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MIFID QUICK FIX AND WHAT'S NEXT FOR THE MIFID2 REVIEW

“Quick fix” amendments to MiFID2 have now been **published** in the Official Journal. These amendments aim to support economic recovery from the COVID-19 pandemic, including via relief from certain administrative requirements on firms. EU Member States are required to transpose the quick fix amendments into their national frameworks by 28 November 2021 and apply them by 28 February 2022. Alongside this, the scheduled MiFID2 review continues, with the Commission expected to publish a further legislative proposal towards the end of 2021.

What changes does the “quick fix” make to MiFID2?

The quick fix amendments to MiFID2 aim to simplify certain existing requirements in a targeted manner to alleviate administrative burdens on firms, while continuing to safeguard investor protection. Key changes include:

Information and reporting requirements

- **Exemption from ex ante costs and charges:** There is a new exemption from the requirement to provide ex ante cost and charges disclosures with respect to agreements to buy or sell financial instruments concluded by means of distance communication. Where the exemption applies, firms will be able to provide cost and charges information without undue delay after the conclusion of the transaction if the client has consented to receiving the information after conclusion of the transaction and has been given the option of delaying the transaction until the client has received the information.
- **Electronic communications with clients:** The default method for firms to communicate with their clients will be switched from paper-based to electronic communication, although retail clients can elect to continue receiving paper communications.
- **Temporary suspension of best execution reports:** The amendments provide for a temporary suspension of the requirement on trading venues and systematic internalisers to submit quarterly best execution reports under RTS 27. The suspension will apply until the date 2 years after the entry into force of the quick fix legislation (i.e., until 27 February 2023). However, because the suspension cannot take effect until it has been transposed into the national law of Member States, the suspension would only apply from 28 February 2022 until 27 February 2023. It is unclear whether this was the intended effect, or whether the Commission may take action to apply the suspension from an earlier date (e.g., through a forbearance statement or Q&A interpreting the quick fix legislation).

Key points

- MiFID “quick fix” published in the OJ 26 February 2021, with amendments due to apply from 28 February 2022
- Key amendments relate to information and reporting requirements, product governance, research requirements and the commodity derivatives regime
- The MiFID quick fix requires the Commission to report on its review of various aspects of the MiFID regime by 31 July 2021
- The Commission expects to publish a legislative proposal under the broader MiFID2 review by the end of 2021

- **Product switching and cost benefit analysis:** There is a new requirement for firms to carry out a cost benefit analysis where providing investment advice or portfolio management that involves switching of financial instruments. When providing investment advice, firms will need to inform clients whether the benefits of switching outweigh the costs. However, firms will not be required to carry out this cost benefit analysis relating to product switching for professional clients unless those clients decide to opt in to receive this information.

Product governance

- **Exemptions from product governance requirements:** There is a new exemption from product governance requirements for simple corporate bonds with so-called “make whole clauses”, which are generally considered safe and simple products that are eligible for retail clients (provided that they do not include any other embedded derivatives). However, it’s worth noting that currently ‘make whole’ clauses risk bonds being classed as a PRIIP and therefore unsuitable for EEA retail customers without the provision of a Key Information Document (KID). There is also a new general exemption from product governance requirements where financial instruments are exclusively marketed or distributed to eligible counterparties.

Research requirements

- **Research unbundling:** Amendments to the research requirements will allow firms to bundle costs for research and execution with respect to small and mid-cap issuers, whose market capitalisation does not exceed EUR 1 billion. However, to benefit from these amendments, the firm must have informed its clients about the joint payments for research and execution services and must have entered into an agreement with the research provider identifying the part of the combined charges or joint payments for research and execution services that is attributable to research. The aim is to help to increase research on such issuers and their access to funding. This amendment was originally proposed as an amendment to the MiFID2 Delegated Directive (EU) 2017/593 but has now been included in the MiFID quick fix.
- **Meaning of research for unbundling purposes:** The new provisions on joint payments for research and execution services also set out what is meant by “research” for these purposes (and for the purposes of Article 24 MiFID more generally). It is unclear how this relates to the scope of the existing MiFID ancillary service of providing investment research.

Commodity derivatives requirements

- **Ancillary activities:** Amendments to the ancillary activities exemption provide that national competent authorities (**NCA**s) should be able to rely on a combination of quantitative and qualitative elements when establishing whether an activity is considered to be an ancillary activity. The Commission will be empowered to provide guidance on this approach of combining quantitative and qualitative threshold criteria, and to develop a delegated act on the criteria. The Commission is also required to review the impact of the exemption for emission allowances and their derivatives and if appropriate publish an legislative proposal to amend it by 31 December 2021. As part of its review, the Commission is required to consider the impact on investor protection and integrity and transparency of markets in emission allowances and their derivatives and whether measures should be adopted on trading on third country venues.

- **Position limits regime narrowed:** The scope of the commodity derivatives position limits regime is being reduced, such that it will only apply to critical or significant commodity derivatives that are traded on trading venues, and to their economically equivalent OTC contracts. Critical or significant derivatives are commodity derivatives with an open interest of at least 300,000 lots on average over a one-year period, as well as agricultural commodity derivatives. ESMA is mandated to draw up a list of critical or significant commodity derivatives for this purpose as well as regulatory technical standards on the calculation methodology competent authorities should use when setting position limits.
- **New exemptions from the regime:** There are new exemptions from the position limits regime for securitised derivatives and for positions resulting from transactions undertaken to fulfil obligations to provide liquidity. There is also a new, limited hedging exemption for financial entities that trade on behalf of non-financial entities in a predominantly commercial group. ESMA is mandated to develop technical standards on the procedures to apply for these exemptions.

Further review

Article 5 of the MiFID quick fix Directive also requires the Commission to carry out a public consultation and review various aspects of the MiFID regime, with a report due by 31 July 2021. The areas for review identified are:

- the operation of the structure of the securities markets, reflecting the new economic reality after 2020, data and data quality issues related to market structure, and transparency rules, including issues related to third countries;
- the rules on research;
- the rules on payments to advisers and their level of professional qualification;
- product governance;
- loss reporting; and
- client categorisation.

MiFID2 Review

Alongside this, the Commission continues to work on its broader MiFID2 review.

In a [speech](#) published on 24 February 2021, Commissioner Mairead McGuinness indicated that the Commission intends to publish its legislative proposal on the MiFID2 review towards the end of 2021. Areas of focus for the Commission include:

- transparency requirements, assessing whether different execution venues operate on a level playing field and whether existing transparency requirements may need to be strengthened;
- trading data and the establishment of a consolidated tape; and
- investor protection requirements, including a particular focus on retail investors.

There is also the potential for changes made as part of the quick fix to be revisited. In particular, the decision to provide for carve-outs from the requirement for research unbundling faced strong opposition, with a recent ESMA [report](#) also finding that there was no evidence of research into SMEs being adversely affected by the original

unbundling rules or of a decline in the quality of investment research produced following implementation of MiFID2. Similarly, in relation to the temporary suspension of the best execution reports, the Commission has been tasked with undertaking a comprehensive review of the adequacy of these reports by 28 February 2022. The MiFID review may provide an opportunity to reopen this and other issues addressed under the MiFID quick fix.

ESMA has already consulted and reported on various aspects of MiFID2 and MiFIR, as previously **mandated** by the Commission. ESMA is expected to publish a final set of reports during the summer of 2021 with a Commission legislative proposal on amending MiFID2 and MiFIR to follow by the end of 2021.

Table 1 provides an overview of key ESMA consultations and reports published to date that will feed into the broader MiFID2 review. Note that ESMA is not due to report on its review of the interoperability and FMI open access provisions in Article 35-37 MiFIR and Articles 7-8 EMIR until January 2022 and so these are not expected to form part of the current MiFID2 review.

In addition, ESMA issued a **call for evidence** on RTS 1 and 2 relating to transparency requirements in September 2020 and is expected to publish a formal consultation in Q1 2021. Again, this does not technically form part of the current MiFID2 review as this call for evidence relates to Level 2 measures under MiFIR rather than potential changes to MiFIR itself.

Will there be a UK MiFID2 Review?

Neither the MiFID2 quick fix amendments nor future amendments that may be made under the broader MiFID2 review will apply in the UK. However, the UK government and FCA are expected to consider whether to make similar amendments to the onshored UK regime in due course.

Any plans to amend the onshored UK regime will be constrained by the fact that much of the regime can only be altered by or under a new Act of Parliament (so cannot be amended by a statutory instrument or by FCA rules). The Financial Services Bill proposes to give the PRA the power to make rules re-stating elements of the Capital Requirements Regulation and associated level 2 regulations revoked by HM Treasury, so a similar approach could be taken in relation to MiFID and MiFIR.

We know that the UK is already looking at areas of MiFID2 and MiFIR that could be targeted for reforms, including the open access regime for exchange traded derivatives under MiFIR, which currently applies in the UK (because amendments to delay its application were not in effect before the end of the Brexit transition period).

Table 1: An overview of key ESMA consultations and reports published to date that will feed into the broader MiFID2 review

Topic	Official documents	Key recommendations or proposals
Development in prices for pre- and post-trade data and on the consolidated tape for equity instruments	Report published 5 December 2019	<ul style="list-style-type: none"> • Establish a real-time consolidated tape for equity instruments • Targeted legislative changes and supervisory guidance to improve market data transparency
Effects of product intervention measures (relating to CFDs and binary options)	Report published 3 February 2020	<ul style="list-style-type: none"> • Grant NCAs and ESMA powers to apply restrictions/prohibition directly to AIFMs and UCITS management companies • Consolidate pan-European product intervention measures, either making them permanent or via a further extension • Clarify the application, supervision and enforcement of overlapping product intervention measures
Position limits and position management on commodity derivatives markets	Report published 1 April 2020	<ul style="list-style-type: none"> • Refocus the scope of the regime to significant or critical contracts • Introduce a narrow hedging exemption for financial counterparties in relation to groups • Enhance convergent implementation of controls by trading venues
Transparency regime for equity and equity-like instruments, the double volume cap mechanism and the trading obligations for shares	Report published 16 July 2020	<ul style="list-style-type: none"> • Restrict the use of the reference price waiver to larger orders • Increase the minimum quoting obligations and a revised methodology for determining the standard market sizes relevant for quoting by internalisers • Transform the double volume cap mechanism into a single volume cap by deleting the 4% trading venue threshold • Clarify the scope of the share trading obligation in relation to third-country shares
Systematic internalisers in non-equity instruments	Report published 16 July 2020	<ul style="list-style-type: none"> • Allow systematic internalisers to withdraw quotes at any time • Simplify the requirements applicable to quotes in liquid and illiquid non-equity instruments • Extend publishing requirements for quotes to non-equity instruments
Transparency regime for non-equity instruments and the trading obligation for derivatives	Report published 25 September 2020	<ul style="list-style-type: none"> • Delete the specific waiver and deferral, and lower the pre-and post-trade large in scale thresholds • Streamline the deferral regime with a simplified system based on volume masking and full publication after two weeks, and by removing the supplementary deferral options left to national competent authorities • Confer power on ESMA to take a decision with respect to the suspension of transparency • Introduce the possibility to suspend on short notice the application of the derivative trading obligation • Complement the criteria used to grant equivalence to third-country trading venues for the purpose of the derivative trading obligation with conditions relating to transparency and non-discriminatory access

Topic	Official documents	Key recommendations or proposals
Obligations to report transactions and reference data	<p><u>Consultation paper</u> published 24 September 2020</p> <p>Report expected Q1 2021</p>	<ul style="list-style-type: none"> • Proposal to make UCITS management companies and AIFMs providing one or more MiFID services to third parties subject to transaction reporting • Proposal to extend the concept of traded on a trading venue to derivative instruments traded through a systematic internaliser • Proposals to revise the scope of indices subject to the reporting obligation • Proposals to modify, remove or replace data elements • Proposals to further align the MiFIR and EMIR reporting regimes • Proposals to enhance the effectiveness of using the LEI of the issuer of the financial instruments for reference data reporting
Functioning of organised trading facilities	<p><u>Consultation paper</u> published 25 September 2020</p> <p>Report expected March 2021</p>	<ul style="list-style-type: none"> • Proposal to clarify the conditions and boundaries of trading venue authorisation • Proposal to define the concept of bulletin boards • Request for input on the functioning of the regulatory framework applicable to internal crossing systems • Proposal to clarify that the restriction on dealing on own account only applies to the MTF operated by the investment firm
Guidelines on the MiFID II/ MiFIR obligations on market data	<p><u>Consultation paper</u> published 6 November 2020</p> <p>Report expected Q2 2021</p>	<p>Following the Market Data Review Report published on 5 December 2019, seeks views on draft Guidelines on:</p> <ul style="list-style-type: none"> • The provision of market data on the basis of costs • The obligation to provide market data on a non-discriminatory basis • The per-user fee obligation • The obligation to keep data unbundled • Transparency obligations, including standardised publication format, key terminology, cost disclosure and auditing practices • The obligation to make market data free of charge 15 minutes after publication
Algorithmic trading requirements	<p><u>Consultation paper</u> published 18 December 2020</p> <p>Report expected July 2021</p>	<ul style="list-style-type: none"> • Proposal to extend the definition of algorithmic trading to include trading conducted on systematic internalisers • Proposals to clarify the provisions applicable to algorithmic and high-frequency traders • Proposals relating to the organisational requirements for investment firms and trading venues, including testing of algorithms • Proposal to widen the scope of the tick size regime to all exchange traded funds • Request for input on the current market making regime, including speedbumps and trade feeds

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