

ESMA updates its Q&A on MiFID II and MiFIR investor protection topics

On 16 December 2016, the European Securities and Markets Authority (ESMA) published an updated version of the Questions and Answers (Q&As) on the Directive on Markets in Financial Instruments (MiFID II) and the Regulation on Markets in Financial Instruments (MiFIR). As the following selection of examples illustrates, the clarifications that the Q&As update provides concern a range of investor protection topics.

Best Execution

As regards the possibility, for firms, to use a single venue to execute client orders, the ESMA expects them to understand the market for execution venues operators and take into consideration the existence of new players, new venues functionalities or execution services beforehand. Concerning reports required under RTS 27 (data to measure quality of execution) and 28 (information on how and where the firm has executed client orders), the ESMA considers it appropriate to keep each report available in the public domain for a minimum period of two years. The Q&A update also specifies that both types of reports should be published on the firm website in an identifiable location on the page without access limitation, meaning that it should not be placed behind the firewall, registration page, or be subject to password. The ESMA confirms that firms are expected to provide a summary of the analysis and conclusions they draw from their execution policy for each class of financial instrument and should not provide a consolidated summary covering all classes of financial instruments.

Suitability and Appropriateness

With regard to the record keeping and documentation obligations pursuant to Articles 16(6), 25(6) and 16(7) of MiFID II, the Q&A update clarifies that, although the requirements must be complied with individually, it is reasonable to allow the firm to draft one single document as long as it fulfills all the requirements, the record is kept for the prescribed period and is made available to the client under certain prescribed conditions.

Underwriting and placing

The ESMA details the content of the records that firms must keep when providing underwriting or placing services to their clients. For instance, firms must provide a justification of the final allocation made to each client, including reasons for such allocation unless the firm can demonstrate that such detail has been already recorded.

Inducements (research)

The Q&A update clarifies that any money deducted from the client to fund a research payment account (RPA) belongs to the investment firm and is not to be considered as client assets. In this regard, the ESMA believes that the firm should make the best effort to align the timing of the cash paid by the client to the firm and the expenditure of the research paid by the firm to the research provider. In addition, firms must have in place policies and systems to assess the nature of any service, benefit or material paid or provided by any third party to determine whether they can provide or accept it. Firms cannot accept to receive research for free where no assessment has been made under the inducements rules. Rules on inducements apply in the same manner irrespective of the relationship between the provider and the firm (i.e., if they are part of the same group or not). Therefore, firms need to either assess whether accepting the inducement (research) or decide to use the paying arrangements. In the latter case, firms should pay particular attention to any potential

conflicts of interests as well as their obligations to assess the quality of research and keep appropriate controls and oversight over the amounts paid with reference to the quality criteria.

Post-sale reporting

Firms are required to inform their clients when the overall value of their portfolio, as evaluated at the beginning of each reporting period, depreciates by 10% and thereafter at multiples of 10%. The ESMA specifies that this does imply that firms need to have systems in place to value the portfolio on an ongoing basis. Rather, it means that they are obliged to value the overall portfolio at the beginning of the reporting period and at least once each day. The Q&A update also elucidates the treatment of cash withdrawals, indicating that, until a new periodic statement is provided, the 10% threshold shall be calculated after adding back the amounts withdrawn to the value of the remaining portfolio.

Information on costs and charges

The MiFID requires that clients receive once a year an overview of the total costs and charges incurred in the previous year, based on their personal circumstances and actually incurred costs. According to the Q&A update, these costs and charges shall be expressed both as a cash amount and as a percentage. However, firms can decide to provide this information more frequently, for instance, every time the client receives a (quarterly) report about the investments. In this context, firms must ensure that the differences between the annual ex-post figures based on actual costs, and the quarterly cost figures are minimized. For the sake of clarity, firms should inform clients in advance on the characteristics of the ex-post information. The Q&A on MiFID II and MiFIR investor protection topics can be found via the following link.