

# Clients & Friends Memo

## ESMA Publishes Final Report on Technical Standards for the Provision of Investment Services by Non-EU Firms

2 October 2020

The European Securities and Markets Authority (**ESMA**) has published its [Final Report](#) (the **Final Report**) containing draft regulatory and implementing technical standards (**RTS** and **ITS**) on the provision of investment services and activities in the European Union (**EU**) by non-EU firms (known as “third-country” firms (**TCFs**) in EU parlance) under MiFIR and MiFID II.

### Background

The draft RTS and ITS are published following the changes to MiFIR and MiFID II regimes for the provision of investment services and activities in the EU by TCFs, introduced by the Investment Firms Regulation (EU) No 2019/2033 (**IFR**) and Directive (EU) 2019/2034 (**IFD**). In particular:

- Article 46 of MiFIR allows TCFs to provide investment services and activities to eligible counterparties and *per se* professional clients<sup>1</sup> across the EU if, *inter alia*, the third country where the TCF is established is declared equivalent by the European Commission and if the TCF is registered in the register of third-country firms held by ESMA (the **ESMA register**). This provision was designed to effectively allow a single-entry point to the EU for such firms. To date, however, no non-EU jurisdiction has been declared equivalent for the purposes of Article 46 of MiFIR, so TCFs continue to access EU clients in accordance with national member state regimes, pursuant to transitional measures in MiFIR.
- The IFR:
  - introduces changes to the existing MiFIR regime for TCFs that intend to provide investment services and activities to eligible counterparties and *per se* professional clients, requiring a significant reporting flow from third-country firms to ESMA, on an annual basis;

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<sup>1</sup> Within the meaning of Section I of Annex II of MiFID II.

- gives ESMA the power to ask TCFs registered in the ESMA register to provide the data relating to all orders and all transactions in the EU, whether on own account or on behalf of a client, for a period of five years;<sup>2</sup>
- requires ESMA to share information, upon request, with the regulators of the Member States where a TCFs is providing investment services and activities in accordance with Article 46 of MiFIR and enables such regulators to request information from ESMA;<sup>3</sup> and
- gives ESMA the power to conduct on-site inspections.<sup>4</sup>

The changes to the Article 46 TCF access regime and the ESMA registration requirements will take effect from 26 June 2021.

### Summary of the Final Report

The Final Report sets out the full details of the new annual reporting requirements for TCFs, and gives ESMA powers to ask TCFs to provide data relating to all orders and transactions in the EU whether on own account or on behalf of a client, for a period of five years. New annual reporting requirements from branches of TCFs to national competent authorities (**NCAs**) have also been introduced.

### Draft Technical Standards

Pursuant to Article 46(7) and (8) of MiFIR, ESMA has now developed:

- draft RTS to specify the information that TCFs must provide to ESMA for the registration in the ESMA register, and for the information that third-country firms have to report annually to ESMA;
- draft ITS to specify the format in which the information for the registration of the firm and for the annual report to ESMA should be submitted; and
- draft ITS to specify the format in which the new flow of information provided by MiFID II is to be reported to NCAs by branches of TCFs (branches of TCFs authorised under MiFID II are supervised by the relevant regulator of the authorising Member State, but the IFD amends MiFID II to provide for further reporting obligations on such branches to the Member State authorities where they are established).

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<sup>2</sup> Article 46(6b) of MiFIR.

<sup>3</sup> Article 46(6a) of MiFIR

<sup>4</sup> Article 47(2) of MiFIR

### Implications for TCFs

Although clearly the content of these standards has been drafted with Brexit in mind, these new standards will have a wider impact on all TCFs wishing to provide services in the EU.

The new reporting requirements will add to the compliance costs of TCFs and have generally been seen as too granular. The information that ESMA seeks to collect on an annual basis, includes, for example (i) a firm's global operations and strategy, (ii) the estimated number of clients/counterparties, and (iii) how the activities of the TCF in the EU will contribute to the overall strategy of the firm – many of these requirements may be viewed as excessive and/or commercially sensitive. Another objection of market participants is that much of the requested information can and should be obtained through cooperation agreements with the regulators of the relevant third countries rather than from the firms themselves.

A key concern of market participants is that ESMA's new information-gathering responsibilities come close to direct supervision of third-country firms. The powers of ESMA (under the IFR) are extensive and allow it to prohibit or restrict the provision of investment services or activities in the EU by a TCFs for (i) a failure to comply with product intervention measures taken by ESMA, the European Banking Authority or NCAs (ii) a failure to comply with annual reporting obligations to ESMA or with a request for information from ESMA; or (iii) for non-cooperation with an investigation or an on-site inspection carried out by ESMA. In short, the direction of travel is towards ESMA acting as a quasi-regulator for TCFs, which arguably goes beyond the original concept of access through registration set out in the initial version of MIFIR.

In the Brexit context, these proposals show that even if the UK is granted equivalence under the MiFIR regime, UK investment firms may still face a significant compliance burden under the third country access regime. Furthermore, it is not anticipated that the UK will put in a similar requirement for the FCA to gather this granular information from EU27 investment firms wishing to access the UK market. These developments raise the prospect of two divergent regulatory reporting regimes in the UK and EU, with all the extra cost and complexity that this implies.

### Next Steps

The draft Technical Standards have been submitted to the European Commission for the adoption of the final legal text (within the next three months).

Market participants are encouraged to familiarise themselves with the contents of these RTS and ITS, as the registration process requires significant granular information and ultimately, will have compliance costs and implications.

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