in accordance with (a)(i); or (ii) the firm has in place systems and controls which ensure that only financial instruments belonging to clients who have given prior express consent in accordance with (a)(i) are so used[52].

(c) the firm's records must include details of the client on whose instructions the use of the financial instruments has been effected, as well as the number of financial instruments used belonging to each client who has given his consent, so as to enable the correct allocation of any loss[53].

(d) the firm must take appropriate measures to prevent the unauthorised use of client financial instruments for its own account or the account of any other person such as: (i) the conclusion of agreements with clients on measures to be taken by the investment firms in case the client does not have enough provision on its account on the settlement date, such as borrowing of the corresponding securities on behalf of the client or unwinding the position; (ii) the close

51. Commission Delegated Directive (EU) 2017/593 of 7 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits, Art 5(1)
52. Commission Delegated Directive (EU) 2017/593, Art 5(2)
53. Commission Delegated Directive (EU) 2017/593, Art 5(2)

monitoring by the investment firm of its projected ability to deliver on the settlement date and the putting in place of remedial measures if this cannot be done; and (iii) the close monitoring and prompt requesting of undelivered securities outstanding on the settlement day and beyond[54].

9.3 Additional requirements

(a) The MiFID2 Level 2 Directive, Article 5(4) requires firms to "adopt specific arrangements for all clients to ensure that the borrower of client financial instruments provides the appropriate collateral and that the firm monitors the continued appropriateness of such collateral and takes the necessary steps to maintain the balance with the value of client instruments." In addition, Recital (9) of such Directive states: "In order to ensure appropriate protection for clients in relation to securities financing transactions (SFTs), investment firms should adopt specific arrangements to ensure that the borrower of client assets provides the appropriate collateral and that the firm monitors the continued appropriateness of such collateral. Investment firms' duty to monitor collateral should apply where they are party to an SFT agreement, including when acting as an agent for the conclusion of a SFT or in cases of tripartite agreement between the external borrower, the client and the investment firm."

(b) Under the MiFID2 Level 2 Directive, Article 6(1), any firm entering into title transfer collateral arrangements with a professional client or eligible counterparty must "properly consider," and be "able to demonstrate that they have done so, the use of title transfer collateral arrangements in the context of the relationship between the client's obligation to the firm and the client assets subjected to title transfer collateral arrangements by the firm". Under the MiFID2 Level 2 Directive, Article 6(2), "When considering, and documenting, the appropriateness of the use of title transfer collateral arrangements, investment firms shall take into account all of the following factors: (a) whether there is only a very weak connection between the client's obligation to the firm and the use of title transfer collateral arrangements, including whether the likelihood of a clients' liability to the firm is low or negligible; (b) whether the amount of client funds or financial instruments subject to title transfer collateral arrangements far exceeds the client's obligation, or is even unlimited if the client has any obligation at all to the firm; and (c) whether all clients' financial instruments or funds are made subject to title transfer collateral arrangements, without consideration of what obligation each client has to the firm."

For the purposes of MiFID2 and related legislation, "title transfer financial collateral arrangement" has the same meaning as in the Financial Collateral Directive (Directive 2002/47/EC), namely "an arrangement, including repurchase agreements, under which a collateral provider transfers full ownership of, or full entitlement to, financial collateral to a collateral taker for the purpose of securing or otherwise covering the performance of relevant financial obligations"[55].

54. Commission Delegated Directive (EU) 2017/593, Art 5(3)

55. Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements, Article 2(1)(b)

9.4 Type of securities lending activity

(a) Agency lending

(i) All requirements applicable to custodians as described in 9.1 and 9.2 above will apply to the lending agent where it also provides custody services.

(ii) The requirements described in 9.3(b) are not applicable because the agent lender does not enter into a title transfer collateral arrangement with its client who is the lender under the securities loan transaction.

(iii) It might be argued that the requirements regarding control of unauthorised use of client assets described in 9.2(d) above also apply to a firm lending client securities as agent of the client and which controls transfers of the client's assets but does not itself hold the client's assets as custodian. This argument is based on the fact that Article 5(3) of the MiFID2 Level 2 Directive (unlike Articles 5(1) and (2)) does not refer to financial instruments "held on behalf of a client".

However, such an interpretation is considered incorrect, since the wording of Article 5(3) contemplates settlement by the firm, which would not be possible if the firm was not the custodian, and there are no suggestions to the contrary in the Recitals or elsewhere. Moreover the FCA's new CASS rule which will implement Article 5(3) (CASS 6.4.1CR, see PS 17/14) is part of the CASS Chapter 6 rules which only apply to firms providing custody services, and requires a firm to "take appropriate measures to prevent the unauthorised use of safe custody assets for its own account or the account of any other person" and there is no indication that this refers to safe custody assets held by someone other than the firm subject to this rule.

On this basis, an agent lender will only be subject to the requirements of Article 5(3) if it also provide custody services to its client.

(iv) The extent of the application of the requirements to ensure a borrower provides appropriate collateral described in 9.3(a) above is more difficult. Article 5(4) of the MiFID2 Level 2 Directive does not state specifically that it applies just to firms holding assets for clients. Also, Recital (9) of such Directive makes no reference to firms holding assets for clients, but does state that the obligation to monitor collateral should apply to firms which "are party to an SFT agreement, including when acting as an agent for the conclusion of a SFT or in cases of tripartite agreement between the external borrower, the client and the investment firm."

However, the other provisions of Article 5 only apply to firms holding assets for clients, and Recital 9 could be interpreted as referring to firms which provide both custody and agent lending services since it refers to "client assets". In addition, the FCA's new CASS rule which will implement Article 5(4) (CASS 6.4.2AR, see PS 17/14) is part of the CASS Chapter 6 rules which only apply to firms providing custody services, and requires a firm to "ensure that the borrower of client safe custody assets provides the appropriate collateral and that the firm monitors the continued appropriateness of such collateral and takes the necessary steps to maintain the balance with the value of the client safe custody assets" and there is no indication that this refers to safe custody assets held by someone other than the firm subject to this rule.

On this basis, an agent lender will only be subject to the requirements of Article 5(4) if it also provides custody services to its client.

It should be noted that regardless of the contractual terms agreed between the agent lender and its client, an agent lender which is also a custodian and therefore subject to the requirements of Article 5(4) will be obliged to "ensure" that the borrower provides appropriate collateral, monitor the continued appropriateness of such collateral, and take "necessary steps" to maintain the balance with the value of client assets borrowed.

(b) Matched principal

(i) Where a firm enters into borrowing and lending transactions on a matched principal basis, all requirements applicable to custodians as described in 9.1, 9.2 and 9.3(a) above will apply in relation to a borrowing transaction if the firm is borrowing securities from a client to whom it also provides custody services.

(ii) The requirements described in 9.3(b) will apply to a lending transaction where the firm receives title transfer collateral from the borrower, and the borrower is a client of the firm.

(c) Borrowing/lending for own account

(i) Where a firm enters into borrowing and lending transactions for its own account, all requirements applicable to custodians as described in 9.1, 9.2 and 9.3(a) above will apply in relation to a borrowing transaction if the firm is borrowing securities from a client to whom it also provides custody services.

(ii) The requirements described in 9.3(b) will apply to a lending transaction where the firm receives title transfer collateral from the borrower, and the borrower is a client of the firm.

10. Product governance

10.1 General

Various obligations apply under Articles 16 and 24 of MiFID2, and the corresponding provisions of the MiFID2 Level 2 Directive, to a firm which "manufactures financial instruments". There is no definition of the manufacture of financial instruments, but in the MiFID2 Level 2 Directive, Recital (15) states "investment firms that create, develop, issue and/or design financial instruments, including when advising corporate issuers on the launch of new financial instruments, should be considered as manufacturers", and Article 9 refers to "manufacturing financial instruments, which encompasses the creation, development, issuance and/or design of financial instruments."

MiFID2 Level 2 Directive, Recital (15) states "investment firms that offer or sell financial instrument and services to clients should be considered distributors". Article 10 of the MiFID2 Level 2 Directive contains various obligations for distributors, although it is important to note that firms are required to comply "in a way that is appropriate and proportionate... taking into account the nature of the... investment service and the target market for the product".

In the FCA Glossary, "distributor" is defined as "a firm which offers, recommends or sells investments or provides investment services to clients."

10.2 Type of securities lending activity

(a) Agency lending

When acting as an agency lender, a firm does not create, develop, issue or design financial instruments, therefore in such capacity the firm is not subject to the MiFID2 requirements applicable to manufacturers.

Because a "distributor" includes an investment firm which provides investment services to clients, a firm providing agency lending services will be a distributor of such services for this purpose. Since the firm is a distributor of services, rather than a distributor of financial instruments, some aspects of Article 10 will not be relevant. For example, Article 10(2), second paragraph, as implemented in the UK as PROD 3.3.3R, applies to distributors of financial instruments not to distributors of investment services.

(b) Matched principal

When entering into securities loans on a matched principal basis, a firm does not create, develop, issue or design financial instruments, therefore in such capacity the firm is not subject to the MiFID2 requirements applicable to manufacturers.

Because a "distributor" includes an investment firm which provides investment services to clients, a firm providing these services will be a distributor of such services for this purpose. Since the firm is a distributor of services, rather than a distributor of financial instruments, some aspects of Article 10 will not be relevant. For example, Article 10(2), second paragraph, as implemented in the UK as PROD 3.3.3R, applies to distributors of financial instruments not to distributors of investment services.

(c) Borrowing/lending for own account

When entering into securities loans for its own account, a firm does not create, develop, issue or design financial instruments, therefore in such capacity the firm is not subject to the MiFID2 requirements applicable to manufacturers.

Where a firm borrows or lends securities for its own account, it is dealing on its own account[56] (trading against proprietary capital resulting in the conclusion of transactions in one or more financial instruments), therefore should not be regarded as providing a service to a client (provided that on the particular facts the counterparty does not satisfy the criteria to be regarded as a client for this purpose – see Part (A), para 6.4 above), and so will not be a distributor for this purpose.

56. Note assumption in 6.3(b) on p.14.

11. General requirements applicable under MiFID2/MiFIR

The following general requirements are applicable to firms carrying out agency lending, lending on a matched principal basis, or borrowing and lending for their own account, although in the context of lending on a matched principal basis, or borrowing and lending for own account, requirements relating to clients will not apply unless the counterparty to the securities loan transaction is a client (including an eligible counterparty) of the firm. Some exceptions apply respecting eligible counterparties (see Schedule 2).

11.1 Client Reporting: MiFID2 Art 25(6) and Level 2 Regulation Art 59 re reporting client execution of client orders; Level 2 Regulation Art 63 re statements on holdings of client financial instruments and client funds

MiFID2 Art 25(6). The investment firm shall provide the client with adequate reports on the service provided in a durable medium. Those reports shall include periodic communications to clients, taking into account the type and the complexity of financial instruments involved and the nature of the service provided to the client and shall include, where applicable, the costs associated with the transactions and services undertaken on behalf of the client.

When providing investment advice, the investment firm shall, before the transaction is made, provide the client with a statement on suitability in a durable medium specifying the advice given and how that advice meets the preferences, objectives and other characteristics of the retail client.

Where the agreement to buy or sell a financial instrument is concluded using a means of distance communication which prevents the prior delivery of the suitability statement, the investment firm may provide the written statement on suitability in a durable medium immediately after the client is bound by any agreement, provided both the following conditions are met:

(a) the client has consented to receiving the suitability statement without undue delay after the conclusion of the transaction; and

(b) the investment firm has given the client the option of delaying the transaction in order to receive the statement on suitability in advance.

Where an investment firm provides portfolio management or has informed the client that it will carry out a periodic assessment of suitability, the periodic report shall contain an updated statement of how the investment meets the client's preferences, objectives and other characteristics of the retail client.

L2 Reg, Article 59. Reporting obligations in respect of execution of orders other than for portfolio management (Article 25(6) of Directive 2014/65/EU)

1. Investment firms having carried out an order on behalf of a client, other than for portfolio management, shall, in respect of that order:

   (a) promptly provide the client, in a durable medium, with the essential information concerning the execution of that order;

(b) send a notice to the client in a durable medium confirming execution of the order as soon as possible and no later than the first business day following execution or, where the confirmation is received by the investment firm from a third party, no later than the first business day following receipt of the confirmation from the third party.

Point (b) shall not apply where the confirmation would contain the same information as a confirmation that is to be promptly dispatched to the client by another person.

Points (a) and (b) shall not apply where orders executed on behalf of clients relate to bonds funding mortgage loan agreements with the said clients, in which case the report on the transaction shall be made at the same time as the terms of the mortgage loan are communicated, but no later than one month after the execution of the order.

2. In addition to the requirements under paragraph 1, investment firms shall supply the client, on request, with information about the status of his order.

3. In the case of client orders relating to units or shares in a collective investment undertaking which are executed periodically, investment firms shall either take the action specified in point (b) of paragraph 1 or provide the client, at least once every six months, with the information listed in paragraph 4 in respect of those transactions.

4. The notice referred to in point (b) of paragraph 1 shall include such of the following information as is applicable and, where relevant, in accordance with the regulatory technical standards on reporting obligations adopted in accordance with Article 26 of Regulation (EU) No 600/2014:

(a) the reporting firm identification;

(b) the name or other designation of the client;

(c) the trading day;

(d) the trading time;

(e) the type of the order;

(f) the venue identification;

(g) the instrument identification;

(h) the buy/sell indicator;

(i) the nature of the order if other than buy/sell;

(j) the quantity;

(k) the unit price;

(l) the total consideration;

(m) a total sum of the commissions and expenses charged and, where the client so requests, an itemised breakdown including, where relevant, the amount of any mark-up or mark-down imposed where the transaction was executed by an investment firm when dealing on own account, and the investment firm owes a duty of best execution to the client;

(n) the rate of exchange obtained where the transaction involves a conversion of currency;

(o) the client's responsibilities in relation to the settlement of the transaction, including the time limit for payment or delivery as well as the appropriate account details where these details and responsibilities have not previously been notified to the client;

(p) where the client's counterparty was the investment firm itself or any person in the investment firm's group or another client of the investment firm, the fact that this was the case unless the order was executed through a trading system that facilitates anonymous trading.

For the purposes of point (k), where the order is executed in tranches, the investment firm may supply the client with information about the price of each tranche or the average price. Where the average price is provided, the investment firm shall supply the client with information about the price of each tranche upon request.

5. The investment firm may provide the client with the information referred to in paragraph 4 using standard codes if it also provides an explanation of the codes used.

L2 Reg, Article 63 Statements of client financial instruments or client funds (Article 25(6) of Directive 2014/65/EU)

1. Investment firms that hold client financial instruments or client funds shall send at least on a quarterly basis, to each client for whom they hold financial instruments or funds, a statement in a durable medium of those financial instruments or funds unless such a statement has been provided in any other periodic statement. Upon client request, firms shall provide such statement more frequently at a commercial cost.

   The first subparagraph shall not apply to a credit institution authorised under Directive 2000/12/EC of the European Parliament and of the Council (1) in respect of deposits within the meaning of that Directive held by that institution.

2. The statement of client assets referred to in paragraph 1 shall include the following information:

   (a) details of all the financial instruments or funds held by the investment firm for the client at the end of the period covered by the statement;

   (b) the extent to which any client financial instruments or client funds have been the subject of securities financing transactions;

   (c) the extent of any benefit that has accrued to the client by virtue of participation in any securities financing transactions, and the basis on which that benefit has accrued;

   (d) a clear indication of the assets or funds which are subject to the rules of Directive 2014/65/EU and its implementing measures and those that are not, such as those that are subject to Title Transfer Collateral Agreement;

   (e) a clear indication of which assets are affected by some peculiarities in their ownership status, for instance due to a security interest;

(f) the market or estimated value, when the market value is not available, of the financial instruments included in the statement with a clear indication of the fact that the absence of a market price is likely to be indicative of a lack of liquidity. The evaluation of the estimated value shall be performed by the firm on a best effort basis.

In cases where the portfolio of a client includes the proceeds of one or more unsettled transactions, the information referred to in point (a) may be based either on the trade date or the settlement date, provided that the same basis is applied consistently to all such information in the statement.

The periodic statement of client assets referred to in paragraph 1 shall not be provided where the investment firm provides its clients with access to an online system, which qualifies as a durable medium, where up-to-date statements of client's financial instruments or funds can be easily accessed by the client and the firm has evidence that the client has accessed this statement at least once during the relevant quarter.

3.Investment firms which hold financial instruments or funds and which carry out the service of portfolio management for a client may include the statement of client assets referred to in paragraph 1 in the periodic statement it provides to that client pursuant to Article 60(1).

11.2 Client classification (Level 2 Regulation. Art 45)

L2 Reg, Art 45. Information concerning client categorisation (Article 24(4) of Directive 2014/65/EU)

1. Investment firms shall notify new clients, and existing clients that the investment firm has newly categorised as required by Directive 2014/65/EU, of their categorisation as a retail client, a professional client or an eligible counterparty in accordance with that Directive.
2. Investment firms shall inform clients in a durable medium about any right that client has to request a different categorisation and about any limitations to the level of client protection that a different categorisation would entail.
3. Investment firms may, either on their own initiative or at the request of the client concerned treat a client in the following manner:
   (a) as a professional or retail client where that client might otherwise be classified as an eligible counterparty pursuant to Article 30(2) of Directive 2014/65/EU;
   (b) a retail client where that client that is considered a professional client pursuant to Section I of Annex II to Directive 2014/65/EU.

11.3 Systems and resources (MiFID2, Art 16(4))

MiFID2 Art 16(4). An investment firm shall take reasonable steps to ensure continuity and regularity in the performance of investment services and activities. To that end the investment firm shall employ appropriate and proportionate systems, resources and procedures.

11.4 Outsourcing (MiFID2 Art 16(5), Level 2 Regulation Art 23, 24, 30 to 32)

MiFID2 Art 16(5). An investment firm shall ensure, when relying on a third party for the performance of operational functions which are critical for the provision of continuous and satisfactory service to clients and the performance of investment activities on a continuous and satisfactory basis, that it takes reasonable steps to avoid undue additional operational risk. Outsourcing of important operational functions may not be undertaken in such a way as to impair materially the quality of its internal control and the ability of the supervisor to monitor the firm's compliance with all obligations.

L2 Reg, Art 23. Risk management (Article 16(5) of Directive 2014/65/EU)

1. Investment firms shall take the following actions relating to risk management:

   (a) establish, implement and maintain adequate risk management policies and procedures which identify the risks relating to the firm's activities, processes and systems, and where appropriate, set the level of risk tolerated by the firm;

   (b) adopt effective arrangements, processes and mechanisms to manage the risks relating to the firm's activities, processes and systems, in light of that level of risk tolerance;

   (c) monitor the following:

   (i) the adequacy and effectiveness of the investment firm's risk management policies and procedures;

   (ii) the level of compliance by the investment firm and its relevant persons with the arrangements, processes and mechanisms adopted in accordance with point (b);

   (iii) the adequacy and effectiveness of measures taken to address any deficiencies in those policies, procedures, arrangements, processes and mechanisms, including failures by the relevant persons to comply with such arrangements, processes and mechanisms or follow such policies and procedures.

2. Investment firms shall, where appropriate and proportionate in view of the nature, scale and complexity of their business and the nature and range of the investment services and activities undertaken in the course of that business, establish and maintain a risk management function that operates independently and carries out the following tasks:

   (a) implementation of the policy and procedures referred to in paragraph 1;

   (b) provision of reports and advice to senior management in accordance with Article 25(2).

Where an investment firm does not establish and maintain a risk management function under the first sub-paragraph, it shall be able to demonstrate upon request that the policies and procedures which it is has adopted in accordance with paragraph 1 satisfy the requirements therein.

L2 Reg, Art 24. Internal audit (Article 16(5) of Directive 2014/65/EU)

Investment firms shall, where appropriate and proportionate in view of the nature, scale and complexity of their business and the nature and range of investment services and

activities undertaken in the course of that business, establish and maintain an internal audit function which is separate and independent from the other functions and activities of the investment firm and which has the following responsibilities:

(a) establish, implement and maintain an audit plan to examine and evaluate the adequacy and effectiveness of the investment firm's systems, internal control mechanisms and arrangements;

(b) issue recommendations based on the result of work carried out in accordance with point (a) and verify compliance with those recommendations;

(c) report in relation to internal audit matters in accordance with Article 25(2).

L2 Reg, Art 30. Scope of critical and important operational functions (Article 16(2) and first subparagraph of Article 16(5) of Directive 2014/65/EU)

1. For the purposes of the first subparagraph of Article 16(5) of Directive 2014/65/EU, an operational function shall be regarded as critical or important where a defect or failure in its performance would materially impair the continuing compliance of an investment firm with the conditions and obligations of its authorisation or its other obligations under Directive 2014/65/EU, or its financial performance, or the soundness or the continuity of its investment services and activities.

2. Without prejudice to the status of any other function, the following functions shall not be considered as critical or important for the purposes of paragraph 1:

(a) the provision to the firm of advisory services, and other services which do not form part of the investment business of the firm, including the provision of legal advice to the firm, the training of personnel of the firm, billing services and the security of the firm's premises and personnel;

(b) the purchase of standardised services, including market information services and the provision of price feeds.

L2 Reg, Art 31 Outsourcing critical or important operational functions (Article 16(2) and of Article 16(5) first subparagraph of Directive 2014/65/EU)

1. Investment firms outsourcing critical or important operational functions shall remain fully responsible for discharging all of their obligations under Directive 2014/65/EU and shall comply with the following conditions:

(a) the outsourcing does not result in the delegation by senior management of its responsibility;

(b) the relationship and obligations of the investment firm towards its clients under the terms of Directive 2014/65/EU is not altered;

(c) the conditions with which the investment firm must comply in order to be authorised in accordance with Article 5 of Directive 2014/65/EU, and to remain so, are not undermined;

(d) none of the other conditions subject to which the firm's authorisation was granted is removed or modified.

2. Investment firms shall exercise due skill, care and diligence when entering into, managing or terminating any arrangement for the outsourcing to a service provider of critical or important operational functions and shall take the necessary steps to ensure that the following conditions are satisfied:

   (a) the service provider has the ability, capacity, sufficient resources, appropriate organisational structure supporting the performance of the outsourced functions, and any authorisation required by law to perform the outsourced functions, reliably and professionally;

   (b) the service provider carries out the outsourced services effectively and in compliance with applicable law and regulatory requirements, and to this end the firm has established methods and procedures for assessing the standard of performance of the service provider and for reviewing on an ongoing basis the services provided by the service provider;

   (c) the service provider properly supervises the carrying out of the outsourced functions, and adequately manage the risks associated with the outsourcing;

   (d) appropriate action is taken where it appears that the service provider may not be carrying out the functions effectively or in compliance with applicable laws and regulatory requirements;

   (e) the investment firm effectively supervises the outsourced functions or services and manage the risks associated with the outsourcing and to this end the firm retains the necessary expertise and resources to supervise the outsourced functions effectively and manage those risks;

   (f) the service provider has disclosed to the investment firm any development that may have a material impact on its ability to carry out the outsourced functions effectively and in compliance with applicable laws and regulatory requirements;

   (g) the investment firm is able to terminate the arrangement for outsourcing where necessary, with immediate effect when this is in the interests of its clients, without detriment to the continuity and quality of its provision of services to clients;

   (h) the service provider cooperates with the competent authorities of the investment firm in connection with the outsourced functions;

   (i) the investment firm, its auditors and the relevant competent authorities have effective access to data related to the outsourced functions, as well as to the relevant business premises of the service provider, where necessary for the purpose of effective oversight in accordance with this article, and the competent authorities are able to exercise those rights of access;

   (j) the service provider protects any confidential information relating to the investment firm and its clients;

   (k) the investment firm and the service provider have established, implemented and maintained a contingency plan for disaster recovery and periodic testing of backup facilities, where that is necessary having regard to the function, service or activity that has been outsourced;

   (l) the investment firm has ensured that the continuity and quality of the outsourced functions or services are maintained also in the event of termination of the

outsourcing either by transferring the outsourced functions or services to another third party or by performing them itself.

3. The respective rights and obligations of the investment firms and of the service provider shall be clearly allocated and set out in a written agreement. In particular, the investment firm shall keep its instruction and termination rights, its rights of information, and its right to inspections and access to books and premises. The agreement shall ensure that outsourcing by the service provider only takes place with the consent, in writing, of the investment firm.
4. Where the investment firm and the service provider are members of the same group, the investment firm may, for the purposes of complying with this Article and Article 32, take into account the extent to which the firm controls the service provider or has the ability to influence its actions.
5. Investment firms shall make available on request to the competent authority all information necessary to enable the authority to supervise the compliance of the performance of the outsourced functions with the requirements of Directive 2014/65/EU and its implementing measures.

L2 Reg, Art 32. Service providers located in third countries (Article 16(2) and first subparagraph of Article 16(5) of Directive 2014/65/EU)

1. In addition to the requirements set out in Article 31, where an investment firm outsources functions related to the investment service of portfolio management provided to clients to a service provider located in a third country, that investment firm ensures that the following conditions are satisfied:
   (a) the service provider is authorised or registered in its home country to provide that service and is effectively supervised by a competent authority in that third country;
   (b) there is an appropriate cooperation agreement between the competent authority of the investment firm and the supervisory authority of the service provider.
2. The cooperation agreement referred to in point (b) of paragraph 1 shall ensure that the competent authorities of the investment firm are able, at least, to:
   (a) obtain on request the information necessary to carry out their supervisory tasks pursuant to Directive 2014/65/EU and Regulation (EU) No 600/2014;
   (b) obtain access to the documents relevant for the performance of their supervisory duties maintained in the third country;
   (c) receive information from the supervisory authority in the third country as soon as possible for the purpose of investigating apparent breaches of the requirements of Directive 2014/65/EU and its implementing measures and Regulation (EU) No 600/2014;
   (d) cooperate with regard to enforcement, in accordance with the national and international law applicable to the supervisory authority of the third country and the competent authorities in the Union in cases of breach of the requirements of Directive 2014/65/EU and its implementing measures and relevant national law.

3. Competent authorities shall publish on their website a list of the supervisory authorities in third countries with which they have a cooperation agreement referred to in point (b) of paragraph 1.

Competent authorities shall update cooperation agreements concluded before the date of entry into application of this Regulation within six months from that date.

11.5 Record keeping (MIFD2 Art 16(6), Level 2 Regulation Art 35, 72 to 76)

MiFI2 Art 16(6). An investment firm shall arrange for records to be kept of all services, activities and transactions undertaken by it which shall be sufficient to enable the competent authority to fulfil its supervisory tasks and to perform the enforcement actions under this Directive, Regulation (EU) No 600/2014, Directive 2014/57/EU and Regulation (EU) No 596/2014, and in particular to ascertain that the investment firm has complied with all obligations including those with respect to clients or potential clients and to the integrity of the market.

L2 Reg, Art 35 Record of services or activities giving rise to detrimental conflict of interest (Article 16(6) of Directive 2014/65/EU)

Investment firms shall keep and regularly update a record of the kinds of investment or ancillary service or investment activity carried out by or on behalf of the firm in which a conflict of interest entailing a risk of damage to the interests of one or more clients has arisen or, in the case of an ongoing service or activity, may arise.

Senior management shall receive on a frequent basis, and at least annually, written reports on situations referred to in this Article.

L2 Reg, Art 72. Retention of records (Article 16(6) of Directive 2014/65/EU)

1. The records shall be retained in a medium that allows the storage of information in a way accessible for future reference by the competent authority, and in such a form and manner that the following conditions are met:
   (a) the competent authority is able to access them readily and to reconstitute each key stage of the processing of each transaction;
   (b) it is possible for any corrections or other amendments, and the contents of the records prior to such corrections or amendments, to be easily ascertained;
   (c) it is not possible for the records otherwise to be manipulated or altered;
   (d) it allows IT or any other efficient exploitation when the analysis of the data cannot be easily carried out due to the volume and the nature of the data; and
   (e) the firm's arrangements comply with the record keeping requirements irrespective of the technology used.

2. Investment firms shall keep at least the records identified in Annex I to this Regulation depending upon the nature of their activities.

The list of records identified in Annex I to this Regulation is without prejudice to any other record-keeping obligations arising from other legislation.

3. Investment firms shall also keep records of any policies and procedures they are required to maintain pursuant to Directive 2014/65/EU, Regulation (EU) No 600/2014, Directive 2014/57/EU and Regulation (EU) No 596/2014 and their respective implementing measures in writing.

Competent authorities may require investment firms to keep additional records to the list identified in Annex I to this Regulation.

L2 Reg, Art 73. Record keeping of rights and obligations of the investment firm and the client (Article 25(5) of Directive 2014/65/EU)

Records which set out the respective rights and obligations of the investment firm and the client under an agreement to provide services, or the terms on which the firm provides services to the client, shall be retained for at least the duration of the relationship with the client.

L2 Reg, Art 74. Record keeping of client orders and decision to deal (Article 16(6) of Directive 2014/65/EU)

An investment firm shall, in relation to every initial order received from a client and in relation to every initial decision to deal taken, immediately record and keep at the disposal of the competent authority at least the details set out in Section 1 of Annex IV to this Regulation to the extent they are applicable to the order or decision to deal in question.

Where the details set out in Section 1 of Annex IV to this Regulation are also prescribed under Articles 25 and 26 of Regulation (EU) No 600/2014, these details should be maintained in a consistent way and according to the same standards prescribed under Articles 25 and 26 of Regulation (EU) No 600/2014.

L2 Reg, Art 75 Record keeping of transactions and order processing (Article 16(6) of Directive 2014/65/EU)

Investment firms shall, immediately after receiving a client order or making a decision to deal to the extent they are applicable to the order or decision to deal in question, record and keep at the disposal of the competent authority at least the details set out in Section 2 of Annex IV.

Where the details set out in Section 2 of Annex IV are also prescribed under Articles 25 and 26 of Regulation (EU) No 600/2014, they shall be maintained in a consistent way and according to the same standards prescribed under Articles 25 and 26 of Regulation (EU) No 600/2014.

L2 Reg, Art 76. Recording of telephone conversations or electronic communications (Article 16(7) of Directive 2014/65/EU)

1. Investment firms shall establish, implement and maintain an effective recording of telephone conversations and electronic communications policy, set out in writing, and appropriate to the size and organisation of the firm, and the nature, scale and complexity of its business. The policy shall include the following content:

(a) the identification of the telephone conversations and electronic communications, including relevant internal telephone conversations and electronic communications, that are subject to the recording requirements in accordance with Article 16(7) of Directive 2014/65/EU; and

(b) the specification of the procedures to be followed and measures to be adopted to ensure the firm's compliance with the third and eighth subparagraphs of Article 16(7) of Directive 2014/65/EU where exceptional circumstances arise and the firm is unable to record the conversation/communication on devices issued, accepted or permitted by the firm. Evidence of such circumstances shall be retained and shall be accessible to competent authorities.

2. Investment firms shall ensure that the management body has effective oversight and control over the policies and procedures relating to the firm's recording of telephone conversations and electronic communications.

3. Investment firms shall ensure that the arrangements to comply with recording requirements are technology-neutral. Firms shall periodically evaluate the effectiveness of the firm's policies and procedures and adopt any such alternative or additional measures and procedures as are necessary and appropriate. At a minimum, such adoption of alternative or additional measures shall occur when a new medium of communication is accepted or permitted for use by the firm.

4. Investment firms shall keep and regularly update a record of those individuals who have firm devices or privately owned devices that have been approved for use by the firm.

5. Investment firms shall educate and train employees in procedures governing the requirements in Article 16(7) of Directive 2014/65/EU.

6. To monitor compliance with the recording and record-keeping requirements in accordance with Article 16(7) of Directive 2014/65/EU, investment firms shall periodically monitor the records of transactions and orders subject to these requirements, including relevant conversations. Such monitoring shall be risk based and proportionate.

7. Investment firms shall demonstrate the policies, procedures and management oversight of the recording rules to the relevant competent authorities upon request.

8. Before investment firms provide investment services and activities relating to the reception, transmission and execution of orders to new and existing clients, firms shall inform the client of the following:

(a) that the conversations and communications are being recorded; and

(b) that a copy of the recording of such conversations with the client and communications with the client will be available on request for a period of five years and, where requested by the competent authority, for a period of up to seven years.

The information referred to in the first sub-paragraph shall be presented in the same language(s) as that used to provide investment services to clients.

9. Investment firms shall record in a durable medium all relevant information related to relevant face-to-face conversations with clients. The information recorded shall include at least the following:

   (a) date and time of meetings;

   (b) location of meetings;

   (c) identity of the attendees;

   (d) initiator of the meetings; and

   (e) relevant information about the client order including the price, volume, type of order and when it shall be transmitted or executed.

10. Records shall be stored in a durable medium, which allows them to be replayed or copied and must be retained in a format that does not allow the original record to be altered or deleted.

Records shall be stored in a medium so that they are readily accessible and available to clients on request.

Firms shall ensure the quality, accuracy and completeness of the records of all telephone recordings and electronic communications.

11. The period of time for the retention of a record shall begin on the date when the record is created.

11.6 Telephone recording and electronic communications (MiFID 2 16(7), Level 2 Regulation Art 76)

MiFID2 Art 16(7). Records shall include the recording of telephone conversations or electronic communications relating to, at least, transactions concluded when dealing on own account and the provision of client order services that relate to the reception, transmission and execution of client orders.

Such telephone conversations and electronic communications shall also include those that are intended to result in transactions concluded when dealing on own account or in the provision of client order services that relate to the reception, transmission and execution of client orders, even if those conversations or communications do not result in the conclusion of such transactions or in the provision of client order services.

For those purposes, an investment firm shall take all reasonable steps to record relevant telephone conversations and electronic communications, made with, sent from or received by equipment provided by the investment firm to an employee or contractor or the use of which by an employee or contractor has been accepted or permitted by the investment firm.

An investment firm shall notify new and existing clients that telephone communications or conversations between the investment firm and its clients that result or may result in transactions will be recorded.

Such a notification may be made once, before the provision of investment services to new and existing clients.

An investment firm shall not provide, by telephone, investment services and activities to clients who have not been notified in advance about the recording of their telephone communications or conversations, where such investment services and activities relate to the reception, transmission and execution of client orders.

Orders may be placed by clients through other channels, however such communications must be made in a durable medium such as mails, faxes, emails or documentation of client orders made at meetings. In particular, the content of relevant face-to-face conversations with a client may be recorded by using written minutes or notes. Such orders shall be considered equivalent to orders received by telephone.

An investment firm shall take all reasonable steps to prevent an employee or contractor from making, sending or receiving relevant telephone conversations and electronic communications on privately-owned equipment which the investment firm is unable to record or copy.

The records kept in accordance with this paragraph shall be provided to the client involved upon request and shall be kept for a period of five years and, where requested by the competent authority, for a period of up to seven years.

L2 Reg, Art 76. Recording of telephone conversations or electronic communications (Article 16(7) of Directive 2014/65/EU)

1. Investment firms shall establish, implement and maintain an effective recording of telephone conversations and electronic communications policy, set out in writing, and appropriate to the size and organisation of the firm, and the nature, scale and complexity of its business. The policy shall include the following content:
   (a) the identification of the telephone conversations and electronic communications, including relevant internal telephone conversations and electronic communications, that are subject to the recording requirements in accordance with Article 16(7) of Directive 2014/65/EU; and
   (b) the specification of the procedures to be followed and measures to be adopted to ensure the firm's compliance with the third and eighth subparagraphs of Article 16(7) of Directive 2014/65/EU where exceptional circumstances arise and the firm is unable to record the conversation/communication on devices issued, accepted or permitted by the firm. Evidence of such circumstances shall be retained and shall be accessible to competent authorities.

2. Investment firms shall ensure that the management body has effective oversight and control over the policies and procedures relating to the firm's recording of telephone conversations and electronic communications.

3. Investment firms shall ensure that the arrangements to comply with recording requirements are technology-neutral. Firms shall periodically evaluate the effectiveness of the firm's policies and procedures and adopt any such alternative or additional measures and procedures as are necessary and appropriate. At a minimum, such adoption of alternative or additional measures shall occur when a new medium of communication is accepted or permitted for use by the firm.

4. Investment firms shall keep and regularly update a record of those individuals who have firm devices or privately owned devices that have been approved for use by the firm.

5. Investment firms shall educate and train employees in procedures governing the requirements in Article 16(7) of Directive 2014/65/EU.

6. To monitor compliance with the recording and record-keeping requirements in accordance with Article 16(7) of Directive 2014/65/EU, investment firms shall periodically monitor the records of transactions and orders subject to these requirements, including relevant conversations. Such monitoring shall be risk based and proportionate.

7. Investment firms shall demonstrate the policies, procedures and management oversight of the recording rules to the relevant competent authorities upon request.

8. Before investment firms provide investment services and activities relating to the reception, transmission and execution of orders to new and existing clients, firms shall inform the client of the following:

   (a) that the conversations and communications are being recorded; and

   (b) that a copy of the recording of such conversations with the client and communications with the client will be available on request for a period of five years and, where requested by the competent authority, for a period of up to seven years.

The information referred to in the first sub-paragraph shall be presented in the same language(s) as that used to provide investment services to clients.

9. Investment firms shall record in a durable medium all relevant information related to relevant face-to-face conversations with clients. The information recorded shall include at least the following:

   (a) date and time of meetings;

   (b) location of meetings;

   (c) identity of the attendees;

   (d) initiator of the meetings; and

   (e) relevant information about the client order including the price, volume, type of order and when it shall be transmitted or executed.

10. Records shall be stored in a durable medium, which allows them to be replayed or copied and must be retained in a format that does not allow the original record to be altered or deleted.

Records shall be stored in a medium so that they are readily accessible and available to clients on request.

Firms shall ensure the quality, accuracy and completeness of the records of all telephone recordings and electronic communications.

11. The period of time for the retention of a record shall begin on the date when the record is created.

11.7 Algo trading (MiFID2 Art 17, Level 2 Regulation Art 18)

MiFID2, Art 17. Algorithmic trading

1. An investment firm that engages in algorithmic trading shall have in place effective systems and risk controls suitable to the business it operates to ensure that its trading systems are resilient and have sufficient capacity, are subject to appropriate trading thresholds and limits and prevent the sending of erroneous orders or the systems otherwise functioning in a way that may create or contribute to a disorderly market. Such a firm shall also have in place effective systems and risk controls to ensure the trading systems cannot be used for any purpose that is contrary to Regulation (EU) No 596/2014 or to the rules of a trading venue to which it is connected. The investment firm shall have in place effective business continuity arrangements to deal with any failure of its trading systems and shall ensure its systems are fully tested and properly monitored to ensure that they meet the requirements laid down in this paragraph.

2. An investment firm that engages in algorithmic trading in a Member State shall notify this to the competent authorities of its home Member State and of the trading venue at which the investment firm engages in algorithmic trading as a member or participant of the trading venue.

   The competent authority of the home Member State of the investment firm may require the investment firm to provide, on a regular or ad-hoc basis, a description of the nature of its algorithmic trading strategies, details of the trading parameters or limits to which the system is subject, the key compliance and risk controls that it has in place to ensure the conditions laid down in paragraph 1 are satisfied and details of the testing of its systems. The competent authority of the home Member State of the investment firm may, at any time, request further information from an investment firm about its algorithmic trading and the systems used for that trading.

   The competent authority of the home Member State of the investment firm shall, on the request of a competent authority of a trading venue at which the investment firm as a member or participant of the trading venue is engaged in algorithmic trading and without undue delay, communicate the information referred to in the second subparagraph that it receives from the investment firm that engages in algorithmic trading.

   The investment firm shall arrange for records to be kept in relation to the matters referred to in this paragraph and shall ensure that those records be sufficient to enable its competent authority to monitor compliance with the requirements of this Directive.

   An investment firm that engages in a high-frequency algorithmic trading technique shall store in an approved form accurate and time sequenced records of all its placed orders, including cancellations of orders, executed orders and quotations on trading venues and shall make them available to the competent authority upon request.

3. An investment firm that engages in algorithmic trading to pursue a market making strategy shall, taking into account the liquidity, scale and nature of the specific market and the characteristics of the instrument traded:

   (a) carry out this market making continuously during a specified proportion of the trading venue's trading hours, except under exceptional circumstances, with the result of providing liquidity on a regular and predictable basis to the trading venue;

   (b) enter into a binding written agreement with the trading venue which shall at least specify the obligations of the investment firm in accordance with point (a); and

   (c) have in place effective systems and controls to ensure that it fulfils its obligations under the agreement referred to in point (b) at all times.

4. For the purposes of this Article and of Article 48 of this Directive, an investment firm that engages in algorithmic trading shall be considered to be pursuing a market making strategy when, as a member or participant of one or more trading venues, its strategy, when dealing on own account, involves posting firm, simultaneous two-way quotes of comparable size and at competitive prices relating to one or more financial instruments on a single trading venue or across different trading venues, with the result of providing liquidity on a regular and frequent basis to the overall market.

5. An investment firm that provides direct electronic access to a trading venue shall have in place effective systems and controls which ensure a proper assessment and review of the suitability of clients using the service, that clients using the service are prevented from exceeding appropriate pre-set trading and credit thresholds, that trading by clients using the service is properly monitored and that appropriate risk controls prevent trading that may create risks to the investment firm itself or that could create or contribute to a disorderly market or could be contrary to Regulation (EU) No 596/2014 or the rules of the trading venue. Direct electronic access without such controls is prohibited.

   An investment firm that provides direct electronic access shall be responsible for ensuring that clients using that service comply with the requirements of this Directive and the rules of the trading venue. The investment firm shall monitor the transactions in order to identify infringements of those rules, disorderly trading conditions or conduct that may involve market abuse and that is to be reported to the competent authority. The investment firm shall ensure that there is a binding written agreement between the investment firm and the client regarding the essential rights and obligations arising from the provision of the service and that under the agreement the investment firm retains responsibility under this Directive.

   An investment firm that provides direct electronic access to a trading venue shall notify the competent authorities of its home Member State and of the trading venue at which the investment firm provides direct electronic access accordingly.

   The competent authority of the home Member State of the investment firm may require the investment firm to provide, on a regular or ad-hoc basis, a description of the systems and controls referred to in first subparagraph and evidence that those have been applied.

The competent authority of the home Member State of the investment firm shall, on the request of a competent authority of a trading venue in relation to which the investment firm provides direct electronic access, communicate without undue delay the information referred to in the fourth subparagraph that it receives from the investment firm.

The investment firm shall arrange for records to be kept in relation to the matters referred to in this paragraph and shall ensure that those records be sufficient to enable its competent authority to monitor compliance with the requirements of this Directive.

6. An investment firm that acts as a general clearing member for other persons shall have in place effective systems and controls to ensure clearing services are only applied to persons who are suitable and meet clear criteria and that appropriate requirements are imposed on those persons to reduce risks to the investment firm and to the market. The investment firm shall ensure that there is a binding written agreement between the investment firm and the person regarding the essential rights and obligations arising from the provision of that service.

7. ESMA shall develop draft regulatory technical standards to specify the following:

   (a) the details of organisational requirements laid down in paragraphs 1 to 6 to be imposed on investment firms providing different investment services and/or activities and ancillary services or combinations thereof, whereby the specifications in relation to the organisational requirements laid down in paragraph 5 shall set out specific requirements for direct market access and for sponsored access in such a way as to ensure that the controls applied to sponsored access are at least equivalent to those applied to direct market access;

   (b) the circumstances in which an investment firm would be obliged to enter into the market making agreement referred to in point (b) of paragraph 3 and the content of such agreements, including the proportion of the trading venue's trading hours laid down in paragraph 3;

   (c) the situations constituting exceptional circumstances referred to in paragraph 3, including circumstances of extreme volatility, political and macroeconomic issues, system and operational matters, and circumstances which contradict the investment firm's ability to maintain prudent risk management practices as laid down in paragraph 1;

   (d) the content and format of the approved form referred to in the fifth subparagraph of paragraph 2 and the length of time for which such records must be kept by the investment firm.

L2 Reg, Art 18 Algorithmic trading (Article 4(1)(39) of Directive 2014/65/EU)

For the purposes of further specifying the definition of algorithmic trading in accordance with Article 4(1)(39) of Directive 2014/65/EU, a system shall be considered as having no or limited human intervention where, for any order or quote generation process or any process to optimise order-execution, an automated system makes decisions at any of the stages of initiating, generating, routing or executing orders or quotes according to pre-determined parameters.

11.8 Conflicts (MIFID2 Art 16(3), 23, 27(2), Level 2 Regulation Art 33 to 35)

MiFID2 Art 16(3). An investment firm shall maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to prevent conflicts of interest as defined in Article 23 from adversely affecting the interests of its clients.

MiFID2, Art 23. Conflicts of interest

1. Member States shall require investment firms to take all appropriate steps to identify and to prevent or manage conflicts of interest between themselves, including their managers, employees and tied agents, or any person directly or indirectly linked to them by control and their clients or between one client and another that arise in the course of providing any investment and ancillary services, or combinations thereof, including those caused by the receipt of inducements from third parties or by the investment firm's own remuneration and other incentive structures.
2. Where organisational or administrative arrangements made by the investment firm in accordance with Article 16(3) to prevent conflicts of interest from adversely affecting the interest of its client are not sufficient to ensure, with reasonable confidence, that risks of damage to client interests will be prevented, the investment firm shall clearly disclose to the client the general nature and/or sources of conflicts of interest and the steps taken to mitigate those risks before undertaking business on its behalf.
3. The disclosure referred to in paragraph 2 shall:
   (a) be made in a durable medium; and
   (b) include sufficient detail, taking into account the nature of the client, to enable that client to take an informed decision with respect to the service in the context of which the conflict of interest arises.
4. The Commission shall be empowered to adopt delegated acts in accordance with Article 89 to:
   (a) define the steps that investment firms might reasonably be expected to take to identify, prevent, manage and disclose conflicts of interest when providing various investment and ancillary services and combinations thereof;
   (b) establish appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of the clients or potential clients of the investment firm.

MiFID2 Art 27(2). An investment firm shall not receive any remuneration, discount or non-monetary benefit for routing client orders to a particular trading venue or execution venue which would infringe the requirements on conflicts of interest or inducements set out in paragraph 1 of this Article and Article 16(3) and Articles 23 and 24.

L2 Reg, Art 33. Conflicts of interest potentially detrimental to a client (Articles 16(3) and 23 of Directive 2014/65/EU)

For the purposes of identifying the types of conflict of interest that arise in the course of providing investment and ancillary services or a combination thereof and whose

existence may damage the interests of a client, investment firms shall take into account, by way of minimum criteria, whether the investment firm or a relevant person, or a person directly or indirectly linked by control to the firm, is in any of the following situations, whether as a result of providing investment or ancillary services or investment activities or otherwise:

(a) the firm or that person is likely to make a financial gain, or avoid a financial loss, at the expense of the client;

(b) the firm or that person has an interest in the outcome of a service provided to the client or of a transaction carried out on behalf of the client, which is distinct from the client's interest in that outcome;

(c) the firm or that person has a financial or other incentive to favour the interest of another client or group of clients over the interests of the client;

(d) the firm or that person carries on the same business as the client;

(e) the firm or that person receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monetary or non-monetary benefits or services.

L2 Reg, Art 34. Conflicts of interest policy (Articles 16(3) and 23 of Directive 2014/65/EU)

1. Investment firms shall establish, implement and maintain an effective conflicts of interest policy set out in writing and appropriate to the size and organisation of the firm and the nature, scale and complexity of its business.

   Where the firm is a member of a group, the policy shall also take into account any circumstances, of which the firm is or should be aware, which may give rise to a conflict of interest arising as a result of the structure and business activities of other members of the group.

2. The conflicts of interest policy established in accordance with paragraph 1 shall include the following content:

   (a) it must identify, with reference to the specific investment services and activities and ancillary services carried out by or on behalf of the investment firm, the circumstances which constitute or may give rise to a conflict of interest entailing a risk of damage to the interests of one or more clients;

   (b) it must specify procedures to be followed and measures to be adopted in order to prevent or manage such conflicts.

3. The procedures and measures referred to in paragraph 2(b) shall be designed to ensure that relevant persons engaged in different business activities involving a conflict of interest of the kind specified in paragraph 2(a) carry on those activities at a level of independence appropriate to the size and activities of the investment firm and of the group to which it belongs, and to the risk of damage to the interests of clients.

For the purposes of paragraph 2(b), the procedures to be followed and measures to be adopted shall include at least those items in the following list that are necessary for the firm to ensure the requisite degree of independence:

(a) effective procedures to prevent or control the exchange of information between relevant persons engaged in activities involving a risk of a conflict of interest where the exchange of that information may harm the interests of one or more clients;

(b) the separate supervision of relevant persons whose principal functions involve carrying out activities on behalf of, or providing services to, clients whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the firm;

(c) the removal of any direct link between the remuneration of relevant persons principally engaged in one activity and the remuneration of, or revenues generated by, different relevant persons principally engaged in another activity, where a conflict of interest may arise in relation to those activities;

(d) measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries out investment or ancillary services or activities;

(e) measures to prevent or control the simultaneous or sequential involvement of a relevant person in separate investment or ancillary services or activities where such involvement may impair the proper management of conflicts of interest.

4. Investment firms shall ensure that disclosure to clients, pursuant to Article 23(2) of Directive 2014/65/EU, is a measure of last resort that shall be used only where the effective organisational and administrative arrangements established by the investment firm to prevent or manage its conflicts of interest in accordance with Article 23 of Directive 2014/65/EU are not sufficient to ensure, with reasonable confidence, that risks of damage to the interests of the client will be prevented.

   The disclosure shall clearly state that the organisational and administrative arrangements established by the investment firm to prevent or manage that conflict are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests of the client will be prevented. The disclosure shall include specific description of the conflicts of interest that arise in the provision of investment and/or ancillary services, taking into account the nature of the client to whom the disclosure is being made. The description shall explain the general nature and sources of conflicts of interest, as well as the risks to the client that arise as a result of the conflicts of interest and the steps undertaken to mitigate these risks, in sufficient detail to enable that client to take an informed decision with respect to the investment or ancillary service in the context of which the conflicts of interest arise.

5. Investment firms shall assess and periodically review, on an at least annual basis, the conflicts of interest policy established in accordance with paragraphs 1 to 4 and shall take all appropriate measures to address any deficiencies. Over-reliance on disclosure of conflicts of interest shall be considered a deficiency in the investment firm's conflicts of interest policy.

L2 Reg, Art 35. Record of services or activities giving rise to detrimental conflict of interest (Article 16(6) of Directive 2014/65/EU)

Investment firms shall keep and regularly update a record of the kinds of investment or ancillary service or investment activity carried out by or on behalf of the firm in which a conflict of interest entailing a risk of damage to the interests of one or more clients has arisen or, in the case of an ongoing service or activity, may arise.

Senior management shall receive on a frequent basis, and at least annually, written reports on situations referred to in this Article.

11.9 Remuneration policies (MiFID2 Art 24(1) and (9), Level 2 Regulation Art 27)

MiFID2 Art 24(1). Member States shall require that, when providing investment services or, where appropriate, ancillary services to clients, an investment firm act honestly, fairly and professionally in accordance with the best interests of its clients and comply, in particular, with the principles set out in this Article and in Article 25.

MiFID2 Art 24(9). Member States shall ensure that investment firms are regarded as not fulfilling their obligations under Article 23 or under paragraph 1 of this Article where they pay or are paid any fee or commission, or provide or are provided with any non-monetary benefit in connection with the provision of an investment service or an ancillary service, to or by any party except the client or a person on behalf of the client, other than where the payment or benefit:

(a) is designed to enhance the quality of the relevant service to the client; and

(b) does not impair compliance with the investment firm's duty to act honestly, fairly and professionally in accordance with the best interest of its clients.

The existence, nature and amount of the payment or benefit referred to in the first subparagraph, or, where the amount cannot be ascertained, the method of calculating that amount, must be clearly disclosed to the client, in a manner that is comprehensive, accurate and understandable, prior to the provision of the relevant investment or ancillary service. Where applicable, the investment firm shall also inform the client on mechanisms for transferring to the client the fee, commission, monetary or non-monetary benefit received in relation to the provision of the investment or ancillary service.

The payment or benefit which enables or is necessary for the provision of investment services, such as custody costs, settlement and exchange fees, regulatory levies or legal fees, and which by its nature cannot give rise to conflicts with the investment firm's duties to act honestly, fairly and professionally in accordance with the best interests of its clients, is not subject to the requirements set out in the first subparagraph.

L2 Reg, Art 27. Remuneration policies and practices (Articles 16, 23 and 24 of Directive 2014/65/EU)

1. Investment firms shall define and implement remuneration policies and practices under appropriate internal procedures taking into account the interests of all the clients of the firm, with a view to ensuring that clients are treated fairly and their interests are not impaired by the remuneration practices adopted by the firm in the short, medium or long term.

Remuneration policies and practices shall be designed in such a way so as not to create a conflict of interest or incentive that may lead relevant persons to favour their own interests or the firm's interests to the potential detriment of any client.

2. Investment firms shall ensure that their remuneration policies and practices apply to all relevant persons with an impact, directly or indirectly, on investment and ancillary services provided by the investment firm or on its corporate behaviour, regardless of the type of clients, to the extent that the remuneration of such persons and similar incentives may create a conflict of interest that encourages them to act against the interests of any of the firm's clients.

3. The management body of the investment firm shall approve, after taking advice from the compliance function, the firm's remuneration policy. The senior management of the investment firm shall be responsible for the day-to-day implementation of the remuneration policy and the monitoring of compliance risks related to the policy.

4. Remuneration and similar incentives shall not be solely or predominantly based on quantitative commercial criteria, and shall take fully into account appropriate qualitative criteria reflecting compliance with the applicable regulations, the fair treatment of clients and the quality of services provided to clients.

   A balance between fixed and variable components of remuneration shall be maintained at all times, so that the remuneration structure does not favour the interests of the investment firm or its relevant persons against the interests of any client.

11.10 Client agreements (MiFID2 Art 24(1), 25(5), Level 2 Regulation Art 58)

MiFID2 Art 24(1). Member States shall require that, when providing investment services or, where appropriate, ancillary services to clients, an investment firm act honestly, fairly and professionally in accordance with the best interests of its clients and comply, in particular, with the principles set out in this Article and in Article 25.

MiFID2 Art 25(5). The investment firm shall establish a record that includes the document or documents agreed between the investment firm and the client that set out the rights and obligations of the parties, and the other terms on which the investment firm will provide services to the client. The rights and duties of the parties to the contract may be incorporated by reference to other documents or legal texts.

L2 Reg, Art 58. Retail and Professional Client agreements (Article 24(1) and 25(5) of Directive 2014/65/EU)

Investment firms providing any investment service or the ancillary service referred to in Section B(1) of Annex I to Directive 2014/65/EU to a client after the date of application of this Regulation shall enter into a written basic agreement with the client, in paper or another durable medium, with the client setting out the essential rights and obligations of the firm and the client. Investment firms providing investment advice shall comply with this obligation only where a periodic assessment of the suitability of the financial instruments or services recommended is performed.

The written agreement shall set out the essential rights and obligations of the parties, and shall include the following:

(a) a description of the services, and where relevant the nature and extent of the investment advice, to be provided;

(b) in case of portfolio management services, the types of financial instruments that may be purchased and sold and the types of transactions that may be undertaken on behalf of the client, as well as any instruments or transactions prohibited; and

(c) a description of the main features of any services referred to in Section B(1) of Annex I to Directive 2014/65/EU to be provided, including where applicable the role of the firm with respect to corporate actions relating to client instruments and the terms on which securities financing transactions involving client securities will generate a return for the client.

11.11 Costs and Charges (MiFID2 24(4), Level 2 Regulation Art 50)

MiFID2 Art 24(4). Appropriate information shall be provided in good time to clients or potential clients with regard to the investment firm and its services, the financial instruments and proposed investment strategies, execution venues and all costs and related charges. That information shall include the following:

(a) when investment advice is provided, the investment firm must, in good time before it provides investment advice, inform the client:

(i) whether or not the advice is provided on an independent basis;

(ii) whether the advice is based on a broad or on a more restricted analysis of different types of financial instruments and, in particular, whether the range is limited to financial instruments issued or provided by entities having close links with the investment firm or any other legal or economic relationships, such as contractual relationships, so close as to pose a risk of impairing the independent basis of the advice provided;

(iii) whether the investment firm will provide the client with a periodic assessment of the suitability of the financial instruments recommended to that client;

(b) the information on financial instruments and proposed investment strategies must include appropriate guidance on and warnings of the risks associated with investments in those instruments or in respect of particular investment strategies and whether the financial instrument is intended for retail or professional clients, taking account of the identified target market in accordance with paragraph 2;

(c) the information on all costs and associated charges must include information relating to both investment and ancillary services, including the cost of advice, where relevant, the cost of the financial instrument recommended or marketed to the client and how the client may pay for it, also encompassing any third-party payments.

The information about all costs and charges, including costs and charges in connection with the investment service and the financial instrument, which are not caused by the occurrence of underlying market risk, shall be aggregated to allow the client to understand the overall cost as well as the cumulative effect on return

of the investment, and where the client so requests, an itemised breakdown shall be provided. Where applicable, such information shall be provided to the client on a regular basis, at least annually, during the life of the investment.

L2 Reg, Art 50. Information on costs and associated charges (Article 24(4) of Directive 2014/65/EU)

1. For the purposes of providing information to clients on all costs and charges pursuant to Article 24(4) of Directive 2014/65/EU, investment firms shall comply with the detailed requirements in paragraphs 2 to 10.

   Without prejudice to the obligations set out in Article 24(4) of Directive 2014/65/EU, investment firms providing investment services to professional clients shall have the right to agree to a limited application of the detailed requirements set out in this Article with these clients. Investment firms shall not be allowed to agree such limitations when the services of investment advice or portfolio management are provided or when, irrespective of the investment service provided, the financial instruments concerned embed a derivative.

   Without prejudice to the obligations set out in Article 24(4) of Directive 2014/65/EU, investment firms providing investment services to eligible counterparties shall have the right to agree to a limited application of the detailed requirements set out in this Article, except when, irrespective of the investment service provided, the financial instruments concerned embed a derivative and the eligible counterparty intends to offer them to its clients.

2. For ex-ante and ex-post disclosure of information on costs and charges to clients, investment firms shall aggregate the following:

   (a) all costs and associated charges charged by the investment firm or other parties where the client has been directed to such other parties, for the investment services(s) and/or ancillary services provided to the client; and

   (b) all costs and associated charges associated with the manufacturing and managing of the financial instruments.

   Costs referred to in points (a) and (b) are listed in Annex II to this Regulation. For the purposes of point (a), third party payments received by investment firms in connection with the investment service provided to a client shall be itemised separately and the aggregated costs and charges shall be totalled and expressed both as a cash amount and as a percentage.

3. Where any part of the total costs and charges is to be paid in or represents an amount of foreign currency, investment firms shall provide an indication of the currency involved and the applicable currency conversion rates and costs. Investments firms shall also inform about the arrangements for payment or other performance.

4. In relation to the disclosure of product costs and charges that are not included in the UCITS KIID, the investment firms shall calculate and disclose these costs, for example, by liaising with UCITS management companies to obtain the relevant information.

5. The obligation to provide in good time a full ex-ante disclosure of information about the aggregated costs and charges related to the financial instrument and to the investment or ancillary service provided shall apply to investment firms in the following situations:

   (a) where the investment firm recommends or markets financial instruments to clients; or

   (b) where the investment firm providing any investment services is required to provide clients with a UCITS KIID or PRIIPs KID in relation to the relevant financial instruments, in accordance with relevant Union legislation.

6. Investment firms that do not recommend or market a financial instrument to the client or are not obliged to provide the client with a KID/KIID in accordance with relevant Union legislation shall inform their clients about all costs and charges relating to the investment and/or ancillary service provided.

7. Where more than one investment firm provides investment or ancillary services to the client, each investment firm shall provide information about the costs of the investment or ancillary services it provides. An investment firm that recommends or markets to its clients the services provided by another firm, shall aggregate the cost and charges of its services together with the cost and charges of the services provided by the other firm. An investment firm shall take into account the costs and charges associated to the provision of other investment or ancillary services by other firms where it has directed the client to these other firms.

8. Where calculating costs and charges on an ex-ante basis, investment firms shall use actually incurred costs as a proxy for the expected costs and charges. Where actual costs are not available, the investment firm shall make reasonable estimations of these costs. Investment firms shall review ex-ante assumptions based on the ex-post experience and shall make adjustment to these assumptions, where necessary.

9. Investment firms shall provide annual ex-post information about all costs and charges related to both the financial instrument(s) and investment and ancillary service(s) where they have recommended or marketed the financial instrument(s) or where they have provided the client with the KID/KIID in relation to the financial instrument(s) and they have or have had an ongoing relationship with the client during the year. Such information shall be based on costs incurred and shall be provided on a personalised basis.

   Investment firms may choose to provide such aggregated information on costs and charges of the investment services and the financial instruments together with any existing periodic reporting to clients.

10. Investment firms shall provide their clients with an illustration showing the cumulative effect of costs on return when providing investment services. Such an illustration shall be provided both on an ex-ante and ex-post basis. Investment firms shall ensure that the illustration meets the following requirements:

    (a) the illustration shows the effect of the overall costs and charges on the return of the investment;

(b) the illustration shows any anticipated spikes or fluctuations in the costs; and

(c) the illustration is accompanied by a description of the illustration.

11.12 Services disclosures (MiFID2 24(3),(4),(5), Level 2 Regulation Art 44, 46, 47, 48)

MiFID2 Art 24(3). All information, including marketing communications, addressed by the investment firm to clients or potential clients shall be fair, clear and not misleading. Marketing communications shall be clearly identifiable as such.

MiFID2 Art 24(4). Appropriate information shall be provided in good time to clients or potential clients with regard to the investment firm and its services, the financial instruments and proposed investment strategies, execution venues and all costs and related charges. That information shall include the following:

(a) when investment advice is provided, the investment firm must, in good time before it provides investment advice, inform the client:

(i) whether or not the advice is provided on an independent basis;

(ii) whether the advice is based on a broad or on a more restricted analysis of different types of financial instruments and, in particular, whether the range is limited to financial instruments issued or provided by entities having close links with the investment firm or any other legal or economic relationships, such as contractual relationships, so close as to pose a risk of impairing the independent basis of the advice provided;

(iii) whether the investment firm will provide the client with a periodic assessment of the suitability of the financial instruments recommended to that client;

(b) the information on financial instruments and proposed investment strategies must include appropriate guidance on and warnings of the risks associated with investments in those instruments or in respect of particular investment strategies and whether the financial instrument is intended for retail or professional clients, taking account of the identified target market in accordance with paragraph 2;

(c) the information on all costs and associated charges must include information relating to both investment and ancillary services, including the cost of advice, where relevant, the cost of the financial instrument recommended or marketed to the client and how the client may pay for it, also encompassing any third-party payments.

The information about all costs and charges, including costs and charges in connection with the investment service and the financial instrument, which are not caused by the occurrence of underlying market risk, shall be aggregated to allow the client to understand the overall cost as well as the cumulative effect on return of the investment, and where the client so requests, an itemised breakdown shall be provided. Where applicable, such information shall be provided to the client on a regular basis, at least annually, during the life of the investment.

MiFID2 Art 24(5). The information referred to in paragraphs 4 and 9 shall be provided in a comprehensible form in such a manner that clients or potential clients are reasonably

able to understand the nature and risks of the investment service and of the specific type of financial instrument that is being offered and, consequently, to take investment decisions on an informed basis. Member States may allow that information to be provided in a standardised format.

L2 Reg, Art 44. Fair, clear and not misleading information requirements (Article 24(3) of Directive 2014/65/EU)

1. Investment firms shall ensure that all information they address to, or disseminate in such a way that it is likely to be received by, retail or professional clients or potential retail or professional clients, including marketing communications, satisfies the conditions laid down in paragraphs 2 to 8.
2. Investment firm shall ensure that the information referred to in paragraph 1 complies with the following conditions:
   (a) the information includes the name of the investment firm,
   (b) the information is accurate and always gives a fair and prominent indication of any relevant risks when referencing any potential benefits of an investment service or financial instrument,
   (c) the information uses a font size in the indication of relevant risks that is at least equal to the predominant font size used throughout the information provided, as well as a layout ensuring such indication is prominent,
   (d) the information is sufficient for, and presented in a way that is likely to be understood by, the average member of the group to whom it is directed, or by whom it is likely to be received,
   (e) the information does not disguise, diminish or obscure important items, statements or warnings,
   (f) the information is consistently presented in the same language throughout all forms of information and marketing materials that are provided to each client, unless the client has accepted to receive information in more than one language,
   (g) the information is up-to-date and relevant to the means of communication used.
3. Where the information compares investment or ancillary services, financial instruments, or persons providing investment or ancillary services, investment firms shall ensure that the following conditions are satisfied:
   (a) the comparison is meaningful and presented in a fair and balanced way;
   (b) the sources of the information used for the comparison are specified;
   (c) the key facts and assumptions used to make the comparison are included.
4. Where the information contains an indication of past performance of a financial instrument, a financial index or an investment service, investment firms shall ensure that the following conditions are satisfied:
   (a) that indication is not the most prominent feature of the communication;

(b) the information must include appropriate performance information which covers the preceding 5 years, or the whole period for which the financial instrument has been offered, the financial index has been established, or the investment service has been provided where less than five years, or such longer period as the firm may decide, and in every case that performance information is based on complete 12-month periods;

(c) the reference period and the source of information is clearly stated;

(d) the information contains a prominent warning that the figures refer to the past and that past performance is not a reliable indicator of future results;

(e) where the indication relies on figures denominated in a currency other than that of the Member State in which the retail client or potential retail client is resident, the currency is clearly stated, together with a warning that the return may increase or decrease as a result of currency fluctuations;

(f) where the indication is based on gross performance, the effect of commissions, fees or other charges are disclosed.

5. Where the information includes or refers to simulated past performance, investment firms shall ensure that the information relates to a financial instrument or a financial index, and the following conditions are satisfied:

(a) the simulated past performance is based on the actual past performance of one or more financial instruments or financial indices which are the same as, or substantially the same as, or underlie, the financial instrument concerned;

(b) in respect of the actual past performance referred to in point (a), the conditions set out in points (a) to (c), (e) and (f) of paragraph 4 are satisfied;

(c) the information contains a prominent warning that the figures refer to simulated past performance and that past performance is not a reliable indicator of future performance.

6. Where the information contains information on future performance, investment firms shall ensure that the following conditions are satisfied:

(a) the information is not based on or refer to simulated past performance;

(b) the information is based on reasonable assumptions supported by objective data;

(c) where the information is based on gross performance, the effect of commissions, fees or other charges is disclosed;

(d) the information is based on performance scenarios in different market conditions (both negative and positive scenarios), and reflects the nature and risks of the specific types of instruments included in the analysis;

(e) the information contains a prominent warning that such forecasts are not a reliable indicator of future performance.

7. Where the information refers to a particular tax treatment, it shall prominently state that the tax treatment depends on the individual circumstances of each client and may be subject to change in the future.

8. The information shall not use the name of any competent authority in such a way that would indicate or suggest endorsement or approval by that authority of the products or services of the investment firm.

L2 Reg, Art 46. General requirements for information to clients (Article 24(4) of Directive 2014/65/EU)

1. Investment firms shall, in good time before a client or potential client is bound by any agreement for the provision of investment services or ancillary services or before the provision of those services, whichever is the earlier to provide that client or potential client with the following information:

   (a) the terms of any such agreement;

   (b) the information required by Article 47 relating to that agreement or to those investment or ancillary services.

2. Investment firms shall, in good time before the provision of investment services or ancillary services to clients or potential clients, to provide the information required under Articles 47 to 50.

3. The information referred to in paragraphs 1 and 2 shall be provided in a durable medium or by means of a website (where it does not constitute a durable medium) provided that the conditions specified in Article 3(2) are satisfied.

4. Investment firms shall notify a client in good time about any material change to the information provided under Articles 47 to 50 which is relevant to a service that the firm is providing to that client. That notification shall be given in a durable medium if the information to which it relates is given in a durable medium.

5. Investment firms shall ensure that information contained in a marketing communication is consistent with any information the firm provides to clients in the course of carrying on investment and ancillary services.

6. Marketing communications containing an offer or invitation of the following nature and specifying the manner of response or including a form by which any response may be made, shall include such of the information referred to in Articles 47 to 50 as is relevant to that offer or invitation:

   (a) an offer to enter into an agreement in relation to a financial instrument or investment service or ancillary service with any person who responds to the communication;

   (b) an invitation to any person who responds to the communication to make an offer to enter into an agreement in relation to a financial instrument or investment service or ancillary service.

However, the first subparagraph shall not apply if, in order to respond to an offer or invitation contained in the marketing communication, the potential client must refer to another document or documents, which, alone or in combination, contain that information.

L2 Reg, Art 47. Information about the investment firm and its services for clients and potential clients (Article 24(4) of Directive 2014/65/EU)

1. Investment firms shall provide clients or potential clients with the following general information, where relevant:
   (a) the name and address of the investment firm, and the contact details necessary to enable clients to communicate effectively with the firm;
   (b) the languages in which the client may communicate with the investment firm, and receive documents and other information from the firm;
   (c) the methods of communication to be used between the investment firm and the client including, where relevant, those for the sending and reception of orders;
   (d) a statement of the fact that the investment firm is authorised and the name and contact address of the competent authority that has authorised it;
   (e) where the investment firm is acting through a tied agent, a statement of this fact specifying the Member State in which that agent is registered;
   (f) the nature, frequency and timing of the reports on the performance of the service to be provided by the investment firm to the client in accordance with Article 25(6) of Directive 2014/65/EU;
   (g) where the investment firm holds client financial instruments or client funds, a summary description of the steps which it takes to ensure their protection, including summary details of any relevant investor compensation or deposit guarantee scheme which applies to the firm by virtue of its activities in a Member State;
   (h) a description, which may be provided in summary form, of the conflicts of interest policy maintained by the firm in accordance with Article 34;
   (i) at the request of the client, further details of that conflicts of interest policy in a durable medium or by means of a website (where that does not constitute a durable medium) provided that the conditions set out Article 3(2) are satisfied.

The information listed in points (a) to (i) shall be provided in good time before the provision of investment services or ancillary services to clients or potential clients.

2. When providing the service of portfolio management, investment firms shall establish an appropriate method of evaluation and comparison such as a meaningful benchmark, based on the investment objectives of the client and the types of financial instruments included in the client portfolio, so as to enable the client for whom the service is provided to assess the firm's performance.

3. Where investment firms propose to provide portfolio management services to a client or potential client, they shall provide the client, in addition to the information required under paragraph 1, with such of the following information as is applicable:

(a) information on the method and frequency of valuation of the financial instruments in the client portfolio;

(b) details of any delegation of the discretionary management of all or part of the financial instruments or funds in the client portfolio;

(c) a specification of any benchmark against which the performance of the client portfolio will be compared;

(d) the types of financial instrument that may be included in the client portfolio and types of transaction that may be carried out in such instruments, including any limits;

(e) the management objectives, the level of risk to be reflected in the manager's exercise of discretion, and any specific constraints on that discretion.

The information listed in points (a) to (e) shall be provided in good time before the provision of investment services or ancillary services to clients or potential clients.

L2 Reg, Art 48. Information about financial instruments (Article 24(4) of Directive 2014/65/EU)

1. Investment firms shall provide clients or potential clients in good time before the provision of investment services or ancillary services to clients or potential clients with a general description of the nature and risks of financial instruments, taking into account, in particular, the client's categorisation as either a retail client, professional client or eligible counterparty. That description shall explain the nature of the specific type of instrument concerned, the functioning and performance of the financial instrument in different market conditions, including both positive and negative conditions, as well as the risks particular to that specific type of instrument in sufficient detail to enable the client to take investment decisions on an informed basis.

2. The description of risks referred to in paragraph 1 shall include, where relevant to the specific type of instrument concerned and the status and level of knowledge of the client, the following elements:

   (a) the risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as bail in;

   (b) the volatility of the price of such instruments and any limitations on the available market for such instruments;

   (c) information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments;

(d) the fact that an investor might assume, as a result of transactions in such instruments, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the instruments;

(e) any margin requirements or similar obligations, applicable to instruments of that type.

3. Where an investment firm provides a retail client or potential retail client with information about a financial instrument that is the subject of a current offer to the public and a prospectus has been published in connection with that offer in accordance with Directive 2003/71/EC, that firm shall in good time before the provision of investment services or ancillary services to clients or potential clients inform the client or potential client where that prospectus is made available to the public.

4. Where a financial instrument is composed of two or more different financial instruments or services, the investment firm shall provide an adequate description of the legal nature of the financial instrument, the components of that instrument and the way in which the interaction between the components affects the risks of the investment.

5. In the case of financial instruments that incorporate a guarantee or capital protection, the investment firm shall provide a client or a potential client with information about the scope and nature of such guarantee or capital protection. When the guarantee is provided by a third party, information about the guarantee shall include sufficient detail about the guarantor and the guarantee to enable the client or potential client to make a fair assessment of the guarantee.

11.13 Investment research/marketing (Level 2 Regulation Art 36, 37)

L2 Reg, Art 36. Investment research and marketing communications (Article 24(3) of Directive 2014/65/EU)

1. For the purposes of Article 37 investment research shall be research or other information recommending or suggesting an investment strategy, explicitly or implicitly, concerning one or several financial instruments or the issuers of financial instruments, including any opinion as to the present or future value or price of such instruments, intended for distribution channels or for the public, and in relation to which the following conditions are met:

   (a) the research or information is labelled or described as investment research or in similar terms, or is otherwise presented as an objective or independent explanation of the matters contained in the recommendation;

   (b) if the recommendation in question were made by an investment firm to a client, it would not constitute the provision of investment advice for the purposes of Directive 2014/65/EU.

2. A recommendation of the type covered by point (35) of Article 3(1) of Regulation (EU) No 596/2014 that does not meet the conditions set out in paragraph 1 shall be treated as a marketing communication for the purposes of Directive 2014/65/EU and investment firms that produce or disseminate that recommendation shall ensure that it is clearly identified as such.

Additionally, firms shall ensure that any such recommendation contains a clear and prominent statement that (or, in the case of an oral recommendation, to the effect that) it has not been prepared in accordance with legal requirements designed to promote the independence of investment research, and that it is not subject to any prohibition on dealing ahead of the dissemination of investment research.

L2 Reg, Art 37. Additional organisational requirements in relation to investment research or marketing communications (Article 16(3) of Directive 2014/65/EU)

1. Investment firms which produce, or arrange for the production of, investment research that is intended or likely to be subsequently disseminated to clients of the firm or to the public, under their own responsibility or that of a member of their group, shall ensure the implementation of all the measures set out in Article 34(3) in relation to the financial analysts involved in the production of the investment research and other relevant persons whose responsibilities or business interests may conflict with the interests of the persons to whom the investment research is disseminated. The obligations in the first subparagraph shall also apply in relation to recommendations referred to in Article 36(2).
2. Investment firms referred to in the first subparagraph of paragraph 1 shall have in place arrangements designed to ensure that the following conditions are satisfied:
   (a) financial analysts and other relevant persons do not undertake personal transactions or trade, other than as market makers acting in good faith and in the ordinary course of market making or in the execution of an unsolicited client order, on behalf of any other person, including the investment firm, in financial instruments to which investment research relates, or in any related financial instruments, with knowledge of the likely timing or content of that investment research which is not publicly available or available to clients and cannot readily be inferred from information that is so available, until the recipients of the investment research have had a reasonable opportunity to act on it;
   (b) in circumstances not covered by point (a), financial analysts and any other relevant persons involved in the production of investment research do not undertake personal transactions in financial instruments to which the investment research relates, or in any related financial instruments, contrary to current recommendations, except in exceptional circumstances and with the prior approval of a member of the firm's legal or compliance function;
   (c) a physical separation exists between the financial analysts involved in the production of investment research and other relevant persons whose responsibilities or business interests may conflict with the interests of the persons to whom the investment research is disseminated or, when considered not appropriate to the size and organisation of the firm as well as the nature, scale and complexity of its business, the establishment and implementation of appropriate alternative information barriers;
   (d) the investment firms themselves, financial analysts, and other relevant persons involved in the production of the investment research do not accept inducements from those with a material interest in the subject-matter of the investment research;

(e) the investment firms themselves, financial analysts, and other relevant persons involved in the production of the investment research do not promise issuers favourable research coverage;

(f) before the dissemination of investment research issuers, relevant persons other than financial analysts, and any other persons are not permitted to review a draft of the investment research for the purpose of verifying the accuracy of factual statements made in that research, or for any purpose other than verifying compliance with the firm's legal obligations, where the draft includes a recommendation or a target price.

For the purposes of this paragraph, 'related financial instrument' shall be any financial instrument the price of which is closely affected by price movements in another financial instrument which is the subject of investment research, and includes a derivative on that other financial instrument.

3. Investment firms which disseminate investment research produced by another person to the public or to clients shall be exempt from complying with paragraph 1 if the following criteria are met:

(a) the person that produces the investment research is not a member of the group to which the investment firm belongs;

(b) the investment firm does not substantially alter the recommendations within the investment research;

(c) the investment firm does not present the investment research as having been produced by it;

(d) the investment firm verifies that the producer of the research is subject to requirements equivalent to the requirements under this Regulation in relation to the production of that research, or has established a policy setting such requirements.

11.14 Inducements (MiFID2 Art 24(9), Level 2 Directive Art 11 to 13)

MiFID2 Art 24(9). Member States shall ensure that investment firms are regarded as not fulfilling their obligations under Article 23 or under paragraph 1 of this Article where they pay or are paid any fee or commission, or provide or are provided with any non-monetary benefit in connection with the provision of an investment service or an ancillary service, to or by any party except the client or a person on behalf of the client, other than where the payment or benefit:

(a) is designed to enhance the quality of the relevant service to the client; and

(b) does not impair compliance with the investment firm's duty to act honestly, fairly and professionally in accordance with the best interest of its clients.

The existence, nature and amount of the payment or benefit referred to in the first subparagraph, or, where the amount cannot be ascertained, the method of calculating that amount, must be clearly disclosed to the client, in a manner that is comprehensive, accurate and understandable, prior to the provision of the relevant investment or ancillary

service. Where applicable, the investment firm shall also inform the client on mechanisms for transferring to the client the fee, commission, monetary or non-monetary benefit received in relation to the provision of the investment or ancillary service.

The payment or benefit which enables or is necessary for the provision of investment services, such as custody costs, settlement and exchange fees, regulatory levies or legal fees, and which by its nature cannot give rise to conflicts with the investment firm's duties to act honestly, fairly and professionally in accordance with the best interests of its clients, is not subject to the requirements set out in the first subparagraph.

L2 Dir, Art 11. Inducements

1. Member States shall require investment firms paying or being paid any fee or commission or providing or being provided with any non-monetary benefit in connection with the provision of an investment service or ancillary service to the client to ensure that all the conditions set out in Article 24(9) of Directive 2014/65/EU and requirements set out in paragraphs 2-5 are met at all times.
2. A fee, commission or non-monetary benefit shall be considered to be designed to enhance the quality of the relevant service to the client if all of the following conditions are met:
   (a) it is justified by the provision of an additional or higher level service to the relevant client, proportional to the level of inducements received, such as:
   (i) the provision of non-independent investment advice on and access to a wide range of suitable financial instruments including an appropriate number of instruments from third party product providers having no close links with the investment firm;
   (ii) the provision of non-independent investment advice combined with either: an offer to the client, at least on an annual basis, to assess the continuing suitability of the financial instruments in which the client has invested; or with another on-going service that is likely to be of value to the client such as advice about the suggested optimal asset allocation of the client; or
   (iii) the provision of access, at a competitive price, to a wide range of financial instruments that are likely to meet the needs of the client, including an appropriate number of instruments from third party product providers having no close links with the investment firm, together with either the provision of added-value tools, such as objective information tools helping the relevant client to take investment decisions or enabling the relevant client to monitor, model and adjust the range of financial instruments in which they have invested, or providing periodic reports of the performance and costs and charges associated with the financial instruments
   (b) it does not directly benefit the recipient firm, its shareholders or employees without tangible benefit to the relevant client;
   (c) it is justified by the provision of an on-going benefit to the relevant client in relation to an on-going inducement.

A fee, commission, or non-monetary benefit shall not be considered acceptable if the provision of relevant services to the client is biased or distorted as a result of the fee, commission or non-monetary benefit.

3. Investment firms shall fulfil the requirements set out in paragraph 2 on an ongoing basis as long as they continue to pay or receive the fee, commission or non-monetary benefit.

4. Investment firms shall hold evidence that any fees, commissions or non-monetary benefits paid or received by the firm are designed to enhance the quality of the relevant service to the client:

   (a) by keeping an internal list of all fees, commissions and non-monetary benefits received by the investment firm from a third party in relation to the provision of investment or ancillary services; and

   (b) by recording how the fees, commissions and non-monetary benefits paid or received by the investment firm, or that it intends to use, enhance the quality of the services provided to the relevant clients and the steps taken in order not to impair the firm's duty to act honestly, fairly and professionally in accordance with the best interests of the client.

5. In relation to any payment or benefit received from or paid to third parties, investment firms shall disclose to the client the following information:

   (a) prior to the provision of the relevant investment or ancillary service, the investment firm shall disclose to the client information on the payment or benefit concerned in accordance with the second subparagraph of Article 24(9) of Directive 2014/65/EU. Minor non-monetary benefits may be described in a generic way. Other non-monetary benefits received or paid by the investment firm in connection with the investment service provided to a client shall be priced and disclosed separately;

   (b) where an investment firm was unable to ascertain on an ex-ante basis the amount of any payment or benefit to be received or paid, and instead disclosed to the client the method of calculating that amount, the firm shall also provide its clients with information of the exact amount of the payment or benefit received or paid on an ex-post basis; and

   (c) at least once a year, as long as (on-going) inducements are received by the investment firm in relation to the investment services provided to the relevant clients, the investment firm shall inform its clients on an individual basis about the actual amount of payments or benefits received or paid. Minor non-monetary benefits may be described in a generic way.

In implementing these requirements, investment firms shall take into account the rules on costs and charges set out in Article 24(4)(c) of Directive 2014/65/EU and in Article 50 of Commission Delegated Regulation (EU) 2017/565 (1).

When more firms are involved in a distribution channel, each investment firm providing an investment or ancillary service shall comply with its obligations to make disclosures to its clients.

L2 Dir, Art 12. Inducements in respect of investment advice on an independent basis or portfolio management services

1. Member States shall ensure that investment firms providing investment advice on an independent basis or portfolio management return to clients any fees, commissions or any monetary benefits paid or provided by any third party or a person acting on behalf of a third party in relation to the services provided to that client as soon as reasonably possible after receipt. All fees, commissions or monetary benefits received from third parties in relation to the provision of independent investment advice and portfolio management shall be transferred in full to the client.

   Investment firms shall set up and implement a policy to ensure that any fees, commissions or any monetary benefits paid or provided by any third party or a person acting on behalf of a third party in relation to the provision of independent investment advice and portfolio management are allocated and transferred to each individual client.

   Investment firms shall inform clients about the fees, commissions or any monetary benefits transferred to them, such as through the periodic reporting statements provided to the client.

2. Investment firms providing investment advice on an independent basis or portfolio management shall not accept non-monetary benefits that do not qualify as acceptable minor non-monetary benefits in accordance with paragraph 3.

3. The following benefits shall qualify as acceptable minor non-monetary benefits only if they are:

   (a) information or documentation relating to a financial instrument or an investment service, is generic in nature or personalised to reflect the circumstances of an individual client;

   (b) written material from a third party that is commissioned and paid for by an corporate issuer or potential issuer to promote a new issuance by the company, or where the third party firm is contractually engaged and paid by the issuer to produce such material on an ongoing basis, provided that the relationship is clearly disclosed in the material and that the material is made available at the same time to any investment firms wishing to receive it or to the general public;

   (c) participation in conferences, seminars and other training events on the benefits and features of a specific financial instrument or an investment service;

   (d) hospitality of a reasonable de minimis value, such as food and drink during a business meeting or a conference, seminar or other training events mentioned under point (c); and

   (e) other minor non-monetary benefits which a Member States deems capable of enhancing the quality of service provided to a client and, having regard to the total level of benefits provided by one entity or group of entities, are of a scale and nature that are unlikely to impair compliance with an investment firm's duty to act in the best interest of the client.

Acceptable minor non-monetary benefits shall be reasonable and proportionate and of such a scale that they are unlikely to influence the investment firm's behaviour in any way that is detrimental to the interests of the relevant client.

Disclosure of minor non-monetary benefits shall be made prior to the provision of the relevant investment or ancillary services to clients. In accordance with Article 11(5) (a) minor non-monetary benefits may be described in a generic way.

L2 Dir, Art 13. Inducements in relation to research

1. Member States shall ensure that the provision of research by third parties to investment firms providing portfolio management or other investment or ancillary services to clients shall not be regarded as an inducement if it is received in return for either of the following:

   (a) direct payments by the investment firm out of its own resources;

   (b) payments from a separate research payment account controlled by the investment firm, provided the following conditions relating to the operation of the account are met:

   (i) the research payment account is funded by a specific research charge to the client;

   (ii) as part of establishing a research payment account and agreeing the research charge with their clients, investment firms set and regularly assess a research budget as an internal administrative measure;

   (iii) the investment firm is held responsible for the research payment account;

   (iv) the investment firm regularly assesses the quality of the research purchased based on robust quality criteria and its ability to contribute to better investment decisions.

With regard to point (b) of the first subparagraph, where an investment firm makes use of the research payment account, it shall provide the following information to clients:

   (a) before the provision of an investment service to clients, information about the budgeted amount for research and the amount of the estimated research charge for each of them;

   (b) annual information on the total costs that each of them has incurred for third party research.

2. Where an investment firm operates a research payment account, Member States shall ensure that the investment firm shall also be required, upon request by their clients or by competent authorities, to provide a summary of the providers paid from this account, the total amount they were paid over a defined period, the benefits and services received by the investment firm, and how the total amount spent from the account compares to the budget set by the firm for that period, noting any rebate or carry-over if residual funds remain in the account. For the purposes of point (b)(i) of paragraph 1, the specific research charge shall:

(a) only be based on a research budget set by the investment firm for the purpose of establishing the need for third party research in respect of investment services rendered to its clients; and

(b) not be linked to the volume and/or value of transactions executed on behalf of the clients.

3. Every operational arrangement for the collection of the client research charge, where it is not collected separately but alongside a transaction commission, shall indicate a separately identifiable research charge and shall fully comply with the conditions set out in point (b) of the first subparagraph of paragraph 1 and in the second subparagraph of paragraph 1.

4. The total amount of research charges received may not exceed the research budget.

5. The investment firm shall agree with clients, in the firm's investment management agreement or general terms of business, the research charge as budgeted by the firm and the frequency with which the specific research charge will be deducted from the resources of the client over the year. Increases in the research budget shall only take place after the provision of clear information to clients about such intended increases. If there is a surplus in the research payment account at the end of a period, the firm should have a process to rebate those funds to the client or to offset it against the research budget and charge calculated for the following period.

6. For the purposes of point (b)(ii) of the first subparagraph of paragraph 1, the research budget shall be managed solely by the investment firm and shall be based on a reasonable assessment of the need for third party research. The allocation of the research budget to purchase third party research shall be subject to appropriate controls and senior management oversight to ensure it is managed and used in the best interests of the firm's clients. Those controls include a clear audit trail of payments made to research providers and how the amounts paid were determined with reference to the quality criteria referred to in paragraph 1(b)(iv). Investment firms shall not use the research budget and research payment account to fund internal research.

7. For the purposes of point (b)(iii) of paragraph 1, the investment firm may delegate the administration of the research payment account to a third party, provided that the arrangement facilitates the purchase of third party research and payments to research providers in the name of the investment firm without any undue delay in accordance with the investment firm's instruction.

8. For the purposes of point (b)(iv) of paragraph 1, investment firms shall establish all necessary elements in a written policy and provide it to their clients. It shall also address the extent to which research purchased through the research payment account may benefit clients' portfolios, including, where relevant, by taking into account investment strategies applicable to various types of portfolios, and the approach the firm will take to allocate such costs fairly to the various clients' portfolios.

9. An investment firm providing execution services shall identify separate charges for these services that only reflect the cost of executing the transaction. The provision of each other benefit or service by the same investment firm to investment firms, established in the Union shall be subject to a separately identifiable charge; the supply of and charges for those benefits or services shall not be influenced or conditioned by levels of payment for execution services.

11.15 Unbundling (MiFID2 Art 24(11))

MiFID2 Art 24(11). When an investment service is offered together with another service or product as part of a package or as a condition for the same agreement or package, the investment firm shall inform the client whether it is possible to buy the different components separately and shall provide for a separate evidence of the costs and charges of each component.

Where the risks resulting from such an agreement or package offered to a retail client are likely to be different from the risks associated with the components taken separately, the investment firm shall provide an adequate description of the different components of the agreement or package and the way in which its interaction modifies the risks.

11.16 Client order handling rules (MiFID2 Art 28, Level 2 Regulation Art 67 to 70)

MiFID2 Art 28. Client order handling rules

1. Member States shall require that investment firms authorised to execute orders on behalf of clients implement procedures and arrangements which provide for the prompt, fair and expeditious execution of client orders, relative to other client orders or the trading interests of the investment firm.

   Those procedures or arrangements shall allow for the execution of otherwise comparable client orders in accordance with the time of their reception by the investment firm.

2. Member States shall require that, in the case of a client limit order in respect of shares admitted to trading on a regulated market or traded on a trading venue which are not immediately executed under prevailing market conditions, investment firms are, unless the client expressly instructs otherwise, to take measures to facilitate the earliest possible execution of that order by making public immediately that client limit order in a manner which is easily accessible to other market participants. Member States may decide that investment firms comply with that obligation by transmitting the client limit order to a trading venue. Member States shall provide that the competent authorities may waive the obligation to make public a limit order that is large in scale compared with normal market size as determined under Article 4 of Regulation (EU) No 600/2014.

3. The Commission shall be empowered to adopt delegated acts in accordance with Article 89 to define:

   (a) the conditions and nature of the procedures and arrangements which result in the prompt, fair and expeditious execution of client orders and the situations in which or

types of transaction for which investment firms may reasonably deviate from prompt execution so as to obtain more favourable terms for clients;

(b) the different methods through which an investment firm can be deemed to have met its obligation to disclose not immediately executable client limit orders to the market.

L2 Reg, Art 67. General principles (Articles 28(1) and 24(1) of Directive 2014/65/EU)

1. Investment firms shall satisfy the following conditions when carrying out client orders:

   (a) ensure that orders executed on behalf of clients are promptly and accurately recorded and allocated;

   (b) carry out otherwise comparable client orders sequentially and promptly unless the characteristics of the order or prevailing market conditions make this impracticable, or the interests of the client require otherwise;

   (c) inform a retail client about any material difficulty relevant to the proper carrying out of orders promptly upon becoming aware of the difficulty.

2. Where an investment firm is responsible for overseeing or arranging the settlement of an executed order, it shall take all reasonable steps to ensure that any client financial instruments or client funds received in settlement of that executed order are promptly and correctly delivered to the account of the appropriate client.

3. An investment firm shall not misuse information relating to pending client orders, and shall take all reasonable steps to prevent the misuse of such information by any of its relevant persons.

L2 Reg, Art 68 Aggregation and allocation of orders (Articles 28(1) and 24(1) of Directive 2014/65/EU)

1. Investment firms shall not carry out a client order or a transaction for own account in aggregation with another client order unless the following conditions are met:

   (a) it is unlikely that the aggregation of orders and transactions will work overall to the disadvantage of any client whose order is to be aggregated;

   (b) it is disclosed to each client whose order is to be aggregated that the effect of aggregation may work to its disadvantage in relation to a particular order;

   (c) an order allocation policy is established and effectively implemented, providing for the fair allocation of aggregated orders and transactions, including how the volume and price of orders determines allocations and the treatment of partial executions.

2. Where an investment firm aggregates an order with one or more other client orders and the aggregated order is partially executed, it shall allocate the related trades in accordance with its order allocation policy.

L2 Reg, Art 69. Aggregation and allocation of transactions for own account (Articles 28(1) and 24(1) of Directive 2014/65/EU)

1. Investment firms which have aggregated transactions for own account with one or more client orders shall not allocate the related trades in a way that is detrimental to a client.

2. Where an investment firm aggregates a client order with a transaction for own account and the aggregated order is partially executed, it shall allocate the related trades to the client in priority to the firm.

   Where an investment firm is able to demonstrate on reasonable grounds that without the combination it would not have been able to carry out the order on such advantageous terms, or at all, it may allocate the transaction for own account proportionally, in accordance with its order allocation policy referred to in Article 68(1) c).

3. As part of the order allocation policy referred to in Article 68(1)(c), investment firms shall put in place procedures designed to prevent the reallocation, in a way that is detrimental to the client, of transactions for own account which are executed in combination with client orders.

L2 Reg, Art 70. Prompt fair and expeditious execution of client orders and publication of unexecuted client limit orders for shares traded on a trading venue (Article 28 of Directive 2014/65/ EU)

1. A client limit order in respect of shares admitted to trading on a regulated market or traded on a trading venue which have not been immediately executed under prevailing market conditions as referred to in Article 28(2) of Directive 2014/65/EU shall be considered available to the public when the investment firm has submitted the order for execution to a regulated market or a MTF or the order has been published by a data reporting services provider located in one Member State and can be easily executed as soon as market conditions allow.

2. Regulated markets and MTFs shall be prioritised according to the firm's execution policy to ensure execution as soon as market conditions allow.

SCHEDULE 1
SECURITIES FINANCING EXEMPTIONS

1. MiFIR, Article 1(5a) states that Titles II and III of MiFIR (Articles 3 to 23) do not apply to securities financing transactions (as defined under SFTR). This means that none of the requirements of such provisions are applicable to securities lending transactions, including the following:

   - requirement for market operators and investment firms operating a trading venue to make public current bid and offer prices and the depth of trading interests at those prices which are advertised through their systems for shares, depositary receipts, ETFs, certificates and other similar financial instruments traded on a trading venue[57].
   - requirement for market operators and investment firms operating a trading venue to make public the price, volume and time of transactions executed in respect of shares, depositary receipts, ETFs, certificates and other similar financial instruments traded on that trading venue[58].
   - requirement for market operators and investment firms operating a trading venue to make public current bid and offer prices and the depth of trading interests at those prices which are advertised through their systems for bonds, and structured finance products, emission allowances, derivatives traded on a trading venue, and package orders [59].
   - requirement for market operators and investment firms operating a trading venue to make public the price, volume and time of transactions executed in respect of bonds, structured finance products, emission allowances, and derivatives traded on a trading venue[60].
   - requirement for firms to make public firm quotes in respect of those shares, depositary receipts, ETFs, certificates and other similar financial instruments traded on a trading venue for which they are systematic internalisers and for which there is a liquid market[61].
   - requirement for firms to make public firm quotes in respect of bonds, structured finance products, emission allowances and derivatives traded on a trading venue for which they are systematic internalisers and for which there is a liquid market[62].

57. MiFIR (Regulation (EU) No 600/2014), Article 3(1)
58. MiFIR (Regulation (EU) No 600/2014), Article 6(1)
59. MiFIR (Regulation (EU) No 600/2014), Article 8(1)
60. MiFIR (Regulation (EU) No 600/2014), Article 10(1)
61. MiFIR (Regulation (EU) No 600/2014), Article 14(1)
62. MiFIR (Regulation (EU) No 600/2014), Article 18(1)

- requirement for firms which, either on own account or on behalf of clients, conclude transactions in shares, depositary receipts, ETFs, certificates and other similar financing instruments traded on a trading venue, to make public the volume and price of those transactions and the time at which they were concluded[63].
- requirement for firms which, either on own account or on behalf of clients, conclude transactions in bonds, structured finance products, emission allowances and derivatives traded on a trading venue, to make public the volume and price of those transactions and the time at which they were concluded[64].
- requirement for firm to ensure trades it undertakes in shares admitted to trading on a regulated market, or traded on a trading venue, take place on a regulated market, MTF or systematic internaliser, or a third-country trading venue assessed as equivalent[65].
- requirement for firm that operates an internal matching system which executes client orders in shares, depositary receipts, ETFs, certificates and other similar financial instruments on a multilateral basis to ensure it is authorised as an MTF[66].

2. RTS 22[67] states that for the purposes of MiFIR Article 26 (obligation to report transactions) the term "transaction" does not include securities financing transactions as defined in the SFTR, unless a member of the European System of Central Banks is counterparty to the securities financing transaction.[68]

However, it should be noted that item 65 in Table 2 of RTS 22 includes the following: "Securities financing transaction indicator – 'true' shall be populated where the transaction falls within the scope of activity but is exempted from reporting under Regulation (EU) 2015/2365. 'false' otherwise."

63. MiFIR (Regulation (EU) No 600/2014), Article 20(1)
64. MiFIR (Regulation (EU) No 600/2014), Article 21(1)
65. MiFIR (Regulation (EU) No 600/2014), Article 23(1)
66. MiFIR (Regulation (EU) No 600/2014), Article 23(2)
67. RTS 22 (Commission Delegated Regulation (EU) 2017/590 of 28 July 2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regard to regulatory technical standards for the reporting of transactions to competent authorities), Art 2(5)(a)
68. Although generally RTS 22 applies from 3 January 2018, this limited reporting requirement respecting securities financing transactions only applies 12 months after the date of entry into force of the delegated act adopted by the Commission pursuant to SFTR, Article 4(9), i.e. the same time as when the obligations under SFTR, Article 4(1) will apply to financial counterparties referred to in SFTR Article 3(3)(a) and (b) (investment firms authorised under MiFID and credit institutions authorised in the EU), and third country entities referred to SFTR Article 3(3)(i) which would require authorisation or registration in accordance with SFTR, Article 3(3)(a) and (b) if they were EU entities.

3. RTS 27[69] concerns the specific content, the format and the periodicity of the data to be published by execution venues[70] relating to the quality of execution of transactions, and contains no specific exemption for securities financing transactions, but ESMA has stated that it considers that the best execution reporting requirements set out in RTS 27 should not apply to securities financing transactions[71].

RTS 28[72] contains rules on the content and the format of information to be published by investment firms on an annual basis in relation to client orders executed on trading venues, systematic internalisers, market makers or other liquidity providers or entities that perform a similar function to those performed by any of the foregoing in a third country. The main publication obligation under Article 3(1) specifically excludes "orders in Securities Financing Transactions (SFTs)", but, in relation to securities financing transactions, Article 3(2) imposes a separate obligation regarding publication of the top five execution venues in terms of trading volumes for all executed client orders in SFTs, and Article 3(3) (requiring publication for each class of financial instruments, a summary of the analysis and conclusions they draw from their detailed monitoring of the quality of execution obtained on the execution venues where they executed all client orders in the previous year) will also apply.

69. RTS 27 (Commission Delegated Regulation (EU) 2017/575 of 8 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council on markets in financial instruments with regard to regulatory technical standards concerning the data to be published by execution venues on the quality of execution of transactions)

70. The term "execution venue" is not defined, but Article 1 of RTS 27 states that it applies to "trading venues [this term is defined in MiFID2 to mean a regulated market, MTF or OTF], systematic internalisers, market makers, or other liquidity providers". This is similar to the definition in the MiFID2 Level 2 Regulation, Article 64(1), which states "For the purposes of this Article and Articles 65 and 66, 'execution venue' includes a regulated market, an MTF, an OTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing."

71. ESMA Q&A on MiFID II and MiFIR investor protection and intermediaries topics: "**Question 15** [Last update: 10 July 2017] *Do the RTS 27 reporting requirements apply to Securities Financing Transactions (SFTs)?*

    Answer 15 - Article 1(5)(a) of MiFIR, subsequent to amending Regulation (EU) 2016/1033 of 23 June 2016, states that SFTs are not subject to the pre and post trade transparency obligations set out in Title II and III of MiFIR. While no specific exemption was included with respect to the RTS 27 best execution reporting obligations, Recital 10 of RTS 27 refers to the need for regulatory consistency between its requirements and those on post trade transparency. In this context, ESMA considers that the best execution reporting requirements set out in RTS 27 should not apply to SFTs.

    ESMA wishes to make clear that, irrespective of the above clarification concerning the application of RTS 27 to SFTs, the MiFID II best execution requirements otherwise apply to investment firms when carrying out SFTs.

    ESMA also wishes to clarify that while RTS 27 would not apply to SFTs, this would not lead to a complete absence of execution quality reports for SFTs, as RTS 28 explicitly requires investment firms to report, inter alia, on order routing behaviours specifically with respect to SFTs and to provide a summary on the quality of execution obtained. Investment firms should also note that RTS 28 already makes specific reference to how data concerning SFTs should be published."

72. RTS 28 (Commission Delegated Regulation (EU) 2017/576 of 8 June 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to regulatory technical standards for the annual publication by investment firms of information on the identity of execution venues and on the quality of execution)

SCHEDULE 2
SUMMARY TABLE

MIFID2 LEGISLATION SUMMARY

Securities lending

This summary table does not consider specific requirements applicable to provision of investment advice, underwriting, placing or pricing of offerings, or SMEs.

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Application	M2 Art 1(1)			Directive applies to investment firms, market operators, data reporting service providers, and third-country firms providing investment services or performing investment activities through the establishment of a branch in the Union.	Yes	Yes	Yes	Yes	All requirements generally apply where the client is an ecp, except as noted (see M2 Art 30, considered below). Note that "client" is defined in M2 Art 4(1)(9) to mean "any natural or legal person to whom an investment firm provides investment or ancillary services" therefore references to a "client" include an ecp unless otherwise stated.
	M2 Art 1(3).			Rules applicable to credit institutions authorised under Directive 2013/36/EU when providing one or more investment services and/or performing investment activities: (a) Article 2(2), Article 9(3) and Articles 14 and 16 to 20, (b) Chapter II of Title II excluding second subparagraph of Article 29(2), (c) Chapter III of Title II excluding Article 34(2) and (3) and Article 35(2) to (6) and (9), (d) Articles 67 to 75 and Articles 80, 85 and 86.	Yes	Yes	Yes	Yes	
	M2 Art 1(5)			Article 17(1) to (6) shall also apply to members or participants of regulated markets and MTFs who are not required to be authorised under this Directive pursuant to points (a), (e), (i) and (j) of Article 2(1).	Yes	Yes	Yes	Yes	
	M2 Art 1(7)			All multilateral systems in financial instruments shall operate either in accordance with the provisions of Title II concerning MTFs or OTFs or the provisions of Title III concerning regulated markets. Any investment firms which, on an organised, frequent, systematic and substantial basis, deal on own account when executing client orders outside a regulated market, an MTF or an OTF shall operate in accordance with Title III of Regulation (EU) No 600/2014 (MiFIR).					Relevant if arrangements for providing relevant services constitute an MTF, OTF or SI. Note specific exemption from MiFIR Title II and Title III for securities financing transactions in MiFIR Art 1(5a).

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
				Without prejudice to Articles 23 and 28 of Regulation (EU) No 600/2014, all transactions in financial instruments as referred to in the first and the second subparagraphs which are not concluded on multilateral systems or systematic internalisers shall comply with the relevant provisions of Title III of Regulation (EU) No 600/2014.					
	M2 Art 2(1)	RTS 20 (Criteria to establish when an activity is considered to be ancillary to the main business)		This Directive shall not apply to: (b) persons providing investment services exclusively for their parent undertakings, for their subsidiaries or for other subsidiaries of their parent undertakings;					Exemptions may apply, depending on context of services.
				(f) persons providing investment services consisting exclusively in the administration of employee-participation schemes;					
				(g) persons providing investment services which only involve both the administration of employee-participation schemes and the provision of investment services exclusively for their parent undertakings, for their subsidiaries or for other subsidiaries of their parent undertakings;					
				(i) collective investment undertakings and pension funds whether coordinated at Union level or not and the depositaries and managers of such undertakings;					
Passport	M2 Art 34	RTS re MiFID2 Art 34(8), 3rd subpara, Art 35(11), 3rd subpara (Passporting) ITS re MiFID2 Art 34(9) and 35(12)		Passport arrangements. NB: "Ancillary services may only be provided together with an investment service and/or activity."	Yes	Yes	Yes	Yes	
Branch	M2 Art 35			Branch arrangements. NB. "Ancillary services may only be provided together with an investment service and/or activity."	Yes	Yes	Yes	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
	M2 Art 35(8)			The competent authority of the Member State in which the branch is located shall assume responsibility for ensuring that the services provided by the branch within its territory comply with the obligations laid down in Articles 24, 25, 27, 28, of this Directive and Articles 14 to 26 of Regulation (EU) No 600/2014 and the measures adopted pursuant thereto by the host Member State where allowed in accordance with Article 24(12). The competent authority of the Member State in which the branch is located shall have the right to examine branch arrangements and to request such changes as are strictly needed to enable the competent authority to enforce the obligations under Articles 24, 25, 27, 28 of this Directive and Articles 14 to 26 of Regulation (EU) No 600/2014 and measures adopted pursuant thereto with respect to the services and/or activities provided by the branch within its territory.					
Third country firms	M2 Arts 39 to 42			Rules regarding operations of third country firms. NB Art 41(2): The branch of the third-country firm authorised in accordance with paragraph 1, shall comply with the obligations laid down in Articles 16 to 20, 23, 24, 25 and 27, Article 28(1), and Articles 30, 31 and 32 of this Directive and in Articles 3 to 26 of Regulation (EU) No 600/2014 and the measures adopted pursuant thereto and shall be subject to the supervision of the competent authority in the Member State where the authorisation was granted. Member States shall not impose any additional requirements on the organisation and operation of the branch in respect of the matters covered by this Directive and shall not treat any branch of third-country firms more favourably than Union firms.	Yes	Yes	Yes	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Execution of client orders	M2 Art 4(1)(5)			'execution of orders on behalf of clients' means acting to conclude agreements to buy or sell one or more financial instruments on behalf of clients and includes the conclusion of agreements to sell financial instruments issued by an investment firm or a credit institution at the moment of their issuance;	Yes	Yes	No	Yes	
Dealing on own account	M2 Art 4(1)(6)			'dealing on own account' means trading against proprietary capital resulting in the conclusion of transactions in one or more financial instruments;	No	Yes	Yes	No	
	M2 Recital (24)			Dealing on own account when executing client orders should include firms executing orders from different clients by matching them on a matched principal basis (back-to-back trading), which should be regarded as acting as principal and should be subject to the provisions of this Directive covering both the execution of orders on behalf of clients and dealing on own account.	No	Yes	Yes	No	Principal to principal lending on a matched basis for clients will require compliance with both obligations for dealing on own account, and obligations for execution of orders on behalf of clients.
Portfolio management	M2 Art 4(1)(8)			'portfolio management' means managing portfolios in accordance with mandates given by clients on a discretionary client-by-client basis where such portfolios include one or more financial instruments;	Possible	Possible	No	Yes	
	M2 Art 4(1) (19)			'multilateral system' means any system or facility in which multiple third-party buying and selling trading interests in financial instruments are able to interact in the system;					Relevant if arrangements for providing relevant services constitute a multilateral system.
Systematic internaliser	M2 Art 4(1) (20)			'systematic internaliser' means an investment firm which, on an organised, frequent systematic and substantial basis, deals on own account when executing client orders outside a regulated market, an MTF or an OTF without operating a multilateral system;					Relevant if arrangements for providing relevant services constitute SI.

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
				The frequent and systematic basis shall be measured by the number of OTC trades in the financial instrument carried out by the investment firm on own account when executing client orders. The substantial basis shall be measured either by the size of the OTC trading carried out by the investment firm in relation to the total trading of the investment firm in a specific financial instrument or by the size of the OTC trading carried out by the investment firm in relation to the total trading in the Union in a specific financial instrument. The definition of a systematic internaliser shall apply only where the pre-set limits for a frequent and systematic basis and for a substantial basis are both crossed or where an investment firm chooses to opt-in under the systematic internaliser regime; NB. Proposed amendment published by Commission 19/6/2017: "Article 16a Participation in matching arrangements An investment firm shall not be considered to be dealing on own account for the purposes of Article 4(1)(20) of Directive 2014/65/EU where that investment firm participates in matching arrangements with the objective or consequence of carrying out de facto riskless back-to-back transactions in a financial instrument outside a trading venue".					
	L2 Reg, Art 12 - 16			Further detail re systematic internaliser for shares, and various other types of assets.					

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Regulated market	M2 Art 4(1) (21)			'regulated market' means a multilateral system operated and/ or managed by a market operator, which brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments – in the system and in accordance with its non-discretionary rules – in a way that results in a contract, in respect of the financial instruments admitted to trading under its rules and/or systems, and which is authorised and functions regularly and in accordance with Title III of this Directive;					Relevant if arrangements for providing relevant services constitute a regulated market.
MTF	M2 Art 4(1) (22)			'multilateral trading facility' or 'MTF' means a multilateral system, operated by an investment firm or a market operator, which brings together multiple third-party buying and selling interests in financial instruments – in the system and in accordance with non-discretionary rules – in a way that results in a contract in accordance with Title II of this Directive;					Relevant if arrangements for providing relevant services constitute an MTF.
OTF	M2 Art 4(1) (23)			'organised trading facility' or 'OTF' means a multilateral system which is not a regulated market or an MTF and in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in the system in a way that results in a contract in accordance with Title II of this Directive;					Relevant if arrangements for providing relevant services constitute an OTF.
Trading venue	M2 Art 4(1) (24)			'trading venue' means a regulated market, an MTF or an OTF;					Relevant if arrangements for providing relevant services constitute a regulated market, MTF or OTF.
Execution Venue	L2 Reg, Art 64(1)			"For the purposes of this Article and Articles 65 and 66, 'execution venue' includes a regulated market, an MTF, an OTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing."					Note difference from definition of trading venue.

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Matched principal	M2 Art 4(1) (38)			'matched principal trading' means a transaction where the facilitator interposes itself between the buyer and the seller to the transaction in such a way that it is never exposed to market risk throughout the execution of the transaction, with both sides executed simultaneously, and where the transaction is concluded at a price where the facilitator makes no profit or loss, other than a previously disclosed commission, fee or charge for the transaction;	No	Yes	No	Yes	
	M2 Recital (24)			Dealing on own account when executing client orders should include firms executing orders from different clients by matching them on a matched principal basis (back-to-back trading), which should be regarded as acting as principal and should be subject to the provisions of this Directive covering both the execution of orders on behalf of clients and dealing on own account.	No	Yes	No	Yes	
Algo trading	M2 Art 4(1) (39)			'algorithmic trading' means trading in financial instruments where a computer algorithm automatically determines individual parameters of orders such as whether to initiate the order, the timing, price or quantity of the order or how to manage the order after its submission, with limited or no human intervention, and does not include any system that is only used for the purpose of routing orders to one or more trading venues or for the processing of orders involving no determination of any trading parameters or for the confirmation of orders or the post-trade processing of executed transactions;					May be relevant to securities lending, depending on structure.
	L2 Reg, Art 18			Further detail re algo trading.					

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Securities financing transactions	L2 Dir, Art 1(3)			"securities financing transaction" means transactions as defined in Article 3 point (11) of Regulation (EU) 2015/2365 on transparency of securities financing transactions and of reuse.	Yes	Yes	Yes	Yes	
	SFTR Art 3(11)			(11) 'securities financing transaction' or 'SFT' means: (a) a repurchase transaction; (b) securities or commodities lending and securities or commodities borrowing; (c) a buy-sell back transaction or sell-buy back transaction; (d) a margin lending transaction; (9) 'repurchase transaction' means a transaction governed by an agreement by which a counterparty transfers securities, commodities, or guaranteed rights relating to title to securities or commodities where that guarantee is issued by a recognised exchange which holds the rights to the securities or commodities and the agreement does not allow a counterparty to transfer or pledge a particular security or commodity to more than one counterparty at a time, subject to a commitment to repurchase them, or substituted securities or commodities of the same description at a specified price on a future date specified, or to be specified, by the transferor, being a repurchase agreement for the counterparty selling the securities or commodities and a reverse repurchase agreement for the counterparty buying them;	Yes	Yes	Yes	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
				(7) 'securities or commodities lending' or 'securities or commodities borrowing' means a transaction by which a counterparty transfers securities or commodities subject to a commitment that the borrower will return equivalent securities or commodities on a future date or when requested to do so by the transferor, that transaction being considered as securities or commodities lending for the counterparty transferring the securities or commodities and being considered as securities or commodities borrowing for the counterparty to which they are transferred; (8) 'buy-sell back transaction' or 'sell-buy back transaction' means a transaction by which a counterparty buys or sells securities, commodities, or guaranteed rights relating to title to securities or commodities, agreeing, respectively, to sell or to buy back securities, commodities or such guaranteed rights of the same description at a specified price on a future date, that transaction being a buy-sell back transaction for the counterparty buying the securities, commodities or guaranteed rights, and a sell-buy back transaction for the counterparty selling them, such buy-sell back transaction or sell-buy back transaction not being governed by a repurchase agreement or by a reverse-repurchase agreement within the meaning of point (9); (10) 'margin lending transaction' means a transaction in which a counterparty extends credit in connection with the purchase, sale, carrying or trading of securities, but not including other loans that are secured by collateral in the form of securities;					

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Title transfer collateral arrangement	M2 Recital (52)			"title transfer financial collateral arrangements as defined under Directive 2002/47/EC of the European Parliament and of the Council"	Yes	Yes	Yes	Yes	Relevant where collateral is provided by title transfer.
	Directive 2002/47/EC (Financial Collateral Directive) Article 2(1)(b)			'title transfer financial collateral arrangement' means an arrangement, including repurchase agreements, under which a collateral provider transfers full ownership of financial collateral to a collateral taker for the purpose of securing or otherwise covering the performance of relevant financial obligations;					
General									
	M2 Arts 5-10, 14,15	RTS re MiFID2 Art 7(4) (Authorisation) ITS re MIFID2 Art 7(5), 3rd subpara (Authorisation)		Authorisation requirements	Yes	Yes	Yes	Yes	
	M2 Art 11-13			Notification re proposed acquisition of relevant holding in investment firm.					Unlikely in securities lending context.
	M2 16(2)			Adequate policies and procedures to ensure compliance	Yes	Yes	Yes	Yes	
	L2 Reg, Art 21			General organisational requirements	Yes	Yes	Yes	Yes	
	L2 Reg, Art 22			Compliance. Increased obligations for compliance function: – annual report to management body, monitoring operations of complaints-handling process, establish a risk-based monitoring programme – compliance officer to be appointed and replaced by management body, must report on ad hoc basis to management body when detects significant risk of failure by firm to comply with MiFID obligations – firm to assess effectiveness and review regularly if using exception allowing compliance officer to be involved in services monitored	Yes	Yes	Yes	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
	L2 Reg, Art 25, 26			Senior management, complaints handling Applies to all clients and potential clients, not just retail More detailed requirements regarding policy Firms require to establish a complaints management function (may be carried out by compliance function).	Yes	Yes	Yes	Yes	
Remuneration	M2, Art 24(10) L2 Reg, Remuneration policies (Art 27)		SYSC 19F	Remuneration policy not to conflict with duty to act in clients' bests interests. New policies required, to apply to all persons impacting investment and ancillary services.	Yes	Yes	Yes	No	
Personal transactions	M2 Art 16(2) L2 Reg, Art 28, 29		COBS 11.7A	Rules re personal transactions	Yes	Yes	Yes	Yes	
Conflicts	M2 16(3), first para M2 Art 23		SYSC 10	Effective arrangements to prevent conflicts from adversely affecting client interests. Appropriate steps to indentify, and prevent or manage conflicts.	Yes	Yes	No	Yes	
	L2 Reg, Art 33			Conflicts of interest potentially detrimental to client	Yes	Yes	No	Yes	
	L2 Reg, Art 34			Conflicts policy. Obligations more onerous (reference now to "risk" rather than "material" risk, procedures are to "prevent" not just "manage" conflicts). Disclosure of conflicts to be only a last resort, and to include specific description of conflicts that arise. Conflicts policy to be reviewed at least annually and deficiencies addressed; over-reliance on disclosure will be a deficiency.	Yes	Yes	No	Yes	
	L2 Reg, Art 35			Conflicts record. Obligation more onerous, as records must refer to conflicts entailing any risk of damage to clients, not just "material" risk. Senior management must receive reports of the above "on a frequent basis, and at least annually".	Yes	Yes	No	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
	L2 Reg, Art 37		COBS 12.2.19EU	Additional conflicts requirements re persons producing investment research or marketing communications.	Yes	Yes	No	Yes	Relevant if produce such information.
Manufacturing	M2, 16(3), paras 2 to 7 M2, 24(2)		PROD 3.2	Obligations re manufacturing/ offering/marketing/ recommending financial instruments.	No	No	No	No re M2 Art 24	Only PROD 3.3.1R is disapplied re ecp business
	L2 Dir, Art 9		PROD 3	Product governance obligations for investment firms manufacturing financial instruments	No	No	No	Yes in part	Only PROD 3.3.1R is disapplied re ecp business
Distributors	L2 Dir, Art 10		PROD 3.3	Product governance obligations for distributors	Yes	Yes	Yes (if an investment service)	Yes in part	Only PROD 3.3.1R is disapplied re ecp business Note - UK FCA considers portfolio management is an activity constituting distribution.
Systems and resources	M2 Art 16(4)		SYSC 4.1.6R	Appropriate systems and resources to ensure continuity of investment services.	Yes	Yes	Yes	Yes	
Outsourcing	M2 Art 16(5)		SYSC 4.1.1R 8.1.1R	Outsourcing.				Yes	Relevant if outsource functions.
	L2 Reg, Art 23, 24		SYSC 10A.8	Risk management, internal audit				Yes	
	L2 Reg, Arts 30 – 32		SYSC 1 Annex 1 re application	Arguably clarificatory changes, BUT – must be able to terminate outsourcing immediately when in interests of clients – continuity/quality of outsourced functions to be maintained if outsourcing terminated – service provider must only outsource with consent in writing from firm – requirements regarding outsourcing of portfolio management to a third country apply in relation to all clients, not just retail clients				Yes	
			SYSC 4.1.1R	Risk assessment. Security mechanisms.				Yes	
Records	M2 Art 16(6)		COBS 3.8.2R SYSC 9.1.1AR	Records	Yes	Yes	Yes	Yes	
	L2 Reg, Art 35		SYSC 10.1	Records re conflicts.	Yes	Yes	Yes	Yes	
	L2 Reg, Art 72		SYSC 1 Annex 1 Table C	Retention of records, inc obligation to keep records listed in Annex I.	Yes	Yes	Yes	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
	L2 Reg, Art 73		COBS 8A.1.10EU	Retention of records setting out rights and obligations of firm and client.	Yes	Yes	No	No	
	L2 Reg Art 74		COBS 11.5A.2EU	Re initial orders from clients and initial decisions to deal, obligation to maintain records in accordance with Annex IV, Section 1.	Yes	Yes	Yes	Yes	
	L2 Reg Art 75		COBS 11.5A.3EU	Re receipt of client order and decisions to deal, obligation to maintain records in accordance with Annex IV, Section 2.	Yes	Yes	Yes	Yes	
	L2 Reg Art 76		SYSC 10A.1.5G	All firms must establish, implement and maintain an effective recording of telephone conversations and electronic communications policy, set out in writing, and appropriate to the size and organisation of the firm, and the nature, scale and complexity of its business. More detailed requirements regarding arrangements to be put in place, including procedures, oversight and disclosure to clients.	Yes	Yes	Yes	Yes	
	M2 Art 16(7)		SYSC 10A.1.6R	Telephone records, etc	Yes	Yes	Yes	Yes	
Gen operating conditions	M2 Art 21, 22			Regular review, ongoing supervision	Yes	Yes	Yes	Yes	
TTCA	M2 Art 16(10)		CASS 6.1.6R(3)	No title transfer collateral arrangements with retail clients.	No	Yes	Yes	Yes	This prohibition is not just in relation to firms acting as custodian. See also L2 Dir, Recital (8): "While some securities financing transactions may require the transfer of title of clients' assets, in that context investment firms should not be able to effect arrangements prohibited under Article 16(10) of Directive 2014/65/EU."
Algo trading	M2 Art 17(1) to (4)	RTS 6, 8		Obligations where engage in algo trading.					May be relevant to securities lending, depending on structure.
	M2 Art 17(5)			Obligations where provide direct electronic access to a trading venue (regulated market, MTF or OTF).					
	M2 Art 17(6)			Obligations for general clearing members.					
MTFs/ OTFs									
MTF/OTF processes	M2, Art 18	ITS 19		Obligations where operate an MTF or OTF.					Relevant if arrangements for providing relevant services constitute an MTF or OTF.

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
	M2, Art 18(8)			No obligations to MTF or OTF of issuer whose transferable securities have been admitted to trading on a regulated market and are also trade on MTF or OTF without issuer's consent.					
MTFs	M2 Art 19			Additional requirements for operator of MTF.					
OTFs	M2 Art 20			Additional requirements for operator of OTF.					
MTFs/OTFs	M2 Art 31			Obligations for ongoing monitoring of compliance by operators of MTF or OTF.					
	M2 Art 32	RTS 18 ITS 2		Requirements re suspension and removal of financial instruments from trading on MTF or OTF.					
	L2 Reg, Art 80			Circumstances constituting significant damage to investors' interests and the orderly functioning of the market, relevant to operating MTF or OTF.					
	L2 Reg, Art 81			Circumstances where significant infringements of the rules of a trading venue or disorderly trading conditions or system disruptions in relation to a financial instrument may be assumed.					
	L2 Reg, Art 82			Circumstances where a conduct indicating behaviour that is prohibited under Regulation (EU) No 596/2014 may be assumed.					
	M2 Art 38			Limits on restricting arrangements between MTFs and CCPs or settlement systems.					
Best interests	M2, Art 24(1)		COBS 2.1.1R	Obligation for firms to act honestly, fairly and professionally in the best interest of clients.	Yes	Yes	No	No	
Best execution	M2 Art 27(1)		COBS 11.2A.2R 11.2A.3G 11.2A.9R 11.2A.12R 11.2A.15R	Firm to take all sufficient steps to obtain, when executing orders, the best possible result for clients except where there is a specific instruction from the client.	Yes	Yes	No	No	
	L2 Reg Art 64		COBS 11.2A.8EU	Best execution criteria for M2 Art 27(1)	Yes	Yes	No	No	
	L2 Reg Art 65		COBS 11.2A.34EU	Best interests obligations re portfolio management and RTO	Yes	Yes	No	No	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Order execution policy	M2 Art 27(4), (5)		COBS 11.2A.20R to 11.2A.24R	Effective arrangements required for compliance with 27(1) and order execution policy. See also L2 Reg, Recital (99) re expectations for order execution policy for SFTs, inc listing separately execution venues used for SFTs.	Yes	Yes	No	No	
	L2 Reg, Art 66		COBS 11.2A.25EU	Annual review of execution policy, and on material change.	Yes	Yes	No	No	
	M2 Art 27(7)		COBS 11.2A.31R	Obligation to monitor effectiveness of order execution arrangements; notify clients of material changes to order execution arrangements or execution policy.	Yes	Yes	No	No	
	M2 Art 27(8)		COBS 11.2A.32R	Firms must be able to demonstrate to clients, on request, that they have executed their orders in accordance with the investment firm's execution policy; and to demonstrate to the competent authority, on request, compliance with this Article.	Yes	Yes	No	No	
Publication of execution venues	M2 Art 27(6)	RTS 27, 28	COBS 11.2A.39R	Firms who execute client orders to summarise and make public on an annual basis, for each class of financial instruments, the top five execution venues in terms of trading volumes where they executed client orders in the preceding year and information on the quality of execution obtained.	Yes	Yes	No	No	
		RTS 27		[Extract from ESMA Q&A on MiFID II and MiFIR investor protection and intermediaries topics: Question 15 [Last update: 10 July 2017] Do the RTS 27 reporting requirements apply to Securities Financing Transactions (SFTs)?	No	No	No		RTS 27 n/a re securities financing transactions.

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
				Answer 15 Article 1(5)(a) of MiFIR, subsequent to amending Regulation (EU) 2016/1033 of 23 June 2016, states that SFTs are not subject to the pre and post trade transparency obligations set out in Title II and III of MiFIR. While no specific exemption was included with respect to the RTS 27 best execution reporting obligations, Recital 10 of RTS 27 refers to the need for regulatory consistency between its requirements and those on post trade transparency. In this context, ESMA considers that the best execution reporting requirements set out in RTS 27 should not apply to SFTs. ESMA wishes to make clear that, irrespective of the above clarification concerning the application of RTS 27 to SFTs, the MiFID II best execution requirements otherwise apply to investment firms when carrying out SFTs. ESMA also wishes to clarify that while RTS 27 would not apply to SFTs, this would not lead to a complete absence of execution quality reports for SFTs, as RTS 28 explicitly requires investment firms to report, inter alia, on order routing behaviours specifically with respect to SFTs and to provide a summary on the quality of execution obtained. Investment firms should also note that RTS 28 already makes specific reference to how data concerning SFTs should be published.]					

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
		RTS 28		RTS 28: Recital (10) In order to comply with the legal obligation of best execution, investment firms, when applying the criteria for best execution for professional clients, will typically not use the same execution venues for securities financing transactions (SFTs) and other transactions. This is because the SFTs are used as a source of funding subject to a commitment that the borrower will return equivalent securities on a future date and the terms of SFTs are typically defined bilaterally between the counterparties ahead of the execution. Therefore, the choice of execution venues for SFTs is more limited than in the case of other transactions, given that it depends on the particular terms defined in advance between the counterparties and on whether there is a specific demand on those execution venues for the financial instruments involved. It is therefore appropriate that investment firms summarise and make public the top five execution venues in terms of trading volumes where they executed SFTs in a separate report so that that a qualitative assessment can be made of the order flow to such venues. Due to the specific nature of SFTs, and given that their large size would likely distort the more representative set of client transactions (namely, those not involving SFTs), it is also necessary to exclude them from the tables concerning the top five execution venues on which investment firms execute other client orders.	Yes	Yes	No	No	RTS 28: Art 3(1): Reporting obligation excludes SFTs BUT Art 3(2): separate report required re SFTs
Client agreements	M2 Art 24(1), 25(5).		COBS 8A, 8A.1.11R	Written agreement to set out rights and obligations of firm and client.	Yes	Yes	No	No	
	L2 Reg, Art 58		COBS 8A.1.4EU	Client agreement to contain essential rights and obligations.	Yes	Yes	No	No	
Information to clients	M2 Art 24(3).		COBS 4.2.1R	All information to clients, inc marketing communications, to be fair, clear and not misleading.	Yes	Yes	No	?	Per M2 Art 30(1) n/a re ecps, BUT COBS rules not disapplied re ecps

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
	L2 Reg, Art 44		COBS 4.5A.3EU	Fair, clear and not misleading.	Yes	Yes	No	No	
	L2 Reg, Art 36.		COBS 12.2.17EU	Investment research and marketing communications.	Yes	Yes	Yes	?	Per M2 Art 30(1), n/a re ecps, BUT COBS rule not disapplied re ecps.
	M2 Art 24(4).		COBS 2.2A.2R 6.1ZA.11R 6.1ZA.12R 6.2B.33R 9A.3.6R14. 3A.3R	Appropriate information in good time to clients re firm, services, financial instruments, investment strategies, execution venues, all costs and related charges.	Yes	Yes	No	Yes	
	L2 Reg, Art 45.		COBS 3.3.1AEU	Client categorisation.	Yes	Yes	No	Yes	
	L2 Reg, Art 46, 47		COBS 8A.1.5EU 8A.1.6EU 8A.1.7EU 6.1ZA.5EU 4.5A.8EU 4.7.-1AEU	Gen requirements re information to clients	Yes	Yes	No	Yes	But note COBS disapplies the following re ecps: 6.1ZA.16R, 6.1ZA.22R COBS 4 other than 4.5A.9EU and 4.7.-1AEU (and 4.2 and 4.4.1R)
	L2 Reg, Art 48		COBS 14.3A	Information about financial instruments	Yes	Yes	No	Yes	
	M2 Art 24(5).		COBS 2.2A.3R 6.1ZA.13R 6.2B.34R	Information in comprehensible form, client to be able to understand risks, make informed decision.	Yes	Yes	No	Yes	
Costs and charges	M2 Art 24(4) L2 Reg, Art 50		COBS 6.1ZA.14EU	Information re costs and associated charges to clients.	Yes	Yes	No	Yes	
	M2 Art 24(4) (a), (7) L2 Reg, Art 52,53		COBS 6.1A, 6.2B	Specific requirements re investment advice.	No	No	No	Yes	
Fees/ commissions	M2 Art 24(8)		COBS 2.3A	When providing portfolio management the investment firm shall not accept and retain fees, commissions or any monetary or non-monetary benefits paid or provided by any third party or a person acting on behalf of a third party in relation to the provision of the service to clients. Minor non-monetary benefits that are capable of enhancing the quality of service provided to a client and are of a scale and nature such that they could not be judged to impair compliance with the investment firm's duty to act in the best interest of the client shall be clearly disclosed and are excluded from this paragraph.	Possible	Possible	No	No	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Inducements	M2 Art 24(9)		COBS 2.3A	Restrictions on fees, commissions, non-monetary benefits, in connection with investment service or ancillary service to clients.	Yes	Yes	No	No	
	L2 Dir, Art 11		COBS 2.3A	Detailed requirements regarding fees, commissions etc., records, disclosure and repayments to clients, re any investment service or ancillary service provided to client, to be satisfied "at all times".	Yes	Yes	No	No	
	L2 Dir, Art 12		COBS 2.3A	Inducement rules re investment advice on an independent basis or portfolio management services.	Possible	Possible	No	No	
	L2 Dir, Art 13		COBS 2.3B	Inducements rules re research provided to firm which provides portfolio management or other investment or ancillary services to clients.	Yes	Yes	No	No	
	M2 Art 27(2)		COBS 11.2A.19R	Firm must not receive remuneration for routing client orders which conflicts with rules re conflicts, inducements, MiFID2 16(3), 23 and 24.	Yes	Yes	No	No	
Unbundling	M2 Art 24(11)		COBS 6.1ZA.16R	Firm to provide information to client regarding separate services provided as a package.	Yes	Yes	No	No	
Staff competence	M2 Art 25(1)		SYSC 5.1.5ABR	Persons giving investment advice or information to clients about financial instruments, investment services or ancillary services to have necessary knowledge and competence to fulfil firm's obligations under Art 24.	Yes	Yes	No	No	But note application re all clients re personal recommendations
Suitability	M2 Art 25(2) L2 Reg, Art 54, 55		COBS 9A	When providing investment advice or portfolio management, firm "shall obtain" information re client to enable firm to recommend suitable investment services and financial instruments.	Possible	Possible	No	?	Per M2 Art 30(1) n/a re ecps, BUT COBS 9A not disapplied re ecps, although some rules apply specifically to professional clients or retail clients.

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Appropriateness	M2 Art 25(3), (5) L2 Reg Art, 55, 56 M2 Art 25(4) L2 Reg Art 57		COBS 10A	Re investment services other than those referred to in 25(2) (investment advice/portfolio management), firm must "ask" client to provide information to enable firm to assess whether the investment service or product is appropriate for the client. Exception to 25(3) where only provide execution or RTO (with or without ancillary services) re non-complex instruments.	Yes if no portfolio management	Yes if no portfolio management	No	No	NB. No reference to ancillary services.
Client reporting obligations	M2 Art 25(6) L2 Reg, Art 59		COBS 16A	Periodic reports to client from firm other than re portfolio management.	Yes if no portfolio management	Yes if no portfolio management	No	Yes	
	M2 Art 25(6), L2 Reg Art 60		COBS 16A.2.1	eporting obligations re p ortfolio management. P	ossible P ortfolio management. P	ossible N	No	Yes	
	L2 Reg, Art 61		COBS 16A.3.5EU	Requirements under Art 49 (information re safeguarding client assets) and 59 (reporting other than for portfolio management) disapplied if firm has agreement with ecp to determine content and timing of reporting.	Possible	Possible	No	Yes	
	L2 Reg Art 62		COBS 16A.4.3EU	Additional reporting obligations re portfolio management or contingent liability transactions.	Possible	Possible	No	Yes	Note Commission comments in MiFID1 Q&A: "Securities lending arrangements may take many technical forms and it is necessary to take into account the specific circumstances when assessing an individual arrangement. Normally, lending an instrument already held in a portfolio does not in itself create a potential liability exceeding the cost of acquiring the instrument. Similarly, borrowing a financial instrument does not necessarily in itself create a contingent liability exceeding the cost of acquiring the instrument."

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Publication of transaction data	M2 Art 27(3) L2 Reg, Art 64(1)	RTS 27	COBS 11.2A.37R 11.2A.38G 11.2C.2R	Re financial instruments subject to the trading obligation in Articles 23 and 28 Regulation (EU) No 600/2014 each trading venue and systematic internaliser, and for other financial instruments each execution venue, must make available to the public, without charge, data relating to the quality of execution of transactions on that venue on at least an annual basis and that following execution of a transaction on behalf of a client the investment firm shall inform the client where the order was executed. Periodic reports shall include details about price, costs, speed and likelihood of execution for individual financial instruments. For the purposes of this Article and Articles 65 and 66, 'execution venue' includes a regulated market, an MTF, an OTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing.	No	No	No	No	RTS 27 n/a re securities financing transactions.
Order handling	M2 Art 28(1)		COBS 11.3	Obligation to implement procedures and arrangements which provide for the prompt, fair and expeditious execution of client orders.	Yes	Yes	No	No	But note M2 Art 30(1), second para.
	L2 Reg, Art 67 to 69		COBS 11.3	Further obligations re execution of orders, aggregation and allocation of orders, aggregation and allocation for own account.	Yes	Yes	No	No	
	M2 Art 28(2)		COBS 11.4	Rules re client limit orders in respect of shares admitted to trading on a regulated market or traded on a trading venue which are not immediately executed under prevailing market conditions.	Yes	Yes	No	Yes	
	L2 Reg Art 70		COBS 11.4	Additional rules re client limit orders.	Yes	Yes	No	Yes	
eligible counterparties	M2 Art 30(1), first para.		COBS 3.6	Where firms execute orders on behalf of clients and/or deal on own account and/or receive and transmit orders, where client is an ecp, Art 24 (except paras 4 and 5), Art 25 (except para 6), Art 27 and 28(1) do not apply to those transactions (or ancillary services directly related to those transactions).	Yes	Yes	No	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
	M2 Art 30(1), second para.		COBS 1 Annex 1 2.1.1AR 3.6.1R	Firms must, in relationship with eligible counterparties, act honestly, fairly and professionally and communicate in a way which is fair, clear and not misleading, taking into account the nature of the eligible counterparty and of its business.	Yes	Yes	No	Yes	
	M2 Art 30(2), (3)		COBS 3.6.2R 3.7.1R 3.7.7G	Rules re what is an ecp.	Yes	Yes	No	Yes	
	M2 Art 30(3), second para.		COBS 3.6.6R	Obligation to obtain express confirmation from counterparty that it agrees to be treated as an eligible counterparty, confirmation to be either in the form of a general agreement or in respect of each individual transaction.	Yes	Yes	No	Yes	
	L2 Reg Art 61		COBS 16A.3.5EU	Requirements re reports in Arts 49 and 59 apply to reports to ecps unless firm agrees with ecp other terms re content and timing of report.	Yes	Yes	No	Yes	
	L2 Reg Art 71		COBS 3.7.3B 3.6.4B	Further rules re what is an ecp and requests for different treatment.	Yes	Yes	No	Yes	
Regulated markets	M2 Title III (Art 44 to 56)	RTS 7, 8, 9, 10, 11, 12, 17, 18, 25 RTS 7, 8, 9, 10, 11, 12, 17, 18, 25 ITS 2 (Suspension and removal of financial instruments from trading on a Regulated Market, Multilateral Trading Facility (MTF) or Organised Trading Facility (OTF))			No	No	No		May impact securities lending if affects securities which are the subject to securities loans.
Commodity Derivatives	M2 Title IV (Art 57 to 58)	RTS 21, ITS 4, ITS 5 ITS 5			No	No	No		

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Data Reporting Services	M2 Title V (Art 59 to 66)	RTS 13, RTS re MiFID2 Article 65(8)(c) (The scope of the consolidated tape for non-equity financial instruments) ITS 3			No	No	No		
Competent authorities	M2 Title VI (Art 67 to Art 88)	RTS re MiFID2 Art 80(3) (Cooperation between authorities) ITS 1, 6, 7, 8			No	No	No		
Safeguarding client assets									
Adequate arrangements	M2 Art 16(8), (9)		CASS 6.2.1R, 7.10.41G	Adequate arrangements to safeguard client financial instruments and clients funds.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
Client agreements	M2 Art 24(1), 25(5).		COBS 8A	Written agreement to set out rights and obligations of firm and client.	Yes	Yes	Yes	No in part	M2 Art 24 not applicable where client is an eligible counterparty, except 24(4) and (5). M2 Art 25 not applicable where client is an eligible counterparty, except 25(6). COBS 8A.1.5EU to COBS 8A.1.8G do apply to ecps
	L2 Reg, Art 58(c)		COBS 8A.1.4EU	Client agreement to contain essential rights and obligations, and re custody services contain a description of the main features of the services, including "where applicable" services re "corporate actions relating to client instruments, and the terms on which securities financing transactions involving client securities will generate a return for the client."	Yes if custodian	Yes if custodian	Yes if custodian	No	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Client asset risk warnings	M2 Art 24(4), L2 Reg Art 49		COBS 6.1ZA.9EU	Information about safeguarding client financial instruments or client funds.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
Statements of client assets	M2 Art 25(6), L2 Reg Art 63		COBS 16A.5.1EU	Statement of client financial instruments or client funds. Statement to be given at least quarterly, and more frequently on request "at a commercial cost". Further details to be included in statement, namely: "a clear indication of the assets or funds which are subject to the rules of Directive 2014/65/EU and its implementing measures and those that are not, such as those that are subject to Title Transfer Collateral Agreement;" and "a clear indication of which assets are affected by some peculiarities in their ownership status, for instance due to a security interest;" and "the market or estimated value, when the market value is not available, of the financial instruments included in the statement with a clear indication of the fact that the absence of a market price is likely to be indicative of a lack of liquidity. The evaluation of the estimated value shall be done by the firm on a best effort basis." Periodic statement NOT required "where the investment firm provides its clients with access to an online system, which qualifies as a durable medium, where up-to-date statements of client's financial instruments or funds can be easily accessed by the client and the firm has evidence that the client has accessed this statement at least once during the relevant quarter."					
Records and accounts	L2 Dir, Art 2(1)		CASS 6.6.2R 6.6.3R 6.6.34R 6.3.4AR-1R 7.13.12R 6.2.2R	Obligations re custody accounts and other organisational arrangements	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
Security interests etc over client assets	L2 Dir, Art 2(4)		CASS 6.3.6AR to 6.3.6DG	Restrictions on grant of security interest etc over client assets Obligation re third party rights granted by firm, or which firm is notified have been granted: must "be recorded in client contracts and the firm's own accounts to make the ownership status of client assets clear, such as in the event of an insolvency".	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
Information for regulators etc	L2 Dir, Art 2(5)		CASS 10.1	Certain information to be readily available to competent authorities, appointed insolvency practitioners and those responsible for the resolution of failed institutions.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Use of delegates	L2 Dir, Art 3		CASS 6.3.1R 6.3.2G 6.3.4R	Requirements when appointing a delegate to hold client securities.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
	L2 Dir, Art 3(2), (3), (4)		CASS 6.3.4R	Restrictions on use of unregulated delegates to hold client securities. Restrictions must also apply when a firm's delegate sub-delegates holding of financial instruments.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
Use of client securities	L2 Dir, Art 5(1)		CASS 6.4.1R(1) and (3)	Use of client securities (firms entering into securities financing transaction re financial instruments held for client, or otherwise using such financial instruments for their own account of the account of any other person or client of the firm) requires express prior consent to use on specified terms, to be clearly evidenced in writing and affirmatively executed by signature or equivalent. Applies to all clients, not just retail.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
	L2 Dir, Art 5(2)		CASS 6.1.4R(2)	Prohibition on securities financing transactions re client financial instruments held in omnibus account, or other use of such financial instruments for own account or account of any other person unless, in addition to 5(1), either all clients whose assets are held in the omnibus account have given prior express consent, or the firm has systems and controls to ensure only assets of clients who have given consent per 5(1) are so used.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
	L2 Dir, Art 5(3)		CASS 6.4.1CR	Obligation to take "appropriate measures" to prevent "unauthorised use" of client securities, "such as": (a) agreeing with clients measures to be taken if client has insufficient securities in its account on settlement date, such as borrowing securities on behalf of client or unwinding position; (b) close monitoring by firm of its projected ability to deliver on settlement date and remedial measures if cannot be done; and (c) close monitoring and prompt request of securities outstanding on settlement day and beyond.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
	L2 Dir, Art 5(4)		CASS 6.4.2AR	Requirement to adopt "specific arrangements for all clients to ensure" borrower provides "appropriate" collateral, and to monitor "continued appropriateness" of collateral, and take "necessary steps to maintain the balance with the value of client instruments".	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
	L2 Dir, Art 5(5)		CASS 6.1.6R(3)	Prohibition of arrangements prohibited under MiFID2 Art 16(10) (i.e. title transfer financial collateral arrangements with retail clients for the purpose of securing or covering present or future, actual or contingent or prospective obligations of clients).	No (because agent does not receive collateral from client)	Yes	Yes	Yes	This does not prohibit entering into repos or stock loans with or for retail clients, but means that provision of collateral by retail clients on a title transfer basis is not possible.

General		RTS	FCA rule	Summary	Application to:				Comment
					Agency lending	Matched principal	Borrowing/ lending for own account	ecps	
Inappropriate use of title transfer collateral arrangements	L2 Dir, Art 6		CASS 6.1.6DR	Requirements when firm receives title transfer collateral from clients, including obligation to "properly consider" use of title transfer collateral with client (and demonstrate have done so), to consider and document "the appropriateness of the use of title transfer collateral arrangements", and to "take into account all of the following factors: (a) whether there is only a very weak connection between the client's obligation to the firm and the use of title transfer collateral arrangements, including whether the likelihood of a client's liability to the firm is low or negligible; (b) whether the amount of client funds or financial instruments subject to title transfer collateral arrangements far exceeds the client's obligation, or is even unlimited if the client has any obligation at all to the firm; or (c) whether all clients' financial instruments or funds are made subject to title transfer collateral arrangements, without consideration of what obligation each client has to the firm." Additional risk warnings required.	No (because agent does not receive collateral from client)	Yes	Yes	Yes	Applies in any case where firm receives title transfer collateral from clients, not just where such clients are custody clients. Note also FCA implementation.
Governance arrangements when safeguarding client assets	L2 Dir, Art 7		CASS 1A.3.1AR	Requirement to appoint "a single officer of sufficient skill and authority" with specific responsibility for compliance with obligations regarding safeguarding of client financial instruments and funds. Firms allowed to decide "ensuring full compliance with this Directive" whether the appointed officer is to be dedicated solely to this task or can discharge responsibilities effectively whilst having additional responsibilities.	Yes if custodian	Yes if custodian	Yes if custodian	Yes	
Audit reports	L2 Dir, Art 8		SUP 3.10.7R		Yes	Yes	Yes	Yes	

MiFIR	RTS		Agency lending	Matched principal	Borrowing/ lending for own account	
Title II (Art 3 to 13)	RTS 1, 2, 3, 14 RTS re MiFIR Art 9(6) (Treatment of package orders for which there is a liquid market)	Title II (Transparency for Trading Venues), inc pre and post-trade requirements re equity and non-equity.	No	No	No	Art 1(5a): Title II does not apply to SFTs.
Title III (Art 14 to 23)	RTS 1, 2, 3,	Title III (Transparency For Systematic Internalisers And Investment Firms Trading OTC), inc obligations to make public firm quotes.	No	No	No	Art 1(5a): Title III does not apply to SFTs.
Title IV (Art 24 to 27), Transaction Reporting	RTS 22, 23, 24					
Art 24		Obligation to uphold integrity of markets.	Yes	Yes	Yes	
Art 25		Obligation to maintain records. Investment firms to retain records of orders and transactions in FIs for 5 years.	Yes	Yes	Yes	
Art 26	RTS 22	Investment firms to report executed transactions in financial instruments, where FIs traded on RM/OTF/MTF, or where underlying is an FI so traded, or underlying is an index or basket composed of FIs so traded, to relevant authority (even if transaction not executed on trading venue)	No	No	No	Exemption: RTS 22 Art 2(5)(a). Transaction within MiFIR Art 26 does not include securities financing transactions as defined in Article 3(11) of Regulation (EU) 2015/2365 (unless a member of the European System of Central Banks is counterparty to the SFT). But note item 65 in Table 2: "Securities financing transaction indicator - 'true' shall be populated where the transaction falls within the scope of activity but is exempted from reporting under Regulation (EU) 2015/2365. 'false' otherwise."
Art 27		Obligation of trading venues, and SIs, to provide reference date re financial instruments traded on such.				Relevant if arrangements for providing relevant services constitute a trading venue (a regulated market, MT or OTF) or an SI.
Title V (Art 28 to 34) re derivatives	RTS 4, 5, 26, RTS re MiFIR Art 30(2) (Indirect clearing arrangements), RTS re trading obligation for derivatives under MiFIR		No	No	No	
Title VI (Art 35 to 38), re CCP access	RTS 15, 16		No	No	No	
Title VII (Art 39 to 45), re market monitoring						Relevant if intervention powers affect securities lending transactions or financial instruments which are the subject of securities lending transactions.
Title VIII (Art 46 to 49), third country firms	RTS re MiFIR Art 46(7) (Registration of third country firms)					Relevant to third country firms.

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