

**Report to:** Pension Board

**Date:** 26 June 2017

**By:** Chief Operating Officer

**Title of report:** Markets in Financial Instruments Directive (MiFID II) - Update

**Purpose of report:** This report provides Members with an update on MiFID II, a framework of European legislation governing investment firms providing certain investment services to clients.

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## **RECOMMENDATIONS**

**The Board is recommended to consider and note the Markets in Financial Instruments Directive (MiFID II) updates.**

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### **1. Background**

1.1 The Markets in Financial Instruments Directive is the EU legislation that regulates firms who provide services to clients linked to 'financial instruments' (shares, bonds, units in collective investment schemes and derivatives), and the venues where those instruments are traded.

1.2 MiFID was applied in the UK from November 2007, but is now being revised to improve the functioning of financial markets in light of the financial crisis and to strengthen investor protection. The changes are currently set to take effect from **3 January 2018**, with the new legislation being known as MiFID II - this includes a revised MiFID and new Markets in Financial Instruments Regulation (MiFIR).

### **2. Markets in Financial Instruments Directive (MiFID II)**

2.1 Under MiFID II, UK local authorities will be re-classified as "retail" clients as opposed to their current classification of "professional" clients. If the local authority retains the retail client classification, they will be restricted in the investment managers they can use and the investments they can make as there are fewer investment managers permitted to deal with retail clients and certain investments are not deemed suitable for retail clients.

2.2 There is an option for local authorities to opt-up to "elective professional" client status with individual asset managers in order to continue 'complex' investments. This procedure will include both a qualitative and quantitative test to be assessed by the asset manager. It is proposed that the opt-up criteria will be applied separately for local authorities depending on the capacity in which they are acting (i.e. either as treasury managers or as pension fund administrators).

2.3 At the end of October 2016, the FCA published its consultation on the implementation proposals for MiFID II. It received significant number of responses specifically focused on the opt-up criteria, including the East Sussex Pension Fund.

### **3. MiFID II - update**

3.1 There has been a recent negotiation on the proposal between the Investment Association (IA), Financial Conduct Authority (FCA) and the LGA. The FCA Board met on 25<sup>th</sup> May 2017, and awaiting outcome from this meeting, which may include fourth criteria in the quantitative test with investors having to satisfy two of the four.

3.2 CIPFA is currently working on a project to simplify the process for local authorities to supply critical information to hundreds of financial institutions tasked with testing whether councils qualify for "professional" investor status under new MiFID II regulations. This move comes as Councils up and down the Country await the result of a Financial Conduct Authority (FCA) consultation on how

councils will qualify for professional status. Many fear the current proposed criteria will rule them out, thus reducing investment opportunities.

#### **4. Implications for the ACCESS Pool**

4.1 All ACCESS Funds will need to satisfy the criteria in order to opt up to “elective professional” status for existing investments from 3 January 2018. ACCESS will have to assess each Fund to determine whether they meet the criteria for opting up to “elective professional” status.

#### **5. Conclusion and reasons for recommendations**

5.1 Though the regulatory demands are yet to be finalised, CIPFA’s project will kick-start research designed to see how the information needed to satisfy MiFID II requirements can be standardised and, as a result, reduce the burden on Councils.

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Background Documents

None