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Growing Asia's Markets

MiFID II:

Extraterritorial Impacts on Asia

September 2017

In constructing this grid, there are several highly nuanced views that we have taken into account – while it is generally true that a non-EU branch is part of the same legal entity as its EU parent, it is worth mentioning and taking into consideration several legal interpretation principles used when determining ET scope, namely:

(i) reliance in part on historical interpretation principles under MiFID I (which had no - or very limited application - to non-EU branches of EU firms);
(ii) ET application depends on the nature of the MiFID II obligations (organizational or investor protection in nature) as well as underlying rationale for the obligation;
(iii) (no precedent and continuing lack of clear regulatory guidance for determining MiFIR scope (thereby presenting the biggest challenge for firms when determining ET scope for MIFIR requirements); and
(iv) some of the MiFIR requirements can be read purposively as not being applicable (or appropriate) for transactions with no EU nexus.

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MIFID II Extraterritorial Impacts Grid

for both EU & non-EU entities

MiFID II Full Text | MiFIR Full Text | Links to MiFID II/MiFIR RTS and ITS Documents

*For the purposes of this grid, all references to EU include the EEA countries as well

Extraterritorial Reach → **Topic / MiFID II Area** ↓	EU Firm ↓ Non-EU Branch ↓ EU Client / Non-EU Client	Non-EU Firm ↓ EU Branch ↓ EU Client / Non-EU Client	Non-EU Firm ↓ EU Client / Non-EU Client
General Comments	On the specific topic of non-EU branches of EU firms providing services back into the EU, this depends on the varying approaches that the different EU regulators and/or national competent authorities (NCAs) may take in relation to access issues. Also, EU clients are often required to trade with local branches if they are accessing local-currency denominated products (because these are exchange-controlled). Finally, there could be situations where reverse inquiry by EU-based clients to non-EU branches may result in these non-EU branches providing services back into the EU.	The EU branch of a non-EU Firm which is authorised under the EU member state's current national (non-MiFID II) regime will not have a passport for services cross-border within the EU. Where the EU member state in which the branch is located, opts in under MiFID II (Directive) Art 39 (which requires a local authorised branch for the provision of services to retail/elective professionals), then that branch may have a passport to provide cross-border services to eligible counterparties (ECPS)/per se professionals (but not retail/elective professionals) in other member states if the relevant 3rd country's regulatory regime has been assessed as 'equivalent' by ESMA (under MiFIR Art 47). Where the member state does not opt in to Art 39, the branch is subject to the member state's national law, which most likely would be MiFID II/MiFIR equivalent so as not to treat non-EU branches more favourably than EU firms. [There would be no obligation on the non-EU branch to register with ESMA.]	Cross–border services to ECPS/per se professionals: if the relevant 3rd country's regulatory regime has been assessed as 'equivalent' (under MiFIR), the Non-EU firm could provide services cross-border into the EU without local authorisation requirements. Cross-border services to retail/elective professionals: a locally licensed presence may be required, depending on each EU member state's national licensing regime. No change under MiFID II.

Extraterritorial Reach → **Topic / MiFID II Area** ↓	EU Firm → Non-EU Branch → EU Client	EU Firm → Non-EU Branch → Non-EU Client	Non-EU Firm → EU Branch → EU Client	Non-EU Firm → EU Branch → Non-EU Client	Non-EU Firm → EU Client	Non-EU Firm → Non-EU Client
Pre- and Post-Trade Transparency (General)	There is the view that pre-trade transparency may be construed as not applicable to trades conducted by persons operating outside of the EU (even if remotely booked into EU locations) because Pre-Trade is a market rule (MIFIR requirement with no precedence) applicable to EU trading activity, namely trading activity conducted from EU firms through their EU branches. Pre-trade applies to firms when acting as Systematic Internalisers only, and SI status is assessed based on trading activity conducted from EU branches of EU investment firms. The rules make no provision for how pre-trade should (or could) be complied with when servicing clients from non-EU branch locations. Recent level 3 guidance on the topic of trade reporting extended post trade transparency to trades conducted on “similar” 3rd country venues, or with 3rd country firms, when filling EU client orders from EU branch locations, but made no mention of imposing pre-trade requirements. In any event, pre- trade pricing offered outside the EU is not consistent or directly comparable to pricing offered in the EU due to the fact that market risk will most likely be hedged on different markets giving rise to different pricing criteria.					
Off-Venue Pre-Trade Transparency for Equities **MiFIR Art 14, 15 and 17 (RTS 1)** The pre-trade transparency obligations apply to systematic internalisers (**SIs**) in respect of equity instruments. Equity instruments are shares, depository receipts, ETFs, certificates and other similar products (**Equities**). The obligations apply where the trade is below standard market size. Limited obligations apply in respect of illiquid equities. The pre-trade transparency obligations require the SI to make public firm two-way quotes on a regular and continuous basis during normal trading hours.	While European passporting legislation does not contemplate non-EU branches of EU firms providing services back into the EU, please refer to the discussion in “general comments” above. As discussed in “general comments” above, in certain member states, there may be limited local exceptions which would require local advice. See also comment re non-EU clients.	It is arguable that the obligation applies to investment firms that are SIs in the relevant Equity instrument, even where the activity is undertaken in the non-EU branch (irrespective of client location). However, see discussion in the “Pre- and Post-Trade Transparency – General” section above and the observation immediately below. There is however some conflicting guidance and no clear expression of policy intent.	The obligations do not apply to a non-EU firm. However, if the non-EU firm has an EU branch, that branch will be subject to the local regulatory regime in which it is based. Even though the requirements for non-EU branches is determined on the basis of local law, local jurisdictions implementing MiFID II can treat EU branches of non-EU firms no better off than EU investment firms. As such, we expect that local regimes will require EU branches of non-EU firms to undertake the SI calculations and be subject to the pre-trade transparency regime in relation to local branch business (NB. Branch will not have EU passporting rights, absent MiFIR third country equivalence).		The obligations do not apply to a non-EU firm. However, if a non-EU firm is providing services to an EU client, it will need to consider the local licensing regime of the jurisdiction in which the client is based	N.A.
Booking Location **EU**	See above as to whether the obligation applies. Location of trade booking is unlikely to be determinative.		If the EU branch is deemed an SI in the relevant financial instrument, the pre-trade transparency requirements will be applicable for relevant branch business.			
Booking Location **Non-EU**						

Extraterritorial Reach → **Topic / MiFID II Area ↓**	EU Firm → Non-EU Branch → EU Client	EU Firm → Non-EU Branch → Non-EU Client	Non-EU Firm → EU Branch → EU Client	Non-EU Firm → EU Branch → Non-EU Client	Non-EU Firm → EU Client	Non-EU Firm → Non-EU Client
Off-Venue Pre-Trade Transparency for Non-Equities MiFIR Art 18 (RTS 2) Pre-trade transparency obligations apply to SIs in respect of non-equities, which are bonds, structured finance products, emission allowances and derivatives (**Non-Equities**). The obligations apply where there is a liquid market (noting that there are limited obligations in respect of illiquid instruments) and where the trade is below SSTI. If a client requests a quote from an SI and the SI agrees to provide the quote, the pre-trade transparency obligations require the SI to make the quote firm. The quote must also be disclosed to the public and made available to other clients on an executable basis, subject to the commercial policy of the SI.	While European passporting legislation does not contemplate non-EU branches of EU firms providing services back into the EU, please refer to the discussion in "general comments" above. As discussed in "general comments" above, in certain member states, there may be limited local exceptions which would require local advice. See also comment re non-EU clients.	It is arguable that the obligation applies to investment firms that are SIs in the relevant non-equity instrument, even where the activity is undertaken in the non-EU branch (irrespective of client location). However, see discussion in the "Pre- and Post-Trade Transparency – General" section above and the observation immediately below. There is however some conflicting guidance and no clear expression of policy intent.	The obligations do not apply to a non-EU firm. However, if the non-EU firm has an EU branch, that branch will be subject to the local regulatory regime in which it is based. Even though the requirements for non-EU branches is determined on the basis of local law, local jurisdictions implementing MiFID II can treat EU branches of non-EU firms no better off than EU investment firms. As such, we expect that local regimes will require EU branches of non-EU firms to undertake the SI calculations and be subject to the pre-trade transparency regime in relation to local branch business (NB. Branch will not have EU passporting rights, absent MiFIR third country equivalence).		The obligations do not apply to a non-EU firm. However, if a non-EU firm is providing services to an EU client, it will need to consider the local licensing regime of the jurisdiction in which the client is based	N.A.
Booking Location EU	See above as to whether the obligation applies. Location of trade booking is unlikely to be determinative.		If the EU branch is deemed an SI in the relevant financial instrument, the pre-trade transparency requirements will be applicable for relevant branch business.			
Booking Location Non-EU						
On-Venue Pre-Trade Transparency for Equities and Non-Equities MiFIR Art 3 and 8 (RTS 1 and RTS 2) Where the instrument is traded on a venue, the venue provides pre-trade transparency.	N.A.		N.A.		N.A.	

Extraterritorial Reach → Topic / MiFID II Area ↓	EU Firm → Non-EU Branch → EU Client	EU Firm → Non-EU Branch → Non-EU Client	Non-EU Firm → EU Branch → EU Client	Non-EU Firm → EU Branch → Non-EU Client	Non-EU Firm → EU Client	Non-EU Firm → Non-EU Client
Off-Venue Post-Trade Transparency for Equities **MiFIR Art 20 (RTS 2)** Investment firms are required to disclose to the public details of transactions which they conclude either on own account or on behalf of clients. The details must be disclosed as technically possible to real time as possible, or no later than 1 minute. Where the trade is large in scale compared with normal market size, the disclosure may be deferred.	While European passporting legislation does not contemplate non-EU branches of EU firms providing services back into the EU, please refer to the discussion in "general comments" above. As discussed in "general comments" above, in certain member states, there may be limited local exceptions which would require local advice. See also comment re non-EU clients.	It is arguable that the obligation applies to investment firms that are SIs in the relevant Equity instrument, even where the activity is undertaken in the non-EU branch (irrespective of client location). However, see discussion in the "Pre- and Post-Trade Transparency – General" section above and the observation immediately below. There is however some conflicting guidance and no clear expression of policy intent, as our discussions evidently demonstrate.	The obligations do not apply to a non-EU firm. However, if the non-EU firm has an EU branch, that branch will be subject to the local regulatory regime in which it is based. Even though the requirements for non-EU branches is determined on the basis of local law, local jurisdictions implementing MiFID II can treat EU branches of non-EU firms no better off than EU investment firms. As such, we expect that local regimes will require EU branches of non-EU firms to comply with the post trade transparency regime in relation to local branch business (NB. Branch will not have EU passporting rights, absent MiFIR third country equivalence).		The obligations do not apply to a non-EU firm. However, if a non-EU firm is providing services to an EU client, it will need to consider the local licensing regime of the jurisdiction in which the client is based.	The obligations do not apply to a non-EU firm.
<u>Booking Location</u> **EU**	EU investment firm likely to be subject to the post trade transparency obligations.		The post trade transparency obligations should apply to branch business irrespective of booking location.			
<u>Booking Location</u> **Non-EU**	EU investment firm likely to be subject to the post trade transparency obligations, though there may be less clarity regarding non-EU traded and booked business.		The post trade transparency obligations should apply to branch business irrespective of booking location.			

Extraterritorial Reach → **Topic / MiFID II Area** ↓	EU Firm → Non-EU Branch → EU Client	EU Firm → Non-EU Branch → Non-EU Client	Non-EU Firm → EU Branch → EU Client	Non-EU Firm → EU Branch → Non-EU Client	Non-EU Firm → EU Client	Non-EU Firm → Non-EU Client
Off-Venue Post-Trade Transparency for Non-Equities MiFIR Art 21 (RTS 2) Investment firms are required to disclose to the public details of transactions which they conclude either on own account or on behalf of clients. The details must be disclosed as technically possible to real time as possible, or no later than 15 minutes. Certain deferrals are available were certain conditions are met: LIS, SSTI and where the instrument is illiquid (determined on the basis of the ESMA Liquidity assessment). Where post-trade obligations apply, LIS, SSTI and Liquidity (defined below) deferrals will apply for those instruments that do not meet the respective thresholds pertaining to that instrument.	While European passporting legislation does not contemplate non-EU branches of EU firms providing services back into the EU, please refer to the discussion in "general comments" above. As discussed in "general comments" above, in certain member states, there may be limited local exceptions which would require local advice. See also comment re non-EU clients.	It is arguable that the obligation applies to investment firms that are SIs in the relevant non-equity instrument, even where the activity is undertaken in the non-EU branch (irrespective of client location). However, see discussion in the "Pre- and Post-Trade Transparency – General" section above and the observation immediately below. There is however some conflicting guidance and no clear expression of policy intent, as our discussions evidently demonstrate.	The obligations do not apply to a non-EU firm. However, if the non-EU firm has an EU branch, that branch will be subject to the local regulatory regime in which it is based. Even though the requirements for non-EU branches is determined on the basis of local law, local jurisdictions implementing MiFID II can treat EU branches of non-EU firms no better off than EU investment firms. As such, we expect that local regimes will require EU branches of non-EU firms to comply with the post trade transparency regime in relation to local branch business (NB. Branch will not have EU passporting rights, absent MiFIR third country equivalence).		The obligations do not apply to a non-EU firm. However, if a non-EU firm is providing services to an EU client, it will need to consider the local licensing regime of the jurisdiction in which the client is based.	The obligations do not apply to a non-EU firm.
Booking Location **EU**	EU investment firm likely to be subject to the post trade transparency obligations. If an instrument is considered to be "Traded on a Trading Venue" (TOTV), ESMA has given guidance that the post-trade transparency obligations apply. For instance, if an underlying derivative instrument (such as a swap or an option) has identical features to a listed derivative instrument, then the post-trade transparency obligations apply		The post trade transparency obligations should apply to branch business irrespective of booking location.			
Booking Location **Non-EU**	EU investment firm likely to be subject to the post trade transparency obligations, though there may be less clarity regarding non-EU traded and booked business.		The post trade transparency obligations should apply to branch business irrespective of booking location.			

Extraterritorial Reach **Topic / MiFID II Area**	EU Firm Non-EU Branch EU Client Non-EU Client	Non-EU Firm EU Branch EU Client Non-EU Client	Non-EU Firm EU Client	 Non-EU Client
Transaction Reporting **MiFIR Art 26 (RTS 22)**	**Scenario 1: Non-EU branch of an EU firm executes a trade for EU client and/ or non-EU client outside EU** As branches are not a separate legal entity of their parent company, the Transaction Reporting obligation lies within the parent company (EU firm) for all its branches for all reportable instruments*. The parent company (EU firm) has the obligation to report the transactions regardless of booking location. **Scenario 2: Non-EU subsidiary of an EU firm executes a trade for EU client outside EU** If the non-EU subsidiary executes a trade in a reportable instrument that has been transmitted by the parent company (EU firm), the obligation to report the transaction is with the EU firm, however, the non-EU subsidiary will have to provide relevant information to the parent firm for the purpose of Transaction Reporting. **Scenario 3: Non-EU subsidiary of an EU firm executes a trade for non-EU client outside EU** When a subsidiary executes a transaction directly for a non-EU client, there are no transaction reporting requirements. *Note: For the purpose of this exercise, we define reportable instruments as financial instruments according to Article 26(2)(a), (b), (c) MiFIR.	**Scenario: EU branch/ subsidiary of a non-EU firm executes a trade for EU client and/ or non-EU client in EU:** Transaction Reporting requirements apply to all authorised EU branches of 3rd country investment firms (Article 41(2) MiFID II) independent of the ultimate booking location of the transaction or client, as long as a reportable instrument has been transacted. The same requirements apply if this is a subsidiary of a non-EU firm. In either case of branch or subsidiary, the non-EU parent firm may assist in the operational aspects of Transaction Reporting.	**Scenario 1: Non-EU firm executes a trade for EU client outside EU** In the event that a client is classified as an investment firm according to MiFID and is directly accessing a non-EU firm without going through its branch/ subsidiary in the EU, the non-EU firm may need to support the EU firm's compliance requirements with provision of required data fields in the case of reportable instruments.	**Scenario 2: Non-EU firm executes a trade for non-EU client outside EU** In the event that the non-EU firm does not have a branch or subsidiary in the EU, Transaction Reporting does not apply in this case.

<table>
<tr>
<th>Extraterritorial Reach →

Topic / MiFID II Area ↓</th>
<th>EU Firm
↓
Non-EU Branch
EU Client / Non-EU Client</th>
<th>Non-EU Firm
↓
EU Branch
EU Client / Non-EU Client</th>
<th>Non-EU Firm
EU Client / Non-EU Client</th>
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<tr>
<td>Instrument Reference Data
MiFIR Art 27 (RTS 23)

Instrument reference data contains details of the underlying instrument used to generate the ISIN.

It is the responsibility of the trading venue or SI to make the relevant reference data available to its respective NCA*

All financial instruments traded on an EU trading venue or SI (including OTC derivatives) would need to be identified via an ISIN.</td>
<td colspan="2">As Systematic Internalisers (SI) are determined on an entity level, the SI designation of a parent entity could apply to the subsidiary or branch; the branch/subsidiary could build their own capability to make available instrument reference data or get support from parent for reporting.

In the event that the EU firm is acting in its capacity as an SI, the EU firm must report instrument reference data of reportable instruments* to its NCA, which will then transmit these on to ESMA.

The EU firm needs to report instrument reference data of the non-EU branch when trading reportable instruments.

Regardless of the booking location, the instrument reference data needs to be made available to respective NCA as long as the reference data refers to reportable instruments traded by an SI.

*Note:
For the purpose of this exercise, we define reportable instruments as financial instruments according to Article 26(2)(a), (b), (c) MiFIR.</td>
<td>Provided that the non-EU firm has no branch or subsidiary in the EU, the non-EU firm cannot obtain the status of an SI in the EU for the purpose of providing MiFID services to EU clients or non-EU clients.</td>
</tr>
</table>

Extraterritorial Reach → / **Topic / MiFID II Area** ↓	EU Firm → Non-EU Branch → EU Client	EU Firm → Non-EU Branch → Non-EU Client	Non-EU Firm → EU Branch → EU Client	Non-EU Firm → EU Branch → Non-EU Client	Non-EU Firm → EU Client	Non-EU Firm → Non-EU Client
Trading Obligation MiFIR Art 28 (for derivatives)	The non-EU branch is not a separate legal entity and is subject to the same obligations as the parent; trading obligation applies for in-scope derivatives. Actual application will be dependent upon counterparty classification as an FC (Financial Counterparty)/NFC+ (Non-Financial Counterparty exceeding certain thresholds) or would be such if the entity in question was established in the EU under EMIR.		Applicable for in-scope derivatives, Actual application will be dependent upon counterparty classification as an FC (Financial Counterparty)/NFC+ (Non-Financial Counterparty exceeding certain thresholds) or would be such if the entity in question was established in the EU under EMIR.	The EU branch is not a separate legal entity and therefore is subject to the same obligations as the parent. Actual application will be dependent upon counterparty classification as entities that would be a FC (Financial Counterparty)/NFC+ (Non-Financial Counterparty exceeding certain thresholds) if they were established in the EU under EMIR. As the parent and the client are both established outside of the EU, the trading obligation will not apply unless the transaction has a direct, substantial and foreseeable impact on the EU (Articles 28(2) and 28(5) of MIFIR)	Applicable for in-scope derivatives. Actual application will be dependent upon counterparty classification as an FC (Financial Counterparty) /NFC+ (Non-Financial Counterparty exceeding certain thresholds) or would be such if the entity in question was established in the EU under EMIR	Actual application will be dependent upon counterparty classification as entities that would be a FC (Financial Counterparty)/NFC + (Non-Financial Counterparty exceeding certain thresholds) if they were established in the EU under EMIR. As the firm and the client are both established outside of the EU, the trading obligation will not apply unless the transaction has a direct, substantial and foreseeable impact on the EU (Articles 28(2) and 28(5) of MIFIR)
Booking Location EU **Booking Location Non-EU**	Applicable for in-scope derivatives. Actual application will be dependent upon counterparty classification as an FC (Financial Counterparty)/NFC+ (Non-Financial Counterparty exceeding certain thresholds) or would be such if the entity in question was established in the EU under EMIR.		Applicable for in-scope derivatives. Actual application will be dependent upon counterparty classification as an FC (Financial Counterparty)/NFC+ (Non-Financial Counterparty exceeding certain thresholds) or would be such if the entity in question was established in the EU under EMIR			

Extraterritorial Reach **Topic / MiFID II Area**	EU Firm Non-EU Branch EU Client / Non-EU Client	Non-EU Firm EU Branch EU Client / Non-EU Client	Non-EU Firm EU Client / Non-EU Client
Trading Obligation **MIFIR Article 23** **(for equities)** **Third Country Venue Equivalence** **MIFID Article 25(4)** Article 23 of MiFIR requires an investment firm to ensure the trades it undertakes in shares admitted to trading on a regulated market or traded on a trading venue take place on: (i) regulated market, multilateral trading facility ("MTF"); (ii) systematic internaliser ("SI"); or (iii) a third country trading venue assessed as equivalent in accordance with Article 25(4)(a) of MiFID II (the "Share Trading Obligation").	The non-EU branch is not a separate legal entity and is subject to the same obligations as the parent; trading obligation applies if the transaction takes place in the EU. There is a market view forming that where a firm places and order or transmits an order to a third-party, it will not be deemed to be undertaking a transaction, which is the trigger for the mandatory trading obligation. Therefore, where a EU firm transmits an order to a non-EU firm for execution, the mandatory share trading obligation may not apply.	EU branches of non-EU entities are considered “Investment Firms” in the EU for Article 39 Opt-in countries. Even for opt-out countries, it is expected that they will adopt MIFID II through a legislative process and therefore, cannot treat non-EU firms’ branches better than branches of EU firms. So all in-scope shares are caught by this obligation.	N.A. (The assumption here is that the trade is transacted outside the EU).
Booking Location **EU**	Applicable for all in-scope shares	Applicable for all in-scope shares	
Booking Location **Non-EU**	If the transaction transmits an order to a third- party outside the EU, the trading obligation may not apply.	If the transaction is undertaken outside the EU, the trading obligation may not apply.	

Extraterritorial Reach **Topic / MiFID II Area**	EU Firm Non-EU Branch		Non-EU Firm EU Branch		Non-EU Firm	
	EU Client	Non-EU Client	EU Client	Non-EU Client	EU Client	Non-EU Client
Best Execution **MiFID II Art 27 (RTS 27 and RTS 28)** Where non-EU Branches of EU firms, or non-EU firms **deal with/have EU Clients,** while the Best Execution requirements themselves do not apply (depending on local EU country approach), the EU Clients can request the non-EU branches of the EU firms and the non-EU firms that they deal/trade with, to provide copies of these branches'/firms' Order Execution Policies (OEPs) or require these branches or firms to have OEPs that are similar/equivalent to those entities within the EU (where the best Execution Obligations apply).	Unclear (Will depend on local EU country implementation) Where non-EU Branches of EU firms, **deal with/have EU Clients,** where the Best Execution requirements themselves do not apply (depending on local EU country approach), the EU Clients can request the non-EU branches of the EU firms that they deal/trade with, to provide copies of these branches' Order Execution Policies (OEPs) or require these branches to have OEPs that are similar or equivalent to those entities within the EU (where the best Execution Obligations apply).	Best Execution Obligations are not applicable since this obligation's objective is investor protection and would therefore be applicable only for EU clients serviced from EU locations.	Obligations apply Trading venues, systematic internalisers, market makers, and other liquidity providers, are required to make data available to the public, on a regular basis, at no cost, on the quality of transaction execution. Entities subject to MiFID II must now take "all sufficient steps" as opposed to "all reasonable steps" to obtain best execution for client transactions. Investment firms are also required to publish annually information on the quality of execution obtained on their top five trading venues, based on volumes (by class of instrument). Order Execution Policies (OEPs) are also required to be in place.		Unclear (Should Not Apply) Where non-EU firms **deal with/have EU Clients,** while the Best Execution requirements themselves do not apply (depending on local EU country approach), the EU Clients can request the non-EU firms that they deal/trade with, to provide copies of these firms' Order Execution Policies (OEPs) or require these firms to have OEPs that are similar/equivalent to those entities within the EU (where the best Execution Obligations apply).	N.A.

Extraterritorial Reach →	EU Firm ↓ Non-EU Branch		Non-EU Firm ↓ EU Branch		Non-EU Firm	
Topic / MiFID II Area ↓	EU Client	Non-EU Client	EU Client	Non-EU Client	EU Client	Non-EU Client
Research Unbundling & Commission Sharing Agreements (CSAs) **MiFID II Art 24** [Commission Delegated Directive – Point 26] MIFID II requires that research should be paid for separately, in one of two ways: through a specially designated Research Payment Account (RPA) – by assessing each piece of research according to its value and then paying for it, or directly by the fund itself. Commission Sharing Agreements (CSAs) now allow for brokers to withhold some of the trading commissions they receive for research. While CSAs are not banned under MIFID II, they cannot be linked to volumes traded (which was the model in the past). The CSAs can be linked to RPAs but in a manner consistent with MIFID II. This may result in a need for re-papering CSA/RPA agreements.	If an EU firm (or a branch of an EU firm) provides research services to an investment firm within the EU, then the research unbundling obligations apply. Research services provided to investment firms outside the EU are not covered by the "research unbundling" requirement.		The branch of the non-EU firm will be subject directly to the MIFID II requirements if the branch is in an Article 39 "Opt-In" country and will most likely be subject to the MIFID II requirements once (as is expected) most of the countries that have not opted in adopt the MIFID II rules. Thus, the branch of the non-EU firm will be subject to the research unbundling obligation. Also, the non-EU branch cannot be treated more favorably than another branch of an EU firm – for that reason too, the research unbundling obligations will apply. There are added issues depending on whether the regulator in the country/ jurisdiction where the EU entity's parent is domiciled, may have rules restricting the ability of broker dealers to charge for research (for instance, in the US, in order to charge for research, an entity has to register as an Investment Advisor. Similar rules may apply in Asian jurisdictions).	The branch of the non-EU firm will be subject directly to the MIFID II requirements if the branch is in an Article 39 "Opt-In" country and will most likely be subject to the MIFID II requirements once (as is expected) most of the countries that have not opted in adopt the MIFID II rules. Thus, the branch of the non-EU firm will be subject to the research unbundling obligation. Also, the non-EU branch cannot be treated more favorably than another branch of an EU firm – for that reason too, the research unbundling obligations will apply.	Where an EU firm delegates to a non-EU firm, it may require the non-EU firm to comply with the MiFID II requirements. So when the non-EU firm has been delegated to act for an EU client by an EU firm that is a portfolio manager or independent adviser the non-EU firm may need to comply with the MiFID II research and unbundling obligation. There are added issues depending on whether the regulator in the country/ jurisdiction where the EU entity's parent is domiciled, may have rules restricting the ability of broker dealers to charge for research (for instance, in the US, in order to charge for research, an entity has to register as an Investment Advisor. Similar rules may apply in Asian jurisdictions).	N.A.

Extraterritorial Reach → **Topic / MiFID II Area** ↓	EU Firm ↓ Non-EU Branch EU Client / Non-EU Client	Non-EU Firm ↓ EU Branch EU Client / Non-EU Client	Non-EU Firm EU Client / Non-EU Client
Post-trade /Clearing STP (Straight-Through-Processing) Requirements Article 29 of MIFIR states that: a) The operator of a regulated market shall ensure that all transactions in derivatives that are concluded on that regulated market are cleared by a CCP and b) CCPs, trading venues and investment firms which act as clearing members shall have in place effective systems, procedures and arrangements in relation to cleared derivatives to ensure that transactions in cleared derivatives are "submitted and accepted for clearing as quickly as technologically practicable using automated systems" (in other words – through "Straight Through Processing (STP).	**EU-regulated entities (including branches/subs of non-EU entities)** – the identity/location of the client is not relevant (since the trade is through a CCP/centrally cleared in Europe) The clearing obligation will apply to all transactions in derivatives that are executed through an EU regulated market. The STP obligation will affect trades which are undertaken through trading venues in the EU, cleared by an EU CCP, or which are cleared through an EU regulated CCP clearing member.		**Non-EU entities with no presence in the EU** - the identity/location of the client is not relevant (since the trade is through a CCP/Centrally cleared The impact will be the same as that for EU-regulated entities – As long as the transaction in derivatives subject to a clearing obligation via a CCP in the EU is executed through an EU regulated market, the non-EU entity located in APAC would still be subject to the STP obligation.

Other Topics

Product Governance: Manufacture and distribution of Financial Products

a) Products manufactured in the EU for distribution outside the EU:
ESMA has now published a final report containing the final version of the guidelines on MiFID II product governance requirements.

For EU manufacturers of financial instruments the guidelines require:

- Elaborate product governance processes centered on the identification of the target market and differentiation across different segments of the target market (including extensive discussions with the distributor on this process)

For distributors of financial instruments (even if they are based outside the EU) the guidelines cover the following:

- Tying in product governance processes with suitability and appropriateness
- Identifying different target market categories and following differentiated distribution strategies for each of these categories
- portfolio management, portfolio approach, hedging and diversification
- Conduct regular reviews with the manufacturer to ensure MIFID II Product Governance requirements are being met
- application of product governance requirements to the distribution of products that were manufactured before the date of application of MiFID II, if they continue to be distributed after January 3, 2018 when MIFID II comes into effect
- Differentiation of retail clients from professional clients (and certain categories of retail clients who "elect" to be treated as professional clients)
- Both manufacturers and distributors should identify "negative" target markets

The distributor obligations are only directly imposed on MIFID firms, but 3rd country distributors facing MIFID manufacturers may be impacted indirectly through contractual obligations passed down by MIFID manufacturers.

b) Products manufactured outside the EU for distribution in the EU.

For non-EU firms (for instance, those in APAC) manufacturing products for distribution for distribution within the EU, there are no direct impacts – however, because the distributors of these products within the EU are caught by the guidelines on MIFID II product governance requirements applicable to distributors, the non-EU manufacturers of such products are **indirectly** impacted. Before distributing non-EU products within the EU, EU distributors would require manufacturers to comply with certain minimum standards as laid down by ESMA, before distributing these products.

For the specific and more detailed guidelines pertaining to EU distributors, please see above.

The manufacturer obligations are only directly imposed on MIFID firms, but 3rd country manufacturers facing MIFID distributors may be impacted indirectly through contractual obligations passed down by MIFID distributors.

Algo Trading: (not directly relevant to non-EU market participants – unless they are admitted/allowed to trade on EU RMs/MTFs/OTFs)

MiFID II introduces closer regulation and monitoring of algorithmic trading, imposing new and detailed requirements on algorithmic traders (in certain cases, even where they are exempt from authorisation under MiFID II) and the trading venues on which they trade (including regulated markets (RMs), multilateral trading facilities (MTFs) and organised trading facilities (OTFs)). An MTF or OTF must have the ability to ensure orderly trading under severe market stress, and must have systems and controls in place that can cope in stressed market conditions. Trading venues will also be required to give their relevant member state "Competent Authority" access to their order book, to enable regulators to monitor trading activity. There are also requirements for minimum tick sizes and synchronization of clocks. Trading venues must also have "circuit breakers" and "controls" in case trading gets disorderly and must have systems to manage volatility arising from "fat finger" type errors.

Firms engaging in algo trading must have effective business continuity arrangements to deal with any system failure and ensure their systems are tested and monitored. MIFID II also places obligations on firms engaging in "market-making strategies" (which are defined in the technical standards) and in addition, there are obligations placed on trading venues to enter into agreements with such firms. Investment firms will also be required to continuously test their algorithms and have "kill switches" in place to cancel all orders at all trading venues (in case any negative impacts that the algos might have, are identified). Finally, investment firms are also required to have in place a number of pre-trade risk limits.

Increased Conduct of Business Requirements

During the summer of 2016, the European Commission published delegated acts containing detailed rules for the Conduct of Business requirements. Specific rules have been formulated by the Commission in relation to the following issues: 1) Inducements and Commissions (**covered above**); 2) recording of telephone calls and e-mails; 3) Product design and the assessment of suitability and appropriateness for clents; 4) Significant enhancements to requirements to manage conflicts of interest 5) product governance (**covered above)** 6). Strengthened arrangements to protect client asset ownership in insolvency 7) Investment Research (**covered above**) and 8) Underwriting and Placing.

Practical Impacts in APAC: MIFID II introduces new requirements on the identification, management and disclosure of conflicts of interest for corporate finance desks before accepting a mandate. This includes prescribed disclosures to clients of specific conflicts of interest regarding fees, underwriting and placing operations, targeted investors, and clients and individuals involved. APAC entities should conduct an impact analysis on the investment banking business, and identify documentation, contracting and operational impact involving investment banking stakeholders, and legal and compliance teams.

Footnotes

1. Liquidity Determination: ESMA will make available a list of instruments that are deemed to be liquid (for the purposes of determining whether pre/post-trade transparency obligations are met). For bonds in particular, our understanding is that this list will be published in December – furthermore, based on submissions made by trading venues to their respective NCAs (National Competent Authorities) which in turn have submitted this information to ESMA, only about 1% of all bonds outstanding (by unique ISIN), but accounting for over 50% of volumes, will be deemed to be liquid – please note that this is not final, but an expectation based on the information available.

As a practical matter, APAC entities, branches or subsidiaries of APAC entities in the EU, or branches or subsidiaries of EU entities in Asia are not involved in the exercise to determine liquidity. ESMA will publish a list of "liquid" instruments, just prior to MIFID II going into effect in January 2018. Liquidity determination for pre- and post-trade transparency and data reporting waivers can then be made with reference to this list.

2. New categories of Trading Venues: Under MIFID, there are several new categories of trading venues – Regulated Markets (RM), Multilateral Trading Facilities (MTFs) and Organized Trading Facilities (OTFs):

a) Regulated Markets (RMs): An RM is defined as a multilateral system operated by and/or managed by a market operator, which brings together or facilitates the bringing together of multiple third-party buying and selling interests in financial instruments. RMs will be subject to enhanced governance requirements such as numerical limits on directorships, diversity obligations, and mandatory nomination committees.

b) Multilateral Trading Facilities (MTFs): means a multilateral system, operated by an investment firm or a market operator, which brings together multiple third-party buying and selling interests in financial instruments – in the system and in accordance with non-discretionary rules. MTFs have been aligned with RMs so that both have systems and measures in place to manage, identify and mitigate risks, (b) effective arrangements for the efficient and timely execution of transactions on its systems and (c) sufficient financial resources.

c) Organized Trading Facilities (OTFs): An OTF is a multilateral system which is not an RM or an MTF and in which multiple third-party buying and selling interests in bonds, structured finance products, emission allowances or derivatives are able to interact in the system. Unlike RMs and MTFs, operators of OTFs will have discretion as to how to execute orders, subject to pre-transparency and best execution obligations. Specifically, OTF operators are permitted to engage in matched principal trading in the products above, whereas an MTF operator cannot. Additionally, OTF operators will be required to comply with the investor protection obligations in articles 24 (information to clients), 25 (suitability), 27 (best execution) and 28 (client order handling) of MiFID 2 whereas MTFs are not required to do so.

3. Systematic Internalisers: Systematic internalisers (SIs) are investment firms which, on an organised, frequent, systematic and substantial basis, deal on own account by executing client orders outside an RM, MTF or OTF without operating a multilateral system. Accordingly, an investment firm will only constitute a systematic internaliser where it is proposing to execute a client order". MTFs, OTFs and Sis cannot co-exist within the same entity. Essentially, a systematic internaliser is a counterparty and not a trading venue. For instance, a single-dealer platform, where trading always takes place against a single investment firm should be considered a systematic internaliser, whereas a multi-dealer platform, with multiple dealers interacting for the same financial instrument, should not be considered a systematic internaliser.

Practical Impacts in APAC/non-EU: The trading volumes in EU instruments traded in non-EU branches of EU-HQ entities could be added to trading volumes in the same instrument at the EU-headquartered parent entity, to determine if that entity is/is not a systematic internaliser. This is an indirect impact.

4. LIS (Large-in-Scale): These orders are those that are "large" in size compared to normal market orders. This determination is made by the National Competent Authority (NCA) where the bond (or other financial instrument) is listed. This determination is necessary for decisions to be made if pre-trade transparency waivers (and post-trade reporting deferrals) are applicable, in the case of the particular financial instrument concerned. This relates to trades carried out on a trading venue.

5. SSTI (Size Specific to Instrument): This refers to Actionable indications of interest (IOIs) in request for quote (RFQ) and voice trading systems that are above a "size specific to the instrument" and this threshold is in turn set by national regulators as a "percentile" of the LIS thresholds (in other words, they are set at a lower level). The SSTI is also the upper limit for Systematic Internaliser (SI) firm quotes. The SSTI determination is necessary for decisions to be made if pre-trade transparency waivers (and post-trade reporting deferrals) are applicable. The SSTI thresholds apply to RFQ, Voice Trading and OTC venues.