

Markets in Financial Instruments Directive

–MiFID II

This fact sheet is prepared by Bank of Ireland Global Markets to give you information on MiFID II, its requirements and the likely impact on you and our relationship with you.

What is MiFID II?

MiFID II provides a European-wide legislative framework for regulating the operation of financial markets in the EU. It represents a major overhaul of the existing law (mainly as a response to the financial crisis), building on and extending the scope of the first Markets in Financial Instruments Directive (MiFID), which originally came into force in November 2007. MiFID II consists of the revised directive and a new regulation (MiFIR). In this document MiFID II refers to the revised directive and MiFIR.

When does MiFID II apply?

MiFID II will apply from 3 January 2018.

What new requirements does MiFID II introduce?

MiFID II introduces new requirements in relation to investor protection, conduct of business and organisational arrangements, for example:

- stricter controls on the products that reach you (product governance);
- changes to the type of information we must supply to you before you invest in a financial instrument;
- information on costs and charges and greater price transparency;
- tighter client categorisation regime; and
- more stringent requirements in relation to best execution quality.

Entities subject to MiFID II

Who, and to what activities, does MiFID II apply?

MiFID II applies to investment firms and credit institutions when providing investment activities and services in respect of financial instruments. However, MiFID II also impacts all customers who trade or deal in MiFID II impacted instruments.

Products subject to MiFID II

What Products does MiFID II apply to?

MiFID II applies to financial instruments. The definition of financial instruments includes shares, debt securities, money market instruments, derivatives, such as swaps, options, futures, and forwards in relation to FX / currencies, interest rates and inflation rates as well as commodities, contracts for differences and emission allowances. Structured deposits are not financial instruments under MiFID II. However, firms selling or advising clients on such products are subject to certain MiFID II requirements. Loans are not subject to regulation under MiFID II.

Preparing for MiFID II

How does MiFID II impact my business?

FX Forwards that do not satisfy certain criteria (see below) fall under the definition of financial instruments under MiFID II and need to be reported by us to the competent authorities, such as the Central Bank of Ireland or the Financial Conduct Authority in the UK. We may require your assistance in assessing whether your FX Forwards need to be reported under MiFID II or not.

What do I need to do to prepare for MiFID II?

Bank of Ireland has already contacted you in late October regarding the proposed treatment of your FX Forward transactions from 3 January 2018 (if relevant to your business). If you disagree with this treatment and haven't responded to the letters received, please do so before the 3 January 2018. Customers impacted by MiFID II need to obtain a Legal Entity Identifier (LEI) prior to entering into a transaction. Bank of Ireland won't be able to enter into a transaction with you if you haven't provided a valid and current LEI. For further details on LEI and how to obtain one, please see below.

Does MiFID II apply to all FX Transactions?

No.

FX transactions are excluded if namely:

- it is an FX Spot transaction; or
- it is entered into as a payment transaction ("means of payment").

What is the exclusion from MiFID II for FX Spot transactions?

An FX Spot transaction will not be a financial instrument and will be excluded from MiFID II if under its terms delivery is scheduled to be made within a specified number of trading days. The number of trading days depends upon the type of contract and the currencies involved. However, a contract does not qualify as an FX Spot transaction if, irrespective of its terms, there is an understanding between the parties that delivery would be postponed and not performed within the periods set out in MiFID II

What is the "means of payment" exclusion from MiFID II for FX Transactions?

An FX forward transaction is excluded from MiFID II if

- it is a means of payment;
- it is settled physically;
- it is entered into in order to facilitate payment for identifiable goods, services or direct investment;
- it is not traded on a trading venue; and
- you are not a financial counterparty as defined in Article 2(8) of EMIR.

Bank of Ireland will advise you whether your transactions are deemed to meet this exclusion but may require certain information from you in order to assess your transactions. Should you disagree with the assessment please contact your Global Markets Relationship Manager.

Summary of (other) new requirements

What new requirements does MiFID II introduce?

- **Enhanced Investor Protection Requirements**, such as tighter client classification regime, additional requirements for information to be provided to clients including information in relation to costs and charges, the appropriateness of products, conflicts of interest and inducements.
- **Enhanced Best Execution Quality**. Firms have to take all sufficient steps to achieve best execution when trading with or for their clients.
- **Transaction Reporting**, such as an expansion of products, client and transactional data fields and a firm's reporting obligations.
- **Enhanced Market Transparency** by expanding the pre- and post-trade transparency regimes that existed under MiFID to almost all financial instruments under MiFID II.
- **New Mandatory Trading Obligation**. Certain market participants and firms will be required to trade certain derivatives and equities on a regulated trading venue, rather than on an OTC basis.
- **Changes to Market Structures** by introducing a new type of multilateral trading venue such as an organised trading facility (OTF), to add to the existing categories of a regulated market and a multilateral trading facility (MTF).
- **Enhanced Governance** including stricter procedures and controls on the products that are sold to the customer (product governance).

Client Categorisation

How are clients categorised under MiFID II and what does this mean for me in practice?

There are three categories of client under MiFID II:

“Eligible Counterparty” means an entity that is either an investment firm, credit institution, insurance company, UCITS and their management company, pension funds and their management company, other financial institutions authorised or regulated under the law of the European Union or under the national law of a Member State, national governments and their corresponding offices including public bodies that deal with public debt at a national level, central banks or supranational organizations.

“Professional Client” means a client that meets the criteria laid down in MiFID II. A Professional Client can be a per se Professional Client or elect (subject to our consent) to be treated as a Professional Client.

“Retail Client” means a client who is not a Professional Client or does not elect to be treated as such or an Eligible Counterparty.

Eligible Counterparties and Professional Clients are subject to fewer investor protection provisions. For instance, we are not required to undertake an appropriateness assessment for Eligible Counterparties. Also, we only have to offer best execution to Professional Clients where they rely on us for best execution. All clients who engage in MiFID II impacted transactions will be notified of how we have categorised them under MiFID II.

Information to Clients

What does MiFID II say about information to clients and what does this mean in practice?

Under MiFID II, firms are obliged to provide clients with a very broad and detailed set of information including details on any terms of an agreement with the client, about the firm itself and its services for clients and potential clients, the financial instruments into which firms may enter with or for their clients, the costs and charges that may be incurred by or for the client and the firm's best execution policy.

Best Execution

What does MiFID II say about best execution and what does this mean in practice?

Firms already have to comply with an obligation of best execution under MiFID, namely to take all reasonable steps to obtain the best possible result for their clients. However, MiFID II enhances the current best execution requirements by for instance requiring firms now to take all sufficient steps to obtain the best possible result for their clients (taking account of factors such as price, costs, speed, likelihood of execution and settlement, size, nature of trading or any other consideration relevant to the execution of the order).

Transaction reporting and Legal Entity Identifiers (LEIs)

What is MiFID II transaction reporting?

Transaction reporting is already a mandatory requirement under MiFID providing market transparency and enabling competent authorities such as the Central Bank of Ireland or the Financial Conduct Authority in the UK to effectively oversee the markets for matters such as market abuse. Transaction reports have to be provided as soon as possible and at the latest by the close of business on the next business day after the relevant transaction is entered into.

MiFID II now expands the transaction reporting regime under MiFID by extending the list of financial instruments covered (for example now including OTC derivative transactions). A much broader set of data has to be provided as well to the competent authorities to ensure they have sufficient information to oversee markets. However, it is important to note that a transaction report is made to regulators only and is not made public. Obtaining and maintaining an LEI will be a mandatory requirement under MiFID II.

What is a Legal Entity Identifier (LEI) and how do I acquire one?

MiFID II explicitly states that a firm will be unable to transact with a client until it has received a valid and current LEI from client. An LEI is a 20-digit, alpha-numeric code based on the ISO 17442 standard assigned to clearly and uniquely identify a legal entity (e.g. companies, charities and trusts) participating in financial Transactions.

LEI codes are issued by appointed Local Operating Units (LOUs) such as the Irish Stock Exchange and the London Stock Exchange. If you are a legal entity and do not already hold a valid LEI, you will require one from 3 January 2018 if you wish to enter into transactions in MiFID II financial instruments.

How to obtain an LEI?

Obtaining a Legal Entity Identifier (LEI) is easy. Simply contact **your preferred business partner** from a list of LEI issuing organizations (such as Irish Stock Exchange or the London Stock Exchange).

Appropriateness

What are firms' obligations in relation to appropriateness under MiFID II?

MiFID II requires firms, when providing investment services other than investment advice or portfolio management, to obtain information regarding their existing or potential clients' knowledge and experience relevant to a specific service or product, to enable the firm to assess whether it is appropriate for the client.

MiFID II requires firms to keep records of appropriateness assessments. These must include the result of the assessment, any warning given, whether the client asked to proceed despite the warning, and whether the firm accepted this request.

Recording Communications

Does MiFID II require communications to be recorded?

Yes.

MiFID II also introduces the obligation on firms to record telephone conversations or electronic communications when they:

- receive and transmit orders;
- execute orders on behalf of clients; or
- deal on own account.

The communications have to be recorded irrespective if the conversations lead to an agreement or not. Records are to be kept for five years, and if requested by the competent authorities for seven years. A copy of the records will be made available to the client on request.

Record keeping

What are the requirements under MiFID II regarding record keeping?

The main purpose of record-keeping is to enable competent authorities to fulfil their supervisory tasks and perform enforcement actions under MiFID II and the market abuse legislation. Therefore, firms are required to keep records in a significant number of areas, such as

- rights and obligations of the firm and the client;
- client orders and decision to deal;
- transactions and order processing;
- client files (including client agreements, information to assess appropriateness); and
- client meeting notes (in a durable format).

Inducements

What does MiFID II say about inducements?

MiFID II currently prohibits the payment or receipt of fees or commissions and other non-monetary benefits between firms and persons other than their clients (e.g. advisory firms and distributors), unless certain criteria are met. This prohibition is intended to ensure such payments and benefits are not inducements and, as such, do not introduce conflicts with clients' interests. Payments and non-monetary benefits are required to be assessed to ensure that they do not impair the firm's duty to act in the best interest of the client, that they are designed to enhance the quality of the service being provided to the client and that they are disclosed to the client. MiFID II confirms these requirements.

What does MiFID II say about conflicts of interest?

MiFID II requires firms to take all appropriate steps to identify, prevent or manage conflicts of interests between themselves and their clients, and also among their clients. If the firm's effective organisational and administrative arrangements are not sufficient to prevent or manage a conflict of interest, firms have to disclose to the client the conflict of interest arising in the provision of an investment service and/or ancillary service, taking into account the nature of the client to whom the disclosure is being made. The disclosure shall explain the general nature and sources of the conflict of interest as well as the risks to the client arising as a result and the steps undertaken to mitigate these risks. Such disclosure must be in sufficient detail and in a durable medium.

Firms must keep and regularly update a record of all services or activities giving rise to actual and potential conflicts, and must also establish, implement and maintain a conflicts of interest policy. The policy has to be reviewed and updated periodically (at least annually).

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