Brexit planning: Changes to UK law

Markets in Financial Instruments (Amendment) (EU Exit) Regulations 2018

Preparing the UK MiFID regime for Brexit

What does this SI do?
> EU regulations are retained in UK law as at exit day. But these EU rules need changing so that they work in a UK-only context. This draft SI proposes changes to that retained EU law where it relates to MiFID II. It also amends parts of existing UK law to ensure that the law continues to operate after the UK leaves the EU.

> These changes are intended to take effect on exit day in the event of a no deal. See the section “What happens next?” below for more detail.

> HM Treasury have also published a policy note for this SI.

What are the key implications?
> Interplay with the temporary permissions regime: Firms that passport into the UK on a branch or cross-border basis immediately before exit day may participate in the TPR. The MiFID SI applies the UK regulatory framework to these TPR firms, but those firms may be deemed to comply with the UK rules if they meet equivalent EU requirements. This “substitute compliance” will not be available for all MiFID obligations (e.g. the derivatives and shares trading obligation and, in the case of UK branches of EEA firms, UK transaction reporting and MiFID conduct of business obligations). See the Annex below for more detail.

> Definition of systematic internaliser: Under MiFID II, a systematic internaliser is a firm that deals on own account on an organised, frequent, systematic and substantial basis outside a regulated market, multilateral trading facility or organised trading facility. The MiFID SI amends the definition to capture all trades done outside a UK regulated market, a UK MTF or UK OTF. This means that trading on EEA venues could be SI activity from a UK perspective, subject to further guidance from the FCA.

> Thresholds for systematic internalisers: The SI threshold calculation currently takes into account total trading in the EEA. The MiFID SI changes the denominator in the SI calculation to total trading within a “relevant area”. The relevant area will be determined by the FCA based on data that it is reliably able to access about trading in a specific country or region. Alternatively, under MiFID II, firms can opt into the SI regime and this option will also be available to UK firms under the UK MiFID framework.

> Changes to transparency regime: The waivers and thresholds in the MiFID transparency regime rely on EU-wide market data. The MiFID SI replaces references to the EU with the “relevant area” (see previous bullet). It also provides

Amended UK legislation
> Financial Services and Markets Act 2000 (Markets in Financial Instruments) Regulations 2017
> Data Reporting Services Regulations 2017
> Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

Amended retained EU legislation
> Markets in Financial Instruments Regulation
> Commission Delegated Regulation 2017/565
> Commission Delegated Regulation 2017/567
the FCA with temporary powers for four years to amend or suspend certain aspects of the transparency regime (e.g., transparency waivers for equities and non-equities, the application of the double volume cap and transparency obligations relating to non-equities).

> Trading on a trading venue (TOTV) for transparency purposes: SI pre-trade transparency obligations and OTC post-trade transparency obligations only apply in respect of instruments that are traded on a UK trading venue.

> Transaction reporting: The instrument scope of transaction reporting is the same as today, i.e. both UK and EU TOTV instruments are covered. Incoming EEA firms with a UK branch (either under the TPR or under the general UK regime) will need to transaction report under both the UK and EU MiFID regimes (and under the MiFID SI the proposed UK regime will be broader as it will cover both EU and UK TOTV instruments).

> Position limits: The MiFID SI applies UK position limits only in respect of positions in instruments traded on UK trading venues (and economically equivalent OTC contracts). This raises the question whether contracts traded on a EU trading venue could be considered as EEOTC under UK law (although we note that the FCA has previously indicated that EEOTC is a very narrow concept).

> Emission allowances: EEA emission allowances will continue to be a financial instrument under the UK regime.

> Definition of sovereign debt: The definition of sovereign debt under MiFIR as retained in UK law will be extended to cover debt issued by the UK and any other country (as opposed to only EU debt).

> Cooperation agreements: UK portfolio managers that wish to delegate management to an EU firm will need to ensure that a cooperation agreement is in place between the UK regulator and the regulator of the relevant EU Member State. This requirement is unchanged by the MiFID SI. The key question is whether there will be flexibility on this if new cooperation agreements are not in place by exit day.

> Status of EU UCITS for appropriateness: Firms will be able to automatically treat EU UCITS as non-complex products.

> Data reporting service providers: The MiFID SI provides for a one-year temporary permissions regime for EU-authorised DRSPs in the event of a no deal.

> Recitals: As for all the Brexit SIs published to date, the recitals to the underlying EU rules have not been retained by the MiFID SI. This may cause uncertainty in some areas of interpretation e.g. the definition of “research” which is effectively contained in the recitals.

> Regulated activities: A separate SI which has not yet been published will make further changes to FSMA and the RAO.

Linklaters commentary

> Transitional powers: The MiFID SI builds significant flexibility for the FCA into the legislation. For example, the power to suspend or adapt the various transparency requirements, and the volume cap mechanism and to apply them with respect to the UK only or a broader “relevant area”. The FCA will before exit day publish a policy statement on how it intends to use these temporary powers.

> Determining UK TOTV instruments: We expect that the EU’s financial instrument reference database would not cover UK instruments after exit day. The FCA will be taking over responsibility for collating financial reference data from UK firms. Firms will need to consider whether they can use that data to determine UK TOTV and whether, for transaction reporting, they should refer to the EU database to determine EU TOTV.
> **Passported firms:** Much of the UK version of MiFIR will apply to incoming EEA firms that benefit from the temporary permissions regime. Apart from reference data, trade and transaction reporting, this is not confined to activity from those firms’ UK branches. Thought will need to be given as to how to evidence “substituted compliance” where this is available. There are also significant exceptions to that policy. Firms will need to work through these carefully to ensure their compliance procedures operate effectively during the transition. See the Annex for more detail.

> **Equivalence decisions:** The Commission has made equivalence decisions in favour of certain third country trading venues under Articles 23 and 28 MiFIR. The MiFID SI proposes to retain these in UK law. It remains to be seen what will happen to the equivalence decision for Switzerland under Article 23 which, as it stands, is due to expire at the end of 2018.

### What happens next?

> The SI is still in draft. HM Treasury plans to lay it before Parliament “in the autumn”. The version that is laid may include changes to this draft. There is no formal consultation process for commenting on Brexit SIs.

> The changes in the draft SI are intended to take effect on exit day in the event of a no deal. If a Withdrawal Agreement is concluded, a transition period is expected to extend all rights and obligations under EU law to the UK until the end of 2020. In that case, the changes under the Brexit SIs, including the MiFID SI, would not be required until the end of that transition.

> The regulators have said that firms do not need to prepare now to implement changes arising from Brexit SIs. This is because the working assumption is that there will be a Withdrawal Agreement which includes a transition period. This approach will be kept under review as negotiations progress.

> In the event of a no deal, firms may struggle to make the operational changes necessary for a March 2019 Brexit. This includes EEA firms benefitting from temporary permissions who may need to apply different rules after exit day. Therefore, HM Treasury intends to grant the FCA and PRA temporary power to waive or modify firms’ regulatory obligations where they change because of Brexit. This will be covered by a separate SI which has not yet been published. There is more background on this proposal in a recent Treasury guidance note.

> Separately, the FCA has started to consult on its approach to Brexit:

1. The first consultation sets out how the FCA proposes to prepare its Handbook and EU technical standards for a no deal outcome. It also sets out the FCA’s approach to recognising EU guidance (see our summary note for more).

2. The second consultation explains how the temporary permissions regime will work and the rules the FCA proposes to apply to participating firms and funds (see our summary note for more).

> Both consultations close on 7 December and the FCA intends to publish feedback in early 2019 and final rules before exit day. These are the first in a series of Brexit-related consultations that the FCA will publish in the coming months. The PRA will also set out more detail on its Brexit approach during the autumn.
Annex

Firms participating in the temporary permissions regime

> In the event of a no deal, EEA firms passporting into the UK (either on a branch or cross-border basis) may choose before exit day to benefit from a unilateral transition regime. The aim of the regime is to allow EEA firms to continue to access the UK market as if their passports still applied. However, there will be changes to the rules that apply to those firms.

> The starting point is that these firms must comply with Titles II to V, VII and Article 38 of MiFIR. This includes in particular SI pre-trade transparency obligations.

> However post-trade transparency, transaction reporting and reference data submission obligations only apply if the incoming EEA firm has a UK branch. The incoming UK branch must also comply with UK MiFID rules that are normally reserved for the host state under the passporting regime (e.g. UK conduct of business rules).

> However, for some of these obligations, the UK regime may be disappplied if the firm complies with the equivalent EEA rules. This approach will be known as “substituted compliance”. For example, UK pre-trade transparency requirements would be switched off if the EEA firm complies with the MiFID pre-trade transparency requirements in its home state.

> For other obligations (Articles 23, 28, 29 (in relation to CCPs), 30, 31 and Title IV), the UK versions of the rules apply regardless of whether the firm complies with equivalent EEA rules. This means that the incoming EEA firm must comply with the UK version of the share and derivatives trading obligations and portfolio compression rules in addition to the EU version. This will mean compliance issues where permitted venues under UK and EU versions of the STO/DTO do not overlap.

Firms not participating in the temporary permissions regime

> If operating via a UK branch, the branch will have to comply with the UK implementation of MiFID II. This includes pre- and post-trade transparency, transaction reporting, STO/DTO and conduct of business rules. Substituted compliance with EEA rules is not permitted.

> If accessing the UK on a cross-border basis (presumably under the overseas persons exemption), the EEA firm will not have to comply with the UK MiFID regime. However, the EEA firm’s access to UK clients will be limited (e.g. according to the conditions of the overseas persons exemption).
Further resources

Our note on the regulators’ approach to preparing for Brexit and our note on the EU Withdrawal Act have more detail on the draft SIs.

For more information on Brexit, and to access all our Brexit SI summaries, please visit our:

> Brexit Knowledge Portal
> Linklaters Brexit homepage

Key Contacts

Sebastian Barling  
Partner  
Tel: +44 20 7456 5352  
sebastian.barling@linklaters.com

Julia Dixon  
Partner  
Tel: +44 20 7456 4406  
julia.dixon@linklaters.com

Martyn Hopper  
Partner  
Tel: +44 20 7456 5126  
martyn.hopper@linklaters.com

Nikunj Kiri  
Partner  
Tel: +44 20 7456 3256  
nikunj.kiri@linklaters.com

Karen Cooper  
Managing PSL  
Tel: +44 20 7456 5693  
karen.cooper@linklaters.com

Peter Bevan  
Partner  
Tel: +44 20 7456 3776  
peter.bevan@linklaters.com

Harry Eddis  
Partner  
Tel: +44 20 7456 3724  
harry.eddis@linklaters.com

Michael Kent  
Partner  
Tel: +44 20 7456 3772  
michael.kent@linklaters.com

Raza Naeem  
Managing Associate  
Tel: +44 20 7456 5272  
raza.naeem@linklaters.com

Katy Pittman  
Professional Support Lawyer  
Tel: +44 20 7456 2665  
katy.pittman@linklaters.com

General enquiries

Linklaters LLP  
One Silk Street  
London, EC2Y 8HQ  
Tel: +44 20 7456 2000  
Fax: +44 20 7456 2222

This publication is intended merely to highlight issues and not to be comprehensive, nor to provide legal advice. Should you have any questions on issues reported here or on other areas of law, please contact one of your regular contacts, or contact the editors.

© Linklaters LLP. All Rights reserved 2018

Linklaters LLP is a limited liability partnership registered in England and Wales with registered number OC326345. It is a law firm authorised and regulated by the Solicitors Regulation Authority. The term partner in relation to Linklaters LLP is used to refer to a member of Linklaters LLP or an employee or consultant of Linklaters LLP or any of its affiliated firms or entities with equivalent standing and qualifications. A list of the names of the members of Linklaters LLP and of the non-members who are designated as partners and their professional qualifications is open to inspection at its registered office, One Silk Street, London EC2Y 8HQ, England or on http://www.linklaters.com and such persons are either solicitors, registered foreign lawyers or European lawyers.