MIFID II - Markets in Financial Instrument Directive

Overview

The amended Markets in Financial Instruments Directive (MiFID) and accompanying Regulation (MiFIR together MiFID II) is a European regulation to enhance the effectiveness of the regulatory framework for Investment Firms.

The objective is to promote the competitiveness of EU financial markets by enhancing the single market for investment services, while ensuring an harmonized level of investor protection among financial markets. MiFID II establishes new trading venues and market structure requirements, enhances transparency on trading activities for a wide range of financial instruments and reinforces existing EU investor protection rules.

What is MIFID II?

The amended Markets in Financial Instruments Directive (MiFID) and accompanying Regulations (MiFIR together MiFID II) is a European regulation to enhance the effectiveness of the regulatory framework for Investment Firms. It came into force since 3rd of January, 2018.

This reform aims to enhance investor protection by refining the protections provided to smaller clients and extend those protections to a wider range of larger, more sophisticated clients. The new rules also improve the transparency of European financial markets with rules for new and existing trading venues (e.g. Regulated Markets such as the Eurex, Multilateral Trading Facilities or Organized Trading Facilities). New transparency obligations will ensure efficient and fair price formation for OTC transactions in financial instruments.

MiFID II aims at addressing the gaps and deficiencies of the original legislation that came into light during the Financial Crisis in 2008 only one year after MiFID came into application. MiFID II therefore takes into account the commitments made by the Pittsburgh G20 in 2009. It mandates venue trading for certain derivatives, which are subject to EMIR clearing requirements. Unique alphanumeric numbers are introduced to identify the banks and the clients called as Legal Entity Identifiers (LEIs).

What is MIFID II’s objectives?

MiFID II addresses three key objectives:

Improving Investment Firms’ Organisational Controls

MiFID II increases Senior Management responsibility for the day-to-day operation of investment firms. It extends requirements on processes, controls, record keeping and similar across the business

Harmonising Investor Protection across Europe

MiFID II reinforces the duty to treat clients fairly by considering the needs of clients as part of product design and distributions and requiring Investment Firms to provide more information on costs incurred and the quality of execution when handling clients’ orders.
**Improving Financial Markets Transparency**

MiFID II aims to increase price transparency, particularly for non-equity instruments. A new regime for multilateral discretionary trading venues or ‘Organised Trading Facilities’ will make trading in non-equity instruments more transparent. For bilateral trading, MiFID II expands the existing Systematic Internaliser (SI) regime to all types of financial instruments. Investment Firms which, on an organised, frequent systematic and substantial basis, deal on own account when executing client orders outside a trading venue will be required to mimic the pre- and post-trade transparency of venues.

**Who is affected by MIFID II?**

Any financial institutions either based within the EU or elsewhere when providing an investment service as defined by MiFID to a European Client or counterparty, and/or operating on European Markets or transacting financial instruments listed on European trading venues are affected.

Investment services and activities could be as follows:

(a) receiving and transmitting of orders in relation to one or more financial instruments  
(b) execution of orders on behalf of clients  
(c) dealing on own account  
(d) portfolio management  
(e) investment advice  
(f) underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis  
(g) placing of financial instruments without a firm commitment basis  
(h) operation of an Multilateral Trading Facility (MTF)  
(i) operation of an Organized Trading Facility (OTF)

**What are the main requirements of MIFID II?**

There are seven key requirements as part of MiFID II:

(a) Market structure and trading obligations

MiFID II introduces new trading obligation for shares and liquid derivatives instruments subject to clearing obligation under EMIR. These transactions will now be required and to be executed on a regulated platform such as a classic stock exchange, a multilateral trading facility or, for derivatives only, an organised trading facility.

(b) Market transparency

MiFID II increases the already existing transparency requirements imposed on equity transactions with the implementation of a double volume cap mechanism to limit the use of reference price waivers and negotiated price waivers.

MiFID II extends the pre-trade transparency requirements to non-equity instruments such as bonds and derivatives, RFQ (Request-for-quotes) and voice trading (VCON). Details around the trade
execution of this transaction in non-equity instrument will also need to be disclosed on real time basis to the public. The objective is to make the price formation process more transparent.

(c) Trading in commodity instruments

A new position-limit regime is introduced for transactions in commodity derivatives to improve transparency and to prevent speculation from having a detrimental impact on the price of the underlying commodities. An associated position reporting obligation will enable regulators to monitor that position limit.

(d) Competitiveness in the trading and clearing of financial instruments

MiFID II introduces a regime to ensure non-discriminatory access to trading venues and Central Counterparties (CPPs)

(e) Trading controls for algorithmic trading, high frequency trading (HFT) and Direct Electronic Access (DEA). New controls are introduced to regulate algorithmic traders and make sure that they provide liquidity when they pursue a market making strategy. When providing DEA service to clients, investment firms need to have adequate systems and risk controls in place to prevent market abuses.

(f) Investor Protection

MiFID II harmonises investor protection requirements across Europe by reinforcing clients’ assets protection strengthening the rules on product governance improving the “Appropriateness & Suitability tests” imposing new restrictions on third party commissions, and improving the transparency on the costs and charges and the information disclosed to clients

(g) Third country firms access to EU markets

A new regime is established to facilitate the access to European markets for Third-Country firms providing investment services or activities to professional clients and eligible counterparties. Firms from equivalent third country jurisdictions are allowed to apply for a passport to provide these cross boarder services without establishing a branch within the EU.

**What are the challenges for Akbank AG and our clients?**

MiFID requires increased interaction between the bank and the clients. Both the clients and the Bank will have to provide additional information, to each other and the regulator. MiFID obligations to clients will be extended to any client opening a Financial Market, Private Banking account with Akbank AG.

Some requirements will also extend to clients based outside of the European Economic Area, where they have an EU link. These obligations include but are not limited to extra client on-boarding documentation checks, new disclosures to clients on charges for transactions and services provided, further evidence of best execution of client orders, greater duty of care based on client’s requests.
MiFID II creates an opportunity for professional and institutional investors to review their organisation and reshape their business services while adapting to the requirements. It also calls for significant system and operational changes to comply with the rules around trade publications in real time, position limit regime for commodity derivatives, data storage for record keeping purpose or transaction reporting at T+1.

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