

### **Markets in Financial Instruments Directive (MiFID) II**

The Financial Conduct Authority (FCA) explains that the Markets in Financial Instruments Directive is the EU legislation that regulates firms who provide services to clients linked to 'financial instruments' (shares, bonds, units in collective investment schemes and derivatives), and the venues where those instruments are traded.

The Markets in Financial Instruments Directive (MiFID) is the framework of European Union (EU) legislation for:

- investment intermediaries that provide services to clients around shares, bonds, units in collective investment schemes and derivatives (collectively known as 'financial instruments'), and
- the organised trading of financial instruments

MiFID was applied in the UK from November 2007, but is now being revised to improve the functioning of financial markets in light of the financial crisis and to strengthen investor protection.

The changes are currently set to take effect from 3 January 2018, with the new legislation being known as MiFID II - this includes a revised MiFID and a new Markets in Financial Instruments Regulation (MiFIR).

The FCA released a new Policy Statement on 3 July 2017. This included a finalised position for the client categorisation of Local Authorities, which will come into effect as part of the full introduction of MiFID II on 3 January 2018.

MiFID II does not cover simple term deposits. It is only focussed on regulated products, which would include direct investments such as Certificates of Deposit, Gilts, Corporate Bonds, and investment funds (including Money Market Funds - MMFs).

Under MiFID II, the FCA is obliged to treat by default all Local Authorities as "retail clients" under EU legislation. However, the regulator does offer the option to "opt up" to being an Elective Professional Client if the authority meets certain criteria.

#### **Opt-Up Process under MiFID II**

To be considered as a professional Client, an authority will now need to make that choice in writing and meet requirements set by the FCA.

Qualitative criteria will be set by the counterparties and will be tailored to the specific products. It is unlikely that a client authority could produce one document that it could use to satisfy all potential requirements. Each firm will present their clients with slightly different forms and content as they will be drafted to the specific products being offered. This introduces a new administrative burden to the treasury management function.

The quantitative test includes a minimum financial instrument portfolio size of £10 million. Previously limits of £15m or even £20m had been considered, which would have prevented many local authorities from opting up to Professional Client status. The portfolio size is likely to be measured at the point at which the authority requests to opt up, rather than at the balance sheet date.

## Appendix D

If local authorities do not meet the minimum portfolio size requirement, the biggest potential consequence could be that they may no longer be able to use MMFs.

In addition to passing the £10m portfolio size test, a local authority would need to satisfy one of the following criteria to opt-up:

- Ten transactions per quarter in a relevant market in the past four quarters; or
- At least one year experience in a professional position in financial markets which requires knowledge of transactions or services envisaged.

The advice of Capita Asset Services is that because opting-up would be product by product, it would be better to prioritise applications to concentrate on those products used most frequently.