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France calls for bolstering of Mifid third-country regime

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The French regulator has called for tough new conditions to be added to the Mifid II third-country passport that UK firms hope to use to maintain their services in the EU post-Brexit.

The third-country passport, which was introduced by Mifid II in January but has not yet been activated, is intended to allow non-EU firms to sell to professional investors in the single market once their home jurisdiction has been deemed equivalent.

The activation of the passport is on hold as the European Commission reviews its equivalence regimes to make sure a level playing field is maintained between EU and non-EU firms after the UK leaves the bloc.

However, speaking in London last week, Robert Ophèle, chairman of the Autorité des Marchés Financiers, said the EU should be “more ambitious in the reform of the Mifid third-country regime”.

This is necessary due to the emergence on the EU border of “a new third country […] the UK, which also happens to be a dominant financial centre”, he says.

Mr Ophèle calls for non-EU firms seeking to use the Mifid passport to serve investors in the single market to be “required to apply certain rules of Mifid II [and] Mifir in those areas where [...] the EU cannot defer to the rules of third countries”.

The subset of rules the AMF chair suggests such firms should be forced to apply includes investor protection measures, such as requirements on product governance, and cost and charge disclosures.

Mr Ophèle says: “Although similar rules may be in place in third countries […] there can be no assurance that they will apply likewise where the same third-country entity deals with EU clients in the EU, let alone that such rules can be effectively enforced by the third-country supervisor in case of a breach in the EU.”

He adds that firms wishing to use the third-country passport should also apply Mifid II rules focused on market transparency and integrity, such as transaction reporting, and pre and post-trade transparency.

Mr Ophèle says that mandating non-EU firms to apply these rules “is not extraterritoriality, it is ensuring a proper level playing field in Europe when European clients are involved”.

When granting Mifid third-country equivalence decisions, the EU “must ensure [that firms wishing to use the passport] comply with the same high standards of investor protection and market integrity that we impose on our EU firms”, he says.

Mr Ophèle also argues for the EU to go a step further than this by directly supervising the application of these rules by third-country firms operating in the EU under the Mifid II passport.

He says: “If we impose a subset of our own rules to third-country firms authorised in their third country, where they operate in the EU, compliance with such rules should be ensured on an ongoing basis.

“This requires some form of supervision of these firms in the EU.”

He suggests that the European Securities and Markets Authority could do this, adding that this enhanced role “should logically entail investigation and sanctioning powers”.

According to Mr Ophèle, the forthcoming legislative review of Esma should empower the agency with “a true supervisory role” over third-country firms, in addition to its existing role in registering non-EU firms.

The AMF chair describes this enhanced third-country framework as “somewhere halfway between the plain equivalence that is currently provided in the text of Mifir and the full imposition of EU rules that characterises other EU financial legislations”, such as the Alternative Investment Fund Managers Directive.

The overhaul proposed by the AMF represents a potential stumbling block for UK firms wishing to use the passport to sell their services to EU professional investors post-Brexit.

Many UK managers are currently registered under Mifid, notably in order to sell segregated account mandates to EU institutional investors, as well as certain wealth management activities.

According to a letter from the UK regulator to the UK Treasury Committee, 2,250 firms in the UK were using an outbound Mifid licence as at July 2016.

Many in the UK had hoped that firms would be able to continue servicing EU investors after Brexit, since it was assumed that the UK would be deemed equivalent under the newly introduced Mifid third-country regime.

The Investment Association has previously urged the UK government to seek immediate access to the Mifid third-country passport as an interim measure between the UK leaving the EU and the introduction of a future trade deal with the bloc.

Attilio Veneziano, founder of London-based law firm Veneziano & Partners, says the AMF’s suggestions to overhaul the Mifid II third-country regime would make it more difficult for non-EU firms to operate in the bloc on the basis of equivalence.

As a result the approach could be seen as protectionist, says Mr Veneziano.

He adds that the proposed regime “frustrates the whole point of the equivalence, where it is the sameness of the regulatory principles of the non-EU and EU country – and sameness of the regulatory outcome – that matters”, rather than identical rules.

But Thomas Donegan, a partner at Shearman & Sterling, says the AMF’s suggestion was to be expected, given that several Esma equivalence studies for central counterparty clearing houses are predicated on third-country firms complying with EU rules.

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