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Additional Information

Level 1 Regulation

Markets in Financial Instruments Directive II (MiFID II) Directive 2014/65/EU- Secondary Markets

Topic

Multilateral and bilateral systems

Subject Matter

Multilateral and bilateral systems - Systematic internalisers - “risk-facing activity”

Question

How does the concept of “risk-facing activity” apply to an EU branch of a third-country firm that operates as an SI in the EU?

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Original language

[ESMA 70-872942901-38 MiFID II MiFIR market structures Q&A, Q&A 5.31]

As clarified in Q&As above, ESMA is of the view that based on the SI definition provided in Article 4(1)(20) of MiFID II, the trading activity of a SI is characterised by risk-facing transactions that impact the Profit and Loss of the SI.

ESMA considers that the SI should carry out a degree of risk on an independent basis. Accordingly, ESMA is of the view that an EU branch of a third-country firm, in order to comply with the SI regime, should at least meet the following criteria:

- Risk management

The EU branch should not transfer the risk resulting from its SI activity through a de facto riskless back-to-back booking for hedging purposes whenever a transaction is executed with a client. Any transactions undertaken in an SI capacity should impact the Profit and Loss of the branch.

- Quote provision

The EU branch should have control over the provision of quotes. This would require the EU branch to have the ability to define its own pricing model through dedicated parameters, set its quotes, define its pricing model update and withdraw its quotes on an independent basis. The EU branch should also have traders located in the EU assigned to the SI activity and providing quotes to EU clients.

- Specific commercial policy

The EU branch should have documentation signed with its clients and a dedicated commercial policy with respect to its SI activity including a definition of the objective, non-discriminatory criteria governing access to its quotes.

- Reporting

The EU branch should have a dedicated MIC code for the purpose of the relevant reporting obligations (including those covered by Article 14(5) of RTS 22 and the Guidelines on transaction reporting section 5.14.4 and 5.17.3) to be done in its SI capacity.