

The MiFID 2 Guide

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Chapter 1

Onshoring for Trading Venues & Data Reporting Service Providers

1.1 Background

- 1.1.1

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This guide sets out an overview of the FCA’s approach to onshoring of the recast Markets in Financial Instruments Directive 2 (MiFID 2) in the MAR and REC sourcebooks. . “Onshoring”, for these purposes, refers to the process by which law deriving from EU legislation at IP completion day is retained or adapted, post IP completion day. This guide focuses on the regulatory regime in MiFID 2 for UK trading venues (as defined by 2(16A) MiFIR: this term comprises UK regulated markets, multilateral trading facilities and organised trading facilities but not systematic internalisers) and UK data reporting services providers (DRSPs)).
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MiFID 2 enables the Commission to make secondary legislation in several places. That legislation takes the form of a combination of delegated acts (for example as provided for in article 4(2) MIFID to specify elements of the definitions), regulatory technical standards (RTS) and implementing technical standards (ITS). Delegated acts under MiFID 2 are both drafted and made by the Commission, after it receives advice from the European Securities and Markets Authority (ESMA), and may take the form of either directives or directly applicable regulations. As for RTS and ITS, these are prepared in draft by ESMA and subject to public consultation, before endorsement and making by the Commission; both take the form of regulations and so are directly applicable. RTS and ITS feature, in particular, in the MiFID 2 provisions relating to trading venues and DRSPs. After IP completion day, in the United Kingdom, in broad terms, the former role of the Commission is discharged by the Treasury and ESMA’s functions are performed by the FCA. For further details, see the Financial Regulators’ Powers (Technical Standards etc.) (Amendment etc.) (EU Exit) Regulations 2018.
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You can be subject to a MiFID derived or MiFIR requirement, even if you are not an authorised financial institution. regulation 30 of the Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017 applies algorithmic trading requirements to certain persons exempt under MiFID, where they are members of a regulated market or multilateral trading facility (article 1(5) MiFID). Similarly, article 1 MiFIR requires non-financial counterparties above the clearing threshold in article 10 of the European Market Infrastructure Regulation (‘EMIR’) (Regulation 648/2012/EU. See our EMIR webpage (<https://www.fca.org.uk/markets/emir>) for further details about non-financial counterparties and the clearing threshold) to comply with the obligations in

Title V MiFIR. This means trading certain classes of derivatives on organised venues only, UK regulated markets, UK multilateral trading facilities (MTFs), UK organised trading facilities (OTFs) and permitted third country venues (article 28 MiFIR). EEA venues are treated as third country venues for these purposes.

1.1 A Transitional onshoring provisions




G The effect of section 3 of the European Union (Withdrawal) Act 2018 is that “direct EU legislation” became part of UK law, as at IP completion day (and is known as “retained EU law” in accordance with section 6 of the same legislation). As such, MiFIR and all directly applicable regulations made under MiFID and MiFIR, including the MiFID Org Regulation (Commission Delegated Regulation 2017/565), the MiFIR Delegated Regulation (Commission Delegated Regulation 2017/567) and technical standards became part of UK law, as at IP completion day.

G Each of these pieces of legislation is subject to the power in section 8 of the European Union (Withdrawal) Act 2018 to deal with deficiencies arising out of the United Kingdom’s withdrawal from the EU. The Treasury has exercised this power in the Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018 (the ‘Exit Regulations’) to amend each of the following:

- MiFIR;
- MiFID Org Regulation;
- MiFIR Delegated Regulation;
- Data Reporting Services Regulations; and
- The Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017.

A reference to any of the above in the remaining text of this guide is to the legislation as amended by the Exit Regulations.

1.2 MiFID onshoring in UK legislation and the FCA Handbook

- 1.2.1  The UK's onshoring of the directive takes the form of a combination of legislation made by HM Treasury, in the form of a number of statutory instruments, and rules contained in the FCA Handbook and the PRA Rulebook.
- 1.2.2  The Treasury legislation is set out in the following statutory instruments as amended by the Exit Regulations:
- Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017 ('MiFI regulations'), SI 2017/701
 - The Data Reporting Services Regulations 2017 ('DRS regulations'), SI 2017/699
 - Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 ('RAO'), SI 2001/544
 - **The MiFI regulations amend** Part XVIII FSMA and the Recognition Requirements Regulations ('RRR') applying to recognised investment exchanges. This includes implementing the regulatory regimes relating to a market operator operating an organised trading facility and data reporting services, as well as obligations in regard to the management body and systems and controls. It also includes applying algorithmic trading requirements in relation to unauthorised entities and position management requirements for trading venues on which commodity derivatives are traded.
 - **The DRS regulations create** a self-standing regime for data reporting services providers including authorisation, operating conditions, reporting and enforcement.
 - **The RAO reflects** scope changes arising out of MiFID, notably the new investment service of operating an organised trading facility and the extension of "financial instruments" to include emission allowances. The onshoring amendments to Part 1 of Schedule 2 to the RAO essentially preserve the pre-IP completion day scope of regulation relating to physically-settled power forward contracts.
- 1.2.3  The FCA Handbook complements the Treasury legislation, referred to above, so for example:

●REC contains, in REC 2, extracts of the RRRs and 'Notes' signposting technical standards which are relevant to recognised investment exchanges' compliance with certain RRRs. These include having adequate systems and controls for algorithmic trading (see REC 2.5), and sufficient price transparency to ensure fair and orderly trading (see REC 2.6).

●REC 3, which contains FCA rules requiring certain notifications to be made by RIEs to the FCA, also includes 'Notes' signposting notification requirements set out in the RRRs or technical standards.

●MAR 5 applies the MiFID requirements on systems and controls for algorithmic trading to MTFs, including requirements in the areas of systems resilience, algorithmic market-making, tick sizes and clock synchronisation. It also aligns further the organisational requirements on MTFs with those for regulated markets, in the areas of conflicts of interest and risk management, and the management of technical operations. Rules on the suspension and removal of financial instruments also align with those for regulated markets. The chapter contains guidance on the ability to register an MTF as an SME Growth Market.

●MAR 5A imposes a regime for OTFs. OTFs are distinguished from MTFs and regulated markets by the requirement for discretionary order execution and by trading only being permitted on these venues in bonds, structured finance products, emission allowances or derivatives. Restrictions on proprietary and matched principal trading applicable to MTFs and regulated markets are more relaxed for OTFs. In other respects, however, the regulation of these venues aligns with that for MTFs, and also, therefore, substantially with that for regulated markets.

●MAR 6 relates to systematic internalisers and the article 27(3) MiFID execution quality publication requirement (applying to systematic internalisers, amongst other execution venues). This requirement has been preserved as part of onshoring as a rule (see MAR 6.3A).

●MAR 7A corresponds to article 17 of the recast MiFID. It imposes systems and controls and notification requirements on firms engaging in algorithmic trading, as well as providing for market making obligations where a firm engages in a high-frequency algorithmic trading technique. It also imposes systems and controls and notification requirements on firms providing direct electronic access services. The services of a general clearing member are also subject to rules of a similar nature.

●MAR 9 provides directions and guidance applicable to the operation of the data reporting services regime, set out in the DRS regulations.

●MAR 10 comprises requirements and guidance relating to the setting of position limits in respect of commodity derivatives traded on trading venues, position management obligations relating to the venues themselves and position reporting by trading venues and investment firms.

- 1.2.4 G More generally, where requirements in MiFID correspond to FCA rules, the source of the corresponding requirement is referred to below the relevant provision, for example MAR 5A.3.5: -
- 5A.3.5 R A firm must not engage in:
- 5A.3.5R (1) *matched principal trading* on an *OTF* operated by it except in bonds, *structured finance products*, *emission allowances* and *derivatives* which have not been declared subject to the clearing obligation in accordance with article 5 of *EMIR*, where the client has consented; or
- 5A.3.5R (2) *dealing on own account* on an *OTF* operated by it, excluding *matched principal trading*, except in *sovereign debt instruments* for which there is not a liquid market.
- [Note: article 20(2) and (3) of *MiFID*]

- 1.2.5 G The scope of MIFID is the subject of guidance in PERG 2 and 13.

1.3 Markets in Financial Instruments
Regulation (‘MiFIR’)

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- 1.3.2
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- 1.3.3
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- MiFIR as onshored provides for delegated acts and technical standards on amongst other things:
 - price transparency for equity and derivative instruments, see REC 2, MAR 5 and MAR 5A;
 - straight-through processing of clearing for derivative instruments, see REC 2, MAR 5 and MAR 5A; and
 - transaction reporting, see SUP 17A.



1.4 Technical standards and delegated acts

- 1.4.1** G Technical standards, submitted by ESMA. These technical standards, which take the form of regulatory technical standards or implementing technical standards, are, as their names suggest, technical in nature.
- 1.4.2** G Where an FCA rule is amplified by a technical standard, the source is referred to below the relevant provision, for example, in MAR 5A.5.10
- 5A.5.10R Where a firm permits colocation in relation to the OTF, its rules on colocation services must be transparent, fair and non-discriminatory.
- [Note: article 48(8) of MiFID and MiFID RTS 10]
- 1.4.3** G We have not copied out the onshored technical standards into the Handbook, but instead adopted the signposting convention illustrated above.
- 1.4.4** G In addition to enabling the FCA and PRA to make technical standards, the Exit Regulations also onshore delegated acts prepared by the Commission, itself, in the form of regulations (see, for example, references to the MiFID Org Regulation (Commission Delegated Regulation (EU) 2017/565) and the MiFIR Delegated Regulation (EU) 2017/567).

1.5 ESMA Guidelines

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- ESMA guidelines are subject to the ‘comply or explain’ process in article 16 Regulation 1095/2010 (establishing ESMA) and are addressed to competent authorities or, as the case may be, market participants. Under article 16(3) Regulation 1095/2010 (establishing ESMA) competent authorities and financial market participants must make every effort to comply with these.
- 1.5.3
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- As a general practice, when the FCA decided to comply with the guidelines issued by ESMA it signposted a reference to these by means of a note at the beginning of the relevant section of the Handbook. The FCA have issued non-handbook guidance setting out the FCA’s approach to ESMA guidelines after IP completion day. The guide can be found on the FCA website at [URL to be added].

1.6 Third country firms

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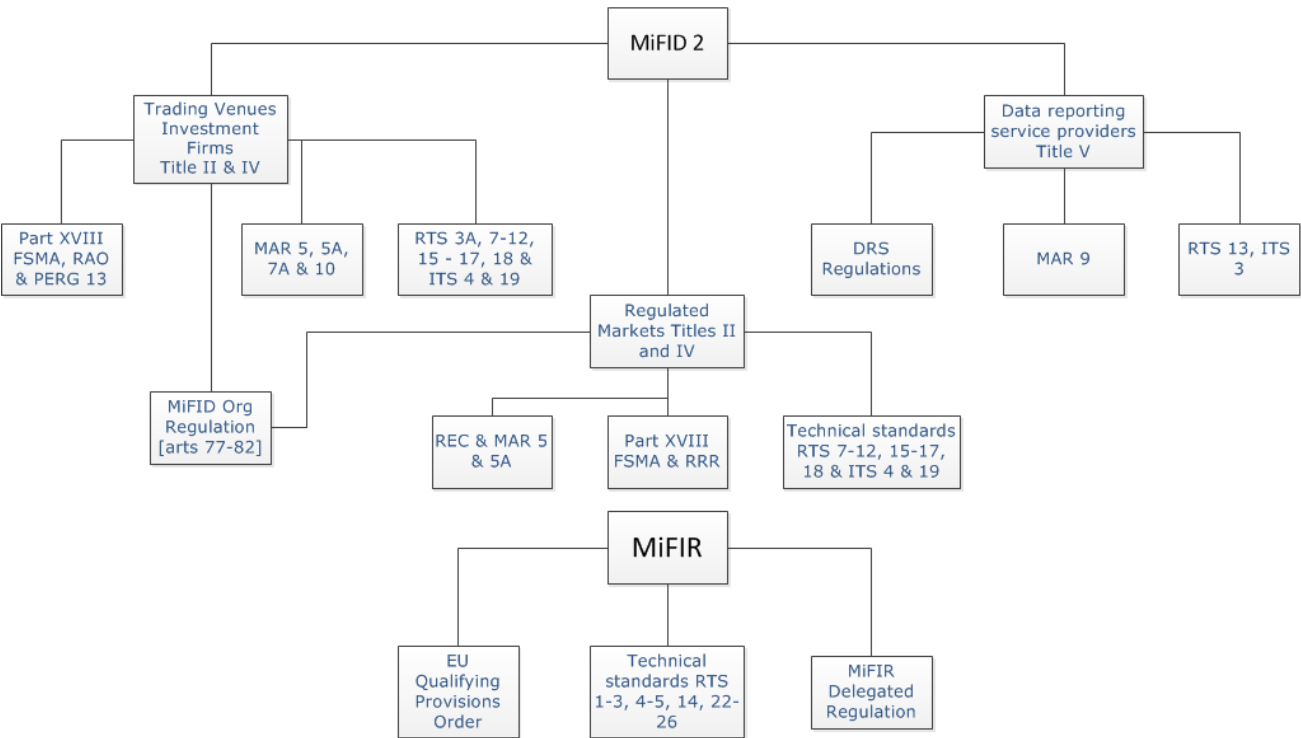
- G** MiFIR and the onshored regulations forming part of “retained EU law” (see M2G 1.1A.1G) apply to UK firms. For the UK branches of non-UK firms (third country firms), these regulations are not of general application and it is necessary to ensure that these branches do not receive more favourable treatment than their UK counterparts. GEN 2.2.22AR is included for this purpose.
- G** MiFIR, the MiFIR Delegated Regulation and the MiFID Org Regulation apply to EEA firms with temporary Part 4A permissions to the extent specified in the Exit Regulations. Technical standards deriving from MiFID apply to these firms to the extent provided for by GEN 2.2.29R.

1.7 Overview

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- The diagram in M2G 1 Annex 1 provides an overview of trading venue and DRSP requirements and the location of their implementation. The references to “technical standards” are to those described in the FCA Handbook Glossary.
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- In addition to MAR and other requirements noted in the overview, firms operating an MTF or OTF will be subject to other requirements applying elsewhere in the Handbook, notably in SYSC, COBS and SUP 17A.
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- SUP 17A sets out rules and guidance for transaction reporting and supply of reference data: it also cross-refers to the relevant legislation in articles 26 and 27 MiFIR and MiFID RTS 22 and 23. It further confirms that we will allow operators of trading venues and investment firms to use third party technology providers when supplying financial instrument reference data to the FCA.

MiFID and Market Infrastructure: An Overview

An overview of MiFID and Market Infrastructure:
MiFID and Market Infrastructure: An Overview



Chapter 2

Onshoring of senior management arrangements and systems and controls obligations

2.1 Background

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This guide sets out an overview of the FCA’s approach to the onshoring of the Markets in Financial Instruments Directive II (MiFID II) in the SYSC sourcebook. The guide focuses on the regulatory regime for UK firms and is aimed at UK MiFID investment firms, that is investment firms that would require authorisation under MiFID and credit institutions carrying on MiFID business, and MiFID Optional exemption firms. The latter comprise advisers or arrangers who do not hold client money or assets and meet other conditions imposed under article 3 MiFID II, so as to be exempt from the Directive’s full application. See PERG 13 Q49.
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MiFID II contains revised senior management and systems and controls obligations relating to firms. With the exception of one aspect of the whistleblowing obligations in MiFID II contained in primary legislation, onshoring of the MiFID II Level 1 requirements takes the form of regulatory rules. The relevant FCA rules are mainly contained in SYSC but PRA- authorised firms will also be subject to rules in the General Organisational Requirements in the PRA Rulebook.
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The Commission Delegated Regulation 2017/565 of 25 April 2016), as onshored by the Exit Regulations, contains detailed organisational requirements for those firms to which it applies, including authorised MiFID investment firms and credit institutions.

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2.3 Main types of senior management and organisational requirements in MiFID II

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MiFID II’s senior management and systems and controls requirements for firms fall into five broad categories:

 - management body (article 9);
 - general organisational requirements (article 16);
 - conflicts of interest (article 23);
 - remuneration and performance management of sales staff (article 24);
 - whistleblowing (article 73).

Firms operating an MTF or an OTF are subject to additional systems and controls for algorithmic trading (see MAR 5 and 5A). Likewise, MAR 7A contains systems and controls requirements for other firms engaged in algorithmic trading or providing direct electronic access.
- 2.3.2

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The general organisational requirements in article 16 are added to by detailed provisions in the MiFID Org Regulation including the following areas:

 - compliance;
 - risk management;
 - internal audit;
 - responsibility of senior management;
 - complaints handling;
 - remuneration policies and practices;

- personal transactions;
- outsourcing;
- conflicts of interest;
- record-keeping.

2.4 MiFID II onshoring and SYSC

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The combination of senior management and systems and controls requirements for firms in a directive and regulation means that FCA rules are used to onshore the provisions in the directive. As such, the approach to onshoring MiFID II retains the familiar approach of the common platform and the following:

- the application of common platform requirements in SYSC 1 Annex 1 Part 3 and Table B for MiFID optional exemption firms;
- a rule which has the effect, amongst other things, of extending the application of certain parts of the MiFID Org Regulation to all of a UK MiFID investment firm's designated investment business, MiFID or otherwise (SYSC 1 Annex 1 2.8AR) (in the Handbook, the definition of 'MiFID investment firm' captures any UK firm to which MiFID would apply if the United Kingdom were a Member State);
- a rule which extends the application of the MiFID Org Regulation in relation to general organisational requirements, compliance, risk management, internal audit, responsibility of senior management, remuneration policies and practices and outsourcing to all of a MiFID optional exemption firm's designated investment business, by way of rule or guidance depending on the individual provision (SYSC 1 Annex 1 3.2CR discussed further in M2G 2.5);
- signposting references in the application provisions to individual SYSC chapters to identify the relevant articles of the MiFID Org Regulation which supplement the rules implementing the MiFID requirements. These are also listed in the new Table C in SYSC 1 Annex 1;
- chapter SYSC 10A on recording telephone conversations and electronic communications;
- section SYSC 18.6 on the whistleblowing obligations imposed upon MiFID investment firms which includes a signposting mechanism pointing firms to similar obligations derived from other single market legislation; and
- section SYSC 19F in respect of remuneration and performance management of sales staff.



2.5 Navigating SYSC

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In order to navigate SYSC material implementing MiFID II, it is essential to follow the relevant application provisions in the sourcebook.
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SYSC 1.1A summarises the application of the sourcebook to different types of firms. UK MiFID investment firms and MiFID optional exemption firms fall into the category of ‘every other firm’ in SYSC 1.1A and so the applicable chapters are 4 to 12, 18, 19A, 19D and 21. The detailed application of the provisions in chapters 4-10 is cut back in SYSC 1 Annex 1 and it is this annex which provides the starting point for understanding and determining the application of the common platform requirements to your business. More specifically, SYSC 1 Annex 1 Part 3.1G provides a roadmap for individual categories of firms, including UK MiFID investment firms and MiFID optional exemption firms, in explaining how the common platform requirements and the MiFID Org Regulation apply to them.

2.6 UK MiFID investment firms

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In the case of UK MiFID investment firms, these are common platform firms for the purposes of the Handbook so are subject to the following MiFID II related obligations:

- SYSC 4 to 10 in accordance with SYSC 1 Annex 1 Part 3 Table A Column A. This table identifies whether individual provisions in these chapters apply:

- (i) either as rules or guidance;
- (ii) only to certain sub-categories of common platform firms; or
- (iii) are non-applicable.

These obligations apply to the firm's regulated activities generally and other activities identified in SYSC 1 Annex 1.2.8R.

- The MiFID Org Regulation.

Certain provisions of the MiFID Org Regulation are also adapted to apply to the firm's non-MiFID business in accordance with SYSC 1 Annex 1.2.8R and SYSC 1 Annex 1.2.8AR. The effect of SYSC 1 Annex 1.2.8AR is to adapt the MiFID Org Regulation so that a small number of its terms are to be read as if they were broader corresponding Handbook terms. For example, references in the MiFID Org Regulation to 'investment service' and 'investment services and activities' are to be read as 'designated investment business'. This helps maintain a common single standard of organisational requirements applying to all of a UK MiFID investment firm's business.

- Other non-common platform requirements including recording telephone conversations and electronic communications (SYSC 10A), whistleblowing (SYSC 18) and remuneration and performance management of sales staff (SYSC 19F). These chapters apply to a firm's MiFID and other business to the extent set out in the application provisions of each chapter.

2.7 MiFID optional exemption firms

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2.7.1

G MiFID optional exemption firms are subject to the following MiFID II related obligations:

- SYSC 4 to 10 in accordance with SYSC 1 Annex 1 Part 3 Table B Column A. This table identifies whether individual provisions in these chapters apply:

- (i) either as rules or guidance; or
- (ii) are non-applicable. These obligations apply to the firm's regulated activities and other activities identified in SYSC 1 Annex 1.2.8R.

- Articles 21 to 25, 27, 30 to 35 and 72 of the MiFID Org Regulation are applied to the business of a MiFID optional exemption firm in accordance with SYSC 1 Annex 1 3.2CR. The effect of SYSC 1 Annex 1 3.2CR is to apply these provisions of the MiFID Org Regulation:

- (i) as either rules or guidance in accordance with SYSC 1 Annex 1 Part 3 Table C; and
- (ii) to the firm's regulated activities generally and other activities identified in SYSC 1 Annex 1.2.8R.

The effect of SYSC 1 Annex 1 3.2CR is to also to adapt articles 21 to 25, 27, 30 to 35 and 72 of the MiFID Org Regulation so that a small number of terms in the regulation are to be read as if they were broader corresponding Handbook terms, as set out in SYSC 1 Annex 1.2.8AR.

- Other non-common platform requirements applying MiFID optional exemption firms include recording telephone conversations and electronic communications (SYSC 10A) and remuneration and performance management of sales staff (SYSC 19F). The requirements in these chapters apply to a firm's business to the extent set out in the application provisions in each chapter.



2.8 Other firms- Collective portfolio management investment firms and authorised professional firms

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This short summary focuses only on MiFID II onshoring and not obligations arising under other single market legislation
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A collective portfolio management investment firm ('CPMI') takes the form of a 'UCITS investment firm' or an 'AIFM investment firm', as defined in the FCA Handbook Glossary. A UCITS investment firm is subject to the common platform requirements as set out in Column A+ in SYSC 1 Annex 1 Table A. An AIFM investment firm is subject to the requirements listed in Column A in SYSC 1 Annex 1 Table A in relation to their MiFID business. More generally, both a UCITS investment firm and an AIFM investment firm fall within the Handbook definition of MiFID investment firm broadly when doing MiFID business - this is relevant as regards the application of SYSC 10A ('Recording telephone conversations and electronic communications'). By contrast, neither SYSC 18 ('Whistleblowing') nor SYSC 19.1 (MiFID remuneration incentives) apply to their MiFID business, as a result of the derogations in the application provisions in these chapters.
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Authorised professional firms falling within the exemption in paragraph 1(d) of Part 1 of Schedule 3 to the RAO will be subject to common platform requirements as set out in Column B in SYSC 1 Annex 1 Table A. If they satisfy the criteria of a MiFID optional exemption firm (in accordance with Chapter 1 of Part 2 of the MiFI regulations) they will be subject to the provisions in the SYSC 1 Annex 1 Part 3 Table B column A. If they fall within both the exemptions in paragraph 1(d) of Part 1 of Schedule 3 to the RAO and Chapter 1 of Part 2 of the MiFI regulations, they are entitled to comply only with the common platform requirements relating to article 2(1)(c) exempt firms in Column B in SYSC 1 Annex 1 Table A. Where they would be required to be authorised by MiFID II, they will be subject to common platform requirements in Column A in SYSC 1 Annex 1 Table A and other SYSC requirements as a UK MiFID investment firm, except to the extent indicated otherwise (including SYSC 1 Annex 1 2.5R).

For an authorised professional firm when carrying on non-mainstream regulated activities, the common platform requirements on financial crime, conflicts of interest and Chinese walls do not apply.

See the definition of authorised professional firms at <https://www.handbook.fca.org.uk/handbook/glossary/?starts-with=A>. In essence, the definition captures persons regulated by a designated professional body under Part XX FSMA, with a Part 4A permission.



2.9 Other organisational requirements

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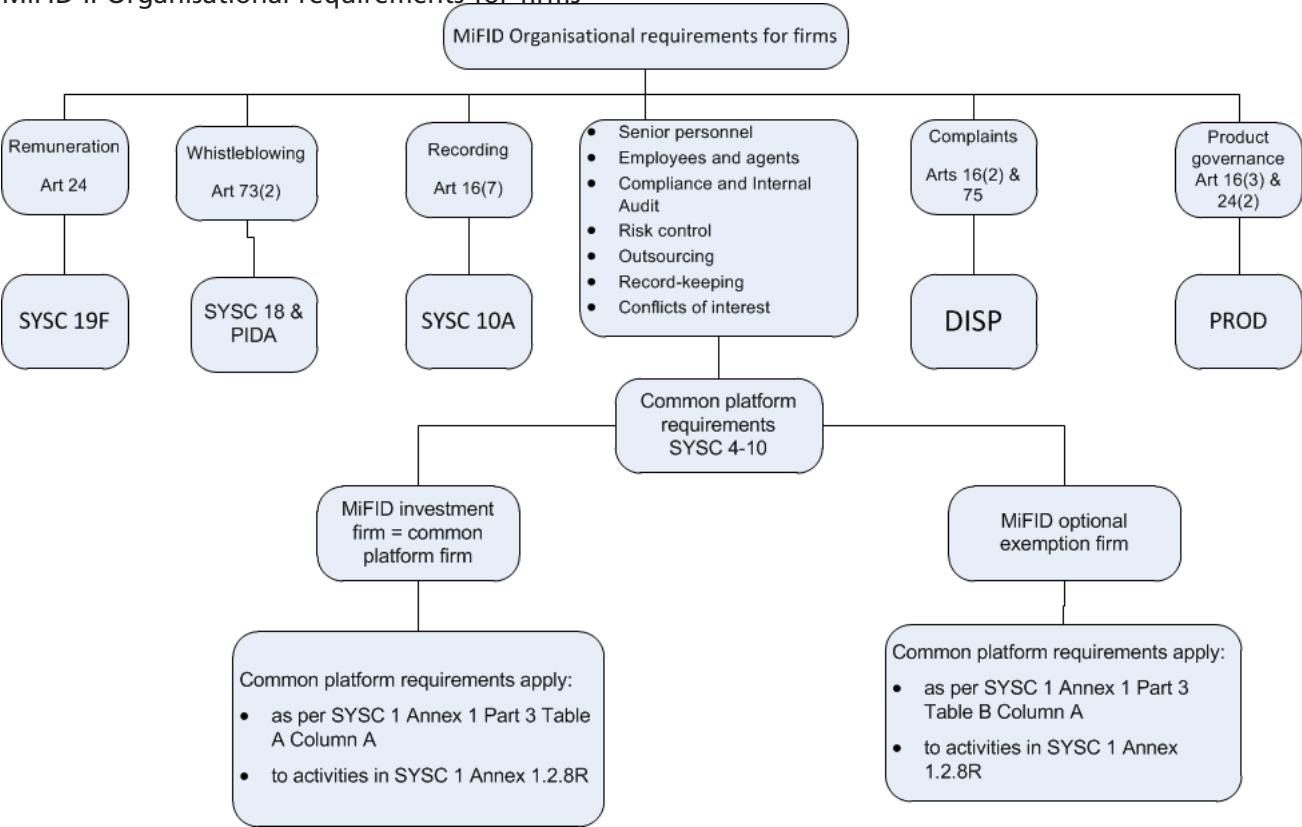
G In addition to the SYSC obligations outlined above, firms will find MiFID II-related organisational requirements in respect of complaints handling in DISP, client money and assets (CASS) and product governance obligations in [PROD]. Firms will also remain subject to obligations in the form of the relevant senior management, certification, COCON and approved persons requirements.

Overview

The diagrams in this Annex provide an overview of organisational requirements deriving from MiFID II and the location of their implementation, as well as the MiFID Org Regulation including its extension to non-MiFID II business in the case of UK MiFID investment firms and MiFID optional exemption firms. The diagram focuses on the position of UK MiFID investment firms (other than CPMI and authorised professional firms

) and MiFID optional exemption firms.

MiFID II Organisational requirements for firms



MiFID Org Regulation

