# Chapter 13

# Guidance on the scope of MiFID and CRD IV

## 13.5 Exemptions from MiFID

13.5

**Introduction**

**Q35.Where do we find a list of MiFID exemptions?**

In articles 2 and 3 of MiFID.

**Q35A. Can you give me a complete list of exemptions?**

| Description of exemption | MiFID reference | Guidance in this chapter |
|---|---|---|
| Insurers | article 2.1(a) | Q36 |
| Intra-group services | article 2.1(b) | Q37 and Q38 |
| Services complementary to other professional activities | article 2.1(c) | Q39 |
| Own account dealing (except in commodities or emission allowances) | article 2.1(d) | Q40 to Q40C |
| An operator with compliance obligations under Directive 2003/87/EC (Emissions Trading Scheme) who, when dealing in emission allowances, does not:<br>● execute client orders; or<br>● provide any investment services or perform any investment activities other than dealing on own account; or<br>● apply a high-frequency algorithmic trading technique. | article 2.1(e) | Q34A |
| Employee share schemes and pension schemes | article 2.1(f) and (g) | Q42 |
| The following public financial institutions:<br>●members of the European System of Central Banks; | article 2.1(h) | None |

13

| Description of exemption | MiFID reference | Guidance in this chapter |
|---|---|---|
| ●other national bodies performing similar functions in the EU;<br>●other public bodies charged with or intervening in the management of the public debt in the EU; or<br>●international financial institutions established by two or more EU Member States which have the purpose of mobilising funding and providing financial assistance to the benefit of their members that are experiencing or threatened by severe financing problems. | | |
| Collective investment undertakings and pension funds | article 2.1(i) | Q43 |
| Activities relating to commodity derivatives or emission allowances | article 2.1(j) | Q44 to Q45 |
| Persons providing investment advice in the course of providing another professional activity not covered by MiFID<br>This only applies if the provision of such advice is not specifically remunerated. | article 2.1(k) | None |
| Transmission system operators as defined in article 2(4) of Directive 2009/72/EC or article 2(4) of Directive 2009/73/EC (Directives about common rules for the internal markets in electricity and natural gas). This exemption is subject to various detailed conditions | article 2.1(n) | None |
| *Central securities depositories* when providing services explicitly listed in Sections A and B of EU Regulation | article 2.1(o) | None |

| Description of exemption | MiFID reference | Guidance in this chapter |
|---|---|---|
| 909/2014 (Securities settlement and central securities depositories regulation) | | |
| Optional article 3 exemption | article 3 | Q48 to Q53 |
| Exemptions relevant to Italy, Denmark and Finland | articles 2.1(l) and (m) | None |

**Insurance**

**Q36. We are an insurer. Does MiFID apply to us?**

No. Insurers are exempt from MiFID (article 2.1(a)).

**Intra-group activities**

**Q37. We are a non-financial services group company providing investment services to other companies in the same group. Are we exempt under the group exemption in article 2.1(b)?**

Yes, if you provide these services exclusively for your parent company, your subsidiaries and those of your parent company. The exemption is narrower than the corresponding exclusion in article 69 of the Regulated Activities Order (groups and joint enterprises) insofar, for example, as it does not apply to investment services supplied to a joint venture participant (see ■ PERG 2.9.10 G).

**Q38. We also buy and sell financial instruments for ourselves. Are we still able to use the group exemption?**

Yes. As long as your own account dealing does not involve you providing an *investment service* (to which MiFID applies) to non-group entities, you can still rely on the group exemption in respect of the services you provide solely to other group companies.

So far as your own account dealing is concerned, you may be able to rely upon the exemption in article 2.1(d) (see Q39) or 2.1(j) (see Q44 to Q45) if you meet the relevant conditions. The ability to combine reliance on article 2.1(b) and articles 2.1(d) or 2.1(j) could be relevant to companies performing group treasury functions.

The answer to Q46 (Is it possible to combine article 2 exemptions?) explains why it is possible to combine exemptions.

**Incidental services as part of a professional activity**

**Q39.We provide investment services as a complement to our main professional activity. Are we exempt (article 2.1(c) of MiFID and article 4 of the MiFID Org Regulation)?**

Yes, you will be exempt under article 2.1(c) MiFID if:

- you provide these services in the course of your professional activity;
- a close and factual connection exists between your professional activity and the provision of the investment service to the same client, such that the investment service can be regarded as accessory to your main professional activity;

- the provision of investment services to the clients of your main professional activity does not aim to provide a systematic source of income to you;
- you do not market or otherwise promote your ability to provide investment services, except where these are disclosed to clients as being accessory to your main professional activity; and
- your professional activity is regulated by legal or regulatory provisions or a code of ethics that do not exclude the provision of investment services.

This exemption is relevant, for example, to firms belonging to *designated professional bodies*, such as accountants, actuaries and solicitors, to whom Part XX of the *Act* applies. It could also apply to *authorised professional firms* which provide investment services in an incidental manner in the course of their professional activity. In our view, the criteria set out in ■ PROF 2.1.14 G in relation to section 327(4) of the *Act* are also relevant to considering whether a firm can rely on the this MiFID exemption (see further guidance in ■ PROF 2.1.16G).

If an *authorised professional firm* has the standard requirement on its permission that it "...must not carry on the specified regulated activities otherwise than in an incidental manner in the course of the provision by it of professional services (that is, services which do not consist of regulated activities)", our assumption is that it is exempt from MiFID if it complies with this requirement.

If you are an *authorised professional firm* not falling within article 2.1(c) MiFID, you may also wish to consider whether you are exempt or otherwise from MiFID requirements by virtue of the domestic implementation of the article 3 exemption (see Q48 and Q49).

The article 2.1(c) MiFID exemption may also apply to journalists, broadcasters and publishers (where they are subject to regulation or a code of ethics), although in most cases the FCA would not expect these persons to fall within the MiFID definition of investment firm (see Q7 and Q8).

**Own account**

**Q40.We regularly buy and sell financial instruments ourselves but never as a service to third parties. Are there any exemptions which might apply to us?**

Yes, you could fall within the article 2.1(d) MiFID exemption but not if you:

- are a market maker (please see Q41 below);
- are a member of, or a participant in, a regulated market or an MTF (except that non-financial entities can be members or participants as described in the answer to Q40A);
- have direct electronic access to a regulated market, an MTF or an OTF (except that non-financial entities can have such access, as described in the answer to Q40A);
- apply a high-frequency *algorithmic trading* technique (see Q41A); or
- deal on own account when executing client orders.

This exemption does not apply to dealing on own account in commodity derivatives, emission allowances or derivatives thereof (the exemption discussed in the answer to Q44 (Activities in relation to commodity derivatives) is relevant instead).

MiFID says that persons exempt under the commodities exemption described in the answer to Q44 are not required to meet the conditions laid down in the own account exemption described in this answer in order to be exempt. In the FCA's view that does not mean that you can do business of the type covered by the article 2.1(d) exemption without meeting the exemption conditions described in this answer just because you qualify for the commodities exemption. Recital 22 to MiFID confirms that the two exemptions apply cumulatively. Another reason for this conclusion is that articles 2.1(d) and (j) apply to different asset classes and there does not seem to be any reason apparent from MiFID why exemption under article 2.1(j) should be relevant to the asset classes in article 2.1(d).

See the answer to Q46 for more information about combining this exemption with other exemptions, particularly the exemption for commodity derivatives business.

**Q40A. When can a non-financial entity have direct electronic access to or be a participant in a trading venue without losing the benefit of the own account exemption described in the answer to Q40?**

The article 2.1(d) exemption can still be available if you are a member of, or a participant in, a regulated market or an MTF or you have direct electronic access to a regulated market, an MTF or an OTF, as long as:

- you are a non-financial entity; and
- your transactions are objectively measurable as reducing risks directly relating to your commercial or treasury financing activity, or the commercial or treasury financing activity of your group.

**Q40B. What does direct reduction of risk mean in the answer to Q40A?**

The second condition described in the answer to Q40A (objectively measurable reduction of risks) is designed to allow a non-financial business to hedge without losing the exemption. The following points are relevant to whether hedging meets this second condition:

- The exception covers hedging for commercial activities as well as treasury activities. It can therefore cover risks to a change in value of your group's assets, services, inputs, products, commodities or liabilities.
- Hedging may cover potential indirect impacts on your business as well as direct ones.
- A transaction may qualify as risk-reducing taken on its own or in combination with other hedging transactions.
- A transaction may be treated as risk-reducing even though it is not a perfect hedge. Thus for example your group may use proxy hedging through a closely correlated instrument to cover an exposure, such as an instrument with a different but very close underlying in terms of economic behaviour.
- If your group uses portfolio or macro hedging, it may not be able to establish a one-to-one link between a specific hedging transaction and a specific risk directly related to the commercial and treasury financing activities being hedged. The risks related to the commercial and treasury financing activities may be complex. For example, the risks may cover several geographic markets, products, time horizons or entities. Nevertheless, macro or portfolio hedging used to hedge a risk in relation to your group's overall risks may be treated as risk-reducing.
- Positions do not qualify as risk-reducing solely on the grounds that they form part of a risk-reducing portfolio on an overall basis. In such cases your

group's risk management systems should prevent such transactions from being categorised as risk-reducing.

• A risk may evolve over time and, in order to adapt to the evolution of the risk, a hedging transaction initially executed for reducing risk may have to be offset through the use of additional hedging transactions. As a result, hedging of a risk may be achieved by a combination of hedging transactions and offsetting transactions that close out earlier hedging transactions that have become unrelated to the risk.

• If a transaction originally qualifies as risk-reducing it does not stop being treated as risk-reducing just because the risk it hedges has since evolved.

• A transaction may be treated as risk-reducing if it qualifies as a hedging contract pursuant to International Financial Reporting Standards adopted in accordance with article 3 of Regulation (EC) No 1606/2002 of the European Parliament and Council.

**Q40C. What does non-financial entity mean in the answer to Q40A?**

In the FCA's view, non-financial entity means the same thing as it does in *MiFID RTS 21*.

**Q41. What is a market maker?**

A market maker is "a person who holds himself out on the financial markets on a continuous basis as being willing to deal on own account by buying and selling financial instruments against that person's proprietary capital at prices defined by that person" (article 4.1(7) MiFID). In our view anyone who satisfies the definition will be a market maker for the purposes of MiFID, even if they have not entered into the agreement with the regulated market required by article 48(2) of MiFID (Systems resilience, circuit breaker and electronic trading).

**Q41A. What is a high-frequency algorithmic trading technique?**

This question is included here because it is relevant to the own account exemption described in the answer to Q40 and to the commodities exemption described in the answer to Q44.

A high-frequency *algorithmic trading* technique is a type of *algorithmic trading* technique.Article 4.1(40) of MiFID defines a high-frequency *algorithmic trading* technique as an *algorithmic trading* technique characterised by:

• infrastructure intended to minimise network and other types of latencies, including at least one of the following facilities for algorithmic order entry:
o co-location;
o proximity hosting; or
o high-speed direct electronic access;

• system-determination of order initiation, generation, routing or execution without human intervention for individual trades or orders; and

• high message intraday rates which constitute orders, quotes or cancellations.

**Employee share and company pension schemes**

**Q42. Is there an exemption relating to employee share schemes and company pension schemes?**

Yes, there is an exemption in article 2(1)(f) MiFID for persons providing investment services consisting exclusively in the administration of employee-participation schemes, for example employee share schemes and company pension schemes. In our view, whilst administration for these purposes could extend to services comprising reception and transmission or execution of orders on behalf of clients or placing, it would not include *personal recommendations* in relation to, or managing, the assets of employee share schemes or company pension schemes.

This exemption can also be combined with the "group exemption" in article 2.1(b) of MiFID, by virtue of article 2.1(g) of MiFID. See the answer to Q46 for more about combining exemptions.

**Collective investment undertakings**

**Q43. Are we right in thinking that MiFID does not apply to collective investment undertakings and their operators?**

Yes. Generally speaking, collective investment undertakings are specifically exempt, as are their *depositaries* and managers. For collective investment undertakings within the scope of the *UCITS Directive* or *AIFMD* the "manager" corresponds to the *management company* or *AIFM* of the undertaking. So far as *collective investment schemes* which are outside the scope of the *UCITS Directive* or *AIFMD* are concerned, the "manager" corresponds, in essence, to the *operator*of a *scheme*and not to a person who is managing the assets of the *scheme* (unless that person is also the *operator*). In our view, the manager of a collective investment undertaking only benefits from the exemption in respect of any investment services or activities it may carry on in that capacity. To the extent that it also provides investment services or performs investment activities in a different capacity, for example, if it provides investment advice to, or manages the assets of, an individual third party, these services and activities fall outside the scope of this exemption.

In the case of *UCITS management companies*, some *MiFID* provisions will apply to those who provide portfolio management services (other than *collective portfolio management*), investment advice or safekeeping and administration services in relation to *units* to third parties, by virtue of article 6.4 of the *UCITS Directive* (see Q6). *UK AIFMs* will also be subject to *MiFID* if they provide *investment services or activities* for an undertaking other than a *fund* for which they are appointed as manager or *operator*. *Full-scope UK AIFMs* are only able to provide a limited range of such activities, for which they are subject to specific *MiFID* provisions by virtue of article 6.6 of *AIFMD* (see Q6A).

**Exemption for commodity derivatives business**

**Q44. Who can rely on the exemption in article 2.1(j)?**

You may be able to rely on the exemption if:

- you deal on own account in commodity derivatives or emission allowances or derivatives thereof; or
- provide other investment services in commodity derivatives or emission allowances or derivatives thereof to clients or suppliers of your main business (or if you are part of a group, the group's main business); or
- both.

This exemption can include someone dealing on own account as a market maker.

If you deal on own account when executing client orders you can only meet the exemption condition if the client is a client or supplier of your group's main business.

The article 2.1(j) exemption does not apply to you if you apply a high frequency *algorithmic trading* technique.

The exemption will only apply if what you do is ancillary to your main business (see Q45 for more about this).

The exemption is not available if your group's main business is any of the following (see the answer to Q44A for what main business means in this context):

- the provision of investment services; or
- the provision of banking services; or
- acting as a market maker in relation to commodity derivatives.

**Q44A. How do I know whether my main business is investment, banking or commodities?**

When considering what is a group's 'main business' for the purpose of the requirement described in the answer to Q44 that your main business should not be investment services, banking services or commodity derivatives market making, in our view various factors are likely to be relevant including turnover, profit, capital employed, numbers of employees and time spent by employees. These factors should then be considered in the round in deciding whether any one operation or business line amounts to your group's main business.

The determination of your main business as described in this answer is not directly related to the test for deciding whether your commodities business is ancillary to your main business (the ancillary test is referred to in the answer to Q45). This is because the ancillary test compares the size of your commodities business with the rest of your business but does not specify how to identify what your main business is within your non-commodities business.

**Q44B. Are there any formalities for using the commodities exemption?**

It is a condition of the commodities exemption described in the answer to Q44 that you:

- should notify annually the relevant competent authority that you make use of this exemption; and
- upon request, report to the competent authority the basis on which you consider that the requirement for the commodities business to be ancillary is met.

If you are a UK firm, the FCA is the relevant competent authority for these purposes.

If you carry out some occasional commodity derivatives activities you may not need to rely on this exemption. See the answer to Q7 (We provide investment services to our clients. How do we know whether we are an investment firm for the purposes of article 4.1(1) MiFID?) for more on this.

**Q44C. Can the commodities exemption be combined with other exemptions?**

Yes.

There is no requirement that someone relying on this exemption must not carry on an activity covered by one of the other exemptions. In particular, this exemption can be combined with the exemption for own account transactions

described in the answer to Q40 (see recital 22 to MiFID). For more on combining exemptions, please see the answer to Q46.

**Q45. What is an ancillary activity for the purposes of the commodities exemption?**

You can find the meaning of 'ancillary' for the purposes of the commodities exemption described in the answer to Q44 in Commission Delegated Regulation (EU) 2017/592 (regulatory technical standards for the criteria to establish when an activity is considered to be ancillary to the main business).

This answer does not give a full summary as the definition is too detailed for *PERG*. Instead this answer summarises the broad approach.

There are two tests. The exemption only applies if you meet both tests. Both are based on commodities trading activities in the EEA.

The first test looks at the size of trading activities of members of your group in various asset classes. For each class, this is calculated by comparing their trading activities in that class with the overall trading activity in the EEA for that class.

The asset classes are made up of emission allowances and various types of commodity derivatives. The emission allowances asset class includes emission allowances to which the exemption for emission allowances in article 2.1(e) (see the table in the answer to Q35A) applies and any bidding under the *auction regulation*.

For this test to be met, the trading level of persons within your group needs to be below the maximum amount for each asset class. There is a different maximum amount for each class.

Certain privileged transactions are excluded from the calculation:

- intra-group transactions that serve group-wide liquidity or risk management purposes;
- transactions in derivatives that reduce risks directly relating to commercial activity or treasury financing activity in accordance with criteria set out in Commission Delegated Regulation (EU) 2017/592 (regulatory technical standards for the criteria to establish when an activity is considered to be ancillary to the main business);
- transactions in commodity derivatives and emission allowances entered into to fulfil obligations to provide liquidity on a *trading venue*, where such obligations are required by:
  o regulatory authorities in accordance with EEA law;
  o national laws, regulations and administrative provisions; or
  o those *trading venues*; and
- transactions executed by a group member authorised under MiFID or the CRD.

The second test has two calculation methods. If the result of either calculation is that you fall below the specified threshold, you meet the second test.

- One method is based on the size of group trading activities in commodity derivatives and emission allowances.
- The second measure compares the estimated capital employed for carrying out commodity derivative and emission allowance activities with group capital.

**Q46.Is it possible to combine article 2 exemptions?**

Various other answers to questions in this section deal with certain detailed combinations of exemptions:

- Q42 deals with employee share schemes and company pension schemes.
- It is possible to combine the exemption for own account dealing in article 2.1(d) and the exemption for commodity derivatives in article 2.1(j). The answer to Q40 deals with the treatment of the commodity derivatives business of a firm relying on article 2.1(d). The answer to Q44C deals with the treatment of business within article 2.1(d) for a firm relying on the commodity derivatives exemption in article 2.1(j).

In certain cases a firm will not need to combine exemptions. For example an insurer relying on the exemption described in the answer to Q36 (We are an insurer. Does MiFID apply to us?) does not need to rely on any other exemption.

The answer to this question (Q46) is about whether there is a more general principle that article 2 exemptions can be combined.

There is an argument that the drafting of some of the exemptions does not allow this approach. For example, the group exemption (see the answer to Q37) says that the exemption is available to persons providing investment services exclusively for their fellow group members. However in the FCA's view it is generally possible to combine article 2 exemptions. Recital 22 to MiFID says that exemptions apply cumulatively and that the ability to combine the exemptions in articles 2.1(d) (own account dealing) and 2.1(j) (commodity derivatives) is just an example of this principle. This is consistent with the point that there is no reason apparent from MiFID why combining exemptions should not be allowed.

Where an exemption is only available if the person only carries on a limited range of investment services or activities (as is the case for example with the group exemption) it can be argued that this restriction does not cover a service or activity which is covered by another exemption. This is on the basis that an exempt activity is not an investment service or activity for these purposes. The European Commission's Q&A's dealing with MiFID 1 take this approach.

Treating an exempt activity as not being a MiFID investment service or activity in this way only applies for the purpose of article 2 of MiFID, meaning that it is only relevant for deciding whether a person is a MiFID investment firm.



**Q46A. Is it possible to combine the article 2 and article 3 exemptions?**

The FCA does not believe that it is generally possible to combine the exemptions in article 2 with the exemption in article 3. However in the FCA's view, a firm that relies on the article 2(1)(i) exemption (see Q43) can combine this with article 3 in relation to business falling outside the article 2(1)(i) exemption.

If however you are subject to the UCITS Directive or the AIFMD you may be restricted in your ability to carry out all the activities within the article 3 exemption.

**Locals**

**Q47. We traded on an investment exchange as a local firm and were exempt from MiFID 1. Are we exempt under MiFID?**

The exemption for locals in MiFID 1 no longer applies. It is unlikely that the own account exemption in article 2.1(d) will be available as that exemption does not apply to members of, or participants in, a regulated market (see Q40).

**The article 3 exemption**

**Q48. Article 3 is an optional exemption. Will the exemption apply to UK firms?**

Yes, in part. The exemption in articles 3.1(a) to (c) has been exercised by The Treasury. The answers to Q49 to Q53 explain the exemption in more detail.

Articles 3.1(d) and (e) of MiFID provide additional optional exemptions, but they have not been implemented in the UK.

**Q49.Which firms might fall within this exemption?**

The exemption applies to persons who meet all the following conditions:

- they do not hold clients' funds or securities and do not, for that reason, at any time, place themselves in debit with their clients;
- they do not provide any investment service other than reception and transmission of orders or investment advice, or both, in relation to transferable securities and units in collective investment undertakings;
- they transmit orders only to one or more of the following:
  - other MiFID investment firms;
  - credit institutions authorised under the *CRD*;
  - branches of third country investment firms or credit institutions which are subject to, and comply with, prudential rules considered by the *appropriate regulator* to be at least as stringent as those laid down in MiFID,MiFID, the *CRD* or the *EU CRR*;
  - collective investment undertakings or their managers authorised under the law of an EEA State to market units to the public;
  - EU incorporated investment companies the securities of which are listed or dealt in on a *regulated market*, for example investment trust companies.

If you are a UK firm that meets these qualifying conditions, you will be exempt from regulations made by the European Commission under MiFID.

Where you provide *personal recommendations* or receive and transmit orders in relation to derivatives which are MiFID financial instruments but not transferable securities, you will fall outside the scope of this exemption. In our view, this would be the case, for example, if you provided either or both of these investment services in relation to OTC derivatives concluded by a confirmation under an ISDA master agreement (see ■ PERG 13 Annex 2 Table 2).

**Q50.We are (or previously were) an IFA and have a permission which covers (i) arranging (bringing about) deals in investments; (ii) making arrangements with a view to transactions; and (iii) advising on investments, in each case in relation to securities but not derivatives. We are not permitted to hold client money or investments and do not have dealing or managing permissions in relation to MiFID financial instruments. Are we exempt?**

The FCA expects so, assuming you do not:

- carry on activities outside your permission; or
- transmit orders to persons other than those listed in Q49 (for example, you will fall outside the exemption if you transmit orders directly to collective investment schemes whose units cannot be marketed to the public in any EEA State either because they are unregulated schemes or non-EEA authorised collective investment schemes); or
- place MiFID financial instruments without a firm commitment basis (see Q22 and Q23).

We would generally not expect IFAs to be placing MiFID financial instruments without a firm commitment basis as we associate placing of financial instruments with situations where a company or other business vehicle wishes

to raise capital for commercial purposes, and in particular with primary market activity.

**Q51.What happens if we breach any of the qualifying conditions (see Q49)? Do we then lose the exemption?**

You are required to notify us of a breach (see ■ SUP 15.3.11 R). We will then consider whether you should continue to benefit from the exemption and what, if any, supervisory or occasionally enforcement action is appropriate in the circumstances.

**Q52. If we fall within the exemption does this prevent us from acquiring passporting rights under MiFID?**

No. Firms which would otherwise be exempt can apply to opt into MiFID regulation with a view to acquiring passport rights (although they would then become subject to the requirements of MiFID, including certain enhanced prudential requirements - see Q58 and Q59).

**Q53.What is the practical effect of exercising the optional exemption for those firms falling within its scope?**

You are not a firm to which MiFID applies and so are not a *MiFID investment firm* for the purposes of the Handbook. As such you are not subject to the requirements of the *CRD* as transposed in the Handbook and the *EU CRR* and cannot exercise passporting rights.

Article 3.2 of MiFID applies certain MiFID requirements to firms making use of the article 3 exemption. These are implemented in the *Handbook* and the *Act*.