

Markets in Financial Instruments Directive II (MiFID II) November 2022

Today's topics for discussion

- What is MiFID?
- Financial Conduct Authority (FCA)
- Types of Customer
- Wiltshire Pension Fund election
- Why and how LGPS is affected?
- Summary

What is MiFID?

- **MiFID – A European Directive effective from 1st November 2007**
 - 1) Aim – To harmonise European Investment Services through standardisation & regulation
 - 2) Aim – To also restore confidence in the industry after the Financial crash in 2008 (changes made in light of the crisis that took shape in MiFID II)
 - 3) Covers services like advising on investments
 - 4) Directive content transferred into the FCA's Code of Business Rules (COBs)
- **MiFID II – A revised Directive started in March 2012**
 - 1) Came into force from 3rd January 2018
 - 2) Aim – To strengthen investor protection and improve the functioning of financial markets making them more efficient, resilient & transparent
 - 3) Introduced new reporting requirements, greater product governance & requirements around independent investment advice
 - 4) Updated guidance issued – Recent guidance on client protection, best execution and derivative transparency.

Financial Conduct Authority - FCA

- Objectives

- 1) Market Confidence
- 2) Financial Stability
- 3) Protection of Customers
- 4) Reduction in financial crime

- Key scope & powers

- 1) An authoriser of activity, enabled to regulate & investigate those activities & where necessary to take action over misconduct with various enforcement powers
- 2) Maintain a public record of authorised & prohibited persons

- Fit & proper test of authorised persons

- 1) Honesty, integrity & reputation
- 2) Competent & capable
- 3) Financial Soundness

Types of Customer

- Retail client
 - 1) A Client not eligible to be an eligible counterparty or a professional client
- Professional client (Wiltshire Pension Fund election)
 - 1) Can be either a “*per se*” or “elective” professional investor
 - 2) Automatically classified by virtue of your characteristic i.e. a local or public authority (per se)
- Eligible counterparty
 - 1) Only applies to certain types of business & where that business deals on its own account, executes its own orders or receives or transmits orders. For example, central banks
- Observations between customer types
 - 1) Retail clients afforded the greatest protection & provided with the fullest standard of advice. Other customer types determined as more financial astute requiring less advice.
 - 2) Professional clients should ensure they maintain their knowledge & understanding

Wiltshire Pension Fund election

- Fund Application for Professional status
 - 1) Application for “per se” status made “as necessitated” in September 2017
 - 2) Aim – The necessitation enables the Fund to invest in the broadest range of investments it can, not just as a result of its “local or public authority” characteristic
- Other Investment Advisers
 - 1) The Fund should ensure that all their Adviser firms continue to be authorised to give advice & services
 - 2) Not just the organisation, but also the individual adviser, advising on regulated activities
- Committee Members
 - 1) Need to have sufficient knowledge & understanding to challenge the advice given to them
 - 2) Risk to the Fund due to the validity of the “Professional Client” status assigned to it
 - 3) Consider whether the Fund is suitably protected against risk

Why and how LGPS is affected?

- Why are LGPS funds considered ‘retail’ investors by default?
 - 1) While it was introduced to protect the treasury management functions of local governments across Europe, because of the unique structure of the LGPS pension fund (i.e. no legal separation between authority and pension fund, unlike all other UK pension funds) the default status is retail
 - 2) The FCA were lobbied by the LGPS Advisory Board, the Local Government Association (LGA) and the Investment Association, to make changes to “quantitative” and “qualitative” tests for clients to be classified as professional
- How do LGPS fund achieve ‘professional’ status?
 - 1) A quantitative test, must be passed, (all LGPS administering authorities can be opted up as they run at least £10m (€11.4m))
 - 2) A qualitative test must be passed; this assessment is made by Asset managers. The “expertise, experience, and knowledge” of decision makers must be verified. MiFID II refers to an individual person, but the FCA’s policy statement made it clear that **“firms may take a collective view of the expertise, experience and knowledge of committee members, taking into account any assistance from authority officers and external advisers where it contributes to the expertise, experience and knowledge of those making the decisions”**.
- What does this mean for Committee Members/Wiltshire Pension Fund?
 - 1) Emphasises the importance of training and the need to have sufficient knowledge & understanding in order to make decisions.
 - 2) That the Committee, advisors and officers must consider the collective expertise, experience and knowledge and inform its asset managers of any significant change that may give rise to the asset manager reconsidering professional status.

Summary

- Self-certification

- 1) No legal requirement to self certify, however it is a good governance recommendation
- 2) Opportunity for members to consider training needs

- Liaise with your investment advisers

- 1) To ensure that they provide you with evidence of their continued authorisation to provide a regulated service & advice
- 2) To establish governance arrangements with them so that they actively update the Fund concerning MiFID II communications & their ongoing compliance

- Ongoing review

- 1) At least annually repeat this exercise & include this compliance review in the Fund's Look Forward plan and other documents within the Fund's governance framework
- 2) Consider the Fund's protection needs

Thank you for your time