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From:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
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To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
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Subject:	COMMISSION DELEGATED REGULATION (EU) .../... of 25.4.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive

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Delegations will find attached document C(2016) 2398 final.

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EUROPEAN  
COMMISSION

Brussels, 25.4.2016  
C(2016) 2398 final

**COMMISSION DELEGATED REGULATION (EU) .../...**

**of 25.4.2016**

**supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive**

(Text with EEA relevance)

## EXPLANATORY MEMORANDUM

### 1. CONTEXT OF THE DELEGATED ACT

#### 1.1 General background and objectives

Directive 2014/65/EU (commonly referred to as 'MiFID II') is due to become applicable on 3 January 2017 and, together with Regulation (EU) No 600/2014 (MiFIR), replace Directive 2004/39/EC (MiFID I). MiFID II/MiFIR provide an updated harmonised legal framework governing the requirements applicable to investment firms, regulated markets, data reporting services providers and third country firms providing investment services or activities in the Union.

MiFID II/MiFIR aim to enhance the efficiency, resilience and integrity of financial markets, notably by:

- Achieving greater transparency: introduction of a pre- and post-trade transparency regime for non-equities and strengthening and broadening of the existing equities trade transparency regime;
- Bringing more trading onto regulated venues: creation of a new category of platforms to trade derivatives and bonds - the Organised Trading Facilities - and of a trading obligation for shares on regulated venues;
- Fulfilling the Union's G20 commitments on derivatives: mandatory trading of derivatives on regulated venues, introduction of position limits and reporting requirements for commodity derivatives, broadening the definition of investment firm to capture firms trading commodity derivatives as a financial activity;
- Facilitating access to capital for SMEs: introduction of the SME Growth Market label;
- Strengthening the protection of investors: enhancement of the rules on inducements, a ban on inducements for independent advice and new product governance rules;
- Keeping pace with technological developments: regulating high-frequency trading (HFT) imposing requirements on trading venues and on firms using HFT;
- Introducing provisions on non-discriminatory access to trading and post-trading services in trading of financial instruments notably for exchange-traded derivatives;
- Strengthening and harmonising sanctions and ensuring effective cooperation between the relevant competent authorities.

Finally, the overarching aim of the MiFID II/MiFIR regulatory package is to level the playing field in financial markets and to enable them to work for the benefit of the economy, supporting jobs and growth.

The present Delegated Regulation aims at specifying, in particular, the rules relating to exemptions, the organisational requirements for investment firms, data reporting services providers, conduct of business obligations in the provision of investment services, the execution of orders on terms most favourable to the client, the handling of client orders, the SME growth markets, the thresholds above which the position reporting obligations apply and the criteria under which the operations of

a trading venue in a host Member State could be considered as of substantial importance for the functioning of the securities markets and the protection of the investors.

## **1.2 Legal background**

The Delegated Regulation is based on a total of 19 empowerments in MiFID II. This Delegated Regulation should be read together with the MiFID II Delegated Directive and the MiFIR Delegated Regulation. The issue of subsidiarity was covered in the impact assessment for the MiFIDII/MiFIR and the EU's and the Commission's right of action in the impact assessment accompanying these delegated measures. All empowerments on which this Delegated Regulation is based are "shall" empowerments.

Some other MiFID II empowerments are for the European Securities and Markets Authority (ESMA) to develop draft Regulatory and Implementing Technical Standards and will be the subject of future delegated or implementing regulations.

## **2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT**

The Commission mandated ESMA to provide it with technical advice on possible delegated acts concerning MiFID II and MiFIR. On 23 April 2014, the Commission services sent a formal request for technical advice (the "Mandate") to ESMA on possible delegated acts and implementing acts concerning MiFID II/MiFIR. On 22 May 2014 ESMA published a consultation paper with regard to its technical advice on delegated acts. ESMA received 330 responses by 1 August 2014. ESMA delivered its technical advice on 19 December 2014. This Delegated Regulation is based on the technical advice provided by ESMA.

The Commission services had numerous meetings with various stakeholders to discuss the future level 2 measures throughout 2014 and the first half of 2015. The Commission has also had several exchanges with Members of the ECON Committee of the European Parliament and held several meetings of the relevant expert group, during which the delegated measures were discussed among Member States' experts and involving observers from the European Parliament and ESMA. This consultation process brought a broad consensus on the draft Delegated Regulation.

## **3. IMPACT ASSESSMENT**

The extensive process of consultation described above was complemented by an Impact Assessment report. The Impact Assessment Board delivered a positive opinion on 24 April 2015.

Given the number of delegated measures captured by this Delegated Regulation, which covers numerous and technical aspects of MiFID II, the Impact Assessment report does not discuss elements in the Delegated Regulation with limited scope or impact, or elements that have been consensual for a long time in the in-depth consultation process described above. Instead, the Impact Assessment report rather concentrates on the measures with greater impact or scope for Commission choice. In particular, these concern definitions of MiFID II concepts, transparency matters, fees for trade data publication, SME Growth Markets or commodity derivatives.

### **3.1 Analysis of costs and benefits**

The costs of the choices made by the Commission described in the impact assessment fall almost entirely on market participants (trading venues, systematic internalisers, organised trading facilities,

SME growth markets, high frequency traders) who will incur costs in setting up trade data publication, in some instances applying for authorisation (in particular for SIs, SME GMs, high frequency traders), for implementing the enhanced organisational and conduct of business rules. The Impact Assessment provided further estimations of the compliance costs triggered by the Level 2 provisions. By ensuring a harmonised implementation and application of MiFID II and MiFIR the delegated acts will make sure that the objectives of level 1 can be achieved without imposing inordinate additional burden on stakeholders. Overall, the impacts of the delegated acts are relatively minor as the scope of possible action has already been determined in MiFID II and MiFIR level 1 texts.

The benefits concern investment firms and other entities subject to MiFID II/MiFIR requirements but also investors and society more widely. This includes the benefits from increased market integration, efficient and transparent financial markets, enhanced competition and availability of services and increased investor protection. The suggested measures should make financial markets more transparent and more secure and improve investor confidence and participation in financial markets. In addition, by contributing to fostering orderly markets and reducing systemic risks, these measures should improve the stability and reliability of financial markets.

The investment plan for Europe highlights reducing fragmentation in the financial markets and contributing to enhanced and more diversified supply of finance to SMEs and long-term projects as key elements of the strategy to improve the framework conditions for growth. Financial markets are one of the most important channels for the optimal allocation of capital within the European economy. However, capital will only flow frictionless if financial markets are stable and trusted by all market participants. A clearly defined legal framework will therefore help to achieve the Commission's top priority to get Europe growing again.

These benefits are considered to considerably outweigh the costs.

There is no effect on the EU budget.

### **3.2 Proportionality**

The need for proportionality is reaffirmed in several provisions and duly taken into account across all of the Delegated Regulation. For instance, requirements in the area of organisational aspects reflect proportionality concerns. In elaborating definitions such as systematic internalisers, high frequency trading, foreign exchange 'other derivatives contracts, the need for proportionality was duly respected in the calibration of quantitative and qualitative thresholds.

## **4. LEGAL ELEMENTS OF THE DELEGATED ACT**

### **Chapter I: Scope and definitions**

This chapter sets out subject matter and scope and include definitions in relation to

- the concept of incidental manner for the purposes of the exemption concerning investment services provided in an incidental manner in the course of another professional activity;
- commodity derivatives, including wholesale energy products that must be physically settled, energy derivatives contracts and wholesale energy products, other derivative financial instruments, derivatives under section C(10) of Annex I to Directive 2014/65/EU;

- the circumstances under which other derivative contracts relating to currencies should be considered financial instruments as well as the meaning of spot contracts for currencies, and specifies a delineation of financial contracts and contracts used to effect payments;
- investment advice;
- trade transparency and market structure rules, including further specification of money-market instruments and definition of systematic internalisers in relation to equity and non-equity instruments,
- trading controls, including further specifications on algorithmic trading, high frequency algorithmic trading technique and direct electronic access

## Chapter II: Organisational requirements

The Chapter specifies organisational requirements for investment firms performing investment services and ancillary services. In particular, it addresses procedures with regard to matters such as the compliance function, risk management, complaints handling, personal transactions, outsourcing and conflicts of interest, including the additional organisational requirements for underwriting and placing services and the production and dissemination of investment research.

## Chapter III: Operating conditions for investment firms

The Chapter sets out the rules with which an investment firm has to comply when providing investment services or ancillary services to its clients. In particular, it further specifies the information provided to clients and potential clients on for instance client categorisation, on investment services and financial instruments or on costs and charges. Directive 2004/39/EU has already introduced the obligation for an investment firm to inform clients about risks of financial instruments, including the risk of losing the entire investment. This Regulation clarifies that such information would also include an explanation of the risks arising from insolvency of the issuer and related events, such as bail in.

The Chapter also specifies:

- the information to clients and potential clients on for instance client categorisation, on investment services and financial instruments or on costs and charges,
- the new requirements concerning the provision of investment advice as well as the assessment of suitability and appropriateness,
- the reporting to clients requirements,
- the best execution obligations and the requirements relating to client order handling,
- the criteria for treatment as an eligible counterparty,
- the record-keeping obligations, including the new rules concerning the recording of telephone conversations or electronic communications,
- certain concepts and conditions which an MTF is required to comply with in order to be registered as an SME growth market.

## Chapter IV: Operating obligations for trading venues

This chapter specifies under what circumstances a removal or suspension of a financial instrument from trading would cause significant damage to investor's interest. It also set out circumstances where significant infringement of the rules of a trading venue or system disruptions in relation to a financial instrument and circumstances where conduct indicating behaviour that is prohibited under Regulation (EU) No 596/2014 (Market abuse regulation) may be assumed

#### Chapter V: Position reporting in relation to commodity derivatives

This chapter specifies the conditions when an aggregate commitment of traders report shall be published on a specific commodity derivative or emission allowances or derivative thereof. The chapter specifies the thresholds in respect of number of persons and their open positions which if exceeded shall be subject to publication.

#### Chapter VI: Data provision obligations for reporting service providers

This chapter contains specifications for the purposes of clarifying the obligation of reporting services providers (approved publication arrangements, APAs and consolidated tape providers, CTPs) to provide market data on a reasonable commercial basis, which is part of the transparency framework under Regulation (EU) No 600/2014). These specifications concern inter alia the requirement that prices are set on the basis of cost and may include a reasonable margin, non-discriminatory provision of market data, the obligation to unbundle and disaggregate data and a transparency to the public around the fees obligation, other conditions as well as cost accounting methodologies. The same rules are also applicable to investment firms and market operators operating a trading venue and systematic internalisers as provided for in MIFIR.

#### Chapter VII: Competent authorities

This chapter specifies the criteria for determining when the operations of a regulated market, an MTF or an OTF are of substantial importance in a host Member State and the consequences of that status in such a way as to avoid creating an obligation on a trading venue to deal with or be made subject to more than one competent authority where otherwise there would be no such obligation.

COMMISSION DELEGATED REGULATION (EU) .../...

of 25.4.2016

supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU<sup>1</sup>, and in particular Article 2(3), the second subparagraph of Article 4(1)(2), Article 4(2), Article 16(12), Article 23(4), Article 24(13), Article 25(8), Article 27(9), Article 28(3), Article 30(5), Article 31(4), Article 32(4), Article 33(8), Article 52(4), Article 54(4), Article 58(6), Article 64(7), Article 65(7) and Article 79(8) thereof,

Whereas:

- (1) Directive 2014/65/EU establishes the framework for a regulatory regime for financial markets in the Union, governing operating conditions relating to the performance by investment firms of investment services and, where appropriate, ancillary services and investment activities; organisational requirements for investment firms performing such services and activities, for regulated markets and data reporting services providers; reporting requirements in respect of transactions in financial instruments; position limits and position management controls in commodity derivatives; transparency requirements in respect of transactions in financial instruments.
- (2) Directive 2014/65/EU empowers the Commission to adopt a number of delegated acts. It is important that all the detailed supplementing rules regarding the authorisation, ongoing operation, market transparency and integrity, which are inextricably-linked aspects inherent to the taking up and pursuit of the services and activities covered by Directive 2014/65/EU, begin to apply at the same time as Directive 2014/65/EU so that the new requirements can operate effectively. To ensure coherence and to facilitate a comprehensive view and compact access to the provisions by persons subject to those obligations as well as by investors, it is desirable to include the delegated acts related to the above-mentioned rules in this Regulation.

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<sup>1</sup> OJ L 173, 12.06.2014, p. 349.



- (3) It is necessary to further specify the criteria to determine under what circumstances contracts in relation to wholesale energy products must be physically settled for the purposes of the limitation of scope set out in Section C(6) of Annex I to Directive 2014/65/EU. In order to ensure that the scope of this exemption is limited to avoid loopholes it is necessary that such contracts require that both buyer and seller should have proportionate arrangements in place to make or receive delivery of the underlying commodity upon the expiry of the contract. In order to avoid loopholes in case of balancing agreements with the Transmission System Operator in the areas of electricity and gas, such balancing arrangements should only be considered as a proportionate arrangement if the parties to the arrangement have the obligation to physically deliver electricity or gas. Contracts should also establish clear obligations for physical delivery which cannot be offset whilst recognising that forms of operational netting as defined in Regulation (EU) No 1227/2011 of the European Parliament and of the Council<sup>2</sup> or national law should not be considered as offsetting. Contracts which must be physically settled should be permitted to deliver in a variety of methods however all methods should involve a form of transfer of right of an ownership nature of the relevant underlying commodity or a relevant quantity thereof.
- (4) In order to clarify when a contract in relation to wholesale energy product must be physically settled, it is necessary to further specify when certain circumstances such as force majeure or bona fide inability to settle provisions are present, and which should not alter the characterisation of those contracts as 'must be physically settled'. It is important to also clarify how oil and coal energy derivatives should be understood for the purposes of Section C6 of Annex I to Directive 2014/65/EU. In this context, contracts related to oil shale should not be understood to be coal energy derivatives.
- (5) A derivative contract should only be considered to be a financial instrument under Section C(7) of Annex I to Directive 2014/65/EU if it relates to a commodity and meets a set of criteria for determining whether a contract should be considered as having the characteristics of other derivative financial instruments and as not being for commercial purposes. This should include contracts which are standardised and traded on venues, or contracts equivalent thereof where all the terms of such contracts are equivalent to contracts traded on venues. In this case, terms of these contracts should also be understood to include provisions such as quality of the commodity or place of delivery.
- (6) In order to provide clarity on the definitions of contracts relating to underlying variables set out in Section C(10) of Directive 2014/65/EU, criteria should be provided relating to their terms and underlying variables in those contracts. The inclusion of actuarial statistics in the list of underlyings should not be understood as extending the scope of those contracts to insurance and reinsurance.
- (7) Directive 2014/65/EU establishes the general framework for a regulatory regime for financial markets in the Union, setting out in Section C of Annex I the list of financial instruments covered. Section C(4) of Annex I of Directive 2014/65/EU includes financial instruments relating to a currency which are therefore under the scope of this Directive.
- (8) In order to ensure the uniform application of Directive 2014/65/EU, it is necessary to clarify the definitions laid down in Section C(4) of Annex I of Directive 2014/65/EU for other derivative contracts relating to currencies and to clarify that spot contracts relating to

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<sup>2</sup> Regulation (EU) No 1227/2011 of the European Parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency (OJ L 326, 8.12.2011, p. 1).

currencies are not other derivative instruments for the purposes of Section C(4) of Annex I to Directive 2014/65/EU.

- (9) The settlement period for a spot contract is generally accepted in most main currencies as taking place within 2 days or less, but where this is not market practice it is necessary to make provision to allow settlement to take place in accordance with normal market practice. In such cases, physical settlement does not require the use of paper money and can include electronic settlement.
- (10) Foreign exchange contracts may also be used for the purpose of effecting payment and those contracts should not be considered financial instruments provided they are not traded on a trading venue. Therefore it is appropriate to consider as spot contracts those foreign exchange contracts that are used to effect payment for financial instruments where the settlement period for those contracts is more than 2 trading days and less than 5 trading days. It is also appropriate to consider as means of payments those foreign exchange contracts that are entered into for the purpose of achieving certainty about the level of payments for goods, services and real investment. This will result in excluding from the definition of financial instruments foreign exchange contracts entered into by non-financial firms receiving payments in foreign currency for exports of identifiable goods and services and non-financial firms making payments in foreign currency to import specific goods and services.
- (11) Payment netting is essential to the effective and efficient operation of currency settlement systems and therefore the classification of a foreign currency contract as a spot transaction should not require that each foreign currency spot contract is settled independently.
- (12) Non deliverable forwards are contracts for the difference between an exchange rate agreed before and the actual spot rate at maturity and therefore should not be considered to be spot contracts, regardless of their settlement period.
- (13) A contract for the exchange of one currency against another currency should be understood as relating to a direct and unconditional exchange of those currencies. In the case of a contract with multiple exchanges, each exchange should be considered separately. However an option or a swap on a currency should not be considered a contract for the sale or exchange of a currency and therefore could not constitute either a spot contract or means of payment regardless of the duration of the swap or option and regardless of whether it is traded on a trading venue or not.
- (14) Advice about financial instruments addressed to the general public should not be considered as a personal recommendation for the purposes of the definition of 'investment advice' in Directive 2014/65/EU. In view of the growing number of intermediaries providing personal recommendations through the use of distribution channels, it should be clarified that a recommendation issued, even exclusively, through distribution channels, such as internet, could qualify as a personal recommendation. Therefore, situations in which, for instance, email correspondence is used to provide personal recommendations to a specific person, rather than to address information to the public in general, may amount to investment advice.
- (15) Generic advice about a type of financial instrument is not considered investment advice for the purposes of Directive 2014/65/EU. However, if an investment firm provides generic advice to a client about a type of financial instrument which it presents as suitable for, or based on a consideration of the circumstances of, that client, and that advice is not in fact

suitable for the client, or is not based on a consideration of his circumstances, the firm is likely to be acting in contravention of Article 24(1) or (3) of Directive 2014/65/EU. In particular, a firm which gives a client such advice would be likely to contravene the requirement of Article 24(1) to act honestly, fairly and professionally in accordance with the best interests of its clients. Similarly or alternatively, such advice would be likely to contravene the requirement of Article 24(3) that information addressed by a firm to a client should be fair, clear and not misleading.

- (16) Acts carried out by an investment firm that are preparatory to the provision of an investment service or carrying out an investment activity should be considered as an integral part of that service or activity. This would include, for example, the provision of generic advice by an investment firm to clients or potential clients prior to or in the course of the provision of investment advice or any other investment service or activity.
- (17) The provision of a general recommendation about a transaction in a financial instrument or a type of financial instrument constitutes the provision of an ancillary service within Section B(5) of Annex I of Directive 2014/65/EU, and consequently Directive 2014/65/EU and its protections apply to the provision of that recommendation.
- (18) In order to ensure the objective and effective application of the definition of systematic internalisers in the Union in accordance with Article 4(1)(20) of Directive 2014/65/EU, further specifications should be provided on the applicable pre-set limits for the purposes of what constitutes frequent systematic and substantial over the counter (OTC) trading. Pre-set limits should be set at an appropriate level to ensure that OTC trading of such a size that it had a material effect on price formation is within scope while at the same time excluding OTC trading of such a small size that it would be disproportionate to require the obligation to comply with the requirements applicable to systematic internalisers.
- (19) Pursuant to Directive 2014/65/EU, a systematic internaliser should not be allowed to bring together third party buying and selling interests in functionally the same way as a trading venue. A systematic internaliser should not consist of an internal matching system which executes client orders on a multilateral basis, an activity which requires authorisation as a multilateral trading facility (MTF). An internal matching system in this context is a system for matching client orders which results in the investment firm undertaking matched principal transactions on a regular and not occasional basis.
- (20) For reasons of clarity and legal certainty and to ensure a uniform application, it is appropriate to provide supplementary provisions in relation to the definitions in relation to algorithmic trading, high frequency algorithmic trading techniques and direct electronic access. In automated trading, various technical arrangements are deployed. It is essential to clarify how those arrangements are to be categorised in relation to the definitions of algorithmic trading and direct electronic access. The trading processes based on direct electronic access are not mutually exclusive to those involving algorithmic trading or its sub-segment high frequency algorithmic trading technique. The trading of a person having direct electronic access may therefore also fall under the algorithmic trading including the high frequency algorithmic trading technique definition.
- (21) Algorithmic trading in accordance with Article 4(1)(39) of Directive 2014/65/EU should include arrangements where the system makes decisions, other than only determining the trading venue or venues on which the order should be submitted, at any stage of the trading processes including at the stage of initiating, generating, routing or executing orders.

Therefore, it should be clarified that algorithmic trading, which encompasses trading with no or limited human intervention, should refer not only to the automatic generation of orders but also to the optimisation of order-execution processes by automated means.

- (22) Algorithmic trading should encompass smart order routers (SORs) where such devices use algorithms for optimisation of order execution processes that determine parameters of the order other than the venue or venues where the order should be submitted. Algorithmic trading should not encompass automated order routers (AOR) where, although using algorithms, such devices only determine the trading venue or venues where the order should be submitted without changing any other parameter of the order.
- (23) High frequency algorithmic trading technique in accordance with Article 4(1)(40) of Directive 2014/65/EU, which is a subset of algorithmic trading, should be further specified through the establishment of criteria to define high message intraday rates which constitutes orders quotes or modifications or cancellations thereof. Using absolute quantitative thresholds on the basis of messaging rates provides legal certainty by allowing firms and competent authorities to assess the individual trading activity of firms. The level and scope of these thresholds should be sufficiently broad to cover trading which constitute high frequency trading technique, including those in relation to single instruments and multiple instruments.
- (24) Since the use of high frequency algorithmic trading technique is predominantly common in liquid instruments, only instruments for which there is a liquid market should be included in the calculation of high intraday message rate. Also, given that high frequency algorithmic trading technique is a subset of algorithmic trading, messages introduced for the purpose of trading that fulfil the criteria in Article 17(4) of Directive 2014/65/EU should be included in the calculation of intraday message rates. In order not to capture trading activity other than high frequency algorithmic trading techniques, having regard to the characteristics of such trading as set out in recital 61 of Directive 2014/65/EU, in particular that such trading is typically done by traders using their own capital to implement more traditional trading strategies such as market making or arbitrage through the use of sophisticated technology, only messages introduced for the purposes of dealing on own account, and not those introduced for the purposes of receiving and transmitting orders or executing orders of behalf of clients, should be included in the calculation of high intraday message rates. However, messages introduced through other techniques than those relying on trading on own account should be included in the calculation of high intraday message rate where, viewed as a whole and taking into account all circumstances, the execution of the technique is structured in such a way as to avoid the execution taking place on own account, such as through the transmission of orders between entities within the same group. In order to take into account, when determining what constitutes high message intra-day rates, the identity of the client ultimately behind the activity, messages which were originated by clients of DEA providers should be excluded from the calculation of high intraday message rate in relation to such providers.
- (25) The definition of direct electronic access should be further specified. The definition of direct electronic access should not encompass any other activity beyond the provision of direct market access and sponsored access. Therefore, arrangements where client orders are intermediated through electronic means by members or participants of a trading venue such as online brokerage and arrangements where clients have direct electronic access to a trading venue should be distinguished.

- (26) In case of order intermediation, submitters of orders do not have sufficient control over the parameters of the arrangement for market access and should therefore not fall within scope of direct electronic access. Therefore, arrangements that allow clients to transmit orders to an investment firm in an electronic format, such as online brokerage, should not be considered direct electronic access provided that clients do not have the ability to determine the fraction of a second of order entry and the life time of orders within that time frame.
- (27) Arrangements where the client of a member or participant of a trading venue, including the client of a direct clients of organised trading facilities (OTFs), submit their orders through arrangements for optimisation of order execution processes that determine parameters of the order other than the venue or venues where the order should be submitted through SORs embedded into the provider's infrastructure and not on the client's infrastructure should be excluded from the scope of direct electronic access since the client of the provider does not have control over the time of submission of the order and its lifetime. The characterisation of direct electronic access when deploying smart order routers should therefore be dependent on whether the smart order router is embedded in the clients' systems and not in that of the provider.
- (28) The rules for the implementation of the regime governing organisational requirements for investment firms performing investment services and, where appropriate, ancillary services and investment activities on a professional basis, for regulated markets, and data reporting services providers should be consistent with the aim of Directive 2014/65/EU. They should be designed to ensure a high level of integrity, competence and soundness among investment firms and entities that operate regulated markets, MTFs or OTFs, and to be applied in a uniform manner.
- (29) It is necessary to specify concrete organisational requirements and procedures for investment firms performing such services or activities. In particular, rigorous procedures should be provided for with regard to matters such as compliance, risk management, complaints handling, personal transactions, outsourcing and the identification, management and disclosure of conflicts of interest.
- (30) The organisational requirements and conditions for authorisation for investment firms should be set out in the form of a set of rules that ensures the uniform application of the relevant provisions of Directive 2014/65/EU. This is necessary in order to ensure that investment firms have equal access on equivalent terms to all markets in the Union and to eliminate obstacles, linked to authorisation procedures, to cross-border activities in the field of investment services.
- (31) The rules for the implementation of the regime governing operating conditions for the performance of investment and ancillary services and investment activities should reflect the aim underlying that regime. They should be designed to ensure a high level of investor protection to be applied in a uniform manner through the introduction of clear standards and requirements governing the relationship between an investment firm and its client. On the other hand, as regards investor protection, and in particular the provision of investors with information or the seeking of information from investors, the retail or professional nature of the client or potential client concerned should be taken into account.
- (32) In order to ensure the uniform application of the various relevant provisions of Directive 2014/65/EU, it is necessary to establish a harmonised set of organisational requirements and operating conditions for investment firms.

- (33) Investment firms vary widely in their size, their structure and the nature of their business. A regulatory regime should be adapted to that diversity while imposing certain fundamental regulatory requirements which are appropriate for all firms. Regulated entities should comply with their high level obligations and design and adopt measures that are best suited to their particular nature and circumstances.
- (34) It is appropriate to set out common criteria for assessing whether an investment service is provided by a person in an incidental manner in the course of a professional activity, in order to ensure a harmonised and strict implementation of the exemption granted by Directive 2014/65/EU. The exemption should only apply if the investment service has an intrinsic connection to the main area of the professional activity and is subordinated thereto.
- (35) The organisational requirements established under Directive 2014/65/EU should be without prejudice to systems established by national law for the registration or monitoring by competent authorities or firms of individuals working within investment firms.
- (36) For the purposes of requiring an investment firm to establish, implement and maintain an adequate risk management policy, the risks relating to the firm's activities, processes and systems should include the risks associated with the outsourcing of critical or important functions. Those risks should include those associated with the firm's relationship with the service provider, and the potential risks posed where the outsourced functions of multiple investment firms or other regulated entities are concentrated within a limited number of service providers.
- (37) The fact that risk management and compliance functions are performed by the same person does not necessarily jeopardise the independent functioning of each function. The conditions that persons involved in the compliance function should not also be involved in the performance of the functions that they monitor, and that the method of determining the remuneration of such persons should not be likely to compromise their objectivity, may not be proportionate in the case of small investment firms. However, they would only be disproportionate for larger firms in exceptional circumstances.
- (38) Clients or potential clients should be enabled to express their dissatisfaction with investment services provided by investment firms in the interests of investor protection as well as strengthening investment firms' compliance with their obligations. Clients' or potential clients' complaints should be handled effectively and in an independent manner by a complaints management function. In line with the principle of proportionality, that function could be carried out by the compliance function.
- (39) Investment firms are required to collect and maintain information relating to clients and services provided to clients. Where those requirements involve the collection and processing of personal data, the respect of the right to the protection of personal data in accordance with Directive 95/46/EC of the European Parliament and of the Council<sup>3</sup> and Directive 2002/58/EC of the European Parliament and of the Council<sup>4</sup> which govern the processing of

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<sup>3</sup> Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data (OJ L 281 , 23.11.1995, p. 31).

<sup>4</sup> Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector (OJ L 201, 31.7.2002, p. 37).

personal data carried out in application of this Directive should be ensured. Processing of personal data by the European Securities and Markets Authority (ESMA) in the application of this Regulation is subject to Regulation (EU) No 45/2001 of the European Parliament and of the Council<sup>5</sup>.

- (40) A definition of remuneration should be introduced in order to ensure the efficient and consistent application of the conflicts of interest and conduct of business requirements in the area of remuneration and should include all forms of financial or non-financial benefits or payments provided directly or indirectly by firms to relevant persons in the provision of investment or ancillary services to clients, such as cash, shares, options, cancellations of loans to relevant persons at dismissal, pension contributions, remuneration by third parties for instance through carried interest models, wage increases or promotions, health insurance, discounts or special allowances, generous expense accounts or seminars in exotic destinations.
- (41) In order to ensure that clients' interests are not impaired, investment firms should design and implement remuneration policies to all persons who could have an impact on the service provided or corporate behaviour of the firm, including persons who are front-office staff, sales force staff or other staff indirectly involved in the provision of investment or ancillary services. Persons overseeing the sales forces, such as line managers, who may be incentivised to pressure sales staff, or financial analysts whose literature may be used by sales staff to entice clients to make investment decisions or persons involved in complaints-handling or in product design and development should also be included in the scope of relevant persons concerned by remuneration rules. Relevant persons should also include tied agents. When determining the remuneration for tied agents, firms should take the tied agents' special status and the respective national specificities into consideration. However, in such cases, firms' remuneration policies and practices should still define appropriate criteria to be used to assess the performance of relevant persons, including qualitative criteria encouraging the relevant persons to act in the best interests of the client.
- (42) Where successive personal transactions are carried out on behalf of a person in accordance with prior instructions given by that person, obligations relating to personal transactions should not apply separately to each such successive transaction if those instructions remain in force and unchanged. Similarly, those obligations should not apply to the termination or withdrawal of such instructions, provided that any financial instruments which had previously been acquired pursuant to the instructions are not disposed of at the same time as the instructions terminate or are withdrawn. However, those obligations should apply in relation to a personal transaction, or the commencement of successive personal transactions, carried out on behalf of the same person if those instructions are changed or if new instructions are issued.
- (43) Competent authorities should not make the authorisation to provide investment services or activities subject to a general prohibition on the outsourcing of one or more critical or important functions. Investment firms should be allowed to outsource such functions if the outsourcing arrangements established by the firm comply with certain conditions.

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<sup>5</sup> Regulation (EC) No 45/2001 of the European Parliament and of the Council of 18 December 2000 on the protection of individuals with regard to the processing of personal data by the Community institutions and bodies and on the free movement of such data (OJ L 8, 12.1.2001, p. 1).

- (44) The outsourcing of investment services or activities or critical and important functions is capable of constituting a material change of the conditions for the authorisation of the investment firm, as referred to in Article 21(2) of Directive 2014/65/EU. If such outsourcing arrangements are to be put in place after the investment firm has obtained an authorisation according to Chapter I of Title II of Directive 2014/65/EU, those arrangements should be notified to the competent authority where required by Article 21(2) of that Directive.
- (45) The circumstances which should be treated as giving rise to a conflict of interest should cover cases where there is a conflict between the interests of the firm or certain persons connected to the firm or the firm's group and the duty the firm owes to a client; or between the differing interests of two or more of its clients, to each of whom the firm owes a duty. It is not enough that the firm may gain a benefit if there is not also a possible disadvantage to a client, or that one client to whom the firm owes a duty may make a gain or avoid a loss without there being a concomitant possible loss to another such client.
- (46) Conflicts of interest should be regulated only where an investment service or ancillary service is provided by an investment firm. The status of the client to whom the service is provided — as either retail, professional or eligible counterparty — should be irrelevant for that purpose.
- (47) In complying with its obligation to draw up a conflict of interest policy under Directive 2014/65/EU which identifies circumstances which constitute or may give rise to a conflict of interest, the investment firm should pay special attention to the activities of investment research and advice, proprietary trading, portfolio management and corporate finance business, including underwriting or selling in an offering of securities and advising on mergers and acquisitions. In particular, such special attention is appropriate where the firm or a person directly or indirectly linked by control to the firm performs a combination of two or more of those activities.
- (48) Investment firms should aim to identify and prevent or manage the conflicts of interest arising in relation to their various business lines and their group's activities under a comprehensive conflicts of interest policy. While disclosure of specific conflicts of interest is required by Article 23(2) of Directive 2014/65/EU, it should be a measure of last resort to be used only where the organisational and administrative arrangements established by the investment firm to prevent or manage its conflicts of interest in accordance with Article 23(1) of Directive 2014/65/EU are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests of the client are prevented. Over-reliance on disclosure without adequate consideration as to how conflicts may appropriately be prevented or managed should not be permitted. The disclosure of conflicts of interest by an investment firm should not exempt it from the obligation to maintain and operate the effective organisational and administrative arrangements required under Article 16(3) of Directive 2014/65/EU.
- (49) Firms should always comply with the inducements rules under Article 24 of Directive 2014/65/EU, including when providing placing services. In particular, fees received by investment firms placing the financial instruments issued to its investment clients should comply with these provisions and laddering and spinning should be considered as abusive practices.



- (50) Investment research should be a sub-category of the type of information defined as a recommendation in Regulation (EU) 596/2014 (market abuse)<sup>6</sup>.
- (51) The measures and arrangements adopted by an investment firm to manage the conflicts of interests that might arise from the production and dissemination of material that is presented as investment research should be appropriate to protect the objectivity and independence of financial analysts and of the investment research they produce. Those measures and arrangements should ensure that financial analysts enjoy an adequate degree of independence from the interests of persons whose responsibilities or business interests may reasonably be considered to conflict with the interests of the persons to whom the investment research is disseminated.
- (52) Persons whose responsibilities or business interests may reasonably be considered to conflict with the interests of the persons to whom investment research is disseminated should include corporate finance personnel and persons involved in sales and trading on behalf of clients or the firm.
- (53) Exceptional circumstances in which financial analysts and other persons connected with the investment firm who are involved in the production of investment research may, with prior written approval, undertake personal transactions in instruments to which the research relates should include those circumstances where, for personal reasons relating to financial hardship, the financial analyst or other person is required to liquidate a position.
- (54) Fees, commissions, monetary or non-monetary benefits received by the firm providing investment research from any third party should only be acceptable when they are provided in accordance with requirements specified in Article 24(9) of Directive 2014/65/EU and Article 13 of Commission Delegated Directive (EU) .../... [to be inserted before adoption] of XXX supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, product governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits.
- (55) The concept of dissemination of investment research to clients or the public should not include dissemination exclusively to persons within the group of the investment firm. Current recommendations should be considered to be those recommendations contained in investment research which have not been withdrawn and which have not lapsed. The substantial alteration of investment research produced by a third party should be governed by the same requirements as the production of research.
- (56) Financial analysts should not engage in activities other than the preparation of investment research where engaging in such activities are inconsistent with the maintenance of that person's objectivity. These include participating in investment banking activities such as corporate finance business and underwriting, participating in 'pitches' for new business or 'road shows' for new issues of financial instruments; or being otherwise involved in the preparation of issuer marketing.

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<sup>6</sup> Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC (OJ L 173, 12.6.2014, p. 1).

- (57) Given the specificities of underwriting and placing services and the potential for conflicts of interest to arise in relation to such services, more detailed and tailored requirements should be specified in this Regulation. In particular, such requirements should ensure that the underwriting and placing process is managed in a way which respects the interests of different actors. Investment firms should ensure that their own interests or interests of their other clients do not improperly influence the quality of services provided to the issuer client. Such arrangements should be explained to that client, along with other relevant information about the offering process, before the firm accepts to undertake the offering.
- (58) Investment firms engaged in underwriting or placing activities should have appropriate arrangements in place to ensure that the pricing process, including book-building, is not detrimental to the issuer's interests.
- (59) The placing process involves the exercise of judgement by an investment firm as to the allocation of an issue, and is based on the particular facts and circumstances of the arrangements, which raises conflicts of interest concerns. The firm should have in place effective organisational requirements to ensure that allocations made as part of the placing process do not result in the firm's interest being placed ahead of the interests of the issuer client, or the interests of one investment client over those of another investment client. In particular, firms should clearly set out the process for developing allocation recommendations in an allocation policy.
- (60) Requirements imposed by this Regulation, including those relating to personal transactions, to dealing with knowledge of investment research and to the production or dissemination of investment research, should apply without prejudice to requirements of Directive 2014/65/EU and Regulation (EU) No 596/2014 of the European Parliament and of the Council<sup>7</sup> and their respective implementing measures.
- (61) This Regulation sets out requirements regarding information addressed to clients or potential clients, including marketing communications, in order to ensure that such information be fair, clear and not misleading in accordance with Article 24(3) of Directive 2014/65/EU.
- (62) Nothing in this Regulation requires competent authorities to approve the content and form of marketing communications. However, neither does it prevent them from doing so, insofar as any such pre-approval is based only on compliance with the obligation in Directive 2014/65/EU that information to clients or potential clients, including marketing communications, should be fair, clear and not misleading.
- (63) Information requirements should be established which take account of the status of a client as either retail, professional or eligible counterparty. An objective of Directive 2014/65/EU is to ensure a proportionate balance between investor protection and the disclosure obligations which apply to investment firms. To this end, it is appropriate to establish less stringent specific information requirements with respect to professional clients than to retail clients.
- (64) Investment firms should provide clients or potential clients with the necessary information on the nature of financial instruments and the risks associated with investing in them so that

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<sup>7</sup> Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC (OJ L 173, 12.6.2014, p. 1).

their clients are properly informed. The level of detail of the information to be provided may vary according to whether the client is a retail client or a professional client and the nature and risk profile of the financial instruments that are being offered, but should always include any essential elements. Member States may specify the precise terms, or the contents, of the description of risks required under this Regulation, taking into account the information requirements set out in Regulation (EU) No 1286/2014.

- (65) The conditions with which information addressed by investment firms to clients and potential clients must comply in order to be fair, clear and not misleading should apply to communications intended for retail or professional clients in a way that is appropriate and proportionate, taking into account, for example, the means of communication, and the information that the communication is intended to convey to the clients or potential clients. In particular, it would not be appropriate to apply such conditions to marketing communications which consist only of one or more of the following: the name of the firm, a logo or other image associated with the firm, a contact point, a reference to the types of investment services provided by the firm.
- (66) In order to improve the consistency of information received by investors, investment firms should ensure that the information provided to each client is consistently presented in the same language throughout all forms of information and marketing material provided to that client. However, this should not imply a requirement for firms to translate prospectuses, prepared in accordance with Directive 2003/71/EC of the European Parliament and of the Council<sup>8</sup> or Directive 2009/65/EC of the European Parliament and of the Council<sup>9</sup>, provided to clients.
- (67) In order to provide a fair and balanced presentation of benefits and risks, investment firms should always give a clear and prominent indication of any relevant risks, including drawbacks and weaknesses, when referencing any potential benefits of a service or financial instrument.
- (68) Information should be considered to be misleading if it has a tendency to mislead the person or persons to whom it is addressed or by whom it is likely to be received, regardless of whether the person who provides the information considers or intends it to be misleading.
- (69) In cases where an investment firm is required to provide information to a client before the provision of a service, each transaction in respect of the same type of financial instrument should not be considered as the provision of a new or different service.
- (70) Detailed information on whether investment advice is provided on an independent basis, on the broad or restricted analysis of different types of instruments and on the selection process used should help clients assess the scope of the advice provided. Sufficient details on the number of financial instruments analysed by the firms should be provided to clients. The number and variety of financial instruments to be considered, other than the ones provided by the investment firm or entities close to the firm, should be proportionate to the scope of

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<sup>8</sup> Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC (OJ L 345, 31.12.2003, p. 64).

<sup>9</sup> Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 302, 17.11.2009, p. 32).

the advice to be given, client preferences and needs. However, irrespective of the scope of services offered, all assessments should be based on an adequate number of financial instruments available on the market to allow an appropriate consideration of what the market offers as alternatives.

- (71) The scope of the advice given by investment firms on an independent basis could range from broad and general to specialist and specific. In order to ensure that the scope of the advice allows for a fair and appropriate comparison between different financial instruments, investment advisers specialising in certain categories of financial instruments and focusing on criteria that are not based on the technical structure of the instrument per se, such as 'green' or 'ethical' investments, should comply with certain conditions if they present themselves as independent advisers.
- (72) Enabling the same adviser to provide both independent and non-independent advice could create confusion for the client. In order to ensure clients' understanding of the nature and basis of investment advice provided, certain organisational requirements should also be established.
- (73) The provision by an investment firm to a client of a copy of a prospectus that has been drawn up and published in accordance with Directive 2003/71/EC should not be treated as the provision by the firm of information to a client for the purposes of the operating conditions under Directive 2014/65/EU which relate to the quality and contents of such information, if the firm is not responsible under that Directive for the information given in the prospectus.
- (74) Directive 2014/65/EU strengthens investment firms' obligations to disclose information on all costs and charges and extends these obligations to relationships with professional clients and eligible counterparties. In order to ensure that all categories of clients benefit from such increased transparency on costs and charges, investment firms should be allowed, in certain situations, when providing investment services to professional clients or eligible counterparties, to agree with these clients to limit the detailed requirements set out in this Regulation. This however should never lead to disapplying the obligations imposed on investment firms pursuant to Article 24(4) of Directive 2014/65/EU. In this respect, investment firms should inform professional clients about all costs and charges as set out in this Regulation, when the services of investment advice or portfolio management are provided or when, irrespective of the investment service provided, the financial instruments concerned embed a derivative. Investment firms should also inform eligible counterparties about all costs and charges as set out in this Regulation when, irrespective of the investment service provided, the financial instrument concerned embeds a derivative and intends to be distributed to their clients. However, in other cases, when providing investment services to professional clients or eligible counterparties, investment firms may agree, for instance, at the request of the client concerned, not to provide the illustration showing the cumulative effect of costs on return or an indication of the currency involved and the applicable conversion rates and costs where any part of the total costs and charges is expressed in foreign currency.
- (75) Taking into account the overarching obligation to act in accordance with the best interest of clients and the importance of informing clients, on an *ex-ante* basis, of all costs and charges to be incurred, the reference to financial instruments recommended or marketed should include in particular investment firms providing investment advice or portfolio management services, firms providing general recommendation concerning financial instruments or

promoting certain financial instruments in the provision of investment and ancillary services to clients. This would for instance be the case for investment firms that have entered into distribution or placement agreements with a product manufacturer or issuer.

- (76) In accordance with the overarching obligation to act in accordance with the best interest of clients and taking into account the obligations resulting from specific Union legislation regulating certain financial instruments (in particular, units in collective investment undertakings and packaged retail and insurance-based investment products (PRIIPs)) investment firms should disclose and aggregate all costs and charges, including the costs of the financial instrument, in all cases where investment firms are obliged to provide the client with information about the costs of a financial instrument in accordance with Union legislation.
- (77) Where investment firms have not marketed or recommended a financial instrument or are not required under Union law to provide clients with information about costs of a financial instrument, they may not be in the position to take into account all the costs associated with that financial instrument. Even in these residual instances, investment firms should inform clients, on an ex-ante basis, about all costs and charges associated to the investment service and the price of acquiring the relevant financial instrument. Furthermore, investment firms should comply with any other obligations to provide appropriate information about the risks of the relevant financial instrument in accordance with Article 24(4)(b) of Directive 2014/65/EU or to provide clients, on an ex-post basis, with adequate reports on the services provided in accordance with Article 25(6) of Directive 2014/65/EU, including cost elements.
- (78) In order to ensure clients' awareness of all costs and charges to be incurred as well as evaluation of such information and comparison with different financial instruments and investment services, investment firms should provide clients with clear and comprehensible information on all costs and charges in good time before the provision of services. *Ex-ante* information about the costs related to the financial instrument or ancillary service can be provided based on an assumed investment amount. However, the costs and charges disclosed should represent the costs the client would actually incur based on that assumed investment amount. For example, if an investment firm offers a range of ongoing services with different charges associated with each service, the firm should disclose the costs associated with the service the client subscribed to. For ex-post disclosures, information related to costs and charges should reflect the client's actual investment amount at the time the disclosure is produced.
- (79) In order to ensure investors receive information about all costs and charges pursuant to Article 24(4) of Directive 2014/65/EU, the underlying market risk should be understood as relating only to movements in the value of capital invested caused directly by movements in the value of underlying assets. Transactions costs and ongoing charges on financial instruments should therefore also be included in the required aggregation of costs and charges and should be estimated using reasonable assumptions, accompanied by an explanation that such estimations are based on assumptions and may deviate from costs and charges that will actually be incurred. Following the same objective of full disclosure, practices where there is 'netting' of costs should not be excluded from the obligation to provide information on costs and charges. The costs and charges disclosure is underpinned by the principle that every difference between the price of a position for the firm and the respective price for the client should be disclosed, including mark-ups and mark-downs.

- (80) While investment firms should aggregate all costs and charges in accordance with Article 24(4) of Directive 2014/65/EU and provide clients with the overall costs expressed both as a monetary amount and as a percentage, investment firms should, in addition, be allowed to provide clients or prospective clients with separate figures comprising aggregated initial costs and charges, aggregated on-going costs and charges and aggregated exit costs.
- (81) Investment firms distributing financial instruments, in relation to which information on costs and charges is insufficient, should additionally inform their clients about those costs as well as all the other costs and associated charges relating to the provision of investment services in relation to those financial instruments in order to safeguard clients' rights to full disclosure of costs and charges. This would be the case for investment firms distributing units in collective investment undertakings for which transaction costs have not been provided by for example units in UCITS management company. In such cases, the investment firms should liaise with UCITS management companies to obtain the relevant information.
- (82) In order to improve transparency for clients on the associated costs of their investments and the performance of their investments against the relevant costs and charges over time, periodic *ex-post* disclosure should also be provided where the investment firms have or have had an ongoing relationship with the client during the year. *Ex-post* disclosure on all the relevant costs and charges should be provided on a personalised basis. The *ex-post* periodic disclosure may be made by building on existing reporting obligations, such as obligations for firms providing execution of orders other than portfolio management, portfolio management or holding client financial instruments or funds.
- (83) The information which an investment firm is required to give to clients concerning costs and associated charges includes information about the arrangements for payment or performance of the agreement for the provision of investment services and any other agreement relating to a financial instrument that is being offered. For this purpose, arrangements for payment will generally be relevant where a financial instrument contract is terminated by cash settlement. Arrangements for performance will generally be relevant where, upon termination, a financial instrument requires the delivery of shares, bonds, a warrant, bullion or another instrument or commodity.
- (84) It is necessary to introduce different requirements for the application of the suitability assessment set out in Article 25(2) of Directive 2014/65/EU and the appropriateness assessment set out in Article 25(3) of that Directive. These tests are different in scope with regards to the investment services to which they relate, and have different functions and characteristics.
- (85) Investment firms should include in the suitability report and draw clients' attention to information on whether the recommended services or instruments are likely to require the retail client to seek a periodic review of their arrangements. This includes situations where a client is likely to need to seek advice to bring a portfolio of investments back in line with the original recommended allocation where there is a probability that the portfolio could deviate from the target asset allocation.
- (86) In order to take market developments into account and ensure the same level of investor protection, it should be clarified that investment firms should remain responsible for undertaking suitability assessments where investment advice or portfolio management services are provided in whole or in part through an automated or semi-automated system.

- (87) In accordance with the suitability assessment requirement under Article 25(2) of Directive 2014/65/EU, it should also be clarified that investment firms should undertake a suitability assessment not only in relation to recommendations to buy a financial instrument are made but for all decisions whether to trade including whether or not to buy, hold or sell an investment.
- (88) For the purposes of Article 25(2) of Directive 2014/65/EU, a transaction may be unsuitable for the client or potential client due to the risks of the associated financial instruments, the type of transaction, the characteristics of the order or the frequency of the trading. A series of transactions, each of which are suitable when viewed in isolation may be unsuitable if the recommendation or the decisions to trade are made with a frequency that is not in the best interests of the client. In the case of portfolio management, a transaction might also be unsuitable if it would result in an unsuitable portfolio.
- (89) A recommendation or request made, or advice given, by a portfolio manager to a client to the effect that the client should give or alter a mandate to the portfolio manager that defines the limits of the portfolio manager's discretion should be considered a recommendation as referred to in of Article 25(2) of Directive 2014/65/EU.
- (90) In order to provide legal certainty and enable clients to better understand the nature of the services provided, investment firms that provide investment or ancillary services to clients should enter into a written basic agreement with the client, setting out the essential rights and obligations of the firm and the client.
- (91) This Regulation should not require competent authorities to approve the content of the basic agreement between an investment firm and its clients. Nor should it prevent them from doing so, insofar as any such approval is based only on the firm's compliance with its obligations under Directive 2014/65/EU to act honestly, fairly and professionally in accordance with the best interests of its clients, and to establish a record that sets out the rights and obligations of investment firms and their clients, and the other terms on which firms will provide services to their clients.
- (92) The records an investment firm is required to keep should be adapted to the type of business and the range of investment services and activities performed, provided that the record-keeping obligations set out in Directive 2014/65/EU, Regulation (EU) No 600/2014 of the European Parliament and of the Council<sup>10</sup>, Regulation (EU) No 596/2014, Directive 2014/57/EU of the European Parliament and of the Council<sup>11</sup> and this Regulation are fulfilled and that competent authorities are able to fulfil their supervisory tasks and perform enforcement actions in view of ensuring both investor protection and market integrity.
- (93) In light of the importance of reports and periodic communications for all clients, and the extension of Article 25(6) of Directive 2014/65/EU to the relationship to eligible counterparties, the reporting requirements set in this Regulation should apply to all categories of clients. Taking into account the nature of the interactions with eligible counterparties, investment firms should be allowed to enter into agreements determining the

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<sup>10</sup> Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (OJ L 173, 12.6.2014, p. 84).

<sup>11</sup> Directive 2014/57/EU of the European Parliament and of the Council of 16 April 2014 on criminal sanctions for market abuse, (OJ L 173, 12.6.2014, p. 179).

specific content and timing of reporting different from the ones applicable for retail and professional clients.

- (94) In cases where an investment firm providing portfolio management services is required to provide clients or potential clients with information on the types of financial instruments that may be included in the client portfolio and the types of transactions that may be carried out in such instruments, such information should state separately whether the investment firm will be mandated to invest in financial instruments not admitted to trading on a regulated market, in derivatives, or in illiquid or highly volatile instruments; or to undertake short sales, purchases with borrowed funds, securities financing transactions, or any transactions involving margin payments, deposit of collateral or foreign exchange risk.
- (95) Clients should be informed of the performance of their portfolio and depreciations of their initial investments. In the case of portfolio management, this trigger should be set at the depreciation of 10%, and thereafter at multiples of 10%, of the overall value of the overall portfolio and should not apply to individual holdings.
- (96) For the purposes of the reporting obligations in respect of portfolio management, a contingent liability transaction should involve any actual or potential liability for the client that exceeds the cost of acquiring the instrument.
- (97) For the purposes of the provisions on reporting to clients, a reference to the type of the order should be understood as referring to its status as a limit order, market order, or other specific type of order.
- (98) For the purposes of the provisions on reporting to clients, a reference to the nature of the order should be understood as referring to orders to subscribe for securities, or to exercise an option, or similar client order.
- (99) When establishing its execution policy in accordance with Article 27(4) of Directive 2014/65/EU, an investment firm should determine the relative importance of the factors mentioned in Article 27(1) of that Directive, or at least establish the process by which it determines the relative importance of these factors, so that it can deliver the best possible result to its clients. In order to give effect to that policy, an investment firm should select the execution venues that enable it to obtain on a consistent basis the best possible result for the execution of client orders. In order to comply with the legal obligation of best execution, investment firms, when applying the criteria for best execution for professional clients, will typically not use the same execution venues for securities financing transactions (SFTs) and other transactions. This is because the SFTs are used as a source of funding subject to a commitment that the borrower will return equivalent securities on a future date and the terms of SFTs are typically defined bilaterally between the counterparties ahead of the execution. Therefore, the choice of execution venues for SFTs is more limited than in the case of other transactions, given that it depends on the particular terms defined in advance between the counterparties and on whether there is a specific demand on those execution venues for the financial instruments involved. As a result, the order execution policy established by investment firms should take into account the particular characteristics of SFTs and it should list separately execution venues used for SFTs. An investment firm should apply its execution policy to each client order that it executes with a view to obtaining the best possible result for the client in accordance with that policy.
- (100) In order to ensure that investment firms who transmit or place clients' orders with other entities for execution act in the best interest of their clients in accordance with Article 24 (1)



of Directive 2014/65/EU and with Article 24(4) of Directive 2014/65/EU to provide appropriate information to clients on the firm and its services, investment firms should provide clients with appropriate information on the top five entities for each class of financial instruments to which they transmit or place clients' orders and provide clients with information on the execution quality, in accordance with Article 27(6) of Directive 2014/65/EC and respective implementing measures. Investment firms transmitting or placing orders with other entities for execution may select a single entity for execution only where they are able to show that this allows them to obtain the best possible result for their clients on a consistent basis and where they can reasonably expect that the selected entity will enable them to obtain results for clients that are at least as good as the results that they reasonably could expect from using alternative entities for execution. This reasonable expectation should be supported by relevant data published in accordance with Article 27 of Directive 2014/65/EC or by internal analysis conducted by these investment firms.

- (101) For the purposes of ensuring that an investment firm obtains the best possible result for the client when executing a retail client order in the absence of specific client instructions, the firm should take into consideration all factors that will allow it to deliver the best possible result in terms of the total consideration, representing the price of the financial instrument and the costs related to execution. Speed, likelihood of execution and settlement, the size and nature of the order, market impact and any other implicit transaction costs may be given precedence over the immediate price and cost consideration only insofar as they are instrumental in delivering the best possible result in terms of the total consideration to the retail client.
- (102) When an investment firm executes an order following specific instructions from the client, it should be treated as having satisfied its best execution obligations only in respect of the part or aspect of the order to which the client instructions relate. The fact that the client has given specific instructions which cover one part or aspect of the order should not be treated as releasing the investment firm from its best execution obligations in respect of any other parts or aspects of the client order that are not covered by such instructions. An investment firm should not induce a client to instruct it to execute an order in a particular way, by expressly indicating or implicitly suggesting the content of the instruction to the client, when the firm ought reasonably to know that an instruction to that effect is likely to prevent it from obtaining the best possible result for that client. However, this should not prevent a firm inviting a client to choose between two or more specified trading venues, provided that those venues are consistent with the execution policy of the firm.
- (103) Dealing on own account with clients by an investment firm should be considered as the execution of client orders, and therefore subject to the requirements under Directive 2014/65/EU and this Regulation and, in particular, those obligations in relation to best execution. However, if an investment firm provides a quote to a client and that quote would meet the investment firm's obligations under Article 27(1) of Directive 2014/65/EU if the firm executed that quote at the time the quote was provided, then the firm should meet those same obligations if it executes its quote after the client accepts it, provided that, taking into account the changing market conditions and the time elapsed between the offer and acceptance of the quote, the quote is not manifestly out of date.
- (104) The obligation to deliver the best possible result when executing client orders applies in relation to all types of financial instruments. However, given the differences in market structures or the structure of financial instruments, it may be difficult to identify and apply a uniform standard of and procedure for best execution that would be valid and effective for

all classes of instrument. Best execution obligations should therefore be applied in a manner that takes into account the different circumstances associated with the execution of orders related to particular types of financial instruments. For example, transactions involving a customised OTC financial instrument that involve a unique contractual relationship tailored to the circumstances of the client and the investment firm may not be comparable for best execution purposes with transactions involving shares traded on centralised execution venues. [As best execution obligations apply to all financial instruments, irrespective of whether they are traded on trading venues or OTC, investment firms should gather relevant market data in order to check whether the OTC price offered for a client is fair and delivers on best execution obligation.

- (105) The provisions of this Regulation as to execution policy should be without prejudice to the general obligation of an investment firm under Article 27(7) of Directive 2014/65/EU to monitor the effectiveness of its order execution arrangements and policy and assess the venues in its execution policy on a regular basis.
- (106) This Regulation should not require a duplication of effort as to best execution between an investment firm which provides the service of reception and transmission of order or portfolio management and any investment firm to which that investment firm transmits its orders for execution.
- (107) The best execution obligation under Directive 2014/65/EU requires investment firms to take all sufficient steps to obtain the best possible result for their clients. The quality of execution, which includes aspects such as the speed and likelihood of execution such as fill rate) and the availability and incidence of price improvement, is an important factor in the delivery of best execution. Availability, comparability and consolidation of data related to execution quality provided by the various execution venues is crucial in enabling investment firms and investors to identify those execution venues that deliver the highest quality of execution for their clients. In order to obtain best execution result for a client, investment firms should compare and analyse relevant data including that made public in accordance with Article 27(3) of Directive 2014/65/EU and respective implementing measures.
- (108) Investment firms executing orders should be able to include a single execution venue in their policy only where they are able to show that this allows them to obtain best execution for their clients on a consistent basis. Investment firms should select a single execution venue only where they can reasonably expect that the selected execution venue will enable them to obtain results for clients that are at least as good as the results that they reasonably could expect from using alternative execution venues. This reasonable expectation must be supported by relevant data published in accordance with Article 27 of Directive 2014/65/EC or by other internal analyses conducted by the firms.
- (109) The reallocation of transactions should be considered as detrimental to a client if, as an effect of that reallocation, unfair precedence is given to the investment firm or to any particular client.
- (110) Without prejudice to Regulation (EU) No 596/2014, for the purposes of the provisions of this Regulation concerning client order handling, client orders should not be treated as otherwise comparable if they are received by different media and it would not be practicable for them to be treated sequentially. Any use by an investment firm of information relating to a pending client order in order to deal on own account in the financial instruments to which the client order relates, or in related financial instruments, should be considered a misuse of

that information. However, the mere fact that market makers or bodies authorised to act as counterparties confine themselves to pursuing their legitimate business of buying and selling financial instruments, or that persons authorised to execute orders on behalf of third parties confine themselves to carrying out an order dutifully, should not in itself be deemed to constitute a misuse of information.

- (111) When assessing whether a market fulfils the requirement laid down in point (a) of Article 33(3) of Directive 2014/65/EU that at least 50% of the issuers admitted to trading on that market are small and medium-size enterprises (SMEs), a flexible approach should be taken by competent authorities with regard to markets with no previous operating history, newly created SMEs whose financial instruments have been admitted to trading for less than three years and issuers exclusively of non-equity financial instruments.
- (112) Given the diversity in operating models of existing MTFs with a focus on SMEs in the Union, and to ensure the success of the new category of SME growth market, it is appropriate to grant SME growth markets an appropriate degree of flexibility in evaluating the appropriateness of issuers for admission on their venue. In any case, an SME growth market should not have rules that impose greater burdens on issuers than those applicable to issuers on regulated markets.
- (113) With regard to the content of the admission document which an issuer is required to produce upon initial admission to trading of its securities on an SME growth market, where the requirement to publish a prospectus pursuant to Directive 2003/71/EC does not apply, it is appropriate that competent authorities retain discretion to assess whether the rules set out by the operator of the SME growth market achieve the proper information of investors. While full responsibility for the information featured in the admission document should lie with the issuer, it should be for the operator of an SME growth market to define how the admission document should be appropriately reviewed. This should not necessarily involve a formal approval by the competent authority or the operator.
- (114) The publication by issuers of annual and half-yearly financial reports represents an appropriate minimum standard of transparency which is coherent with the prevailing best practice in existing markets focusing on SMEs. As to the content of financial reports, the operator of an SME growth market should be free to prescribe the use of International Financial Reporting Standards or financial reporting standards permitted by local laws and regulations, or both, by issuers whose financial instruments are traded on its venue. Deadlines for publishing financial reports should be less onerous than those prescribed by Directive 2004/109/EC as less stringent timeframes appear better suited to the needs and circumstances of SMEs.
- (115) Since the rules on dissemination of information about issuers on regulated markets under Directive 2004/109/EC would be too burdensome for issuers on SME growth markets, it is appropriate that the website of the operator of the SME growth market becomes the point of convergence for investors seeking information on the issuers traded on that venue. A publication on the website of the operator of the SME growth market can also be effected by providing a direct link to the website of the issuer in case the information is published there, if the link goes directly to the relevant part of the website of the issuer where the regulatory information can be easily found by investors.
- (116) It is necessary to further specify when a suspension or a removal from trading of a financial instrument is likely to cause significant damages to the investor's interest or to the orderly

functioning of the market. Convergence in that field is necessary to ensure that market participants in a Member State where trading in financial instruments has been suspended or financial instruments have been removed are not disadvantaged in comparison to market participants in another Member State, where trading is still ongoing.

- (117) To ensure the necessary level of convergence, it is appropriate to specify a list of circumstances constituting significant damage to investors' interests and the orderly functioning of the market which could be the basis of a decision by a national competent authority, an investment firm or a market operator operating an MTF or an OTF not to demand the suspension or removal of a financial instrument from trading, or not to follow a notification thereto. It is appropriate for such a list to be non-exhaustive as it will thus provide national competent authorities with a framework for the exercise of their judgement and will leave them a necessary degree of flexibility in the assessment of individual cases.
- (118) Articles 31(2) and 54(2) of Directive 2014/65/EU respectively require investment firms and market operators operating an MTF or an OTF, and market operators of regulated markets to immediately inform their national competent authorities under certain circumstances. This requirement is intended to ensure that national competent authorities can fulfil their regulatory tasks and are informed in a timely manner about relevant incidents which may have a negative impact on the functioning and integrity of the markets. The information received from operators of trading venues should enable national competent authorities to identify and assess the risks for the markets and their participants as well as to react efficiently and to take action if necessary.
- (119) It is appropriate to set up a non-exhaustive list of high-level circumstances where significant infringements of the rules of a trading venue, disorderly trading conditions or system disruptions in relation to a financial instrument may be assumed, thus triggering the obligation for the operators of trading venues to immediately inform their competent authorities as set out in Articles 31(2) and 54(2) of Directive 2014/65/EU. For that purpose, reference to the 'rules of a trading venue' should be understood in a broad sense and should comprise all rules, rulings, orders as well as general terms and conditions of contractual agreements between the trading venue and its participants which contain the conditions for trading and admission to the trading venue.
- (120) With regard to conduct that may indicate abusive behaviour within the scope of Regulation (EU) No 596/2014, it is also appropriate to set up a non-exhaustive list of signals of insider dealing and market manipulation which should be taken into account by the operator of a trading venue when examining transactions or orders to trade in order to determine whether the obligation to inform the relevant national competent authority applies, as set out in Articles 31(2) and 54(2) of Directive 2014/65/EU. For that purpose, reference to 'order to trade' should encompass all types of orders, including initial orders, modifications, updates and cancellations of orders, irrespective of whether or not they have been executed and irrespective of the means used to access the trading venue.
- (121) The list of signals of insider dealing and market manipulation should be neither exhaustive nor determinative of market abuse or attempts of market abuse, as each of the signals may not necessarily constitute market abuse or attempts of market abuse *per se*. Transactions or orders to trade meeting one or more signals may be conducted for legitimate reasons or in compliance with the rules of the trading venue.

- (122) In order to provide transparency to market stakeholders whilst preventing market abuse and preserving confidentiality of the identities of position holders, the publication of aggregate weekly position reports on positions referred to in Article 58(1)(a) of Directive 2014/65/EU should only apply to contracts that are traded by a certain number of persons, above certain sizes as specified in this Regulation.
- (123) In order to ensure that market data is provided on a reasonable commercial basis in a uniform manner in the Union, this Regulation specifies the conditions that APAs and CTPs must fulfil. These conditions are based on the objective to ensure that the obligation to provide market data on a reasonable commercial basis is sufficiently clear to allow for an effective and uniform application whilst taking into account different operating models and costs structures of data providers.
- (124) To ensure that fees for market data are set at a reasonable level, the fulfilment of the obligation to provide market data on a reasonable commercial basis requires that prices be based on a reasonable relationship to the cost of producing and disseminating that data. Therefore, without prejudice to the application of competition rules, data providers should determine their fees on the basis of their costs whilst being allowed to obtain a reasonable margin, based on factors such as the operating profit margin, the return on costs, the return on operating assets and the return on capital. Where data providers incur joint costs for data provision and the provision of other services, costs of data provision may include an appropriate share of costs arising from any other relevant service provided. Since specifying the exact cost is very complex, cost allocation and cost apportionment methodologies should be specified instead, leaving the specification of those costs to the discretion of market data providers.
- (125) Market data should be provided on a non-discriminatory basis, which requires that the same price and other terms and conditions should be offered to all customers who are in the same category according to published objective criteria.
- (126) To allow data users to obtain market data without having to buy other services, market data should be offered unbundled from other services. To avoid that data users are charged more than once for the same market data when buying data from different market data distributors, market data should be offered on a per user basis unless doing so would be disproportionate to the cost of such way of offering that data in respect of the scale and the scope of the market data provided by the APA and the CTP.
- (127) In order to allow for data users and competent authorities to effectively assess whether market data is provided on a reasonable commercial basis, it is necessary that all the essential conditions for its provision are disclosed to the public. Data providers should therefore disclose information about their fees and the content of the market data As well as the cost accounting methodologies used to determine their costs without having to disclose their actual costs.
- (128) It is appropriate to set the criteria for determining when the operations of a regulated market, an MTF or an OTF are of substantial importance in a host Member State so as to avoid creating an obligation on a trading venue to deal with or be made subject to the supervision of more than one competent authority where this would not be necessary according to Directive 2014/65/EU. For MTFs and OTFs, it is appropriate that only MTFs and OTFs with a significant market share be considered as being of substantial importance, so that not any relocation or acquisition of an economically insignificant MTF or OTF automatically

triggers the establishment of the cooperation arrangements set out in Article 79(2) of Directive 2014/65/EU.

- (129) This Regulation respects the fundamental rights and observes the principles recognised in the Charter of Fundamental Rights of the European Union (Charter). Accordingly, this Regulation should be interpreted and applied in accordance with those rights and principles in particular the right to protection of personal data, the freedom to conduct business, the right to consumer protection, the right to effective remedy and to a fair trial. Any processing of personal data under this Regulation should respect fundamental rights, including the right to respect for private and family life and the right to protection of personal data under Articles 7 and 8 of the Charter of Fundamental Rights of the European Union and must be in compliance with the Directive 95/46/EC and Regulation (EC) No 45/2001.
- (130) ESMA, established by Regulation (EU) No 1095/2010 of the European Parliament and of the Council<sup>12</sup> has been consulted for technical advice.
- (131) In order to allow competent authorities and investment firms to adapt to the new requirements contained in this Regulation so that they can be applied in an efficient and effective manner, the starting date of application of this Regulation should be aligned with the entry into application date of Directive 2014/65/EU,

HAS ADOPTED THIS REGULATION:

## **CHAPTER I**

### **SCOPE AND DEFINITIONS**

#### *Article 1*

#### **Subject-matter and scope**

1. Chapter II, and Sections 1 to 4, Articles 59(4) and 60 and Sections 6 and 8 of Chapter III and, to the extent they relate to those provisions, Chapter I and Section 9 of Chapter III and Chapter IV of this Regulation shall apply to management companies in accordance with Article 6(4) of Directive 2009/65/EC of the European Parliament and of the Council<sup>13</sup> and Article 6(6) of Directive 2011/61/EU of the European Parliament and of the Council<sup>14</sup>.
2. References to investment firms shall encompass credit institutions and references to financial instruments shall encompass structured deposits in relation to all the requirements referred to in Article 1(3) and 1(4) of Directive 2014/65/EU and their implementing provisions as set out under this Regulation.

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<sup>12</sup> Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

<sup>13</sup> Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 302, 17.11.2009, p. 32).

<sup>14</sup> Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (OJ L 174, 1.7.2011, p. 1).

## *Article 2* **Definitions**

For the purposes of this Regulation, the following definitions shall apply:

1. 'relevant person' in relation to an investment firm, means any of the following:
  - (a) a director, partner or equivalent, manager or tied agent of the firm;
  - (b) a director, partner or equivalent, or manager of any tied agent of the firm;
  - (c) an employee of the firm or of a tied agent of the firm, as well as any other natural person whose services are placed at the disposal and under the control of the firm or a tied agent of the firm and who is involved in the provision by the firm of investment services and activities;
  - (d) a natural person who is directly involved in the provision of services to the investment firm or to its tied agent under an outsourcing arrangement for the purpose of the provision by the firm of investment services and activities;
2. 'financial analyst' means a relevant person who produces the substance of investment research;
3. 'outsourcing' means an arrangement of any form between an investment firm and a service provider by which that service provider performs a process, a service or an activity which would otherwise be undertaken by the investment firm itself;
  - (a) 'person with whom a relevant person has a family relationship' means any of the following:
    - (b) the spouse of the relevant person or any partner of that person considered by national law as equivalent to a spouse;
    - (c) a dependent child or stepchild of the relevant person;
    - (d) any other relative of the relevant person who has shared the same household as that person for at least one year on the date of the personal transaction concerned;
4. 'securities financing transaction' means security financing transaction as defined in Article 3(11) of Regulation (EU) 2015/2365 of the European Parliament and of the Council<sup>15</sup>.
5. 'remuneration' means all forms of payments or financial or non-financial benefits provided directly or indirectly by firms to relevant persons in the provision of investment or ancillary services to clients;
6. 'commodity' means any goods of a fungible nature that are capable of being delivered, including metals and their ores and alloys, agricultural products, and energy such as electricity.

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<sup>15</sup> Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012 (OJ L 337, 23.12.2015, p. 1).

### Article 3

#### Conditions applying to the provision of information

1. Where, for the purposes of this Regulation, information is required to be provided in a durable medium as defined in Article 4(1) point 62 of Directive 2014/65/EU investment firms shall have the right to provide that information in a durable medium other than on paper only if:
  - (a) the provision of that information in that medium is appropriate to the context in which the business between the firm and the client is, or is to be, carried on; and
  - (b) the person to whom the information is to be provided, when offered the choice between information on paper or in that other durable medium, specifically chooses the provision of the information in that other medium.
2. Where, pursuant to Article 46, 47, 48, 49, 50 or 66(3) of this Regulation, an investment firm provides information to a client by means of a website and that information is not addressed personally to the client, investment firms shall ensure that the following conditions are satisfied:
  - (a) the provision of that information in that medium is appropriate to the context in which the business between the firm and the client is, or is to be, carried on;
  - (b) the client must specifically consent to the provision of that information in that form;
  - (c) the client must be notified electronically of the address of the website, and the place on the website where the information may be accessed;
  - (d) the information must be up to date;
  - (e) the information must be accessible continuously by means of that website for such period of time as the client may reasonably need to inspect it.
3. For the purposes of this Article, the provision of information by means of electronic communications shall be treated as appropriate to the context in which the business between the firm and the client is, or is to be, carried on where there is evidence that the client has regular access to the internet. The provision by the client of an e-mail address for the purposes of the carrying on of that business shall be treated as such evidence.

### Article 4

#### Provision of investment service in an incidental manner

(Article 2(1) of Directive 2014/65/EU)

For the purpose of the exemption in point (c) of Article 2(1) of Directive 2014/65/EU, an investment service shall be deemed to be provided in an incidental manner in the course of a professional activity where the following conditions are satisfied:

- (a) a close and factual connection exists between the professional activity and the provision of the investment service to the same client, such that the investment service can be regarded as accessory to the main professional activity;



- (b) the provision of investment services to the clients of the main professional activity does not aim to provide a systematic source of income to the person providing the professional activity; and
- (c) the person providing the professional activity does not market or otherwise promote his ability to provide investment services, except where these are disclosed to clients as being accessory to the main professional activity.

#### *Article 5*

### **Wholesale energy products that must be physically settled**

*(Article 4(1)(2) of Directive 2014/65/EU)*

1. For the purposes of Section C(6) of Annex I to Directive 2014/65/EU, a wholesale energy product must be physically settled where all the following conditions are satisfied:
  - (a) it contains provisions which ensure that parties to the contract have proportionate arrangements in place to be able to make or take delivery of the underlying commodity; a balancing agreement with the Transmission System Operator in the area of electricity and gas shall be considered a proportionate arrangement where the parties to the agreement have to ensure physical delivery of electricity or gas.
  - (b) it establishes unconditional, unrestricted and enforceable obligations of the parties to the contract to deliver and take delivery of the underlying commodity;
  - (c) it does not allow either party to replace physical delivery with cash settlement;
  - (d) the obligations under the contract cannot be offset against obligations from other contracts between the parties concerned, without prejudice to the rights of the parties to the contract, to net their cash payment obligations.

For the purposes of point (d), operational netting in power and gas markets shall not be considered as offsetting of obligations under a contract against obligations from other contracts.

2. Operational netting shall be understood as any nomination of quantities of power and gas to be fed into a gridwork upon being so required by the rules or requests of a Transmission System Operator as defined in Article 2(4) of Directive 2009/72/EC of the European Parliament and of the Council<sup>16</sup> for an entity performing an equivalent function to a Transmission System Operator at the national level. Any nomination of quantities based on operational netting shall not be at the discretion of the parties to the contract.
3. For the purposes of Section C(6) of Annex I to Directive 2014/65/EU, force majeure shall include any exceptional event or a set of circumstances which are outside the control of the parties to the contract, which the parties to the contract could not have reasonably foreseen or avoided by the exercise of appropriate and reasonable due diligence and which prevent one or both parties to the contract from fulfilling their contractual obligations.

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<sup>16</sup> Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC (OJ L 211, 14.8.2009, p. 55).

4. For the purposes of Section C(6) of Annex I to Directive 2014/65/EU bona fide inability to settle shall include any event or set of circumstances, not qualifying as force majeure as referred to in paragraph 3, which are objectively and expressly defined in the contract terms, for one or both parties to the contract, acting in good faith, not to fulfil their contractual obligations.
5. The existence of force majeure or bona fide inability to settle provisions shall not prevent a contract from being considered as 'physically settled' for the purposes of Section C(6) of Annex I to Directive 2014/65/EU.
6. The existence of default clauses providing that a party is entitled to financial compensation in the case of non- or defective performance of the contract shall not prevent the contract from being considered as 'physically settled' within the meaning of Section C(6) of Annex I to Directive 2014/65/EU.
7. The delivery methods for the contracts being considered as 'physically settled' within the meaning of Section C(6) of Annex I to Directive 2014/65/EU shall include at least:
  - (a) physical delivery of the relevant commodities themselves;
  - (b) delivery of a document giving rights of an ownership nature to the relevant commodities or the relevant quantity of the commodities concerned;
  - (c) other methods of bringing about the transfer of rights of an ownership nature in relation to the relevant quantity of goods without physically delivering them including notification, scheduling or nomination to the operator of an energy supply network, that entitles the recipient to the relevant quantity of the goods.

#### *Article 6*

### **Energy derivative contracts relating to oil and coal and wholesale energy products**

*(Article 4(1)(2) of Directive 2014/65/EU)*

1. For the purposes of Section C(6) of Annex I to Directive 2014/65/EU, energy derivative contracts relating to oil shall be contracts with mineral oil, of any description and petroleum gases, whether in liquid or vapour form, including products, components and derivatives of oil and oil transport fuels, including those with biofuel additives, as an underlying.
2. For the purposes of Section C(6) of Annex I to Directive 2014/65/EU, energy derivative contracts relating to coal shall be contracts with coal, defined as a black or dark-brown combustible mineral substance consisting of carbonised vegetable matter, used as a fuel, as an underlying.
3. For the purposes of Section C(6) of Annex I to Directive 2014/65/EU derivative contracts that have the characteristics of wholesale energy products as defined in Article 2(4) of Regulation (EU) 1227/2011 of the European Parliament and Council<sup>17</sup> shall be derivatives

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<sup>17</sup> Regulation (EU) No 1227/2011 of the European Parliament and of the Council of 25 October 2011 on wholesale energy market integrity and transparency (OJ L 326, 8.12.2011, p. 1).

with electricity or natural gas as an underlying, in accordance with points (b) and (d) of Article 2(4) of that Regulation.

#### *Article 7*

### **Other derivative financial instruments** (Article 4(1)(2) of Directive 2014/65/EU)

1. For the purposes of Section C(7) of Annex I to Directive 2014/65/EU, a contract which is not a spot contract in accordance with paragraph 2 and which is not for commercial purposes as laid down in paragraph 4 shall be considered as having the characteristics of other derivative financial instruments where it satisfies the following conditions:
  - (a) it meets one of the following criteria:
    - (i) it is traded on a third country trading venue that performs a similar function to a regulated market, an MTF or an OTF;
    - (ii) it is expressly stated to be traded on, or is subject to the rules of, a regulated market, an MTF, an OTF or such a third country trading venue;
    - (iii) it is equivalent to a contract traded on a regulated market, MTF, an OTF or such a third country trading venue, with regards to the price, the lot, the delivery date and other contractual terms;
  - (b) it is standardised so that the price, the lot, the delivery date and other terms are determined principally by reference to regularly published prices, standard lots or standard delivery dates.
2. A spot contract for the purposes of paragraph 1 shall be a contract for the sale of a commodity, asset or right, under the terms of which delivery is scheduled to be made within the longer of the following periods:
  - (a) 2 trading days;
  - (b) the period generally accepted in the market for that commodity, asset or right as the standard delivery period.

A contract shall not be considered a spot contract where, irrespective of its explicit terms, there is an understanding between the parties to the contract that delivery of the underlying is to be postponed and not to be performed within the period referred to in paragraph 2.

3. For the purposes of Section C(10) of Annex I to Directive 2004/39/EU, a derivative contract relating to an underlying referred to in that Section or in Article 8 of this Regulation shall be considered to have the characteristics of other derivative financial instruments where one of the following conditions is satisfied:
  - (a) it is settled in cash or may be settled in cash at the option of one or more of the parties, otherwise than by reason of a default or other termination event;
  - (b) it is traded on a regulated market, an MTF, an OTF, or a third country trading venue that performs a similar function to a regulated market, MTF or an OTF;

(c) the conditions laid down in paragraph 1 are satisfied in relation to that contract.

4. A contract shall be considered to be for commercial purposes for the purposes of Section C(7) of Annex I to Directive 2014/65/EU, and as not having the characteristics of other derivative financial instruments for the purposes of Sections C(7) and (10) of that Annex, where the following conditions are both met:

- (a) it is entered into with or by an operator or administrator of an energy transmission grid, energy balancing mechanism or pipeline network,
- (b) it is necessary to keep in balance the supplies and uses of energy at a given time, including the case when the reserve capacity contracted by an electricity transmission system operator as defined in Article 2(4) of Directive 2009/72/EC is being transferred from one prequalified balancing service provider to another prequalified balancing service provider with the consent of the relevant transmission system operator.

#### *Article 8*

#### **Derivatives under Section C(10) of Annex I to Directive 2014/65/EU**

*(Article 4(1)(2) of Directive 2014/65/EU)*

In addition to derivative contracts expressly referred to in Section C(10) of Annex I to Directive 2014/65/EU, a derivative contract shall be subject to the provisions in that Section where it meets the criteria set out in that Section and in Article 7(3) of this Regulation and it relates to any of the following:

- (a) telecommunications bandwidth;
- (b) commodity storage capacity;
- (c) transmission or transportation capacity relating to commodities, whether cable, pipeline or other means with the exception of transmission rights related to electricity transmission cross zonal capacities when they are, on the primary market, entered into with or by a transmission system operator or any persons acting as service providers on their behalf and in order to allocate the transmission capacity;
- (d) an allowance, credit, permit, right or similar asset which is directly linked to the supply, distribution or consumption of energy derived from renewable resources, except if the contract is already within the scope of Section C(4) of Annex I to Directive 2014/65/EU;
- (e) a geological, environmental or other physical variable, except if the contract is relating to any units recognised for compliance with the requirements of Directive 2003/87/EC of the European Parliament and of the Council<sup>18</sup>;
- (f) any other asset or right of a fungible nature, other than a right to receive a service, that is capable of being transferred;

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<sup>18</sup> Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC (OJ L 275, 25.10.2003, p. 32).

- (g) an index or measure related to the price or value of, or volume of transactions in any asset, right, service or obligation;
- (h) an index or measure based on actuarial statistics.

#### *Article 9*

#### **Investment advice**

*(Article 4(1)(4) of Directive 2014/65/EU)*

For the purposes of the definition of 'investment advice' in Article 4(1)(4) of Directive 2014/65/EU, a personal recommendation shall be considered a recommendation that is made to a person in his capacity as an investor or potential investor, or in his capacity as an agent for an investor or potential investor.

That recommendation shall be presented as suitable for that person, or shall be based on a consideration of the circumstances of that person, and shall constitute a recommendation to take one of the following sets of steps:

- (a) to buy, sell, subscribe for, exchange, redeem, hold or underwrite a particular financial instrument;
- (b) to exercise or not to exercise any right conferred by a particular financial instrument to buy, sell, subscribe for, exchange, or redeem a financial instrument.

A recommendation shall not be considered a personal recommendation if it is issued exclusively to the public.

#### *Article 10*

#### **Characteristics of other derivative contracts relating to currencies**

1. For the purposes of Section C (4) of Annex I to Directive 2014/65/EC, other derivative contracts relating to a currency shall not be a financial instrument where the contract is one of the following:
  - (a) a spot contract within the meaning of paragraph 2 of this Article,
  - (b) a means of payment that:
    - (i) must be settled physically otherwise than by reason of a default or other termination event;
    - (ii) is entered into by at least a person which is not a financial counterparty within the meaning of Article 2(8) of Regulation (EU) No. 648/2012 of the European Parliament and of the Council<sup>19</sup>;
    - (iii) is entered into in order to facilitate payment for identifiable goods, services or direct investment; and

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<sup>19</sup> Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (OJ L 201, 27.7.2012, p. 1).

(iv) is not traded on a trading venue.

2. A spot contract for the purposes of paragraph 1 shall be a contract for the exchange of one currency against another currency, under the terms of which delivery is scheduled to be made within the longer of the following periods:
- (a) 2 trading days in respect of any pair of the major currencies set out in paragraph 3;
  - (b) for any pair of currencies where at least one currency is not a major currency, the longer of 2 trading days or the period generally accepted in the market for that currency pair as the standard delivery period;
  - (c) where the contract for the exchange of those currencies is used for the main purpose of the sale or purchase of a transferable security or a unit in a collective investment undertaking, the period generally accepted in the market for the settlement of that transferable security or a unit in a collective investment undertaking as the standard delivery period or 5 trading days, whichever is shorter.

A contract shall not be considered a spot contract where, irrespective of its explicit terms, there is an understanding between the parties to the contract that delivery of the currency is to be postponed and not to be performed within the period set out in the first subparagraph.

3. The major currencies for the purposes of paragraph 2 shall only include the US dollar, Euro, Japanese yen, Pound sterling, Australian dollar, Swiss franc, Canadian dollar, Hong Kong dollar, Swedish krona, New Zealand dollar, Singapore dollar, Norwegian krone, Mexican peso, Croatian kuna, Bulgarian lev, Czech koruna, Danish krone, Hungarian forint, Polish zloty and Romanian leu.
4. For the purposes of paragraph 2, a trading day shall mean any day of normal trading in the jurisdiction of both the currencies that are exchanged pursuant to the contract for the exchange of those currencies and in the jurisdiction of a third currency where any of the following conditions are met:
- (a) the exchange of those currencies involves converting them through that third currency for the purposes of liquidity;
  - (b) the standard delivery period for the exchange of those currencies references the jurisdiction of that third currency.

#### *Article 11*

#### **Money-market instruments**

*(Article 4(1)(17) of Directive 2014/65/EU)*

Money-market instruments in accordance with Article 4(1)(17) of Directive 2014/65/EU, shall include treasury bills, certificates of deposits, commercial papers and other instruments with substantively equivalent features where they have the following characteristics:

- (a) they have a value that can be determined at any time;
- (b) they are not derivatives;
- (c) they have a maturity at issuance of 397 days or less.

## Article 12

### **Systematic internalisers for shares, depositary receipts, ETFs, certificates and other similar financial instruments**

(Article 4(1)(20) of Directive 2014/65/EU)

An investment firm shall be considered to be a systematic internaliser in accordance with Article 4(1)(20) of Directive 2014/65/EU in respect of each share, depositary receipt, exchange traded fund (ETF), certificate and other similar financial instrument where it internalises according to the following criteria:

- (a) on a frequent and systematic basis in the financial instrument for which there is a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months:
  - (i) the number of OTC transactions carried out by it on own account when executing client orders is equal to or larger than 0.4% of the total number of transactions in the relevant financial instrument executed in the Union on any trading venue or OTC during the same period;
  - (ii) the OTC transactions carried out by it on own account when executing client orders in the relevant financial instrument take place on average on a daily basis;
- (b) on a frequent and systematic basis in the financial instrument for which there is not a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months the OTC transactions carried out by it on own account when executing client orders takes place on average on a daily basis;
- (c) on a substantial basis in the financial instrument where the number of OTC trades carried out by it on own account when executing client orders is, during the past 6 months, equal to or larger than either:
  - (i) 15% of the total turnover in that financial instrument executed by the investment firm on own account or on behalf of clients and executed on a trading venue or OTC;
  - (ii) 0.4% of the total turnover in that financial instrument executed in the Union on a trading venue or OTC.

## Article 13

### **Systematic internalisers for bonds**

(Article 4(1)(20) of Directive 2014/65/EU)

An investment firm shall be considered to be a systematic internaliser in accordance with Article 4(1)(20) of Directive 2014/65/EU in respect of all bonds belonging to a class of bonds issued by the same entity or by any entity within the same group where, in relation to any such bond, it internalises according to the following criteria:

- (a) on a frequent and systematic basis in a bond for which there is a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months:

- (i) the number of OTC transactions carried out by it on own account when executing client orders is equal to or larger than 2.5% of the total number of transactions in the relevant bond executed in the Union on any trading venue or OTC during the same period;
  - (ii) the OTC transactions carried out by it on own account when executing client orders in the relevant financial instrument take place on average once a week;
- (b) on a frequent and systematic basis in a bond for which there is not a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months the OTC transactions carried out by it on own account when executing client orders takes place on average once a week;
- (c) on a substantial basis in a bond where the number of OTC trades carried out by it on own account when executing client orders is, during the past 6 months, equal to or larger than either:
- (i) 25% of the total nominal amount traded in that bond executed by the investment firm on own account or on behalf of clients and executed on a trading venue or OTC;
  - (ii) 1% of the total nominal amount traded in that bond executed in the Union on a trading venue or OTC.

#### *Article 14*

#### **Systematic internalisers for structured finance products**

*(Article 4(1)(20) of Directive 2014/65/EU)*

An investment firm shall be considered to be a systematic internaliser in accordance with Article 4(1)(20) of Directive 2014/65/EU in respect of all structured finance products belonging to a class of structured finance products issued by the same entity or by any entity within the same group where, in relation to any such structured finance product, it internalises according to the following criteria:

- (a) on a frequent and systematic basis in a structured finance product for which there is a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months:
- (i) the number of OTC transactions carried out by it on own account when executing client orders is equal to or larger than 4% of the total number of transactions in the relevant structured finance product executed in the Union on any trading venue or OTC during the same period;
  - (ii) the OTC transactions carried out by it on own account when executing client orders in the relevant financial instrument take place on average once a week;
- (b) on a frequent and systematic basis in a structured finance product for which there is not a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months the OTC transactions carried out by it on own account when executing client orders takes place on average once a week;



- (c) on a substantial basis in a structured finance product where the number of OTC trades carried out by it on own account when executing client orders is, during the past 6 months, equal to or larger than either:
- (i) 30% of the total nominal amount traded in that structured finance product executed by the investment firm on own account or on behalf of clients and executed on a trading venue or OTC;
  - (ii) 2.25% of the total nominal amount traded in that structured finance product executed in the Union on a trading venue or OTC.

*Article 15*

**Systematic internalisers for derivatives**  
(Article 4(1)(20) of Directive 2014/65/EU)

An investment firm shall be considered to be a systematic internaliser in accordance with Article 4(1)(20) of Directive 2014/65/EU in respect of all derivatives belonging to a class of derivatives where, in relation to any such derivative, it internalises according to the following criteria:

- (a) on a frequent and systematic basis in a derivative for which there is a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months:
- (i) the number of OTC transactions carried out by it on own account when executing client orders is equal to or larger than 2.5% of the total number of transactions in the relevant class of derivatives executed in the Union on any trading venue or OTC during the same period;
  - (ii) the OTC transactions carried out by it on own account when executing client orders in this class of derivatives take place on average once a week;
- (b) on a frequent and systematic basis in a derivative for which there is not a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months the OTC transactions carried out by it on own account in the relevant class of derivatives when executing client orders takes place on average once a week;
- (c) on a substantial basis in a derivative where the number of OTC trades carried out by it on own account when executing client orders is, during the past 6 months, equal to or larger than either:
- (i) 25% of the total nominal amount traded in that class of derivatives executed by the investment firm on own account or on behalf of clients and executed on a trading venue or OTC; or
  - (ii) 1% of the total nominal amount traded in that class of derivatives executed in the Union on a trading venue or OTC.

*Article 16*  
**Systematic internalisers for emission allowances**  
*(Article 4(1)(20) of Directive 2014/65/EU)*

An investment firm shall be considered to be a systematic internaliser in accordance with Article 4(1)(20) of Directive 2014/65/EU in respect of emission allowances where, in relation to any such instrument, it internalises according to the following criteria:

- (a) on a frequent and systematic basis in an emission allowance for which there is a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months:
  - (i) the number of OTC transactions carried out by it on own account when executing client orders is equal to or larger than 4% of the total number of transactions in the relevant type of emission allowances executed in the Union on any trading venue or OTC during the same period;
  - (ii) the OTC transactions carried out by it on own account when executing client orders in this type of emission allowances take place on average once a week;
- (b) on a frequent and systematic basis in an emission allowance for which there is not a liquid market in accordance with Article 2(1)(17)(b) of Regulation (EU) No 600/2014 where during the past 6 months the OTC transactions carried out by it on own account in the relevant type of emission allowances when executing client orders takes place on average once a week;
- (c) an investment firm internalises on a substantial basis in an emission allowance where the number of OTC trades carried out by it on own account when executing client orders is, during the past 6 months, equal to or larger than either of the following:
  - (i) 30% of the total nominal amount traded in that type of emission allowances executed by the investment firm on own account or on behalf of clients and executed on a trading venue or OTC;
  - (ii) 2.25% of the total nominal amount traded in that type of emission allowances executed in the Union on a trading venue or OTC.

*Article 17*  
**Relevant assessment periods**  
*(Article 4(1)(20) of Directive 2014/65/EU)*

The conditions set out in Articles 12 to 16 shall be assessed on a quarterly basis on the basis of data from the past 6 months. The assessment period shall start on the first working day of the months of January, April, July and October.

Newly issued instruments shall only be considered in the assessment when historical data covers a period of at least three months in the case of shares, depositary receipts, ETFs, certificates and other similar financial instruments, and six weeks in the case of bonds, structured finance products and derivatives.

*Article 18*

**Algorithmic trading**

*(Article 4(1)(39) of Directive 2014/65/EU)*

For the purposes of further specifying the definition of algorithmic trading in accordance with Article 4(1)(39) of Directive 2014/65/EU, a system shall be considered as having no or limited human intervention where, for any order or quote generation process or any process to optimise order-execution, an automated system makes decisions at any of the stages of initiating, generating, routing or executing orders or quotes according to pre-determined parameters.

*Article 19*

**High frequency algorithmic trading technique**

*(Article 4(1)(40) of Directive 2014/65/EU)*

1. A high message intraday rate in accordance with Article 4(1)(40) of Directive 2014/65/EU shall consist of the submission on average of any of the following:
  - (a) at least 2 messages per second with respect to any single financial instrument traded on a trading venue;
  - (b) at least 4 messages per second with respect to all financial instruments traded on a trading venue.
2. For the purposes of paragraph 1, messages concerning financial instruments for which there is a liquid market in accordance with Article 2(1)(17) of Regulation (EU) No 600/2014 shall be included in the calculation. Messages introduced for the purpose of trading that fulfil the criteria in Article 17(4) of Directive No 2014/65/EU shall be included in the calculation.
3. For the purposes of paragraph 1, messages introduced for the purpose of dealing on own account shall be included in the calculation. Messages introduced through other trading techniques than those relying on dealing on own account shall be included in the calculation where the firm's execution technique is structured in such a way as to avoid that the execution takes place on own account.
4. For the purposes of paragraph 1, for the calculation of high message intraday rate in relation to DEA providers, messages submitted by their DEA clients shall be excluded from the calculations.
5. For the purposes of paragraph 1, trading venues shall make available to the firms concerned, on request, estimates of the average of messages per second on a monthly basis two weeks after the end of each calendar month taking into account all messages submitted during the preceding 12 months.

*Article 20*

**Direct electronic access**

*(Article 4(1)(41) of Directive 2014/65/EU)*

1. A person shall be considered not capable of electronically transmitting orders relating to a financial instrument directly to a trading venue in accordance with Article 4(1)(41) of

Directive 2014/65/EU where that person cannot exercise discretion regarding the exact fraction of a second of order entry and the lifetime of the order within that timeframe.

2. A person shall be considered not capable of such direct electronic order transmission where it takes place through arrangements for optimisation of order execution processes that determine the parameters of the order other than the venue or venues where the order should be submitted, unless these arrangements are embedded into the clients' systems and not into those of the member or participant of a regulated market or of an MTF or a client of an OTF.

## **CHAPTER II**

### **ORGANISATIONAL REQUIREMENTS**

#### **SECTION 1**

#### **ORGANISATION**

##### *Article 21*

##### **General organisational requirements**

*(Article 16(2) to (10) of Directive 2014/65/EU)*

1. Investment firms shall comply with the following organisational requirements:
  - (a) establish, implement and maintain decision-making procedures and an organisational structure which clearly and in documented manner specifies reporting lines and allocates functions and responsibilities;
  - (b) ensure that their relevant persons are aware of the procedures which must be followed for the proper discharge of their responsibilities;
  - (c) establish, implement and maintain adequate internal control mechanisms designed to secure compliance with decisions and procedures at all levels of the investment firm;
  - (d) employ personnel with the skills, knowledge and expertise necessary for the discharge of the responsibilities allocated to them;
  - (e) establish, implement and maintain effective internal reporting and communication of information at all relevant levels of the investment firm;
  - (f) maintain adequate and orderly records of their business and internal organisation;
  - (g) ensure that the performance of multiple functions by their relevant persons does not and is not likely to prevent those persons from discharging any particular function soundly, honestly, and professionally.

When complying with the requirements set out in the this paragraph, investment firms shall take into account the nature, scale and complexity of the business of the firm, and the nature and range of investment services and activities undertaken in the course of that business.

2. Investment firms shall establish, implement and maintain systems and procedures that are adequate to safeguard the security, integrity and confidentiality of information, taking into account the nature of the information in question.
3. Investment firms shall establish, implement and maintain an adequate business continuity policy aimed at ensuring, in the case of an interruption to their systems and procedures, the preservation of essential data and functions, and the maintenance of investment services and activities, or, where that is not possible, the timely recovery of such data and functions and the timely resumption of their investment services and activities.
4. Investment firms shall establish, implement and maintain accounting policies and procedures that enable them, at the request of the competent authority, to deliver in a timely manner to the competent authority financial reports which reflect a true and fair view of their financial position and which comply with all applicable accounting standards and rules.
5. Investment firms shall monitor and, on a regular basis, evaluate the adequacy and effectiveness of their systems, internal control mechanisms and arrangements established in accordance with paragraphs 1 to 4, and take appropriate measures to address any deficiencies.

#### *Article 22*

#### **Compliance**

*(Article 16(2) of Directive 2014/65/EU)*

1. Investment firms shall establish, implement and maintain adequate policies and procedures designed to detect any risk of failure by the firm to comply with its obligations under Directive 2014/65/EU, as well as the associated risks, and put in place adequate measures and procedures designed to minimise such risk and to enable the competent authorities to exercise their powers effectively under that Directive.

Investment firms shall take into account the nature, scale and complexity of the business of the firm, and the nature and range of investment services and activities undertaken in the course of that business.

2. Investment firms shall establish and maintain a permanent and effective compliance function which operates independently and which has the following responsibilities:
  - (a) to monitor on a permanent basis and to assess, on a regular basis, the adequacy and effectiveness of the measures, policies and procedures put in place in accordance with the first subparagraph of paragraph 1, and the actions taken to address any deficiencies in the firm's compliance with its obligations;
  - (b) to advise and assist the relevant persons responsible for carrying out investment services and activities to comply with the firm's obligations under Directive 2014/65/EU;
  - (c) to report to the management body, on at least an annual basis, on the implementation and effectiveness of the overall control environment for investment services and activities, on the risks that have been identified and on the complaints-handling reporting as well as remedies undertaken or to be undertaken;

- (d) to monitor the operations of the complaints-handling process and consider complaints as a source of relevant information in the context of its general monitoring responsibilities.

In order to comply with points (a) and (b) of this paragraph, the compliance function shall conduct an assessment on the basis of which it shall establish a risk-based monitoring programme that takes into consideration all areas of the investment firm's investment services, activities and any relevant ancillary services, including relevant information gathered in relation to the monitoring of complaints handling. The monitoring programme shall establish priorities determined by the compliance risk assessment ensuring that compliance risk is comprehensively monitored.

3. In order to enable the compliance function referred to in paragraph 2 to discharge its responsibilities properly and independently, investment firms shall ensure that the following conditions are satisfied:
  - (a) the compliance function has the necessary authority, resources, expertise and access to all relevant information;
  - (b) a compliance officer is appointed and replaced by the management body and is responsible for the compliance function and for any reporting as to compliance required by Directive 2014/65/EU and Article 25(2) of this Regulation;
  - (c) the compliance function reports on an ad-hoc basis directly to the management body where it detects a significant risk of failure by the firm to comply with its obligations under Directive 2014/65/EU;
  - (d) the relevant persons involved in the compliance function are not involved in the performance of services or activities they monitor;
  - (e) the method of determining the remuneration of the relevant persons involved in the compliance function does not compromise their objectivity and is not likely to do so.
4. An investment firm shall not be required to comply with point (d) or point (e) of paragraph 3 where it is able to demonstrate that in view of the nature, scale and complexity of its business, and the nature and range of investment services and activities, the requirements under point (d) or (e) are not proportionate and that its compliance function continues to be effective. In that case, the investment firm shall assess whether the effectiveness of the compliance function is compromised. The assessment shall be reviewed on a regular basis.

### *Article 23*

#### **Risk management**

*(Article 16(5) of Directive 2014/65/EU)*

1. Investment firms shall take the following actions relating to risk management:
  - (a) establish, implement and maintain adequate risk management policies and procedures which identify the risks relating to the firm's activities, processes and systems, and where appropriate, set the level of risk tolerated by the firm;

- (b) adopt effective arrangements, processes and mechanisms to manage the risks relating to the firm's activities, processes and systems, in light of that level of risk tolerance;
  - (c) monitor the following:
    - (i) the adequacy and effectiveness of the investment firm's risk management policies and procedures;
    - (ii) the level of compliance by the investment firm and its relevant persons with the arrangements, processes and mechanisms adopted in accordance with point (b);
    - (iii) the adequacy and effectiveness of measures taken to address any deficiencies in those policies, procedures, arrangements, processes and mechanisms, including failures by the relevant persons to comply with such arrangements, processes and mechanisms or follow such policies and procedures.
2. Investment firms shall, where appropriate and proportionate in view of the nature, scale and complexity of their business and the nature and range of the investment services and activities undertaken in the course of that business, establish and maintain a risk management function that operates independently and carries out the following tasks:
- (a) implementation of the policy and procedures referred to in paragraph 1;
  - (b) provision of reports and advice to senior management in accordance with Article 25(2).

Where an investment firm does not establish and maintain a risk management function under the first sub-paragraph, it shall be able to demonstrate upon request that the policies and procedures which it has adopted in accordance with paragraph 1 satisfy the requirements therein.

*Article 24*  
**Internal audit**  
*(Article 16(5) of Directive 2014/65/EU)*

Investment firms shall, where appropriate and proportionate in view of the nature, scale and complexity of their business and the nature and range of investment services and activities undertaken in the course of that business, establish and maintain an internal audit function which is separate and independent from the other functions and activities of the investment firm and which has the following responsibilities:

- (a) establish, implement and maintain an audit plan to examine and evaluate the adequacy and effectiveness of the investment firm's systems, internal control mechanisms and arrangements;
- (b) issue recommendations based on the result of work carried out in accordance with point (a) and verify compliance with those recommendations;
- (c) report in relation to internal audit matters in accordance with Article 25(2).

*Article 25*

**Responsibility of senior management**  
(Article 16(2) of Directive 2014/65/EU)

1. Investment firms shall, when allocating functions internally, ensure that senior management, and, where applicable, the supervisory function, are responsible for ensuring that the firm complies with its obligations under Directive 2014/65/EU. In particular, senior management and, where applicable, the supervisory function shall be required to assess and periodically review the effectiveness of the policies, arrangements and procedures put in place to comply with the obligations under Directive 2014/65/EU and to take appropriate measures to address any deficiencies.

The allocation of significant functions among senior managers shall clearly establish who is responsible for overseeing and maintaining the firm's organisational requirements. Records of the allocation of significant functions shall be kept up-to-date.

2. Investment firms shall ensure that their senior management receive on a frequent basis, and at least annually, written reports on the matters covered by Articles 22, 23 and 24 indicating in particular whether the appropriate remedial measures have been taken in the event of any deficiencies.
3. Investment firms shall ensure that where there is a supervisory function, it receives written reports on the matters covered by Articles 22, 23 and 24 on a regular basis.
4. For the purposes of this Article, the supervisory function shall be the function within an investment firm responsible for the supervision of its senior management.

*Article 26*

**Complaints handling**  
(Article 16(2) of Directive 2014/65/EU)

1. Investment firms shall establish, implement and maintain effective and transparent complaints management policies and procedures for the prompt handling of clients' or potential clients' complaints. Investment firms shall keep a record of the complaints received and the measures taken for their resolution.

The complaints management policy shall provide clear, accurate and up-to-date information about the complaints-handling process. This policy shall be endorsed by the firm's management body.

2. Investment firms shall publish the details of the process to be followed when handling a complaint. Such details shall include information about the complaints management policy and the contact details of the complaints management function. The information shall be provided to clients or potential clients, on request, or when acknowledging a complaint. Investment firms shall enable clients and potential clients to submit complaints free of charge.
3. Investment firms shall establish a complaints management function responsible for the investigation of complaints. This function may be carried out by the compliance function.



4. When handling a complaint, investment firms shall communicate with clients or potential clients clearly, in plain language that is easy to understand and shall reply to the complaint without undue delay.
5. Investment firms shall communicate the firm's position on the complaint to clients or potential clients and inform the clients or potential clients about their options, including that they may be able to refer the complaint to an alternative dispute resolution entity, as defined in Article 4(h) of Directive 2013/11/EU of the European Parliament and the Council on consumer ADR or that the client may be able to take civil action.
6. Investment firms shall provide information on complaints and complaints-handling to the relevant competent authorities and, where applicable under national law, to an alternative dispute resolution (ADR) entity.
7. Investment firms' compliance function shall analyse complaints and complaints-handling data to ensure that they identify and address any risks or issues.

#### *Article 27*

#### **Remuneration policies and practices**

*(Articles 16, 23 and 24 of Directive 2014/65/EU)*

1. Investment firms shall define and implement remuneration policies and practices under appropriate internal procedures taking into account the interests of all the clients of the firm, with a view to ensuring that clients are treated fairly and their interests are not impaired by the remuneration practices adopted by the firm in the short, medium or long term.

Remuneration policies and practices shall be designed in such a way so as not to create a conflict of interest or incentive that may lead relevant persons to favour their own interests or the firm's interests to the potential detriment of any client.

2. Investment firms shall ensure that their remuneration policies and practices apply to all relevant persons with an impact, directly or indirectly, on investment and ancillary services provided by the investment firm or on its corporate behaviour, regardless of the type of clients, to the extent that the remuneration of such persons and similar incentives may create a conflict of interest that encourages them to act against the interests of any of the firm's clients.
3. The management body of the investment firm shall approve, after taking advice from the compliance function, the firm's remuneration policy. The senior management of the investment firm shall be responsible for the day-to-day implementation of the remuneration policy and the monitoring of compliance risks related to the policy.
4. Remuneration and similar incentives shall not be solely or predominantly based on quantitative commercial criteria, and shall take fully into account appropriate qualitative criteria reflecting compliance with the applicable regulations, the fair treatment of clients and the quality of services provided to clients.

A balance between fixed and variable components of remuneration shall be maintained at all times, so that the remuneration structure does not favour the interests of the investment firm or its relevant persons against the interests of any client.

*Article 28*  
**Scope of personal transactions**  
*(Article 16(2) of Directive 2014/65/EU)*

For the purposes of Article 29 and Article 37, a personal transaction shall be a trade in a financial instrument effected by or on behalf of a relevant person, where at least one of the following criteria are met:

- (a) the relevant person is acting outside the scope of the activities he carries out in his professional capacity;
- (b) the trade is carried out for the account of any of the following persons:
  - (i) the relevant person;
  - (ii) any person with whom he has a family relationship, or with whom he has close links;
  - (iii) a person in respect of whom the relevant person has a direct or indirect material interest in the outcome of the trade, other than obtaining a fee or commission for the execution of the trade.

*Article 29*  
**Personal transactions**  
*(Article 16(2) of Directive 2014/65/EU)*

1. Investment firms shall establish, implement and maintain adequate arrangements aimed at preventing the activities set out in paragraphs 2, 3 and 4 in the case of any relevant person who is involved in activities that may give rise to a conflict of interest, or who has access to inside information within the meaning of Article 7(1) of Regulation (EU) No 596/2014 or to other confidential information relating to clients or transactions with or for clients by virtue of an activity carried out by him on behalf of the firm.
2. Investment firms shall ensure that relevant persons do not enter into a personal transaction which meets at least one of the following criteria:
  - (a) that person is prohibited from entering into it under Regulation (EU) No 596/2014;
  - (b) it involves the misuse or improper disclosure of that confidential information;
  - (c) it conflicts or is likely to conflict with an obligation of the investment firm under Directive 2014/65/EU.
3. Investment firms shall ensure that relevant persons do not advise or recommend, other than in the proper course of employment or contract for services, any other person to enter into a transaction in financial instruments which, if it were a personal transaction of the relevant person, would be covered by paragraph 2 or Article 37(2)(a) or (b) or Article 67(3).
4. Without prejudice to Article 10(1) of Regulation (EU) No 596/2014, investment firms shall ensure that relevant persons do not disclose, other than in the normal course of his employment or contract for services, any information or opinion to any other person where

the relevant person knows, or reasonably ought to know, that as a result of that disclosure that other person will or would be likely to take either of the following steps:

- (a) to enter into a transaction in financial instruments which, if it were a personal transaction of the relevant person, would be covered by paragraphs 2 or 3 or Article 37(2)(a) or (b) or Article 67(3);
- (b) to advise or procure another person to enter into such a transaction.

5. The arrangements required under paragraph 1 shall be designed to ensure that:

- (a) each relevant person covered by paragraphs 1, 2, 3 and 4 is aware of the restrictions on personal transactions, and of the measures established by the investment firm in connection with personal transactions and disclosure, in accordance with paragraphs 1, 2, 3 and 4.
- (b) the firm is informed promptly of any personal transaction entered into by a relevant person, either by notification of that transaction or by other procedures enabling the firm to identify such transactions;
- (c) a record is kept of the personal transaction notified to the firm or identified by it, including any authorisation or prohibition in connection with such a transaction.

In the case of outsourcing arrangements, the investment firm shall ensure that the firm to which the activity is outsourced maintains a record of personal transactions entered into by any relevant person and provides that information to the investment firm promptly on request.

6. Paragraphs 1 to 5 shall not apply to the following personal transactions:

- (a) personal transactions effected under a discretionary portfolio management service where there is no prior communication in connection with the transaction between the portfolio manager and the relevant person or other person for whose account the transaction is executed;
- (b) personal transactions in undertakings for collective investments in transferable securities (UCITS) or AIFs that are subject to supervision under the law of a Member State which requires an equivalent level of risk spreading in their assets, where the relevant person and any other person for whose account the transactions are effected are not involved in the management of that undertaking.

## **SECTION 2 OUTSOURCING**

### *Article 30*

#### **Scope of critical and important operational functions**

*(Article 16(2) and first subparagraph of Article 16(5) of Directive 2014/65/EU)*

1. For the purposes of the first subparagraph of Article 16(5) of Directive 2014/65/EU, an operational function shall be regarded as critical or important where a defect or failure in

its performance would materially impair the continuing compliance of an investment firm with the conditions and obligations of its authorisation or its other obligations under Directive 2014/65/EU, or its financial performance, or the soundness or the continuity of its investment services and activities.

2. Without prejudice to the status of any other function, the following functions shall not be considered as critical or important for the purposes of paragraph 1:
  - (a) the provision to the firm of advisory services, and other services which do not form part of the investment business of the firm, including the provision of legal advice to the firm, the training of personnel of the firm, billing services and the security of the firm's premises and personnel;
  - (b) the purchase of standardised services, including market information services and the provision of price feeds.

### *Article 31*

#### **Outsourcing critical or important operational functions**

*(Article 16(2) and of Article 16(5) first subparagraph of Directive 2014/65/EU)*

1. Investment firms outsourcing critical or important operational functions shall remain fully responsible for discharging all of their obligations under Directive 2014/65/EU and shall comply with the following conditions:
  - (a) the outsourcing does not result in the delegation by senior management of its responsibility;
  - (b) the relationship and obligations of the investment firm towards its clients under the terms of Directive 2014/65/EU is not altered;
  - (c) the conditions with which the investment firm must comply in order to be authorised in accordance with Article 5 of Directive 2014/65/EU, and to remain so, are not undermined;
  - (d) none of the other conditions subject to which the firm's authorisation was granted is removed or modified.
2. Investment firms shall exercise due skill, care and diligence when entering into, managing or terminating any arrangement for the outsourcing to a service provider of critical or important operational functions and shall take the necessary steps to ensure that the following conditions are satisfied:
  - (a) the service provider has the ability, capacity, sufficient resources, appropriate organisational structure supporting the performance of the outsourced functions, and any authorisation required by law to perform the outsourced functions, reliably and professionally;
  - (b) the service provider carries out the outsourced services effectively and in compliance with applicable law and regulatory requirements, and to this end the firm has established methods and procedures for assessing the standard of performance of the

service provider and for reviewing on an ongoing basis the services provided by the service provider;

- (c) the service provider properly supervises the carrying out of the outsourced functions, and adequately manage the risks associated with the outsourcing;
- (d) appropriate action is taken where it appears that the service provider may not be carrying out the functions effectively or in compliance with applicable laws and regulatory requirements;
- (e) the investment firm effectively supervises the outsourced functions or services and manage the risks associated with the outsourcing and to this end the firm retains the necessary expertise and resources to supervise the outsourced functions effectively and manage those risks;
- (f) the service provider has disclosed to the investment firm any development that may have a material impact on its ability to carry out the outsourced functions effectively and in compliance with applicable laws and regulatory requirements;
- (g) the investment firm is able to terminate the arrangement for outsourcing where necessary, with immediate effect when this is in the interests of its clients, without detriment to the continuity and quality of its provision of services to clients;
- (h) the service provider cooperates with the competent authorities of the investment firm in connection with the outsourced functions;
- (i) the investment firm, its auditors and the relevant competent authorities have effective access to data related to the outsourced functions, as well as to the relevant business premises of the service provider, where necessary for the purpose of effective oversight in accordance with this article, and the competent authorities are able to exercise those rights of access;
- (j) the service provider protects any confidential information relating to the investment firm and its clients;
- (k) the investment firm and the service provider have established, implemented and maintained a contingency plan for disaster recovery and periodic testing of backup facilities, where that is necessary having regard to the function, service or activity that has been outsourced;
- (l) the investment firm has ensured that the continuity and quality of the outsourced functions or services are maintained also in the event of termination of the outsourcing either by transferring the outsourced functions or services to another third party or by performing them itself.

3. The respective rights and obligations of the investment firms and of the service provider shall be clearly allocated and set out in a written agreement. In particular, the investment firm shall keep its instruction and termination rights, its rights of information, and its right to inspections and access to books and premises. The agreement shall ensure that outsourcing by the service provider only takes place with the consent, in writing, of the investment firm.

4. Where the investment firm and the service provider are members of the same group, the investment firm may, for the purposes of complying with this Article and Article 32, take into account the extent to which the firm controls the service provider or has the ability to influence its actions.
5. Investment firms shall make available on request to the competent authority all information necessary to enable the authority to supervise the compliance of the performance of the outsourced functions with the requirements of Directive 2014/65/EU and its implementing measures.

#### *Article 32*

#### **Service providers located in third countries**

*(Article 16(2) and first subparagraph of Article 16(5) of Directive 2014/65/EU)*

1. In addition to the requirements set out in Article 31, where an investment firm outsources functions related to the investment service of portfolio management provided to clients to a service provider located in a third country, that investment firm ensures that the following conditions are satisfied:
  - (a) the service provider is authorised or registered in its home country to provide that service and is effectively supervised by a competent authority in that third country;
  - (b) there is an appropriate cooperation agreement between the competent authority of the investment firm and the supervisory authority of the service provider.
2. The cooperation agreement referred to in point (b) of paragraph 1 shall ensure that the competent authorities of the investment firm are able, at least, to:
  - (a) obtain on request the information necessary to carry out their supervisory tasks pursuant to Directive 2014/65/EU and Regulation (EU) No 600/2014;
  - (b) obtain access to the documents relevant for the performance of their supervisory duties maintained in the third country;
  - (c) receive information from the supervisory authority in the third country as soon as possible for the purpose of investigating apparent breaches of the requirements of Directive 2014/65/EU and its implementing measures and Regulation (EU) No 600/2014;
  - (d) cooperate with regard to enforcement, in accordance with the national and international law applicable to the supervisory authority of the third country and the competent authorities in the Union in cases of breach of the requirements of Directive 2014/65/EU and its implementing measures and relevant national law.
3. Competent authorities shall publish on their website a list of the supervisory authorities in third countries with which they have a cooperation agreement referred to in point (b) of paragraph 1.

Competent authorities shall update cooperation agreements concluded before the date of entry into application of this Regulation within six months from that date.

## SECTION 3 CONFLICTS OF INTEREST

### *Article 33*

#### **Conflicts of interest potentially detrimental to a client**

*(Articles 16(3) and 23 of Directive 2014/65/EU)*

For the purposes of identifying the types of conflict of interest that arise in the course of providing investment and ancillary services or a combination thereof and whose existence may damage the interests of a client, investment firms shall take into account, by way of minimum criteria, whether the investment firm or a relevant person, or a person directly or indirectly linked by control to the firm, is in any of the following situations, whether as a result of providing investment or ancillary services or investment activities or otherwise:

- (a) the firm or that person is likely to make a financial gain, or avoid a financial loss, at the expense of the client;
- (b) the firm or that person has an interest in the outcome of a service provided to the client or of a transaction carried out on behalf of the client, which is distinct from the client's interest in that outcome;
- (c) the firm or that person has a financial or other incentive to favour the interest of another client or group of clients over the interests of the client;
- (d) the firm or that person carries on the same business as the client;
- (e) the firm or that person receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monetary or non-monetary benefits or services.

### *Article 34*

#### **Conflicts of interest policy**

*(Articles 16(3) and 23 of Directive 2014/65/EU)*

1. Investment firms shall establish, implement and maintain an effective conflicts of interest policy set out in writing and appropriate to the size and organisation of the firm and the nature, scale and complexity of its business.

Where the firm is a member of a group, the policy shall also take into account any circumstances, of which the firm is or should be aware, which may give rise to a conflict of interest arising as a result of the structure and business activities of other members of the group.

2. The conflicts of interest policy established in accordance with paragraph 1 shall include the following content:
  - (a) it must identify, with reference to the specific investment services and activities and ancillary services carried out by or on behalf of the investment firm, the

circumstances which constitute or may give rise to a conflict of interest entailing a risk of damage to the interests of one or more clients;

(b) it must specify procedures to be followed and measures to be adopted in order to prevent or manage such conflicts.

3. The procedures and measures referred to in paragraph 2(b) shall be designed to ensure that relevant persons engaged in different business activities involving a conflict of interest of the kind specified in paragraph 2(a) carry on those activities at a level of independence appropriate to the size and activities of the investment firm and of the group to which it belongs, and to the risk of damage to the interests of clients.

For the purposes of paragraph 2(b), the procedures to be followed and measures to be adopted shall include at least those items in the following list that are necessary for the firm to ensure the requisite degree of independence:

(a) effective procedures to prevent or control the exchange of information between relevant persons engaged in activities involving a risk of a conflict of interest where the exchange of that information may harm the interests of one or more clients;

(b) the separate supervision of relevant persons whose principal functions involve carrying out activities on behalf of, or providing services to, clients whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the firm;

(c) the removal of any direct link between the remuneration of relevant persons principally engaged in one activity and the remuneration of, or revenues generated by, different relevant persons principally engaged in another activity, where a conflict of interest may arise in relation to those activities;

(d) measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries out investment or ancillary services or activities;

(e) measures to prevent or control the simultaneous or sequential involvement of a relevant person in separate investment or ancillary services or activities where such involvement may impair the proper management of conflicts of interest.

4. Investment firms shall ensure that disclosure to clients, pursuant to Article 23(2) of Directive 2014/65/EU, is a measure of last resort that shall be used only where the effective organisational and administrative arrangements established by the investment firm to prevent or manage its conflicts of interest in accordance with Article 23 of Directive 2014/65/EU are not sufficient to ensure, with reasonable confidence, that risks of damage to the interests of the client will be prevented.

The disclosure shall clearly state that the organisational and administrative arrangements established by the investment firm to prevent or manage that conflict are not sufficient to ensure, with reasonable confidence, that the risks of damage to the interests of the client will be prevented. The disclosure shall include specific description of the conflicts of interest that arise in the provision of investment and/or ancillary services, taking into account the nature of the client to whom the disclosure is being made. The description shall explain the general nature and sources of conflicts of interest, as well as the risks to the



client that arise as a result of the conflicts of interest and the steps undertaken to mitigate these risks, in sufficient detail to enable that client to take an informed decision with respect to the investment or ancillary service in the context of which the conflicts of interest arise.

5. Investment firms shall assess and periodically review, on an at least annual basis, the conflicts of interest policy established in accordance with paragraphs 1 to 4 and shall take all appropriate measures to address any deficiencies. Over-reliance on disclosure of conflicts of interest shall be considered a deficiency in the investment firm's conflicts of interest policy.

#### *Article 35*

### **Record of services or activities giving rise to detrimental conflict of interest**

*(Article 16(6) of Directive 2014/65/EU)*

Investment firms shall keep and regularly update a record of the kinds of investment or ancillary service or investment activity carried out by or on behalf of the firm in which a conflict of interest entailing a risk of damage to the interests of one or more clients has arisen or, in the case of an ongoing service or activity, may arise.

Senior management shall receive on a frequent basis, and at least annually, written reports on situations referred to in this Article.

#### *Article 36*

### **Investment research and marketing communications**

*(Article 24(3) of Directive 2014/65/EU)*

1. For the purposes of Article 37 investment research shall be research or other information recommending or suggesting an investment strategy, explicitly or implicitly, concerning one or several financial instruments or the issuers of financial instruments, including any opinion as to the present or future value or price of such instruments, intended for distribution channels or for the public, and in relation to which the following conditions are met:
  - (a) the research or information is labelled or described as investment research or in similar terms, or is otherwise presented as an objective or independent explanation of the matters contained in the recommendation;
  - (b) if the recommendation in question were made by an investment firm to a client, it would not constitute the provision of investment advice for the purposes of Directive 2014/65/EU.
2. A recommendation of the type covered by point (35) of Article 3(1) of Regulation (EU) 596/2014 that does not meet the conditions set out in paragraph 1 shall be treated as a marketing communication for the purposes of Directive 2014/65/EU and investment firms that produce or disseminate that recommendation shall ensure that it is clearly identified as such.

Additionally, firms shall ensure that any such recommendation contains a clear and prominent statement that (or, in the case of an oral recommendation, to the effect that) it

has not been prepared in accordance with legal requirements designed to promote the independence of investment research, and that it is not subject to any prohibition on dealing ahead of the dissemination of investment research.

### *Article 37*

## **Additional organisational requirements in relation to investment research or marketing communications**

*(Article 16(3) of Directive 2014/65/EU)*

1. Investment firms which produce, or arrange for the production of, investment research that is intended or likely to be subsequently disseminated to clients of the firm or to the public, under their own responsibility or that of a member of their group, shall ensure the implementation of all the measures set out in Article 34(3) in relation to the financial analysts involved in the production of the investment research and other relevant persons whose responsibilities or business interests may conflict with the interests of the persons to whom the investment research is disseminated.

The obligations in the first subparagraph shall also apply in relation to recommendations referred to in Article 36(2).

2. Investment firms referred to in the first subparagraph of paragraph 1 shall have in place arrangements designed to ensure that the following conditions are satisfied:
  - (a) financial analysts and other relevant persons do not undertake personal transactions or trade, other than as market makers acting in good faith and in the ordinary course of market making or in the execution of an unsolicited client order, on behalf of any other person, including the investment firm, in financial instruments to which investment research relates, or in any related financial instruments, with knowledge of the likely timing or content of that investment research which is not publicly available or available to clients and cannot readily be inferred from information that is so available, until the recipients of the investment research have had a reasonable opportunity to act on it;
  - (b) in circumstances not covered by point (a), financial analysts and any other relevant persons involved in the production of investment research do not undertake personal transactions in financial instruments to which the investment research relates, or in any related financial instruments, contrary to current recommendations, except in exceptional circumstances and with the prior approval of a member of the firm's legal or compliance function;
  - (c) a physical separation exists between the financial analysts involved in the production of investment research and other relevant persons whose responsibilities or business interests may conflict with the interests of the persons to whom the investment research is disseminated or, when considered not appropriate to the size and organisation of the firm as well as the nature, scale and complexity of its business, the establishment and implementation of appropriate alternative information barriers;
  - (d) the investment firms themselves, financial analysts, and other relevant persons involved in the production of the investment research do not accept inducements from those with a material interest in the subject-matter of the investment research;

- (e) the investment firms themselves, financial analysts, and other relevant persons involved in the production of the investment research do not promise issuers favourable research coverage;
- (f) before the dissemination of investment research issuers, relevant persons other than financial analysts, and any other persons are not permitted to review a draft of the investment research for the purpose of verifying the accuracy of factual statements made in that research, or for any purpose other than verifying compliance with the firm's legal obligations, where the draft includes a recommendation or a target price.

For the purposes of this paragraph, 'related financial instrument' shall be any financial instrument the price of which is closely affected by price movements in another financial instrument which is the subject of investment research, and includes a derivative on that other financial instrument.

3. Investment firms which disseminate investment research produced by another person to the public or to clients shall be exempt from complying with paragraph 1 if the following criteria are met:
- (a) the person that produces the investment research is not a member of the group to which the investment firm belongs;
  - (b) the investment firm does not substantially alter the recommendations within the investment research;
  - (c) the investment firm does not present the investment research as having been produced by it;
  - (d) the investment firm verifies that the producer of the research is subject to requirements equivalent to the requirements under this Regulation in relation to the production of that research, or has established a policy setting such requirements.

#### *Article 38*

#### **Additional general requirements in relation to underwriting or placing** *(Articles 16(3), 23 and 24 of Directive 2014/65/EU)*

1. Investment firms which provide advice on corporate finance strategy, as set out in Section B (3) of Annex I, and provide the service of underwriting or placing of financial instruments, shall, before accepting a mandate to manage the offering, have arrangements in place to inform the issuer client of the following:
- (a) the various financing alternatives available with the firm, and an indication of the amount of transaction fees associated with each alternative;
  - (b) the timing and the process with regard to the corporate finance advice on pricing of the offer;
  - (c) the timing and the process with regard to the corporate finance advice on placing of the offering;
  - (d) details of the targeted investors, to whom the firm intends to offer the financial instruments;

- (e) the job titles and departments of the relevant persons individuals involved in the provision of corporate finance advice on the price and allotment; and
  - (f) firm's arrangements to prevent or manage conflicts of interest that may arise where the firm places the relevant financial instruments with its investment clients or with its own proprietary book.
2. Investment firms shall have in place a centralised process to identify all underwriting and placing operations of the firm and record such information, including the date on which the firm was informed of potential underwriting and placing operations. Firms shall identify all potential conflicts of interest arising from other activities of the investment firm, or group, and implement appropriate management procedures. In cases where an investment firm cannot manage a conflict of interest by way of implementing appropriate procedures, the investment firm shall not engage in the operation.
  3. Investment firms providing execution and research services as well as carrying out underwriting and placing activities shall ensure adequate controls are in place to manage any potential conflicts of interest between these activities and between their different clients receiving those services.

#### *Article 39*

### **Additional requirements in relation to pricing of offerings in relation to issuance of financial instruments**

*(Articles 16(3), 23 and 24 of Directive 2014/65/EU)*

1. Investment firms shall have in place systems, controls and procedures to identify and prevent or manage conflicts of interest that arise in relation to possible under-pricing or over-pricing of an issue or involvement of relevant parties in the process. In particular, investment firms shall as a minimum requirement establish, implement and maintain internal arrangements to ensure both of the following:
  - (a) that the pricing of the offer does not promote the interests of other clients or firm's own interests, in a way that may conflict with the issuer client's interests; and
  - (b) the prevention or management of a situation where persons responsible for providing services to the firm's investment clients are directly involved in decisions about corporate finance advice on pricing to the issuer client.
2. Investment firms shall provide clients with information about how the recommendation as to the price of the offering and the timings involved is determined. In particular, the firm shall inform and engage with the issuer client about any hedging or stabilisation strategies it intends to undertake with respect to the offering, including how these strategies may impact the issuer clients' interests. During the offering process, firms shall also take all reasonable steps to keep the issuer client informed about developments with respect to the pricing of the issue.

#### Article 40

### **Additional requirements in relation to placing** (Articles 16(3), 23 and 24 of Directive 2014/65/EU)

1. Investment firms placing financial instruments shall establish, implement and maintain effective arrangements to prevent recommendations on placing from being inappropriately influenced by any existing or future relationships.
2. Investment firms shall establish, implement and maintain effective internal arrangements to prevent or manage conflicts of interests that arise where persons responsible for providing services to the firm's investment clients are directly involved in decisions about recommendations to the issuer client on allocation.
3. Investment firms shall not accept any third-party payments or benefits unless such payments or benefits comply with the inducements requirements laid down in Article 24 of Directive 2014/65/EU. In particular, the following practices shall be considered not compliant with those requirements and shall therefore be considered not acceptable:
  - (a) an allocation made to incentivise the payment of disproportionately high fees for unrelated services provided by the investment firm ('laddering'), such as disproportionately high fees or commissions paid by an investment client, or disproportionately high volumes of business at normal levels of commission provided by the investment client as a compensation for receiving an allocation of the issue;
  - (b) an allocation made to a senior executive or a corporate officer of an existing or potential issuer client, in consideration for the future or past award of corporate finance business ('spinning');
  - (c) an allocation that is expressly or implicitly conditional on the receipt of future orders or the purchase of any other service from the investment firm by an investment client, or any entity of which the investor is a corporate officer.
4. Investment firms shall establish, implement and maintain an allocation policy that sets out the process for developing allocation recommendations. The allocation policy shall be provided to the issuer client before agreeing to undertake any placing services. The policy shall set out relevant information that is available at that stage, about the proposed allocation methodology for the issue.
5. Investment firms shall involve the issuer client in discussions about the placing process in order for the firm to be able to understand and take into account the client's interests and objectives. The investment firm shall obtain the issuer client's agreement to its proposed allocation per type of client for the transaction in accordance with the allocation policy.

#### Article 41

### **Additional requirements in relation to advice, distribution and self-placement** (Articles 16(3), 23 and 24 of Directive 2014/65/EU)

1. Investment firms shall have in place systems, controls and procedures to identify and manage the conflicts of interest that arise when providing investment service to an investment client to participate in a new issue, where the investment firm receives

commissions, fees or any monetary or non-monetary benefits in relation to arranging the issuance. Any commissions, fees or monetary or non-monetary benefits shall comply with the requirements in Article 24(7), 24(8) and 24(9) of Directive 2014/65/EU and be documented in the investment firm's conflicts of interest policies and reflected in the firm's inducements arrangements.

2. Investment firms engaging in the placement of financial instruments issued by themselves or by entities within the same group, to their own clients, including their existing depositor clients in the case of credit institutions, or investment funds managed by entities of their group, shall establish, implement and maintain clear and effective arrangements for the identification, prevention or management of the potential conflicts of interest that arise in relation to this type of activity. Such arrangements shall include consideration of refraining from engaging in the activity, where conflicts of interest cannot be appropriately managed so as to prevent any adverse effects on clients.
3. When disclosure of conflicts of interest is required, investment firms shall comply with the requirements in Article 34(4), including an explanation of the nature and source of the conflicts of interest inherent to this type of activity, providing details about the specific risks related to such practices in order to enable clients to make an informed investment decision.
4. Investment firms engaging in the offering of financial instruments issued by themselves or other group entities to their clients and those instruments are included in the calculation of prudential requirements specified in Regulation (EU) No 575/2013 of the European Parliament and of the Council<sup>20</sup>, Directive 2013/36/EU of the European Parliament and of the Council<sup>21</sup> or Directive 2014/59/EU of the European Parliament and of the Council<sup>22</sup>, shall provide such clients with additional information explaining the differences between the financial instrument and bank deposits in terms of yield, risk, liquidity and any protection provided in accordance with Directive 2014/49/EU of the European Parliament and of the Council<sup>23</sup>.

#### *Article 42*

### **Additional requirements in relation to lending or provision of credit in the context of underwriting or placement**

*(Articles 16(3), 23 and 24 of Directive 2014/65/EU)*

1. Where any previous lending or credit to the issuer client by an investment firm, or an entity within the same group, may be repaid with the proceeds of an issue, the investment firm

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<sup>20</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

<sup>21</sup> Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

<sup>22</sup> Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council (OJ L 173, 12.6.2014, p. 190).

<sup>23</sup> Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes (OJ L 173, 12.6.2014, p. 149).

shall have arrangements in place to identify and prevent or manage any conflicts of interest that may arise as a result.

2. Where the arrangements taken to manage conflicts of interest prove insufficient to ensure that the risk of damage to the issuer client would be prevented, investment firms shall disclose to the issuer client the specific conflicts of interest that have arisen in relation to their, or group entities', activities in a capacity of credit provider, and their activities related to the securities offering.
3. Investment firms' conflict of interest policy shall require the sharing of information about the issuer's financial situation with group entities acting as credit providers, provided this would not breach information barriers set up by the firm to protect the interests of a client.

#### *Article 43*

#### **Record keeping in relation to underwriting or placing**

*(Articles 16(3), 23 and 24 of Directive 2014/65/EU)*

Investment firms shall keep records of the content and timing of instructions received from clients. A record of the allocation decisions taken for each operation shall be kept to provide for a complete audit trail between the movements registered in clients' accounts and the instructions received by the investment firm. In particular, the final allocation made to each investment client shall be clearly justified and recorded. The complete audit trail of the material steps in the underwriting and placing process shall be made available to competent authorities upon request.

## **CHAPTER III**

### **OPERATING CONDITIONS FOR INVESTMENT FIRMS**

#### **SECTION 1**

#### **INFORMATION TO CLIENTS AND POTENTIAL CLIENTS**

#### *Article 44*

#### **Fair, clear and not misleading information requirements**

*(Article 24(3) of Directive 2014/65/EU)*

1. Investment firms shall ensure that all information they address to, or disseminate in such a way that it is likely to be received by, retail or professional clients or potential retail or professional clients, including marketing communications, satisfies the conditions laid down in paragraphs 2 to 8.
2. Investment firm shall ensure that the information referred to in paragraph 1 complies with the following conditions:
  - (a) the information includes the name of the investment firm,

- (b) the information is accurate and always gives a fair and prominent indication of any relevant risks when referencing any potential benefits of an investment service or financial instrument,
  - (c) the information uses a font size in the indication of relevant risks that is at least equal to the predominant font size used throughout the information provided, as well as a layout ensuring such indication is prominent,
  - (d) the information is sufficient for, and presented in a way that is likely to be understood by, the average member of the group to whom it is directed, or by whom it is likely to be received,
  - (e) the information does not disguise, diminish or obscure important items, statements or warnings,
  - (f) the information is consistently presented in the same language throughout all forms of information and marketing materials that are provided to each client, unless the client has accepted to receive information in more than one language,
  - (g) the information is up-to-date and relevant to the means of communication used.
3. Where the information compares investment or ancillary services, financial instruments, or persons providing investment or ancillary services, investment firms shall ensure that the following conditions are satisfied:
- (a) the comparison is meaningful and presented in a fair and balanced way;
  - (b) the sources of the information used for the comparison are specified;
  - (c) the key facts and assumptions used to make the comparison are included.
4. Where the information contains an indication of past performance of a financial instrument, a financial index or an investment service, investment firms shall ensure that the following conditions are satisfied:
- (a) that indication is not the most prominent feature of the communication;
  - (b) the information must include appropriate performance information which covers the preceding 5 years, or the whole period for which the financial instrument has been offered, the financial index has been established, or the investment service has been provided where less than five years, or such longer period as the firm may decide, and in every case that performance information is based on complete 12-month periods;
  - (c) the reference period and the source of information is clearly stated;
  - (d) the information contains a prominent warning that the figures refer to the past and that past performance is not a reliable indicator of future results;
  - (e) where the indication relies on figures denominated in a currency other than that of the Member State in which the retail client or potential retail client is resident, the currency is clearly stated, together with a warning that the return may increase or decrease as a result of currency fluctuations;



- (f) where the indication is based on gross performance, the effect of commissions, fees or other charges are disclosed.
5. Where the information includes or refers to simulated past performance, investment firms shall ensure that the information relates to a financial instrument or a financial index, and the following conditions are satisfied:
- (a) the simulated past performance is based on the actual past performance of one or more financial instruments or financial indices which are the same as, or substantially the same as, or underlie, the financial instrument concerned;
  - (b) in respect of the actual past performance referred to in point (a), the conditions set out in points (a) to (c), (e) and (f) of paragraph 4 are satisfied;
  - (c) the information contains a prominent warning that the figures refer to simulated past performance and that past performance is not a reliable indicator of future performance.
6. Where the information contains information on future performance, investment firms shall ensure that the following conditions are satisfied:
- (a) the information is not based on or refer to simulated past performance;
  - (b) the information is based on reasonable assumptions supported by objective data;
  - (c) where the information is based on gross performance, the effect of commissions, fees or other charges is disclosed;
  - (d) the information is based on performance scenarios in different market conditions (both negative and positive scenarios), and reflects the nature and risks of the specific types of instruments included in the analysis;
  - (e) the information contains a prominent warning that such forecasts are not a reliable indicator of future performance.
7. Where the information refers to a particular tax treatment, it shall prominently state that the tax treatment depends on the individual circumstances of each client and may be subject to change in the future.
8. The information shall not use the name of any competent authority in such a way that would indicate or suggest endorsement or approval by that authority of the products or services of the investment firm.

#### *Article 45*

#### **Information concerning client categorisation**

*(Article 24(4) of Directive 2014/65/EU)*

1. Investment firms shall notify new clients, and existing clients that the investment firm has newly categorised as required by Directive 2014/65/EU, of their categorisation as a retail client, a professional client or an eligible counterparty in accordance with that Directive.

2. Investment firms shall inform clients in a durable medium about any right that client has to request a different categorisation and about any limitations to the level of client protection that a different categorisation would entail.
3. Investment firms may, either on their own initiative or at the request of the client concerned treat a client in the following manner:
  - (a) as a professional or retail client where that client might otherwise be classified as an eligible counterparty pursuant to Article 30(2) of Directive 2014/65/EU;
  - (b) a retail client where that client that is considered as a professional client pursuant to Section I of Annex II to Directive 2014/65/EU.

#### *Article 46*

#### **General requirements for information to clients**

*(Article 24(4) of Directive 2014/65/EU)*

1. Investment firms shall, in good time before a client or potential client is bound by any agreement for the provision of investment services or ancillary services or before the provision of those services, whichever is the earlier to provide that client or potential client with the following information:
  - (a) the terms of any such agreement;
  - (b) the information required by Article 47 relating to that agreement or to those investment or ancillary services.
2. Investment firms shall, in good time before the provision of investment services or ancillary services to clients or potential clients, to provide the information required under Articles 47 to 50.
3. The information referred to in paragraphs 1 and 2 shall be provided in a durable medium or by means of a website (where it does not constitute a durable medium) provided that the conditions specified in Article 3(2) are satisfied.
4. Investment firms shall notify a client in good time about any material change to the information provided under Articles 47 to 50 which is relevant to a service that the firm is providing to that client. That notification shall be given in a durable medium if the information to which it relates is given in a durable medium.
5. Investment firms shall ensure that information contained in a marketing communication is consistent with any information the firm provides to clients in the course of carrying on investment and ancillary services.
6. Marketing communications containing an offer or invitation of the following nature and specifying the manner of response or including a form by which any response may be made, shall include such of the information referred to in Articles 47 to 50 as is relevant to that offer or invitation:
  - (a) an offer to enter into an agreement in relation to a financial instrument or investment service or ancillary service with any person who responds to the communication;

- (b) an invitation to any person who responds to the communication to make an offer to enter into an agreement in relation to a financial instrument or investment service or ancillary service.

However, the first subparagraph shall not apply if, in order to respond to an offer or invitation contained in the marketing communication, the potential client must refer to another document or documents, which, alone or in combination, contain that information.

#### *Article 47*

### **Information about the investment firm and its services for clients and potential clients** *(Article 24(4) of Directive 2014/65/EU)*

1. Investment firms shall provide clients or potential clients with the following general information, where relevant:
  - (a) the name and address of the investment firm, and the contact details necessary to enable clients to communicate effectively with the firm;
  - (b) the languages in which the client may communicate with the investment firm, and receive documents and other information from the firm;
  - (c) the methods of communication to be used between the investment firm and the client including, where relevant, those for the sending and reception of orders;
  - (d) a statement of the fact that the investment firm is authorised and the name and contact address of the competent authority that has authorised it;
  - (e) where the investment firm is acting through a tied agent, a statement of this fact specifying the Member State in which that agent is registered;
  - (f) the nature, frequency and timing of the reports on the performance of the service to be provided by the investment firm to the client in accordance with Article 25(6) of Directive 2014/65/EU;
  - (g) where the investment firm holds client financial instruments or client funds, a summary description of the steps which it takes to ensure their protection, including summary details of any relevant investor compensation or deposit guarantee scheme which applies to the firm by virtue of its activities in a Member State;
  - (h) a description, which may be provided in summary form, of the conflicts of interest policy maintained by the firm in accordance with Article 34;
  - (i) at the request of the client, further details of that conflicts of interest policy in a durable medium or by means of a website (where that does not constitute a durable medium) provided that the conditions set out Article 3(2) are satisfied.
2. When providing the service of portfolio management, investment firms shall establish an appropriate method of evaluation and comparison such as a meaningful benchmark, based on the investment objectives of the client and the types of financial instruments included in

The information listed in points (a) to (i) shall be provided in good time before the provision of investment services or ancillary services to clients or potential clients.

the client portfolio, so as to enable the client for whom the service is provided to assess the firm's performance.

3. Where investment firms propose to provide portfolio management services to a client or potential client, they shall provide the client, in addition to the information required under paragraph 1, with such of the following information as is applicable:
  - (a) information on the method and frequency of valuation of the financial instruments in the client portfolio;
  - (b) details of any delegation of the discretionary management of all or part of the financial instruments or funds in the client portfolio;
  - (c) a specification of any benchmark against which the performance of the client portfolio will be compared;
  - (d) the types of financial instrument that may be included in the client portfolio and types of transaction that may be carried out in such instruments, including any limits;
  - (e) the management objectives, the level of risk to be reflected in the manager's exercise of discretion, and any specific constraints on that discretion.

The information listed in points (a) to (e) shall be provided in good time before the provision of investment services or ancillary services to clients or potential clients.

#### *Article 48*

#### **Information about financial instruments**

*(Article 24(4) of Directive 2014/65/EU)*

1. Investment firms shall provide clients or potential clients in good time before the provision of investment services or ancillary services to clients or potential clients with a general description of the nature and risks of financial instruments, taking into account, in particular, the client's categorisation as either a retail client, professional client or eligible counterparty. That description shall explain the nature of the specific type of instrument concerned, the functioning and performance of the financial instrument in different market conditions, including both positive and negative conditions, as well as the risks particular to that specific type of instrument in sufficient detail to enable the client to take investment decisions on an informed basis.
2. The description of risks referred to in paragraph 1 shall include, where relevant to the specific type of instrument concerned and the status and level of knowledge of the client, the following elements:
  - (a) the risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as bail in;
  - (b) the volatility of the price of such instruments and any limitations on the available market for such instruments;
  - (c) information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed

investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments;

- (d) the fact that an investor might assume, as a result of transactions in such instruments, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the instruments;
- (e) any margin requirements or similar obligations, applicable to instruments of that type.

3. Where an investment firm provides a retail client or potential retail client with information about a financial instrument that is the subject of a current offer to the public and a prospectus has been published in connection with that offer in accordance with Directive 2003/71/EC, that firm shall in good time before the provision of investment services or ancillary services to clients or potential clients inform the client or potential client where that prospectus is made available to the public.
4. Where a financial instrument is composed of two or more different financial instruments or services, the investment firm shall provide an adequate description of the legal nature of the financial instrument, the components of that instrument and the way in which the interaction between the components affects the risks of the investment.
5. In the case of financial instruments that incorporate a guarantee or capital protection, the investment firm shall provide a client or a potential client with information about the scope and nature of such guarantee or capital protection. When the guarantee is provided by a third party, information about the guarantee shall include sufficient detail about the guarantor and the guarantee to enable the client or potential client to make a fair assessment of the guarantee.

#### *Article 49*

### **Information concerning safeguarding of client financial instruments or client funds**

*(Article 24(4) of Directive 2014/65/EU)*

1. Investment firms holding financial instruments or funds belonging to clients shall provide those clients or potential clients with the information specified in paragraphs 2 to 7 where relevant.
2. The investment firm shall inform the client or potential client where the financial instruments or funds of that client may be held by a third party on behalf of the investment firm and of the responsibility of the investment firm under the applicable national law for any acts or omissions of the third party and the consequences for the client of the insolvency of the third party.
3. Where financial instruments of the client or potential client may, if permitted by national law, be held in an omnibus account by a third party, the investment firm shall inform the client of this fact and shall provide a prominent warning of the resulting risks.
4. The investment firm shall inform the client or potential client where it is not possible under national law for client financial instruments held with a third party to be separately

identifiable from the proprietary financial instruments of that third party or of the investment firm and shall provide a prominent warning of the resulting risks.

5. The investment firm shall inform the client or potential client where accounts that contain financial instruments or funds belonging to that client or potential client are or will be subject to the law of a jurisdiction other than that of a Member State and shall indicate that the rights of the client or potential client relating to those financial instruments or funds may differ accordingly.
6. An investment firm shall inform the client about the existence and the terms of any security interest or lien which the firm has or may have over the client's financial instruments or funds, or any right of set-off it holds in relation to those instruments or funds. Where applicable, it shall also inform the client of the fact that a depository may have a security interest or lien over, or right of set-off in relation to those instruments or funds.
7. An investment firm, before entering into securities financing transactions in relation to financial instruments held by it on behalf of a client, or before otherwise using such financial instruments for its own account or the account of another client shall in good time before the use of those instruments provide the client, in a durable medium, with clear, full and accurate information on the obligations and responsibilities of the investment firm with respect to the use of those financial instruments, including the terms for their restitution, and on the risks involved.

#### *Article 50*

#### **Information on costs and associated charges**

*(Article 24(4) of Directive 2014/65/EU)*

1. For the purposes of providing information to clients on all costs and charges pursuant to Article 24(4) of Directive 2014/65/EU, investment firms shall comply with the detailed requirements in paragraphs 2 to 10.

Without prejudice to the obligations set out in Article 24(4) of Directive 2014/65/EU, investment firms providing investment services to professional clients shall have the right to agree to a limited application of the detailed requirements set out in this Article with these clients. Investment firms shall not be allowed to agree such limitations when the services of investment advice or portfolio management are provided or when, irrespective of the investment service provided, the financial instruments concerned embed a derivative.

Without prejudice to the obligations set out in Article 24(4) of Directive 2014/65/EU, investment firms providing investment services to eligible counterparties shall have the right to agree to a limited application of the detailed requirements set out in this Article, except when, irrespective of the investment service provided, the financial instruments concerned embed a derivative and the eligible counterparty intends to offer them to its clients.

2. For ex-ante and ex-post disclosure of information on costs and charges to clients, investment firms shall aggregate the following:

(a) all costs and associated charges charged by the investment firm or other parties where the client has been directed to such other parties, for the investment services(s) and/or ancillary services provided to the client; and

(b) all costs and associated charges associated with the manufacturing and managing of the financial instruments.

Costs referred to in points (a) and (b) are listed in Annex II to this Regulation. For the purposes of point (a), third party payments received by investment firms in connection with the investment service provided to a client shall be itemised separately and the aggregated costs and charges shall be totalled and expressed both as a cash amount and as a percentage.

3. Where any part of the total costs and charges is to be paid in or represents an amount of foreign currency, investment firms shall provide an indication of the currency involved and the applicable currency conversion rates and costs. Investment firms shall also inform about the arrangements for payment or other performance.
4. In relation to the disclosure of product costs and charges that are not included in the UCITS KIID, the investment firms shall calculate and disclose these costs, for example, by liaising with UCITS management companies to obtain the relevant information.
5. The obligation to provide in good time a full ex-ante disclosure of information about the aggregated costs and charges related to the financial instrument and to the investment or ancillary service provided shall apply to investment firms in the following situations:
  - (a) where the investment firm recommends or markets financial instruments to clients; or
  - (b) where the investment firm providing any investment services is required to provide clients with a UCITS KIID or PRIIPs KID in relation to the relevant financial instruments, in accordance with relevant Union legislation.
6. Investment firms that do not recommend or market a financial instrument to the client or are not obliged to provide the client with a KID/KIID in accordance with relevant Union legislation shall inform their clients about all costs and charges relating to the investment and/or ancillary service provided.
7. Where more than one investment firm provides investment or ancillary services to the client, each investment firm shall provide information about the costs of the investment or ancillary services it provides. An investment firm that recommends or markets to its clients the services provided by another firm, shall aggregate the cost and charges of its services together with the cost and charges of the services provided by the other firm. An investment firm shall take into account the costs and charges associated to the provision of other investment or ancillary services by other firms where it has directed the client to these other firms.
8. Where calculating costs and charges on an ex-ante basis, investment firms shall use actually incurred costs as a proxy for the expected costs and charges. Where actual costs are not available, the investment firm shall make reasonable estimations of these costs. Investment firms shall review ex-ante assumptions based on the ex-post experience and shall make adjustment to these assumptions, where necessary.

9. Investment firms shall provide annual ex-post information about all costs and charges related to both the financial instrument(s) and investment and ancillary service(s) where they have recommended or marketed the financial instrument(s) or where they have provided the client with the KID/KIID in relation to the financial instrument(s) and they have or have had an ongoing relationship with the client during the year. Such information shall be based on costs incurred and shall be provided on a personalised basis.

Investment firms may choose to provide such aggregated information on costs and charges of the investment services and the financial instruments together with any existing periodic reporting to clients.

10. Investment firms shall provide their clients with an illustration showing the cumulative effect of costs on return when providing investment services. Such an illustration shall be provided both on an ex-ante and ex-post basis. Investment firms shall ensure that the illustration meets the following requirements:
- (a) the illustration shows the effect of the overall costs and charges on the return of the investment;
  - (b) the illustration shows any anticipated spikes or fluctuations in the costs; and
  - (c) the illustration is accompanied by a description of the illustration.

#### *Article 51*

### **Information provided in accordance with Directive 2009/65/EC and Regulation (EU) No 1286/2014**

*(Article 24(4) of Directive 2014/65/EU)*

Investment firms distributing units in collective investment undertakings or PRIIPs shall additionally inform their clients about any other costs and associated charges related to the product which may have not been included in the UCITS KID or PRIIPs KID and about the costs and charges relating to their provision of investment services in relation to that financial instrument.

## **SECTION 2 INVESTMENT ADVICE**

#### *Article 52*

### **Information about investment advice** *(Article 24(4) of Directive 2014/65/EU)*

1. Investment firms shall explain in a clear and concise way whether and why investment advice qualifies as independent or non-independent and the type and nature of the restrictions that apply, including, when providing investment advice on an independent basis, the prohibition to receive and retain inducements.

Where advice is offered or provided to the same client on both an independent and non-independent basis, investment firms shall explain the scope of both services to allow investors to understand the differences between them and not present itself as an independent investment adviser for the overall activity. Firms shall not give undue



prominence to their independent investment advice services over non-independent investment services in their communications with clients.

2. Investment firms providing investment advice, on an independent or non-independent basis, shall explain to the client the range of financial instruments that may be recommended, including its relationship with the issuers or providers of the instruments.
3. Investment firms shall provide a description of the types of financial instruments considered, the range of financial instruments and providers analysed per each type of instrument according to the scope of the service, and, when providing independent advice, how the service provided satisfies the conditions for the provision of investment advice on an independent basis and the factors taken into consideration in the selection process used by the investment firm to recommend financial instruments, such as risks, costs and complexity of the financial instruments.
4. When the range of financial instruments assessed by the investment firm providing investment advice on an independent basis includes the investment firm's own financial instruments or those issued or provided by entities having close links or any other close legal or economic relationship with the investment firm as well as other issuers or providers which are not linked or related, the investment firm shall distinguish, for each type of financial instrument, the range of the financial instruments issued or provided by entities not having any links with the investment firm.
5. Investment firms providing a periodic assessment of the suitability of the recommendations provided pursuant to Article 54(12) shall disclose all of the following:
  - (a) the frequency and extent of the periodic suitability assessment and where relevant, the conditions that trigger that assessment;
  - (b) the extent to which the information previously collected will be subject to reassessment; and
  - (c) the way in which an updated recommendation will be communicated to the client.

#### *Article 53*

#### **Investment advice on an independent basis**

*(Article 24(4) and 24(7) of Directive 2014/65/EU)*

1. Investment firms providing investment advice on an independent basis shall define and implement a selection process to assess and compare a sufficient range of financial instruments available on the market in accordance with Article 24(7)(a) of Directive 2014/65/EU. The selection process shall include the following elements:
  - (a) the number and variety of financial instruments considered is proportionate to the scope of investment advice services offered by the independent investment adviser;
  - (b) the number and variety of financial instruments considered is adequately representative of financial instruments available on the market;

- (c) the quantity of financial instruments issued by the investment firm itself or by entities closely linked to the investment firm itself is proportionate to the total amount of financial instruments considered; and
- (d) the criteria for selecting the various financial instruments shall include all relevant aspects such as risks, costs and complexity as well as the characteristics of the investment firm's clients, and shall ensure that the selection of the instruments that may be recommended is not biased.

Where such a comparison is not possible due to the business model or the specific scope of the service provided, the investment firm providing investment advice shall not present itself as independent.

2. An investment firm that provides investment advice on an independent basis and that focuses on certain categories or a specified range of financial instruments shall comply with the following requirements:
  - (a) the firm shall market itself in a way that is intended only to attract clients with a preference for those categories or range of financial instruments;
  - (b) the firm shall require clients to indicate that they are only interested in investing in the specified category or range of financial instruments; and
  - (c) prior to the provision of the service, the firm shall ensure that its service is appropriate for each new client on the basis that its business model matches the client's needs and objectives, and the range of financial instruments that are suitable for the client. Where this is not the case the firm shall not provide such a service to the client.
3. An investment firm offering investment advice on both an independent basis and on a non-independent basis shall comply with the following obligations:
  - (a) in good time before the provision of its services, the investment firm has informed its clients, in a durable medium, whether the advice will be independent or non-independent in accordance with Article 24(4)(a) of Directive [2014/65/EU](#) and the relevant implementing measures;
  - (b) the investment firm has presented itself as independent for its business as a whole but has only done so with respect to the services for which it provides investment advice on an independent basis; and
  - (c) the investment firms has adequate organisational requirements and controls in place to ensure that both types of advice services and advisers are clearly separated from each other and that clients are not likely to be confused about the type of advice that they are receiving and are given the type of advice that is appropriate for them. The investment firm shall not allow a natural person to provide both independent and non-independent advice.

## SECTION 3

### ASSESSMENT OF SUITABILITY AND APPROPRIATENESS

#### *Article 54*

#### **Assessment of suitability and suitability reports**

*(Article 25(2) of Directive 2014/65/EU)*

1. Investment firms shall not create any ambiguity or confusion about their responsibilities in the process when assessing the suitability of investment services or financial instruments in accordance with Article 25(2) of Directive 2014/65/EU. When undertaking the suitability assessment, the firm shall inform clients or potential clients, clearly and simply, that the reason for assessing suitability is to enable the firm to act in the client's best interest.

Where investment advice or portfolio management services are provided in whole or in part through an automated or semi-automated system, the responsibility to undertake the suitability assessment shall lie with the investment firm providing the service and shall not be reduced by the use of an electronic system in making the personal recommendation or decision to trade.

2. Investment firms shall determine the extent of the information to be collected from clients in light of all the features of the investment advice or portfolio management services to be provided to those clients. Investment firms shall obtain from clients or potential clients such information as is necessary for the firm to understand the essential facts about the client and to have a reasonable basis for determining, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of providing a portfolio management service, satisfies the following criteria:

- (a) it meets the investment objectives of the client in question, including client's risk tolerance;
- (b) it is such that the client is able financially to bear any related investment risks consistent with his investment objectives;
- (c) it is such that the client has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio.

3. Where an investment firm provides an investment service to a professional client it shall be entitled to assume that in relation to the products, transactions and services for which it is so classified, the client has the necessary level of experience and knowledge for the purposes of point (c) of paragraph 2.

Where that investment service consists in the provision of investment advice to a professional client covered by Section 1 of Annex II to Directive 2014/65/EU, the investment firm shall be entitled to assume for the purposes of point (b) of paragraph 2 that the client is able financially to bear any related investment risks consistent with the investment objectives of that client.

4. The information regarding the financial situation of the client or potential client shall include, where relevant, information on the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments.
5. The information regarding the investment objectives of the client or potential client shall include, where relevant, information on the length of time for which the client wishes to hold the investment, his preferences regarding risk taking, his risk profile, and the purposes of the investment.
6. Where a client is a legal person or a group of two or more natural persons or where one or more natural persons are represented by another natural person, the investment firm shall establish and implement policy as to who should be subject to the suitability assessment and how this assessment will be done in practice, including from whom information about knowledge and experience, financial situation and investment objectives should be collected. The investment firm shall record this policy.

Where a natural person is represented by another natural person or where a legal person having requested treatment as professional client in accordance with Section 2 of Annex II of Directive 2014/65/EU is to be considered for the suitability assessment, the financial situation and investment objectives shall be those of the legal person or, in relation to the natural person, the underlying client rather than of the representative. The knowledge and experience shall be that of the representative of the natural person or the person authorised to carry out transactions on behalf of the underlying client.

7. Investment firms shall take reasonable steps to ensure that the information collected about their clients or potential clients is reliable. This shall include, but shall not be limited to, the following:
  - (a) ensuring clients are aware of the importance of providing accurate and up-to-date information;
  - (b) ensuring all tools, such as risk assessment profiling tools or tools to assess a client's knowledge and experience, employed in the suitability assessment process are fit-for-purpose and are appropriately designed for use with their clients, with any limitations identified and actively mitigated through the suitability assessment process;
  - (c) ensuring questions used in the process are likely to be understood by clients, capture an accurate reflection of the client's objectives and needs, and the information necessary to undertake the suitability assessment; and
  - (d) taking steps, as appropriate, to ensure the consistency of client information, such as by considering whether there are obvious inaccuracies in the information provided by clients.

Investment firms having an on-going relationship with the client, such as by providing an ongoing advice or portfolio management service, shall have, and be able to demonstrate, appropriate policies and procedures to maintain adequate and up-to-date information about clients to the extent necessary to fulfil the requirements under paragraph 2.

8. Where, when providing the investment service of investment advice or portfolio management, an investment firm does not obtain the information required under Article

25(2) of Directive 2014/65/EU, the firm shall not recommend investment services or financial instruments to the client or potential client.

9. Investment firms shall have, and be able to demonstrate, adequate policies and procedures in place to ensure that they understand the nature, features, including costs and risks of investment services and financial instruments selected for their clients and that they assess, while taking into account cost and complexity, whether equivalent investment services or financial instruments can meet their client's profile.
10. When providing the investment service of investment advice or portfolio management, an investment firm shall not recommend or decide to trade where none of the services or instruments are suitable for the client.
11. When providing investment advice or portfolio management services that involve switching investments, either by selling an instrument and buying another or by exercising a right to make a change in regard to an existing instrument, investment firms shall collect the necessary information on the client's existing investments and the recommended new investments and shall undertake an analysis of the costs and benefits of the switch, such that they are reasonably able to demonstrate that the benefits of switching are greater than the costs.
12. When providing investment advice, investment firms shall provide a report to the retail client that includes an outline of the advice given and how the recommendation provided is suitable for the retail client, including how it meets the client's objectives and personal circumstances with reference to the investment term required, client's knowledge and experience and client's attitude to risk and capacity for loss.

Investment firms shall draw clients' attention to and shall include in the suitability report information on whether the recommended services or instruments are likely to require the retail client to seek a periodic review of their arrangements.

Where an investment firm provides a service that involves periodic suitability assessments and reports, the subsequent reports after the initial service is established may only cover changes in the services or instruments involved and/or the circumstances of the client and may not need to repeat all the details of the first report.

13. Investment firms providing a periodic suitability assessment shall review, in order to enhance the service, the suitability of the recommendations given at least annually. The frequency of this assessment shall be increased depending on the risk profile of the client and the type of financial instruments recommended.

#### *Article 55*

#### **Provisions common to the assessment of suitability or appropriateness**

*(Article 25(2) and 25(3) of Directive 2014/65/EU)*

1. Investment firms shall ensure that the information regarding a client's or potential client's knowledge and experience in the investment field includes the following, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved:

- (a) the types of service, transaction and financial instrument with which the client is familiar;
  - (b) the nature, volume, and frequency of the client's transactions in financial instruments and the period over which they have been carried out;
  - (c) the level of education, and profession or relevant former profession of the client or potential client.
2. An investment firm shall not discourage a client or potential client from providing information required for the purposes of Article 25(2) and (3) of Directive 2014/65/EU.
  3. An investment firm shall be entitled to rely on the information provided by its clients or potential clients unless it is aware or ought to be aware that the information is manifestly out of date, inaccurate or incomplete.

#### *Article 56*

#### **Assessment of appropriateness and related record-keeping obligations** *(Article 25(3) and 25(5) of Directive 2014/65/EU)*

1. Investment firms, shall determine whether that client has the necessary experience and knowledge in order to understand the risks involved in relation to the product or investment service offered or demanded when assessing whether an investment service as referred to in Article 25(3) of Directive 2014/65/EU is appropriate for a client.

An investment firm shall be entitled to assume that a professional client has the necessary experience and knowledge in order to understand the risks involved in relation to those particular investment services or transactions, or types of transaction or product, for which the client is classified as a professional client.

2. Investment firms shall maintain records of the appropriateness assessments undertaken which shall include the following:
  - (a) the result of the appropriateness assessment;
  - (b) any warning given to the client where the investment service or product purchase was assessed as potentially inappropriate for the client, whether the client asked to proceed with the transaction despite the warning and, where applicable, whether the firm accepted the client's request to proceed with the transaction;
  - (c) any warning given to the client where the client did not provide sufficient information to enable the firm to undertake an appropriateness assessment, whether the client asked to proceed with the transaction despite this warning and, where applicable, whether the firm accepted the client's request to proceed with the transaction.

#### Article 57

### **Provision of services in non-complex instruments**

*(Article 25(4) of Directive 2014/65/EU)*

A financial instrument which is not explicitly specified in Article 25(4)(a) of Directive 2014/65/EU shall be considered as non-complex for the purposes of Article 25(4)(a)(vi) of Directive 2014/65/EU if it satisfies the following criteria:

- (a) it does not fall within Article 4(1)(44)(c) of, or points (4) to (11) of Section C of Annex I to Directive 2014/65/EU;
- (b) there are frequent opportunities to dispose of, redeem, or otherwise realise that instrument at prices that are publicly available to market participants and that are either market prices or prices made available, or validated, by valuation systems independent of the issuer;
- (c) it does not involve any actual or potential liability for the client that exceeds the cost of acquiring the instrument;
- (d) it does not incorporate a clause, condition or trigger that could fundamentally alter the nature or risk of the investment or pay out profile, such as investments that incorporate a right to convert the instrument into a different investment;
- (e) it does not include any explicit or implicit exit charges that have the effect of making the investment illiquid even though there are technically frequent opportunities to dispose of, redeem or otherwise realise it;
- (f) adequately comprehensive information on its characteristics is publicly available and is likely to be readily understood so as to enable the average retail client to make an informed judgment as to whether to enter into a transaction in that instrument.

#### Article 58

### **Retail and Professional Client agreements**

*(Article 24(1) and 25(5) of Directive 2014/65/EU)*

Investment firms providing any investment service or the ancillary service referred to in Section B(1) of Annex I to Directive 2014/65/EC to a client after the date of application of this Regulation shall enter into a written basic agreement with the client, in paper or another durable medium, with the client setting out the essential rights and obligations of the firm and the client. Investment firms providing investment advice shall comply with this obligation only where a periodic assessment of the suitability of the financial instruments or services recommended is performed.

The written agreement shall set out the essential rights and obligations of the parties, and shall include the following:

- (a) a description of the services, and where relevant the nature and extent of the investment advice, to be provided;
- (b) in case of portfolio management services, the types of financial instruments that may be purchased and sold and the types of transactions that may be undertaken on behalf of the client, as well as any instruments or transactions prohibited; and

- (c) a description of the main features of any services referred to in Section B(1) of Annex I to Directive 2014/65/EC to be provided, including where applicable the role of the firm with respect to corporate actions relating to client instruments and the terms on which securities financing transactions involving client securities will generate a return for the client.

## **SECTION 4**

### **REPORTING TO CLIENTS**

#### *Article 59*

#### **Reporting obligations in respect of execution of orders other than for portfolio management** *(Article 25(6) of Directive 2014/65/EU)*

1. Investment firms having carried out an order on behalf of a client, other than for portfolio management, shall, in respect of that order:
  - (a) promptly provide the client, in a durable medium, with the essential information concerning the execution of that order;
  - (b) send a notice to the client in a durable medium confirming execution of the order as soon as possible and no later than the first business day following execution or, where the confirmation is received by the investment firm from a third party, no later than the first business day following receipt of the confirmation from the third party.

Point (b) shall not apply where the confirmation would contain the same information as a confirmation that is to be promptly dispatched to the client by another person.

Points (a) and (b) shall not apply where orders executed on behalf of clients relate to bonds funding mortgage loan agreements with the said clients, in which case the report on the transaction shall be made at the same time as the terms of the mortgage loan are communicated, but no later than one month after the execution of the order.
2. In addition to the requirements under paragraph 1, investment firms shall supply the client, on request, with information about the status of his order.
3. In the case of client orders relating to units or shares in a collective investment undertaking which are executed periodically, investment firms shall either take the action specified in point (b) of paragraph 1 or provide the client, at least once every six months, with the information listed in paragraph 4 in respect of those transactions.
4. The notice referred to in point (b) of paragraph 1 shall include such of the following information as is applicable and, where relevant, in accordance with the regulatory technical standards on reporting obligations adopted in accordance with Article 26 of Regulation (EU) No 600/2014:
  - (a) the reporting firm identification;
  - (b) the name or other designation of the client;
  - (c) the trading day;



- (d) the trading time;
- (e) the type of the order;
- (f) the venue identification;
- (g) the instrument identification;
- (h) the buy/sell indicator;
- (i) the nature of the order if other than buy/sell;
- (j) the quantity;
- (k) the unit price;
- (l) the total consideration;
- (m) a total sum of the commissions and expenses charged and, where the client so requests, an itemised breakdown including, where relevant, the amount of any mark-up or mark-down imposed where the transaction was executed by an investment firm when dealing on own account, and the investment firm owes a duty of best execution to the client;
- (n) the rate of exchange obtained where the transaction involves a conversion of currency;
- (o) the client's responsibilities in relation to the settlement of the transaction, including the time limit for payment or delivery as well as the appropriate account details where these details and responsibilities have not previously been notified to the client;
- (p) where the client's counterparty was the investment firm itself or any person in the investment firm's group or another client of the investment firm, the fact that this was the case unless the order was executed through a trading system that facilitates anonymous trading.

For the purposes of point (k), where the order is executed in tranches, the investment firm may supply the client with information about the price of each tranche or the average price. Where the average price is provided, the investment firm shall supply the client with information about the price of each tranche upon request.

5. The investment firm may provide the client with the information referred to in paragraph 4 using standard codes if it also provides an explanation of the codes used.

#### *Article 60*

#### **Reporting obligations in respect of portfolio management**

*(Article 25(6) of Directive 2014/65/EU)*

1. Investment firms which provide the service of portfolio management to clients shall provide each such client with a periodic statement in a durable medium of the portfolio

management activities carried out on behalf of that client unless such a statement is provided by another person.

2. The periodic statement required under paragraph 1 shall provide a fair and balanced review of the activities undertaken and of the performance of the portfolio during the reporting period and shall include, where relevant, the following information:
  - (a) the name of the investment firm;
  - (b) the name or other designation of the client's account;
  - (c) a statement of the contents and the valuation of the portfolio, including details of each financial instrument held, its market value, or fair value if market value is unavailable and the cash balance at the beginning and at the end of the reporting period, and the performance of the portfolio during the reporting period;
  - (d) the total amount of fees and charges incurred during the reporting period, itemising at least total management fees and total costs associated with execution, and including, where relevant, a statement that a more detailed breakdown will be provided on request;
  - (e) a comparison of performance during the period covered by the statement with the investment performance benchmark (if any) agreed between the investment firm and the client;
  - (f) the total amount of dividends, interest and other payments received during the reporting period in relation to the client's portfolio;
  - (g) information about other corporate actions giving rights in relation to financial instruments held in the portfolio;
  - (h) for each transaction executed during the period, the information referred to in Article 59(4)(c) to (l) where relevant, unless the client elects to receive information about executed transactions on a transaction-by-transaction basis, in which case paragraph 4 of this Article shall apply.
3. The periodic statement referred to in paragraph 1 shall be provided once every three months, except in the following cases:
  - (a) where the investment firm provides its clients with access to an online system, which qualifies as a durable medium, where up-to-date valuations of the client's portfolio can be accessed and where the client can easily access the information required by Article 63(2) and the firm has evidence that the client has accessed a valuation of their portfolio at least once during the relevant quarter;
  - (b) in cases where paragraph 4 applies, the periodic statement must be provided at least once every 12 months;
  - (c) where the agreement between an investment firm and a client for a portfolio management service authorises a leveraged portfolio, the periodic statement must be provided at least once a month.

The exception provided for in point (b) shall not apply in the case of transactions in financial instruments covered by Article 4(1)(44)(c) of, or any of points 4 to 11 of Section C in Annex I to Directive 2014/65/EU.

4. Investment firms, in cases where the client elects to receive information about executed transactions on a transaction-by-transaction basis, shall provide promptly to the client, on the execution of a transaction by the portfolio manager, the essential information concerning that transaction in a durable medium.

The investment firm shall send the client a notice confirming the transaction and containing the information referred to in Article 59(4) no later than the first business day following that execution or, where the confirmation is received by the investment firm from a third party, no later than the first business day following receipt of the confirmation from the third party.

The second subparagraph shall not apply where the confirmation would contain the same information as a confirmation that is to be promptly dispatched to the client by another person.

#### *Article 61*

### **Reporting obligations in respect of eligible counterparties**

*(Article 24(4) and Article 25(6) of Directive 2014/65/EU)*

The requirements applicable to reports for retail and professional clients under Articles 49 and 59 shall apply unless investment firms enter into agreements with eligible counterparties to determine content and timing of reporting.

#### *Article 62*

### **Additional reporting obligations for portfolio management or contingent liability transactions**

*(Article 25(6) of Directive 2014/65/EU)*

1. Investment firms providing the service of portfolio management shall inform the client where the overall value of the portfolio, as evaluated at the beginning of each reporting period, depreciates by 10% and thereafter at multiples of 10%, no later than the end of the business day in which the threshold is exceeded or, in a case where the threshold is exceeded on a non-business day, the close of the next business day.
2. Investment firms that hold a retail client account that includes positions in leveraged financial instruments or contingent liability transactions shall inform the client, where the initial value of each instrument depreciates by 10% and thereafter at multiples of 10%. Reporting under this paragraph should be on an instrument-by-instrument basis, unless otherwise agreed with the client, and shall take place no later than the end of the business day in which the threshold is exceeded or, in a case where the threshold is exceeded on a non-business day, the close of the next business day.

*Article 63*

**Statements of client financial instruments or client funds**

*(Article 25(6) of Directive 2014/65/EU)*

1. Investment firms that hold client financial instruments or client funds shall send at least on a quarterly basis, to each client for whom they hold financial instruments or funds, a statement in a durable medium of those financial instruments or funds unless such a statement has been provided in any other periodic statement. Upon client request, firms shall provide such statement more frequently at a commercial cost.

The first subparagraph shall not apply to a credit institution authorised under Directive 2000/12/EC in respect of deposits within the meaning of that Directive held by that institution.

2. The statement of client assets referred to in paragraph 1 shall include the following information:
  - (a) details of all the financial instruments or funds held by the investment firm for the client at the end of the period covered by the statement;
  - (b) the extent to which any client financial instruments or client funds have been the subject of securities financing transactions;
  - (c) the extent of any benefit that has accrued to the client by virtue of participation in any securities financing transactions, and the basis on which that benefit has accrued;
  - (d) a clear indication of the assets or funds which are subject to the rules of Directive 2014/65/EU and its implementing measures and those that are not, such as those that are subject to Title Transfer Collateral Agreement;
  - (e) a clear indication of which assets are affected by some peculiarities in their ownership status, for instance due to a security interest;
  - (f) the market or estimated value, when the market value is not available, of the financial instruments included in the statement with a clear indication of the fact that the absence of a market price is likely to be indicative of a lack of liquidity. The evaluation of the estimated value shall be performed by the firm on a best effort basis.

In cases where the portfolio of a client includes the proceeds of one or more unsettled transactions, the information referred to in point (a) may be based either on the trade date or the settlement date, provided that the same basis is applied consistently to all such information in the statement.

The periodic statement of client assets referred to in paragraph 1 shall not be provided where the investment firm provides its clients with access to an online system, which qualifies as a durable medium, where up-to-date statements of client's financial instruments or funds can be easily accessed by the client and the firm has evidence that the client has accessed this statement at least once during the relevant quarter.

3. Investment firms which hold financial instruments or funds and which carry out the service of portfolio management for a client may include the statement of client assets referred to in paragraph 1 in the periodic statement it provides to that client pursuant to Article 60(1).

## **SECTION 5**

### **BEST EXECUTION**

#### *Article 64*

#### **Best execution criteria**

*(Articles 27(1) and 24(1) of Directive 2014/65/EU)*

1. When executing client orders, investment firms shall take into account the following criteria for determining the relative importance of the factors referred to in Article 27(1) of Directive 2014/65/EU:
  - (a) the characteristics of the client including the categorisation of the client as retail or professional;
  - (b) the characteristics of the client order, including where the order involves a securities financing transaction (SFT);
  - (c) the characteristics of financial instruments that are the subject of that order;
  - (d) the characteristics of the execution venues to which that order can be directed.

For the purposes of this Article and Articles 65 and 66, ‘execution venue’ includes a regulated market, an MTF, an OTF, a systematic internaliser, or a market maker or other liquidity provider or an entity that performs a similar function in a third country to the functions performed by any of the foregoing.

2. An investment firm satisfies its obligation under Article 27(1) of Directive 2014/65/EU to take all sufficient steps to obtain the best possible result for a client to the extent that it executes an order or a specific aspect of an order following specific instructions from the client relating to the order or the specific aspect of the order.
3. Investment firms shall not structure or charge their commissions in such a way as to discriminate unfairly between execution venues.
4. When executing orders or taking decision to deal in OTC products including bespoke products, the investment firm shall check the fairness of the price proposed to the client, by gathering market data used in the estimation of the price of such product and, where possible, by comparing with similar or comparable products.

**Duty of investment firms carrying out portfolio management and reception and transmission of orders to act in the best interests of the client**  
(Article 24(1) and 24(4) of Directive 2014/65/EU)

1. Investment firms, when providing portfolio management, shall comply with the obligation under Article 24(1) of Directive 2014/65/EU to act in accordance with the best interests of their clients when placing orders with other entities for execution that result from decisions by the investment firm to deal in financial instruments on behalf of its client.
2. Investment firms, when providing the service of reception and transmission of orders, shall comply with the obligation under Article 24(1) of Directive 2014/65/EU to act in accordance with the best interests of their clients when transmitting client orders to other entities for execution.
3. In order to comply with paragraphs 1 or 2, investment firms shall comply with paragraphs 4 to 7 of this Article and Article 64(4).
4. Investment firms shall take all sufficient steps to obtain the best possible result for their clients taking into account the factors referred to in Article 27(1) of Directive 2014/65/EU. The relative importance of these factors shall be determined by reference to the criteria set out in Article 59(1) and, for retail clients, to the requirement under Article 27(1) of Directive 2014/65/EU.

An investment firm satisfies its obligations under paragraph 1 or 2, and is not required to take the steps mentioned in this paragraph, to the extent that it follows specific instructions from its client when placing an order with, or transmitting an order to, another entity for execution.

5. Investment firms shall establish and implement a policy that enables them to comply with the obligation in paragraph 4. The policy shall identify, in respect of each class of instruments, the entities with which the orders are placed or to which the investment firm transmits orders for execution. The entities identified shall have execution arrangements that enable the investment firm to comply with its obligations under this Article when it places or transmits orders to that entity for execution.
6. Investment firms shall provide information to their clients on the policy established in accordance with paragraph 5 and paragraphs 2 to 9 of Article 66. Investment firms shall provide clients with appropriate information about the firm and its services and the entities chosen for execution. In particular, when the investment firm select other firms to provide order execution services, it shall summarise and make public, on an annual basis, for each class of financial instruments, the top five investment firms in terms of trading volumes where it transmitted or placed client orders for execution in the preceding year and information on the quality of execution obtained. The information shall be consistent with the information published in accordance with the technical standards developed under Article 27(10)(b) of Directive 2014/65/EU.

Upon reasonable request from a client, investment firms shall provide its clients or potential clients with information about entities where the orders are transmitted or placed for execution.

7. Investment firms shall monitor on a regular basis the effectiveness of the policy established in accordance with paragraph 5 and, in particular, shall monitor the execution quality of the entities identified in that policy and, where appropriate, correct any deficiencies.

Investment firms shall review the policy and arrangements at least annually. Such a review shall also be carried out whenever a material change occurs that affects the firm's ability to continue to obtain the best possible result for their clients.

Investment firms shall assess whether a material change has occurred and shall consider making changes to the execution venues or entities on which they place significant reliance in meeting the overarching best execution requirement.

A material change shall be a significant event that could impact parameters of best execution such as cost, price, speed, likelihood of execution and settlement, size, nature or any other consideration relevant to the execution of the order.

8. This Article shall not apply where the investment firm that provides the service of portfolio management or reception and transmission of orders also executes the orders received or the decisions to deal on behalf of its client's portfolio. In those cases Article 27 of Directive 2014/65/EU shall apply.

#### *Article 66*

#### **Execution policy**

*(Article 27 (5) and (7) of Directive 2014/65/EU)*

1. Investment firms shall review, at least on an annual basis execution policy established pursuant to Article 27(4) of Directive 2014/65/EU, as well as their order execution arrangements.

Such a review shall also be carried out whenever a material change as defined in Article 65(7) occurs that affects the firm's ability to continue to obtain the best possible result for the execution of its client orders on a consistent basis using the venues included in its execution policy. An investment firm shall assess whether a material change has occurred and shall consider making changes to the relative importance of the best execution factors in meeting the overarching best execution requirement.

2. The information on the execution policy shall be customised depending on the class of financial instrument and type of the service provided and shall include information set out in paragraphs 3 to 9.
3. Investment firms shall provide clients with the following details on their execution policy in good time prior to the provision of the service:
- (a) an account of the relative importance the investment firm assigns, in accordance with the criteria specified in Article 59(1), to the factors referred to in Article 27(1) of Directive 2014/65/EU, or the process by which the firm determines the relative importance of those factors.
  - (b) a list of the execution venues on which the firm places significant reliance in meeting its obligation to take all reasonable steps to obtain on a consistent basis the best possible result for the execution of client orders and specifying which execution

venues are used for each class of financial instruments, for retail client orders, professional client orders and SFTs;

- (c) a list of factors used to select an execution venue, including qualitative factors such as clearing schemes, circuit breakers, scheduled actions, or any other relevant consideration, and the relative importance of each factor; The information about the factors used to select an execution venue for execution shall be consistent with the controls used by the firm to demonstrate to clients that best execution has been achieved in a consistent basis when reviewing the adequacy of its policy and arrangements;
- (d) how the execution factors of price costs, speed, likelihood of execution and any other relevant factors are considered as part of all sufficient steps to obtain the best possible result for the client;
- (e) where applicable, information that the firm executes orders outside a trading venue, the consequences, for example counterparty risk arising from execution outside a trading venue, and upon client request, additional information about the consequences of this means of execution;
- (f) a clear and prominent warning that any specific instructions from a client may prevent the firm from taking the steps that it has designed and implemented in its execution policy to obtain the best possible result for the execution of those orders in respect of the elements covered by those instructions;
- (g) a summary of the selection process for execution venues, execution strategies employed, the procedures and process used to analyse the quality of execution obtained and how the firms monitor and verify that the best possible results were obtained for clients.

That information shall be provided in a durable medium, or by means of a website (where that does not constitute a durable medium) provided that the conditions specified in Article 3(2) are satisfied.

- 4. Where investment firms apply different fees depending on the execution venue, the firm shall explain these differences in sufficient detail in order to allow the client to understand the advantages and the disadvantages of the choice of a single execution venue.
- 5. Where investment firms invite clients to choose an execution venue, fair, clear and not misleading information shall be provided to prevent the client from choosing one execution venue rather than another on the sole basis of the price policy applied by the firm.
- 6. Investment firms shall only receive third-party payments that comply with Article 24(9) of Directive 2014/65/EU and shall inform clients about the inducements that the firm may receive from the execution venues. The information shall specify the fees charged by the investment firm to all counterparties involved in the transaction, and where the fees vary depending on the client, the information shall indicate the maximum fees or range of the fees that may be payable.
- 7. Where an investment firm charges more than one participant in a transaction, in compliance with Article 24(9) of Directive 2014/65/EC and its implementing measures, the



firm shall inform its clients of the value of any monetary or non-monetary benefits received by the firm.

8. Where a client makes reasonable and proportionate requests for information about its policies or arrangements and how they are reviewed to an investment firm, that investment firm shall answer clearly and within a reasonable time.
9. Where an investment firm executes orders for retail clients, it shall provide those clients with a summary of the relevant policy, focused on the total costs they incur. The summary shall also provide a link to the most recent execution quality data published in accordance with Article 27(3) of Directive 2014/65/EC for each execution venue listed by the investment firm in its execution policy.

## **SECTION 6**

### **CLIENT ORDER HANDLING**

#### *Article 67*

#### **General principles**

*(Articles 28(1) and 24(1) of Directive 2014/65/EU)*

1. Investment firms shall satisfy the following conditions when carrying out client orders:
  - (a) ensure that orders executed on behalf of clients are promptly and accurately recorded and allocated;
  - (b) carry out otherwise comparable client orders sequentially and promptly unless the characteristics of the order or prevailing market conditions make this impracticable, or the interests of the client require otherwise;
  - (c) inform a retail client about any material difficulty relevant to the proper carrying out of orders promptly upon becoming aware of the difficulty.
2. Where an investment firm is responsible for overseeing or arranging the settlement of an executed order, it shall take all reasonable steps to ensure that any client financial instruments or client funds received in settlement of that executed order are promptly and correctly delivered to the account of the appropriate client.
3. An investment firm shall not misuse information relating to pending client orders, and shall take all reasonable steps to prevent the misuse of such information by any of its relevant persons.

#### *Article 68*

#### **Aggregation and allocation of orders**

*(Articles 28(1) and 24(1) of Directive 2014/65/EU)*

1. Investment firms shall not carry out a client order or a transaction for own account in aggregation with another client order unless the following conditions are met:

- (a) it is unlikely that the aggregation of orders and transactions will work overall to the disadvantage of any client whose order is to be aggregated;
  - (b) it is disclosed to each client whose order is to be aggregated that the effect of aggregation may work to its disadvantage in relation to a particular order;
  - (c) an order allocation policy is established and effectively implemented, providing for the fair allocation of aggregated orders and transactions, including how the volume and price of orders determines allocations and the treatment of partial executions.
2. Where an investment firm aggregates an order with one or more other client orders and the aggregated order is partially executed, it shall allocate the related trades in accordance with its order allocation policy.

#### *Article 69*

### **Aggregation and allocation of transactions for own account**

*(Articles 28(1) and 24(1) of Directive 2014/65/EU)*

1. Investment firms which have aggregated transactions for own account with one or more client orders shall not allocate the related trades in a way that is detrimental to a client.
2. Where an investment firm aggregates a client order with a transaction for own account and the aggregated order is partially executed, it shall allocate the related trades to the client in priority to the firm.

Where an investment firm is able to demonstrate on reasonable grounds that without the combination it would not have been able to carry out the order on such advantageous terms, or at all, it may allocate the transaction for own account proportionally, in accordance with its order allocation policy referred to in Article 68(1)(c).

3. As part of the order allocation policy referred to in Article 68(1)(c), investment firms shall put in place procedures designed to prevent the reallocation, in a way that is detrimental to the client, of transactions for own account which are executed in combination with client orders.

#### *Article 70*

### **Prompt fair and expeditious execution of client orders and publication of unexecuted client limit orders for shares traded on a trading venue**

*(Article 28 of Directive 2014/65/EU)*

1. A client limit order in respect of shares admitted to trading on a regulated market or traded on a trading venue which have not been immediately executed under prevailing market conditions as referred to in Article 28(2) of Directive 2014/65/EU shall be considered available to the public when the investment firm has submitted the order for execution to a regulated market or a MTF or the order has been published by a data reporting services provider located in one Member State and can be easily executed as soon as market conditions allow.
2. Regulated markets and MTFs shall be prioritised according to the firm's execution policy to ensure execution as soon as market conditions allow.

## SECTION 7 ELIGIBLE COUNTERPARTIES

### *Article 71*

#### **Eligible counterparties**

*(Article 30 of Directive 2014/65/EU)*

1. In addition to the categories which are explicitly set out in Article 30(2) of Directive 2014/65/EU, Member States may recognise as eligible counterparty, in accordance with Article 30(3) of that Directive, an undertaking falling within a category of clients who are to be considered professional clients in accordance with paragraphs 1, 2 and 3 of Section I of Annex II to that Directive.
2. Where, pursuant to the second subparagraph of Article 30 (2) of Directive 2014/65/EC, an eligible counterparty requests treatment as a client whose business with an investment firm is subject to Articles 24, 25, 27 and 28 of that Directive, the request should be made in writing, and shall indicate whether the treatment as retail client or professional client refers to one or more investment services or transactions, or one or more types of transaction or product.
3. Where an eligible counterparty requests treatment as a client whose business with an investment firm is subject to Articles 24, 25, 27 and 28 of Directive 2014/65/EC, but does not expressly request treatment as a retail client , the firm shall treat that eligible counterparty as a professional client.
4. Where the eligible counterparty expressly requests treatment as a retail client, the investment firm shall treat the eligible counterparty as a retail client, applying the provisions in respect of requests of non-professional treatment specified in the second, third and fourth sub-paragraphs of Section I of Annex II to Directive 2014/65/EC.
5. Where a client requests to be treated as an eligible counterparty, in accordance with Article 30(3) of Directive 2014/65/EU, the following procedure shall be followed:
  - (a) the investment firm shall provide the client with a clear written warning of the consequences for the client of such a request, including the protections they may lose;
  - (b) the client shall confirm in writing the request to be treated as an eligible counterparty either generally or in respect of one or more investment services or a transaction or type of transaction or product and that they are aware of the consequences of the protection they may lose as a result of the request.

## SECTION 8 RECORD-KEEPING

### *Article 72*

#### **Retention of records**

*(Article 16(6) of Directive 2014/65/EU)*

1. The records shall be retained in a medium that allows the storage of information in a way accessible for future reference by the competent authority, and in such a form and manner that the following conditions are met:
  - (a) the competent authority is able to access them readily and to reconstitute each key stage of the processing of each transaction;
  - (b) it is possible for any corrections or other amendments, and the contents of the records prior to such corrections or amendments, to be easily ascertained;
  - (c) it is not possible for the records otherwise to be manipulated or altered;
  - (d) it allows IT or any other efficient exploitation when the analysis of the data cannot be easily carried out due to the volume and the nature of the data; and
  - (e) the firm's arrangements comply with the record keeping requirements irrespective of the technology used.
2. Investment firms shall keep at least the records identified in Annex I to this Regulation depending upon the nature of their activities.

The list of records identified in Annex I to this Regulation is without prejudice to any other record-keeping obligations arising from other legislation.

3. Investment firms shall also keep records of any policies and procedures they are required to maintain pursuant to Directive 2014/65/EU, Regulation (EU) No 600/2014, Directive 2014/57/EU and Regulation (EU) No 596/2014 and their respective implementing measures in writing.

Competent authorities may require investment firms to keep additional records to the list identified in Annex I to this Regulation.

### *Article 73*

#### **Record keeping of rights and obligations of the investment firm and the client**

*(Article 25(5) of Directive 2014/65/EU)*

Records which set out the respective rights and obligations of the investment firm and the client under an agreement to provide services, or the terms on which the firm provides services to the client, shall be retained for at least the duration of the relationship with the client.

#### *Article 74*

### **Record keeping of client orders and decision to deal**

*(Article 16(6) of Directive 2014/65/EU)*

An investment firm shall, in relation to every initial order received from a client and in relation to every initial decision to deal taken, immediately record and keep at the disposal of the competent authority at least the details set out in Section 1 of Annex IV to this Regulation to the extent they are applicable to the order or decision to deal in question.

Where the details set out in Section 1 of Annex IV to this Regulation are also prescribed under Articles 25 and 26 of Regulation No (EU) 600/2014, these details should be maintained in a consistent way and according to the same standards prescribed under Articles 25 and 26 of Regulation No (EU) 600/2014.

#### *Article 75*

### **Record keeping of transactions and order processing**

*(Article 16(6) of Directive 2014/65/EU)*

Investment firms shall, immediately after receiving a client order or making a decision to deal to the extent they are applicable to the order or decision to deal in question, record and keep at the disposal of the competent authority at least the details set out in Section 2 of Annex IV.

Where the details set out in Section 2 of Annex IV are also prescribed under Articles 25 and 26 of Regulation No (EU) 600/2014, they shall be maintained in a consistent way and according to the same standards prescribed under Articles 25 and 26 of Regulation (EU) No 600/2014.

#### *Article 76*

### **Recording of telephone conversations or electronic communications**

*(Article 16(7) of Directive 2014/65/EU)*

1. Investment firms shall establish, implement and maintain an effective recording of telephone conversations and electronic communications policy, set out in writing, and appropriate to the size and organisation of the firm, and the nature, scale and complexity of its business. The policy shall include the following content:
  - (a) the identification of the telephone conversations and electronic communications, including relevant internal telephone conversations and electronic communications, that are subject to the recording requirements in accordance with Article 16(7) of Directive 2014/65/EU; and
  - (b) the specification of the procedures to be followed and measures to be adopted to ensure the firm's compliance with the third and eighth subparagraphs of Article 16(7) of Directive 2014/65/EU where exceptional circumstances arise and the firm is unable to record the conversation/communication on devices issued, accepted or permitted by the firm. Evidence of such circumstances shall be retained and shall be accessible to competent authorities.
2. Investment firms shall ensure that the management body has effective oversight and control over the policies and procedures relating to the firm's recording of telephone conversations and electronic communications.
3. Investment firms shall ensure that the arrangements to comply with recording requirements are technology-neutral. Firms shall periodically evaluate the effectiveness of the firm's policies and procedures and adopt any such alternative or additional measures and

procedures as are necessary and appropriate. At a minimum, such adoption of alternative or additional measures shall occur when a new medium of communication is accepted or permitted for use by the firm.

4. Investment firms shall keep and regularly update a record of those individuals who have firm devices or privately owned devices that have been approved for use by the firm.
5. Investment firms shall educate and train employees in procedures governing the requirements in Article 16(7) of Directive 2014/65/EU.
6. To monitor compliance with the recording and record-keeping requirements in accordance with Article 16(7) of Directive 2014/65/EU, investment firms shall periodically monitor the records of transactions and orders subject to these requirements, including relevant conversations. Such monitoring shall be risk based and proportionate.
7. Investment firms shall demonstrate the policies, procedures and management oversight of the recording rules to the relevant competent authorities upon request.
8. Before investment firms provide investment services and activities relating to the reception, transmission and execution of orders to new and existing clients, firms shall inform the client of the following:
  - (a) that the conversations and communications are being recorded; and
  - (b) that a copy of the recording of such conversations with the client and communications with the client will be available on request for a period of five years and, where requested by the competent authority, for a period of up to seven years.

The information referred to in the first sub-paragraph shall be presented in the same language(s) as that used to provide investment services to clients.

9. Investment firms shall record in a durable medium all relevant information related to relevant face-to-face conversations with clients. The information recorded shall include at least the following:
  - (a) date and time of meetings;
  - (b) location of meetings;
  - (c) identity of the attendees;
  - (d) initiator of the meetings; and
  - (e) relevant information about the client order including the price, volume, type of order and when it shall be transmitted or executed.
10. Records shall be stored in a durable medium, which allows them to be replayed or copied and must be retained in a format that does not allow the original record to be altered or deleted.

Records shall be stored in a medium so that they are readily accessible and available to clients on request.

Firms shall ensure the quality, accuracy and completeness of the records of all telephone recordings and electronic communications.

11. The period of time for the retention of a record shall begin on the date when the record is created.

## **SECTION 9**

### **SME GROWTH MARKETS**

#### *Article 77*

#### **Qualification as an SME**

*(Article 4(1)(13) of Directive 2014/65/EU)*

1. An issuer whose shares have been admitted to trading for less than three years shall be deemed an SME for the purpose of point (a) of Article 33(3) of Directive 2014/65/EU where its market capitalisation is below EUR 200 million based on any of the following:
  - (a) the closing share price of the first day of trading, if its shares have been admitted to trading for less than one year;
  - (b) the last closing share price of the first year of trading, if its financial instruments have been admitted to trading for more than one year but less than two years;
  - (c) the average of the last closing share prices of each of the first two years of trading, if its financial instruments have been admitted to trading for more than two years but less than three years.
2. An issuer which has no equity instrument traded on any trading venue shall be deemed an SME for the purpose of Article 4(1)(13) of Directive 2014/65/EU if, according to its last annual or consolidated accounts, it meets at least two of the following three criteria: an average number of employees during the financial year of less than 250, a total balance sheet not exceeding EUR 43 000 000 and an annual net turnover not exceeding EUR 50 000 000.

#### *Article 78*

#### **Registration as an SME growth market**

*(Article 33(3) of Directive 2014/65/EU)*

1. When determining whether at least 50% of the issuers admitted to trading on an MTF are SMEs for the purposes of registration as an SME growth market in accordance with point (a) of Article 33(3) of Directive 2014/65/EU, the competent authority of the home Member State of the operator of an MTF shall calculate the average ratio of SMEs over the total number of issuers whose financial instruments are admitted to trading on that market. The average ratio shall be calculated on 31 December of the previous calendar year as the average of the twelve end-of-month ratios of that calendar year.

Without prejudice to the other conditions for registration specified in points (b) to (g) of Article 33(3) of Directive 2014/65/EU, the competent authority shall register as an SME growth market an applicant with no previous operating history and, after three calendar

years have elapsed, shall verify that it complies with the minimum proportion of SMEs, as determined in accordance with the first subparagraph.

2. With regard to the criteria laid out in points (b), (c), (d) and (f) of Article 33(3) of Directive 2014/65/EU, the competent authority of the home Member State of the operator of an MTF shall not register the MTF as an SME growth market unless it is satisfied that the MTF:
- (a) has established and applies rules providing for objective and transparent criteria for the initial and ongoing admission to trading of issuers on its venue;
  - (b) has an operating model which is appropriate for the performance of its functions and ensures the maintenance of fair and orderly trading in the financial instruments admitted to trading on its venue;
  - (c) has established and applies rules that require an issuer seeking admission of its financial instruments to trading on the MTF, to publish, in cases where Directive 2003/71/EC does not apply, an appropriate admission document, drawn up under the responsibility of the issuer and clearly stating whether or not it has been approved or reviewed and by whom;
  - (d) has established and applies rules that define the minimum content of the admission document referred to under point (c), in such a way that sufficient information is provided to investors to enable them to make an informed assessment of the financial position and prospects of the issuer, and the rights attaching to its securities;
  - (e) requires the issuer to state, in the admission document referred to under point (c), whether or not, in its opinion, its working capital is sufficient for its present requirements or, if not, how it proposes to provide the additional working capital needed;
  - (f) has made arrangements for the admission document referred to under point (c) to be subject to an appropriate review of its completeness, consistency and comprehensibility;
  - (g) requires the issuers whose securities are traded on its venue to publish annual financial reports within 6 months after the end of each financial year, half yearly financial reports within 4 months after the end of the first 6 months of each financial year;
  - (h) ensures dissemination to the public of prospectuses drawn up in accordance with Directive 2003/71/EC, admission documents referred to under point (c), financial reports referred to under point (g) and information defined in Article 7(1) of Regulation (EU) No 596/2014 publicly disclosed by the issuers whose securities are traded on its venue, by publishing them on its website, or providing thereon a direct link to the page of the website of the issuers where such documents, reports and information are published;
  - (i) ensures that the regulatory information referred to under point (h) and direct links remain available on its website for a period of at least five years.



*Article 79*

**Deregistration as an SME growth market**

*(Article 33(3) of Directive 2014/65/EU)*

1. With regard to the proportion of SMEs, and without prejudice to the other conditions specified in points (b) to (g) of Article 33(3) of Directive 2014/65/EU and in Article 78(2) of this Regulation, an SME growth market shall only be deregistered by the competent authority of its home Member State where the proportion of SMEs, as determined in accordance with the first subparagraph of Article 78(1) of this Regulation, falls below 50% for three consecutive calendar years.
2. With regard to the conditions specified in points (b) to (g) of Article 33(3) of Directive 2014/65/EU and in Article 78(2) of this Regulation, the operator of an SME growth market shall be deregistered by the competent authority of its home Member State where such conditions are no longer satisfied.

## **CHAPTER IV OPERATING OBLIGATIONS FOR TRADING VENUES**

*Article 80*

**Circumstances constituting significant damage to investors' interests and the orderly functioning of the market**

*(Articles 32(1), 32(2), 52(1) and 52(2) of Directive 2014/65/EU)*

1. For the purpose of Articles 32(1), 32(2), 52(1) and 52(2) of Directive 2014/65/EU, a suspension or a removal from trading of a financial instrument shall be deemed likely to cause significant damage to investors' interests or the orderly functioning of the market at least in the following circumstances:
  - (a) where it would create a systemic risk undermining financial stability, such as where the need exists to unwind a dominant market position, or where settlement obligations would not be met in a significant volume;
  - (b) where the continuation of trading on the market is necessary to perform critical post-trade risk management functions when there is a need for the liquidation of financial instruments due to the default of a clearing member under the default procedures of a CCP and a CCP would be exposed to unacceptable risks as a result of an inability to calculate margin requirements;
  - (c) where the financial viability of the issuer would be threatened, such as where it is involved in a corporate transaction or capital raising.
2. For the purpose of determining whether a suspension or a removal is likely to cause significant damage to the investors' interest or the orderly functioning of the markets in any particular case, the national competent authority, an investment firm or a market operator operating an MTF or an OTF shall consider all relevant factors, including:
  - (a) the relevance of the market in terms of liquidity where the consequences of the actions are likely to be more significant where those markets are more relevant in terms of liquidity than in other markets;

- (b) the nature of the envisaged action where actions with a sustained or lasting impact on the ability of investors to trade a financial instrument on trading venues, such as removals, are likely to have a greater impact on investors than other actions;
  - (c) the knock-on effects of a suspension or removal of sufficiently related derivatives, indices or benchmarks for which the removed or suspended instrument serves as an underlying or constituent;
  - (d) the effects of a suspension on the interests of market end users who are not financial counterparties, such as entities trading in financial instruments to hedge commercial risks.
3. The factors set out in paragraph 3 shall also be taken into consideration where a national competent authority, an investment firm or a market operator operating an MTF or an OTF decides not to suspend or remove a financial instrument on the basis of circumstances not covered by the list of paragraph 1.

#### *Article 81*

#### ***Circumstances where significant infringements of the rules of a trading venue or disorderly trading conditions or system disruptions in relation to a financial instrument may be assumed*** *(Articles 31(2) and 54(2) of Directive 2014/65/EU)*

1. When assessing whether the requirement to immediately inform their competent authorities of significant infringements of the rules of their trading venue or disorderly trading conditions or system disruptions in relation to a financial instrument applies, operators of trading venues shall consider the signals listed in Section A of Annex III to this Regulation.
2. Information shall only be required in cases of significant events which have the potential to jeopardise the role and function of trading venues as part of the financial market infrastructure.

#### *Article 82*

#### ***Circumstances where a conduct indicating behaviour that is prohibited under Regulation (EU) No 596/2014 may be assumed*** *(Articles 31(2) and 54(2) of Directive 2014/65/EU)*

1. When assessing whether the requirement to immediately inform their competent authorities of conduct that may indicate behaviour that is prohibited under Regulation (EU) No 596/2014 applies, operators of trading venues shall consider the signals listed in Section B of Annex III to this Regulation.
2. The operator of one or several trading venues where a financial instrument and/or related financial instrument are traded shall apply a proportionate approach and shall exercise judgment on the signals triggered, including any relevant signals not specifically included in Section B of Annex III to this Regulation, before informing the relevant national competent authority, taking into account the following:
  - (a) the deviations from the usual trading pattern of the financial instruments admitted to trading or traded on its trading venue; and

- (b) the information available or accessible to the operator, whether that be internally as part of the operations of the trading venue or publicly available.
3. The operator of one or several trading venues shall take into account front running behaviours, which consist in a market member or participant trading, for its own account, ahead of its client, and shall use for that purpose the order book data required to be recorded by the trading venue pursuant to Article 25 of Regulation (EU) No 600/2014, in particular those relating to the way the member or participant conducts its trading activity.

## **CHAPTER V**

### **POSITION REPORTING IN COMMODITY DERIVATIVES**

#### *Article 83*

#### **Position reporting**

*(Article 58 (1) of Directive 2014/65/EU)*

1. For the purpose of the weekly reports referred to in Art 58(1)(a) of Directive 2014/65/EU, the obligation for a trading venue to make public such a report shall apply when both of the following two thresholds are met:
- (a) 20 open position holders exist in a given contract on a given trading venue; and
  - (b) the absolute amount of the gross long or short volume of total open interest, expressed in the number of lots of the relevant commodity derivative, exceeds a level of four times the deliverable supply in the same commodity derivative, expressed in number of lots.

Where the commodity derivative does not have a physically deliverable underlying asset and for emission allowances and derivatives thereof, point (b) shall not apply.

2. The threshold set out in point (a) of paragraph 1 shall apply in aggregate on the basis of all of the categories of persons regardless of the numbers of position holders in any single category of persons.
3. For contracts where there are less than five position holders active in a given category of persons, the number of position holders in that category shall not be published.
4. For contracts that meet the conditions set out in points (a) and (b) of paragraph 1 for the first time, trading venues shall publish the contracts first weekly report as soon as it is feasibly practical, and in any event no later than 3 weeks from the date on which the thresholds are first triggered.
5. Where the conditions set out in points (a) and (b) of paragraph 1 are no longer met, trading venues shall continue to publish the weekly reports for a period of three months. The obligation to publish the weekly report no longer applies where the conditions set out in points (a) and (b) of paragraph 1 have not been met continuously upon expiry of that period.

# CHAPTER VI

## DATA PROVISION OBLIGATIONS FOR DATA REPORTING SERVICE PROVIDERS

### *Article 84*

#### **Obligation to provide market data on a reasonable commercial basis**

*(Article 64(1) and 65(1) of Directive 2014/65/EU)*

1. For the purposes of making market data containing the information set out in Articles 6, 20 and 21 of Regulation (EU) No 600/2014 available to the public on a reasonable commercial basis in accordance with Articles 64(1) and 65(1) of Directive 2014/65/EU, approved publication arrangements (APAs) and consolidated tape providers (CTPs) shall comply with the obligations set out in Articles 85 to 89.
2. Articles 85, 86(2), 87, 88(2) and 89 shall not apply to APAs or CTPs that make market data available to the public free of charge.

### *Article 85*

#### **Provision of market data on the basis of cost**

*(Article 64(1) and 65(1) of Directive 2014/65/EU)*

1. The price of market data shall be based on the cost of producing and disseminating such data and may include a reasonable margin.
2. The costs of producing and disseminating market data may include an appropriate share of joint costs for other service provided by APAs and CTPs.

### *Article 86*

#### **Obligation to provide market data on a non-discriminatory basis**

*(Article 64(1) and 65(1) of Directive 2014/65/EU)*

1. APAs and CTPs shall make market data available at the same price and on the same terms and conditions to all customers falling within the same category in accordance with published objective criteria.
2. Any differentials in prices charged to different categories of customers shall be proportionate to the value which the market data represent to those customers, taking into account:
  - (a) the scope and scale of the market data including the number of financial instruments covered and trading volume;
  - (b) the use made by the customer of the market data, including whether it is used for the customer's own trading activities, for resale or for data aggregation.
3. For the purposes of paragraph 1, APAs and CTPs shall have scalable capacities in place to ensure that customers can obtain timely access to market data at all times on a non-discriminatory basis.

*Article 87*

**Per user fees**

*(Article 64(1) and 65(1) of Directive 2014/65/EU)*

1. APAs and CTPs shall charge for the use of market data on the basis of the use made by individual end-users of the market data ('per user basis'). APAs and CTPs shall have arrangements in place to ensure that each individual use of market data is charged only once.
2. By way of derogation from paragraph 1, APAs and CTPs may decide not to make market data available on a per user basis where to charge on a per user basis is disproportionate to the cost of making market data available, having regard to the scale and scope of the market data.
3. APAs or CTPs shall provide grounds for the refusal to make market data available on a per user basis and shall publish those grounds on their webpage.

*Article 88*

**Unbundling and disaggregating market data**

*(Article 64(1) and 65(1) of Directive 2014/65/EU)*

1. APAs and CTPs shall make market data available without being bundled with other services.
2. Prices for market data shall be charged on the basis of the level of market data disaggregation provided for in Article 12(1) of Regulation (EU) No 600/2014 as further specified in Articles [Delegated regulation reference to RTS on data disaggregation].

*Article 89*

**Transparency obligation**

*(Article 64(1) and 65(1) of Directive 2014/65/EU)*

1. APAs and CTPs shall disclose and make easily available to the public the price and other terms and conditions for the provision of the market data in a manner which is easily accessible.
2. The disclosure shall include the following:
  - (a) current price lists, including the following information:
    - (i) fees per display user;
    - (ii) non-display fees;
    - (iii) discount policies;
    - (iv) fees associated with licence conditions;
    - (v) fees for pre-trade and for post-trade market data;

- (vi) fees for other subsets of information, including those required in accordance with the regulatory technical standards pursuant to Article 12(2) of Regulation (EU) No 600/2014;
- (vii) other contractual terms and conditions;
- (b) advance disclosure with a minimum of 90 days' notice of future price changes;
- (c) information on the content of the market data including the following information:
  - (i) the number of instruments covered;
  - (ii) the total turnover of instruments covered;
  - (iii) pre-trade and post-trade market data ratio;
  - (iv) information on any data provided in addition to market data;
  - (v) the date of the last licence fee adaption for market data provided;
- (d) revenue obtained from making market data available and the proportion of that revenue compared to total revenue of the APA or CTP;
- (e) information on how the price was set, including the cost accounting methodologies used and information about the specific principles according to which direct and variable joint costs are allocated and fixed joint costs are apportioned, between the production and dissemination of market data and other services provided by APAs and CTPs.

## **CHAPTER VII**

### **COMPETENT AUTHORITIES AND FINAL PROVISIONS**

#### *Article 90*

#### **Determination of the substantial importance of the operations of a trading venue in a host Member State**

*(Article 79(2) of Directive 2014/65/EU)*

1. The operations of a regulated market in a host Member State shall be considered to be of substantial importance for the functioning of the securities markets and the protection of investors in that host Member State where at least one of the following criteria is met:
  - (a) the host Member State has formerly been the home Member State of the regulated market in question;
  - (b) the regulated market in question has acquired through merger, takeover, or any other form of transfer of the whole or part of the business of a regulated market which was previously operated by a market operator which had its registered office or head office in the host Member State.

2. The operations of an MTF or OTF in a host Member State shall be considered to be of substantial importance for the functioning of the securities markets and the protection of investors in that host Member State where at least one of the criteria laid down in paragraph 1 is met in regard to that MTF or OTF and at least one of the following additional criteria is met:
- (a) before one of the situations set out in paragraph 1 occurred in regard to the MTF or OTF, the trading venue had a market share of at least 10% of trading in terms of total turnover in monetary terms in on-venue trading and systematic internaliser trading in the host Member State in at least one asset class subject to the transparency obligations of Regulation (EU) No 600/2014;
  - (b) the MTF or OTF is registered as an SME growth market.

## **CHAPTER VIII FINAL PROVISIONS**

### *Article 91*

#### **Entry into force and application**

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

It shall apply from the date that appears first in the second subparagraph of Article 93(1) of Directive 65/2014/EU.

### *Article 92*

#### **Addressees**

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 25.4.2016

*For the Commission  
The President  
Jean-Claude JUNCKER*