ROKAS LAW FIRM

Significant amendments on MiFID II by Directive 2021/338

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Six years after Directive 2014/65 (MiFID II) entered into force, the European Parliament and the Council of the E.U. made minor amendments to it with the adoption of the new Directive 2021/338, to which the Member States should have harmonized their legislation by 28 November 2021. The amendments are intended to be part of a set of measures aimed at the recovery of the capital markets that have been affected by the pandemic. The measures also aim to reduce the regulatory complexity and compliance costs of investment services as well as to eliminate distortions of competition, without compromising investor protection. The following are among the most important changes brought by the new Directive.

1. Changes in some organizational requirements for investment service providers combined with exceptions to product governance requirements

A new provision is added to MiFID II with Article 16[a], which abolishes the approval process of existing financial instruments that are related to a specific target market [art.16 (3), subpar. 2-5, και art. 24(2) of MiFID II], which is determined by the nature of the manufactured investment products and by their quality criteria (i.e. the type of clients to whom the product is addressed, their knowledge and experience, their financial situation, risk tolerance and compatibility of the product's risk profile with the target market, the clients' goals and needs), as they emerge from the ESMA Guidelines of 05.02.2018 on the requirements of the MiFID II Directive on monitoring, in the case of,

a. Investment services related to corporate bonds with a **make-whole clause**. Pursuant to this clause, in the event of early redemption of a corporate bond, the issuer is required to pay to the investor holding the bond an amount equal to the sum of the **net present value** of the remaining coupon payments expected until maturity and the principal amount of the bond to be redeemed. Bonds a make-whole clause are generally considered safe and simple products that are eligible for retail clients and as a result the abolition of their approval process does not add any risk.

b. Financial instruments that are available on the market and distributed only to **eligible counterparties** provided by art. 30 MiFID II.

2. Changes in information requirements and transparency

Electronical means are the default option for providing investment information. However, this regulation does not completely abolish the provision of information on paper, as retail clients can request the provisions of information on paper and firms are obliged to inform them that they have this right.

The obligation to provide information to professional clients and eligible counterparties about costs and associated charges is abolished. Ratio of this arrangement is the fact that the above persons are provided information tailored to their needs, which is more detailed than the standardized and mandatory costs information. **The abolition does not include services of investment advice** and **portfolio management** due to the lack of sufficient experience and knowledge of professional clients and eligible counterparties regarding these services.

Investment firms are required to undertake a cost-benefit analysis in the activities of selling a financial instrument and buying another financial instrument or exercising a right to make a change with regard to an existing financial instrument («switching of financial instruments»). They are also required to inform the clients on whether the benefits of such a transaction outweigh the costs. Professional clients, with whom the investment firm maintains ongoing relationships, are exempt from that requirement.

The periodic reporting requirement regarding the execution of client order (RTS 27 reporting requirements), is postponed until 28 February 2023, while the reporting requirement regarding the services that have already been provided to professional clients and eligible counterparties is immediately abolished. ESMA has already submitted a consultation on 24.09.2021.

3. Provision of research by third parties – jointly pay for research and execution services

The possibility for investment firms to pay jointly for research and execution services is stipulated and regulated under 3 conditions: a) if there is such an agreement, in which any combined charges or joint payments for research are stipulated, b) if the clients have been already been informed and c) if the joint payment concern issuers whose market capitalisation did not exceed EUR 1 billion, as expressed by end-year quotes, for the period of 36 months preceding the provision of the research. In the case of non-listed firms this restriction refers to their own capital.

4. Criteria for ancillary investment activity

New criteria are introduced based on which a trading activity is considered ancillary to the main business, and the firm that exercises it may make use of an exemption from the requirement to obtain authorisation as an investment firm. Now firms that exercise ancillary activities must notify the relevant competent authority only after they have applied for the ancillary activity exemption and to provide the necessary elements to satisfy the quantitative tests that determine whether their trading activity is ancillary to their main business. The criteria are a) whether the net outstanding notional exposure in commodity derivatives is below an annual threshold of EUR 3 billion; b) whether the capital employed by the group to which the person belongs is predominantly allocated to the main business of the group and c) whether or not the size of the activities carried out by the firm on its own account exceeds the total size of the other trading activities at group level. ESMA is responsible for developing draft regulatory technical standards regarding

the exemption applications that firms are required to submit in order to avoid being required to obtain an operating license as an investment firm.

Public consultation procedures on these technical standards are ongoing and to date the text of the delegated Commission's Rules of Procedure setting out the ancillary activity criteria has not been finalized.

5. Possession of commodity derivatives Regime

Given that the position limit regime is unfavourable for the development of new markets, position limits are set only for significant or critically important commodity derivatives, with the specification of these concepts for agricultural commodity derivatives, without, however, excluding agricultural commodities and OTC derivatives contracts from the position limit regime. In the Recitals of the Directive the exclusion of securitised derivatives is also proposed.

ESMA undertakes to establish the hedging exemption procedure for financial entities that trade on behalf of non-financial entities within a predominantly commercial group[1], provided that the positions held objectively reduce the risks directly related to the commercial activity of the specific non-financial entity or are performed in order to fulfill a liquidity obligation at a trading venue.

ESMA shall also draw up a list of critical commodity derivatives for the determination of the calculation methodology for establishing the spot month limit and a single position limit shall be established by the central competent authority for all transactions of agricultural commodity derivatives. A consultation document has been submitted for these matters within the competence of ESMA and the delegated Regulation that will result from it will enter into force on 28.02.2022.

Lastly, position management controls of art. 57(6) MiFID II, pursuant to which, for derivatives traded in more than one trading venue/jurisdiction, the position limit is set by the authority of the trading venue where the largest volume of trading takes place and the competent authorities of the trading venues reach cooperation agreements that make possible the setting of a single position limit, is reinforced, while in accordance with the provisions of the Article for the central competent authorities, a detailed list of the positions held shall be submitted to them on a daily basis [art. 58 (2) MiFID II].

[1] A predominantly commercial group within the meaning of the new Directive to which we are referring (2021/338) means any group of which the main business is not the provision of investment services within the meaning of this Directive, or the performance of any activity listed in Annex I to Directive 2013/36/EU (Capital Requirements Directives, known as CRD) on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, or acting as a market maker in relation to commodity derivatives.