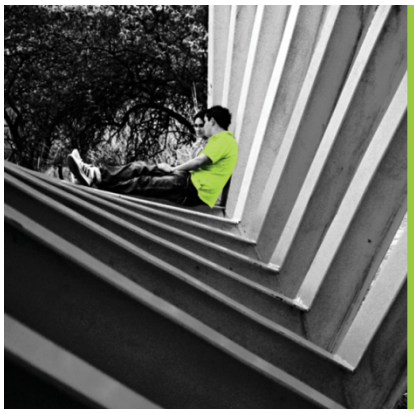

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Luxembourg newsflash

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MiFID 2 and its distinctive Luxembourg features

On 31 May 2018, the law on markets in financial instruments (the "**2018 Law**") as well as the grand-ducal regulation relating 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 (the "**Grand-Ducal Regulation**") were published in the Luxembourg official gazette.

Such texts aim at implementing into Luxembourg law the EU Directive 2014/65 on markets in financial instruments ("**MiFID 2**") and the EU Delegated Directive 2017/593 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 (the "**Delegated Directive**").

Whereas the 2018 Law directly implements MiFID 2, Article 6 of the Delegated Directive (which relates to the inappropriate use of title transfer collateral arrangements) and some specific provisions of the EU Regulation 600/2014 on markets in financial instruments ("**MiFIR**"), the Grand-Ducal Regulation in turn implements the remaining provisions of the Delegated Directive.

In implementing the above, the 2018 Law notably amends in such context quite substantially the law of 5 April 1993 on the financial sector (the **"LFS**") but also replaces the law of 13 July 2007 on markets in financial instruments, as amended. The Grand-Ducal Regulation replaces the grand-ducal regulation of 13 July 2007 on organisational requirements and rules of conduct in the financial sector.

In this context, the Luxembourg supervisory authority for the financial sector, the Commission de Surveillance du Secteur Financier (the "**CSSF**") has in its newsletter of May 2018 already announced that the CSSF circular letters 07/302, 07/306 and 08/365 are now outdated as their content related to the former MiFID regime[1].

[1] Please note that new circular letters are likely to be issued soon by the CSSF in that respect.

1. The approach of Luxembourg in implementing MiFID 2, its related acts and MiFIR

In line with its past practice, Luxembourg has again chosen in its implementation process of the MiFID 2 legislation package to stay really close to the European texts and thus to avoid any material goldplating in this field. Considering the above and the numerous amendments entailed by MiFID 2 and MiFIR, it appears thus more opportune in this newsflash to shed light here on some of the more noticeable and distinctive provisions of the 2018 Law. For the remaining provisions of MiFID 2 (which have essentially been implemented one to one into the 2018 Law), we intend to refer here the reader to our detailed newsflashes released in the past on the subject matter (please refer to the relevant hyperlinks at the end of this newsflash).

2. New third-country firms regime

One of the major changes entailed by the 2018 Law (and to some extent MiFIR) consists in the introduction of a new regime also called the "third-country firms regime". Such regime relates to the provision going forward of investment services and activities in(to) Luxembourg by third-country firms (i.e. firms that are established outside the European Union and the European Economic Area). This third-country firms regime in substance varies depending on whether eligible counterparties and professional *per se* clients or whether retail clients or professional clients upon request are targeted by such a service provision.

2.1. Eligible counterparties and professional per se clients

As regards the first category of clients, pursuant to a newly enacted Article 32-1 of the LFS combined with Article 46 of MiFIR, third-country firms wishing to provide investment services and activities to eligible counterparties and professional *per se* clients in(to) Luxembourg will have the option of:

- either establishing a branch to that effect (which will then be subject to the same authorisation requirements as any Luxembourg branch of a third-country firm under the LFS), or
- merely providing their services on a pure cross-border basis.

In the latter case, they will need to comply with the relevant ESMA registration requirements as further detailed under Article 46 of MiFIR (which, among others, require first the European Commission to render an equivalence decision in relation to the legal and supervisory arrangements of the third-country where the third-country firm is established, etc.).

Article 46(4) of MiFIR further specifies in such context that in the absence of any equivalence decision (or where it is no longer in effect), Member States still have the possibility to allow in the meantime the third-country firms to provide investment services or activities together with ancillary services to eligible counterparties and professional *per se* clients according to their national regime.

2.2. The Luxembourg option under Article 46(4) of MiFIR

This scenario will now immediately play out since MiFID 2 has been implemented into Luxembourg law and since (and for as long as) the European Commission has not yet rendered any such an equivalent decision in relation to a specific third-country.

It is expected that such an equivalence decision will not be rendered at the level of the European Commission before months. Given the number of third-country firms which traditionally service this type of clients in Luxembourg on a cross-border basis, this could prove to become an issue for these service providers.

The 2018 Law provides then in such Article 32-1 of the LFS that the relevant third-country firm wishing to provide in the meantime investment services and activities to eligible counterparties and professional *per se* clients into Luxembourg would still be authorised to do so, provided that:

(i) they are authorized to provide the relevant services in their jurisdiction of establishment,
(ii) they are subject to a supervision and to authorisation rules deemed equivalent to the LFS by the CSSF; and
(iii) the cooperation between the CSSF and the supervisory authority of the relevant third-country firm is ensured.

It remains to be seen thus when and in respect of what jurisdiction the CSSF will be able to issue such a “Luxembourg-based” equivalence decision.

2.3. Retail clients and professional clients upon request

As regards retail clients and professional clients upon request, Luxembourg has decided to use the option under Article 39 of MiFID 2. Therefore, the third-country firms are required now to establish a branch in Luxembourg in order to be able to continue to provide investment services and activities into Luxembourg and will then be subject to the same rules as those applicable to Luxembourg credit institutions and investment firms (as further detailed *i.a.* under Article 32 paragraphs 2-4 of the LFS).

2.4. Services at the initiative of the clients

The aforementioned rules relating to third-country firms do not apply in case a client established or located within the European Union initiates at its own exclusive initiative the provision of investment services or activities by a third-country firm. However, the initiative of the client does then not entitle the third-country professional to promote or market other or additional investment products or services to such client.

It will need to be seen, especially as regards scenario sub. 2.2., how such provision will be interpreted in practical terms by the CSSF in the months to come.

3. Other aspects and entry into force of the 2018 Law

Next to some other less noticeable changes compared with MiFID 2, the 2018 Law has further clarified that the transmission of information to approved reporting mechanisms (i.e. persons authorised under MiFID 2 to provide the service of reporting details of transactions to competent authorities or to ESMA on behalf of investment firms) does not amount to a violation of professional secrecy requirements under the LFS. This thus covers the situation where, in order to fulfil its transaction reporting obligations under Article 26 of MiFIR, a firm transmits complete and accurate details of transactions in financial instruments to such data reporting service provider.

From an investment funds perspective, although not covered by the 2018 Law, funds and management companies should pay attention to indirect MIFID 2 aspects on their business and more particularly on the impact thereof on their distribution network taking into account the new rebate regime including rules on research costs as well as the need to participate in the target market definition.

A last element that is worth bearing in mind is the date of entry into force of the 2018 Law.

You will remember in this context that the draft bill of law which led to the 2018 Law initially suggested an entry into force on 3rd January 2018 in order for it to be aligned with the date of effectiveness of MiFID 2 at European Union level. Following some comments from the Council of State during the legislative process, the 2018 Law finally did not retain this wording along with the consequence that from a strictly legal point of view, the 2018 Law has only now entered into force with some delay compared to the initially required date at European Union level of 3rd January 2018[2].

As regards the Grand-Ducal Regulation, except for minor aspects, Luxembourg has implemented the Delegated Directive one to one.

In case you wish to receive some more detailed information in relation to MiFID 2 or any related aspect or requirement thereunder, please feel free to directly contact the Arendt MiFID 2 team for any further question you may have or please click here below to read one of our many MiFID 2 newsflashes that the Arendt MiFID 2 team has released in the past on the subject matter.

> 26 April 2012: Publication of the Draft Report of the rapporteur of the European Parliament on the MiFID II Proposal
> 30 October 2012: Adoption of the position of the European Parliament on the MiFID II proposal
> 20 February 2013: MiFID II - Presidency's Compromise
> 13 June 2014: MiFID II key aspects
> 9 June 2017: MiFID II: Further guidance on product governance requirements

[2] Note that however, MiFIR, being a regulation, as well as all relevant delegated regulations, directly entered into force on 3rd January 2018.

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