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ARTICLE

The Third Country Regime for Investment Firms

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Abstract

In this article we discuss how an investment firm established outside the EU may provide services (to clients) in the EU. We explore how such third country firms may enter the European market and discuss the current state of the third country regimes as provided (partly) under EU law, their use—or notable lack thereof—and the challenges involved in the supervision of third country firms. We note that the recent updates to the third country equivalence regime for the provision of services to professional clients render the use of this regime even more difficult. In respect of the (optional) third country regime for the provision of services to retail clients, we observe that this regime is much akin to a full license requirement, albeit with notable difficulties when it comes to supervision and enforcement. Altogether, we come to the unfortunate conclusion that the EU third country regime for investment firms established in third countries can barely be called successful.

Keywords Investment firms · Third country · Market access · Equivalence · ESMA registration · Branch office · Subsidiary · Reverse solicitation · Supervision · Member State option · Investment services · Investment activities · MiFID II · MiFIR · IFD · IFR · CRD6

The opinions and thoughts expressed in this article reflect only the authors' views.

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1 Introduction

Investment firms play an important role on the financial markets in the European Union (hereinafter: the 'Union').[1] Their services relating to financial instruments include, among others, the reception and transmission of orders, the provision of investment advice, discretionary portfolio management and the activity of dealing on own account. Of the investment firms active in the Union, many are, however, not established in the Union but in third countries (hereinafter: 'third country firms'). For individual clients it may be essential to have access to such firms, because of their specific offering, although Brexit may have had its impact due to migration of financial services from the United Kingdom (UK) to the EU.[2]

The original Directive governing the provision of investment services, the ISD,[3] did not provide for a third country regime. Instead, it was focused on ensuring that EU firms received the same treatment in third countries as third country firms in the Union.[4] MiFID,[5] which repealed the ISD as of 1 November 2007, did not provide for a third country regime either.[6] Only with the introduction of MiFID II/MiFIR[7] was an attempt made to introduce such a regime.[8]

In short, MiFIR introduced an equivalence regime that entails that the European Commission (hereinafter: 'the Commission') may determine that the regulatory and supervisory regime of a non-EU country with regard to third country firms is equivalent to the corresponding EU framework. This equivalence regime is, however, restricted to third country firms providing investment services to or conducting investment activities[9] – in the remainder of this article these services and activities are, together with ancillary services, referred to simply as 'services' where possible—for so-called professional clients (eligible counterparties, or 'ECPs',[10] and *per*

[1] The term 'investment firm' refers to a natural or legal person whose regular occupation or business is the provision of one or more investment services to third parties and/or the performance of one or more investment activities on a professional basis, as meant in Art. 4(1) of Directive 2014/65/EU of 15 May 2014 on markets in financial instruments (MiFID II). Reference to the 'European market', 'Union' or 'EU' in this article should be understood as including a reference to the European Economic Area.

[2] Donnelly argues that following Brexit, the European Supervisory Authorities and the European Commission view migration from London to the EU as essential to proper regulation and financial stability for the Single Market. See Donnelly (2023), pp 802-803. See also Recital (41) MiFIR.

[3] Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field.

[4] Art. 7 ISD.

[5] Directive 2004/39/EC of 21 April 2004 on markets in financial instruments.

[6] Recital (28) and Art. 15 MiFID.

[7] Regulation (EU) 600/2014 of 15 May 2014 on markets in financial instruments.

[8] However, it should be noted that this is not the only third country regime laid down in MiFID II/MiFIR. MiFIR also, for instance, provides equivalence regimes in regard to third country central banks regarding trade transparency requirements (Art. 1(9) MiFIR) and third country trading venues regarding the obligation to trade shares (Art. 23(1) MiFIR and Art. 25(4) MiFID II) or derivatives(Art. 28(1)(d) MiFIR and Art. 28(4) MiFIR) on regulated markets, MTFs or OTFs. Discussion thereof is, however, out of scope of this article.

[9] As defined in Art. 4(1) under (2) MiFID II.

[10] Art. 30 MiFID II.

se professional clients[11]). Although this equivalence regime already applies from 3 January 2017, it is not active since the Commission has not taken any equivalence decisions yet. In the absence of such equivalence decisions, market access and supervision of third country firms is subject to the national third country regimes of the Member States.[12] In addition, for so-called retail clients[13] (including opt-in professional clients[14]), MiFID II only provides a minimum common regulatory framework at Union level which, if a Member State opts to implement this regime, requires that a branch needs to be established by third country firms in order to be able to enter the market of a Member State. However, a Member State can also decide that no branch is required, in which case it is free to establish the regulatory framework applicable to third country firms.

As a result, market access and supervision of third country firms in respect of services provided to both professional and retail clients is partly regulated at EU level but is, for a large part, still a national matter.[15] This has resulted in quite a patchwork of Union and national legal regimes regulating market access and supervision for third country firms. This article attempts to shed light on these regimes by discussing on what conditions third country firms may provide services (to clients) in the EU.

We start with setting out how third country firms can provide services (to clients) in the Union (Sect. 2). We continue by explaining the third country regime provided in MiFID II/MiFIR while focusing on the changes that have been introduced by the new prudential regime for investment firms laid down in IFR[16]/IFD[17] (Sect. 3). Section 4 concludes.

2 How Can Third Country Firms Provide Services to EU Clients?

In order to answer the question of how third country firms can provide services to EU clients, we make a distinction between *when* third country firms are considered to enter the European market (Sect. 2.1) and *in which ways* third country firms can enter the European market (Sect. 2.2). In addition, in Sect. 2.3, we dive into the specifics of market access by third country credit institutions (hereinafter: 'banks') in order to provide investment services to, or conduct investment activities for, EU clients.

[11] This is a client that meets the criteria laid down in Section I of Annex II of MiFID II.

[12] Art. 46(4), last paragraph MiFIR.

[13] Art. 4(1), under (11) MiFID II.

[14] In this article the term 'opt-in professional clients' refers to clients that are not professional clients, but that may be treated as professional clients on request, as meant in Section II of Annex II of MiFID II.

[15] In a letter dated 26 September 2018 to the European Commission, ESMA already considered this to be an undesirable situation (ESMA (2018)).

[16] Regulation (EU) 2019/2033 of 27 November 2019 on the prudential requirements of investment firms.

[17] Directive (EU) 2019/2034 of 27 November 2019 on the prudential supervision of investment firms.

2.1 When Does a Third Country Firm Enter the EU Market?

It follows from MiFID II that a third country firm enters the European market when it provides services to retail clients *in the territory of a Member State*.[18] Furthermore, it follows from MiFIR that a third country firm enters the European market when it provides services to professional clients *established throughout the Union*.[19]

Hence, the decisive element is whether the third country firm provides a service to a client *located in the EU*. With regard to investment services, such a determination generally does not seem too difficult; after all, an investment service is provided to a specific client (which may or may not be located in the EU).

The localisation of the performance of investment activities seems somewhat less clear. European regulation does not specify when dealing on own account or the operation of an MTF or an OTF is performed for a client located in the EU. Arguably, it may be inferred that dealing on own account takes place in the Union, when the third country firm has exposures to EU counterparties.[20] However, absent European guidance, it remains somewhat ambiguous when investment activities take place in the Union, and national interpretations seem to differ.[21] We will not discuss this issue further here, suffice to note that the issue of localisation of investment activities may benefit from further clarification at EU level.

Both MiFID II and MiFIR provide specific rules for the situation where a third country firm provides a service to a client established or situated in the Union at the exclusive initiative of that client. In this situation, the services should not be deemed to be provided in the territory of the Union.[22] As such, it seems that a service provided at the exclusive initiative of a client, should not be subject to authorisation requirements. However, as discussed below in Sect. 3.1, the exact scope of exception from authorisation remains somewhat uncertain.

2.2 Ways to Enter the EU Market

Basically, third country firms can enter the European market in three different ways. A third country firm may: (i) provide services in a Member State without

[18] See Art. 39(1) MiFID II.

[19] See Art. 46(1) MiFIR.

[20] See Art. 46(6a), sub (a) MiFIR. See also Busch and Louisse (2017), p 254.

[21] For instance, German law distinguishes between dealing on own account (*Eigenhandel*) and trading on own account (*Eigengeschäft*). In contrast to the former—where transactions in financial instruments are made partly as a service to others (such as internalisation and market making)—the latter does not contain a service element. Therefore, under German law, cross-border *Eigengeschäft* from a third country to Germany does not target the German market. See Deutscher Bundestag (2019), p 38. Under Dutch law, on the other hand, no such distinction is made and third country firms that intend to trade for their own account in the Netherlands are, in principle, always required to have a license granted under Dutch law. A specific exemption for the license requirement is, however, provided for third country firms dealing on own account in the Netherlands, provided that they do so with or by means of a party which is allowed to provide investment services or perform dealing on own account under Dutch law. See Art. 10a Exemption Regulation Wft (*Vrijstellingsregeling Wft*).

[22] See Recital (111) MiFID II and Recital (43) MiFIR.

establishing a physical presence in that Member State (cross-border provision of services); (ii) establish a branch office in a Member State; or (iii) establish a subsidiary with a separate market authorisation in a Member State.[23]

2.2.1 Cross-Border Provision of Services

A first potential avenue for third country firms seeking access to the European market involves the provision of cross-border services. This method enables such firms to offer services in the EU without establishing a physical presence, such as a branch or a subsidiary, in the EU. In this scenario, the third county firm provides services to natural or legal persons in the EU on a cross-border basis. Whether a third country firm may provide services in the territory of a Member State on a cross-border basis depends on Union law and, where Union law remains silent or leaves options to the Member States, national law. To determine the applicable legal regime, it is important to consider whether the services of the third country firm target retail or professional clients. Both dimensions are considered below.

2.2.1.1 Cross-Border Provision of Services to Professional Clients Union law provides that a third country firm may provide services to professional clients established throughout the Union without the establishment of a branch, if the Commission has taken an equivalence decision concerning that third country and the third country firm is registered in the register of third country firms kept by ESMA.[24] In such a case, the Member State may not require the third country firm to establish a branch in its territory. Third country firms that provide services in the Union on the basis of an ESMA registration are not allowed to provide services to clients other than professional clients.[25] The equivalence regime is further discussed in Sect. 3.3.

From the foregoing it follows that Union law only explicitly stipulates that third country firms that are active in the Union under an ESMA registration may provide services without the establishment of a branch. In the absence of an equivalence decision by the Commission, it depends on Member States' national regimes whether third country firms may provide services to professional clients on a cross-border basis.

[23] In accordance with Arts. 29 and 34 MiFID II, an investment firm authorised in accordance with MiFID II may also appoint a tied agent which, exclusively for that firm, may provide investment services or ancillary services in another Member State. As a third country firm cannot directly access the European market through the establishment of a tied agent, it is not discussed here. However, it is of note that ESMA, in the context of Brexit, observed some practices concerning investment firms using tied agents as a potential source of circumvention of the third country regimes in the EU. To prevent such circumvention, ESMA underlined that a tied agent should not use references, email accounts or telephone numbers which can be associated with an entity that is different from the appointing firm, a third country or a third country entity. ESMA further stressed that this is particularly important in those cases where the tied agent is a legal person that is controlled by or closely linked to a third country entity that is itself involved in activities concerning manufacturing or distribution of financial instruments. See ESMA (2022).

[24] See Art. 46(1) MiFIR.

[25] See Art. 46(5) MiFIR.

2.2.1.2 Cross-Border Provision of Services to Retail Clients Union law provides an optional harmonised regime, which Member States may choose to use, regarding market access for a third country firm in order to provide services to retail clients. Under this regime, a third country firm is required to establish a branch in the territory of the Member State concerned. If the Member State decides not to make use of this optional regime, it cannot render market access for third country firms conditional upon the establishment of a branch in that Member State's territory.[26] Whether, and under what other conditions, a third country firm can then operate in that Member State—for instance on a cross-border basis or by establishing a subsidiary—is then entirely governed by national law.

2.2.2 Branch Office

A branch means a place of business other than the head office which is part of an investment firm, which has no legal personality and which provides services for which the investment firm has been authorised.[27] As stated above, MiFID II provides for an optional market access regime whereby Member States may require third country firms to establish a branch in their territory. The optional branch regime is discussed further in Sect. 3.2.

2.2.3 Subsidiary

A third country firm can always decide to establish a subsidiary in a Member State. Such a subsidiary will have to obtain a MiFID II authorisation[28] on the basis of which it can provide services throughout the EU, based on a so-called EU passport. There is no difference in that respect between EU investment firms and EU subsidiaries of third country firms.

2.3 Third Country Banks Providing Investment Services or Conducting Investment Activities in the Union

In accordance with CRD,[29] a banking authorisation under CRD is required when the business of an undertaking consists of (i) the combined activity of taking deposits or other repayable funds from the public and granting credits for its own account (i.e., 'banking services'), or (ii) dealing on own account or underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis

[26] See also Busch and Louisse (2017), p 271.

[27] See Art. 4(1), point (30) MiFID II.

[28] Art. 5 MiFID II.

[29] Directive 2013/36/EU of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.

and where the firm concerned meets the size criteria provided under Article 4(1)(b) CRR[30] (i.e., 'systemic investment firms').[31]

An undertaking with a banking authorisation under CRD does not need another authorisation under MiFID II in order to provide investment services or perform investment activities in the EU.[32] When a bank decides to provide these services/activities, the competent authorities, before granting an authorisation under CRD, should verify that it complies with the relevant provisions under MiFID II.[33]

The conditions under which a third country bank may be active in the EU—either through cross-border provision of services or through the establishment of a branch in the EU—are not harmonised under CRD.[34] As a result, national approaches to the authorisation, regulation and supervision of third country banks providing (banking) services in the EU diverge.[35] CRD does, however, stipulate that competent authorities may not apply a more favourable treatment to third country branches than that applied to branches of banks having their head office in the Union.[36] Hence, a banking branch of a third country bank that provides investment services/activities in the EU will, at least, also have to comply with the relevant provisions under MiFID II.[37]

2.3.1 Changes Under the CRD6 Proposal

The draft overall compromise package for the CRD reforms of 14 December 2023, referred to here as 'CRD6 proposal',[38] provides that third country banks[39] that seek to provide core banking services (i.e., taking of deposits and other repayable funds, lending, and providing guarantees and commitments) in the Union should

[30] Regulation (EU) No 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms.

[31] See Art. 8(1) CRD in combination with Art. 4(1), point 1 CRR.

[32] See Recital (38) MiFID II.

[33] A bank that provides services on the basis of its CRD authorisation, may also provide such services in other Member States, either by establishing a branch or by providing services. See Art. 33 CRD and Annex I to CRD. In such cases, the (notification) requirements under Title V CRD apply.

[34] While Article 47(3) CRD allows the Union to conclude agreements with one or more third countries, agreeing 'to apply provisions which accord to branches of a credit institution having its head office in a third country identical treatment throughout the territory of the Union', no such agreements have so far materialised. See further Binder (2024).

[35] See EBA (2021), p 53.

[36] See Art. 47 CRD. This provision also lists reporting obligations for third country branches.

[37] This is also reflected in national practice, as, for instance, in the Netherlands separate authorisation requirements are provided for a banking branch of a third country undertaking depending on whether it will also provide investment services. In the latter case, it must also meet relevant MiFID II requirements. See Arts. 2:21 and 2:22 Dutch Financial Supervisory Act (DFSA).

[38] See the draft overall compromise package for a proposal for a Directive amending Directive 2013/36/EU of 27 October 2021 as regards supervisory powers, sanctions, third country branches, and environmental, social and governance risks, published on 6 December 2023. The analysis in this section is based on the compromise text. The final legislative act may differ from the compromise text.

[39] For ease of reference we use the term 'third country banks'. However, it is important to note that such an entity does not always have to qualify as a bank had it been established within the Union in order to be subject to the third country branch regime of the CRD6 proposal, as subsequently explained in this section.

in principle, at least, establish a branch in a Member State, unless the undertaking wishes to provide banking services in the Union through a subsidiary.[40] Specifically, a third country bank must, at least, establish a branch before commencing or continuing:

- lending or providing guarantees and commitments in the relevant Member State, provided that such an undertaking would qualify as a bank (which, as detailed above, includes 'systemic investment firms') if it were established in the Union;[41]
- taking deposits and other repayable funds in the relevant Member State.[42]

It follows that the taking of deposits or other repayable funds would trigger a branch requirement irrespective of the third country bank's potential qualification as a bank if it were established in the Union. The establishment of a branch will be subject to prior authorisation for which a set of minimum conditions are provided by CRD6 (see further Sect. 3.2.3.3).[43] The branch may only conduct the authorised activities within the Member State where it is established.[44]

However, CRD6 also provides certain exceptions to the requirement to establish a branch subject to an authorisation requirement under CRD6. A third country bank is not required to establish a branch under CRD6 where it provides core banking services on the basis of reverse solicitation,[45] or in case of interbank and interdealer transactions.[46] Importantly, the requirement to establish a branch under CRD6 does not apply either where a third country bank is providing investment services and activities listed in Annex I, Section A, MiFID II, and any accommodating ancillary services such as related deposit-taking, granting credit or loans the purpose of which is to provide services under MiFID II.[47]

Consequently, third country banks can still provide investment services or perform investment activities in the EU on the basis of the third country regime provided in MiFID II/MiFIR after adoption of CRD6.[48] They will not be subject to the EU banking framework as long as they only provide investment services or perform investment activities, with or without core banking services in the EU that are of an ancillary nature to the provision of such services or activities. The public list maintained by ESMA[49] seems to indicate that third country banks mostly make

[40] Recital (3) CRD6 proposal.

[41] Art. 47(1)(a) CRD6 proposal.

[42] Art. 47(1)(b) CRD6 proposal.

[43] Arts. 21c and 48c CRD6 proposal.

[44] Art. 48c(3)(d) CRD6 proposal.

[45] Where the counterparty is a retail client, an eligible counterparty or a professional client established or situated in the Union that approaches an undertaking established in a third country at its own exclusive initiative. See Art. 21c(2)(a) CRD6 proposal.

[46] Where the counterparty established or situated in the Union is a bank or an undertaking of the same group as that of the undertaking established in a third country. See Art. 21c(2)(b)-(c) CRD6 proposal.

[47] Arts. 21c(4) and 47(2) CRD6 proposal.

[48] See also Recital (3a) CRD6 proposal.

[49] See https://www.esma.europa.eu/publications-and-data/databases-and-registers (last accessed on 4 January 2024).

use of the MiFID II branch regime to provide investment services in the Union (see Sect. 3.2.1). It appears that this will in principle remain possible under the CRD6 proposal.

3 The Third Country Regime Provided at Union Level

As already mentioned, at Union level, MiFID II/MiFIR provide two distinct market access regimes for third country firms: the optional branch regime for the provision of services to retail clients and the equivalence regime for the provision of services to professional clients. This section does not discuss these regimes in detail, as this has already been done extensively in academic literature.[50] Rather, it focuses on the current state of these regimes, taking into account that, after their introduction, the UK withdrawal from the EU (Brexit) happened. This warranted a more refined look at the regimes, identifying certain risks. These risks were subsequently considered to be more general, also applying beyond the developments in the international sphere following Brexit.[51] This caused a substantial revision of the regimes applying from 26 June 2021, as the revision was included in IFR/IFD. The following sections discuss the current state of these regimes, their use—or rather the glaring lack thereof when it comes to the equivalence regime—and the challenges involved in the supervision of third country firms.

3.1 Reverse Solicitation

An important aspect of the market access regime under MiFID II concerns the rules on 'reverse solicitation'.[52] In general terms, these entail that '[w]here a third-country firm provides services at the own exclusive initiative of a person established in the Union, the services should not be deemed as provided in the territory of the Union'.[53] In accordance with this premise, MiFID II specifies that Member States may not subject a third country firm to the requirement for authorisation under the optional branch regime (discussed below in Sect. 3.2) if a retail client in the Union initiates at its own exclusive initiative the provision of services by that third country firm.[54] Similarly, MiFIR provides that the registration requirement under the equivalence regime (discussed below in Sect. 3.3) does not apply to a third country firm if it provides services to professional clients on the exclusive initiative of the latter.[55]

50 See, e.g., Busch and Louisse (2017), p 254; Pitz and Nemeczek (2021), pp 55–59.

51 See ESMA (2018).

52 See also, extensively, Pitz and Nemeczek (2021), pp 69–72.

53 Recital (111) MiFID II indicates specifically that the provision of *MiFID II* should not affect the possibility for persons established in the Union to receive investment services by a third country firm at their own exclusive initiative. The reference to MiFID II in this recital may be taken as an indication that the rules on reverse solicitation do not necessarily apply to national regimes not based on MiFID II.

54 Art. 42(1) MiFID II.

55 Art. 46(5) MiFIR.

Whether a service is provided on the basis of a client's exclusive initiative should be assessed on a case by case basis for each service provided, regardless of any contractual clause or disclaimer.[56] The fact that a client initiates on its own exclusive initiative a service or activity, does not entitle the third country firm to market new categories of investment products or investment services to that client otherwise than through an authorised branch, where one is required in accordance with national law.[57]

The IFR/IFD regulatory developments did not entail substantial changes with regard to the rules on 'reverse solicitation'. However, IFR/IFD did provide more clarity in relation to the scope thereof. Specifically, the relevant provisions in MiFID II and MiFIR now stipulate that, without prejudice to intragroup relationships, where a third country firm, including through an entity acting on its behalf or having close links with such third country firm or any other person acting on behalf of such entity, solicits[58] clients or potential clients in the Union, it shall not be deemed to be a service provided at the own exclusive initiative of the client.[59] Consequently, relying on reverse solicitation should be the exception rather than the rule.

3.2 The Optional Branch Regime

The European legislators acknowledged that Member States may consider that the appropriate level of protection for retail clients, when a third country firm offers services to them, can be achieved by the establishment of a branch by the third country firm.[60] Therefore, they found it appropriate to introduce a minimum common regulatory framework at Union level once a Member State exercises this option. This regime is provided by Articles 39 to 42 MiFID II. It concerns a harmonised regulatory framework should a Member State require third country firms to establish a branch in that Member State in order to provide services to retail clients in its territory.

If a Member State chooses to require a third country firm to establish a branch in order to provide services to retail clients, it must follow the minimum common regulatory framework provided by MiFID II. Member States cannot impose any additional requirements on the organisation and operation of the branch in respect of matters covered by MiFID II.[61] National practice shows, however, that Member

[56] See ESMA (2021), question 13 (last updated on 28 March 2019), p 116.

[57] Art. 42(2) MiFID II.

[58] ESMA is of the view that every communication means used—such as press releases, advertising on internet, brochures, phone calls or face-to-face meetings—should be considered to determine if the client or potential client has been subject to any solicitation, promotion or advertising in the Union on the firm's investment services or activities or on financial instruments. See ESMA (2021), question 13 (last updated on 28 March 2019), p 116.

[59] See Art. 42(1), last paragraph MiFID II and Art. 46(5), last paragraph MiFIR. This concerns a codification of ESMA guidance. See ESMA (2021), question 13 (last updated on 28 March 2019), p 116.

[60] See Recital (109) MiFID II.

[61] Art. 41(2) MiFID II.

States may make only partial use of the optional branch regime.[62] Furthermore, the establishment of a branch in a Member State does not 'unlock' passporting rights on the basis of which services may also be provided in other Member States.[63]

3.2.1 Authorisation of the Branch

The conditions for authorisation are exhaustively listed in Articles 39 and 41 MiFID II. Hence, Member States may not impose any additional requirements on the organisation and operation of the branch than those provided under the MIFID II regime in respect of the matters covered by MiFID II.[64] The competent authority must grant authorisation to establish a branch if it is satisfied that the conditions for authorisation are met.[65] The conditions for authorisation are as follows:

1. The provision of services for which the third country firm requests authorisation is subject to authorisation and supervision in the third country, whereby the competent authority pays due regard to any recommendations of the Financial Action Task Force in the context of anti-money laundering and countering the financing of terrorism.[66]
2. Cooperation arrangements, including provisions regulating the exchange of information for the purpose of preserving the integrity of the market and protecting investors, are in place between the competent authorities in the Member State where the branch is to be established and competent supervisory authorities of the third country where the firm is established.[67]
3. Sufficient initial capital is at free disposal of the branch.[68]
4. One or more persons are appointed to be responsible for the management of the branch and they all comply with the requirements laid down in Articles 88 and 91 CRD.[69]

[62] Dutch law requires a third country firm to establish a branch in order to provide investment services to retail clients or opt-in professional clients. At the same time, the Dutch regime does not impose a branch requirement for the performance of investment activities to retail clients or opt-in professional clients. Hence, the Netherlands only made partial use of the optional 'branch-regime' under MiFID II. See Arts. 2:99 and 2:99a DFSA.

[63] This is only different when the country of a third country firm, which has established a branch in accordance with Art.39 MiFID II in a Member State, is declared equivalent by the Commission under Art. 47(1) MiFIR. In such cases, Art. 47(3) MiFIR provides that the third country firm is allowed to provide investment services and activities covered under the authorisation to eligible counterparties and *per se* professional clients in other Member States without the need to establish new branches. Hence, when the conditions under Art. 47(3) MiFIR are met, that provision grants passporting rights to third country firms without needing to register in the ESMA register. See also ESMA (2020), para. 28.

[64] Art. 41(2) MiFID II.

[65] Art. 41(1) MiFID II.

[66] Art. 39(2)(a) MiFID II.

[67] Art. 39(2)(b) MiFID II.

[68] Art. 39(2)(c) MiFID II.

[69] Art. 39(2)(d) MiFID II. Arts. 88 and 91 CRD provide certain governance and fit & proper requirements for the persons responsible for the management.

5. The third country where the third country firm is established has signed an agreement with the Member State where the branch is to be established, which fully complies with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital and ensures an effective exchange of information in tax matters, including, if any, multilateral tax agreements.[70]
6. The firm belongs to an investor-compensation scheme authorised or recognised in accordance with the Investor Compensation Scheme Directive.[71]
7. The branch of the third country firm will be able to comply with (where relevant depending on its intended activities) certain organisational requirements,[72] requirements to ensure investor protection,[73] market transparency and integrity requirements,[74] transparency requirements for trading venues,[75] transparency requirements for systematic internalisers and investment firms trading OTC and tick size regimes for systematic internalisers,[76] and transaction reporting requirements.[77]
8. The branch of the third country firm will be able to comply with the reporting obligations pursuant to Article 41(3) MiFID II (as detailed below).

3.2.2 Changes Introduced by IFD

In September 2018, ESMA observed the following:

> The lack of additional harmonisation in the regime concerning third country firms interacting with retail clients in the EU may pose the risk of legal uncertainty and regulatory and supervisory arbitrage between jurisdictions with potential detrimental implications for investors. The European Commission may therefore wish to consider the opportunity for further harmonisation of the national regimes applicable to third country firms providing investment services to retail clients in the EU.[78]

The Commission, however, did not go so far, as the changes introduced by IFD are limited to facilitating the monitoring and assessment of activities carried out by third country firms through branches in the Union.

Specifically, to facilitate the regular monitoring and assessment of activities carried out by third country firms through branches in the Union, the branch of the third country firm must now annually report certain information to the competent authorities of the Member State where the branch is established.[79] This includes

[70] Art. 39(2)(e) MiFID II.
[71] Art. 39(2)(f) MiFID II. Directive 97/9/EC of 3 March 1997 on investor-compensation schemes.
[72] Art. 40(2) MiFID II in combination with Arts. 16 to 20 MiFID II.
[73] Art. 40(2) MiFID II in combination with Arts. 23-25, 27, 28(1) and 30 MiFID II.
[74] Art. 40(2) MiFID II in combination with Arts. 31 and 32 MiFID II.
[75] Art. 40(2) MiFID II in combination with Arts. 3-13 MiFIR.
[76] Art. 40(2) MiFID II in combination with Arts. 14-23 MiFIR.
[77] Art. 40(2) MiFID II in combination with Arts. 24-26 MiFIR.
[78] ESMA (2018), pp 3–4.
[79] Art. 41(3) MiFID II. See also Recital (38) IFD.

information about the scale and scope of the services and activities of the branch, the turnover and aggregated value of the assets corresponding to those activities, figures detailing the dealing on own account and underwriting and placing activities in relation to EU counterparties, its investor protection and risk management arrangements, and its governance arrangements.[80] In addition, the branch must provide any other information which the competent authority considers necessary to enable comprehensive monitoring of the activities of the branch.[81]

The competent authorities must notify ESMA on an annual basis of the list of branches of third country firms active on their territory. Furthermore, upon request, the competent authorities must inform ESMA of all the authorisations of, and changes thereof regarding, third country branches, the scale and scope of the services carried out by an authorised branch in the Member State, the turnover and the total assets corresponding to those services, and the name of the third country group to which an authorised branch belongs.

ESMA, in turn, is required to publish annually a list of branches of third country firms active in the Union.[82] It can be derived from this list, that, at the time of writing this article, around 50 third country firms have established an authorised branch in the EU. Most third country firms are actually banks providing investment services. They are mainly established in the United Kingdom, the United States of America, China, Japan, Iran, Brazil and Switzerland. Some of them are active in multiple Member States and have therefore several authorised branches in the EU. It can be read that it is expected that several third country firms active in Italy will be cancelled from the register, either because the firm has never initiated its services or because it has stopped its operations. Italy is also the only country regarding which limitations established by the national competent authorities are mentioned. Nearly all third country branches authorised in Italy are subject to the limitation that they may not hold, not even temporarily, customers liquid balance or financial instruments.

3.2.3 Supervision Under the MiFID II Third Country Regime

As shown in Sect. 3.2.1 above, the branch of the third country firm authorised on the basis of MiFID II has to comply on an ongoing basis with a number of obligations under MiFID II.[83] The branch of the third country firm must, for instance, meet MiFID II's organisational requirements including the rules on the segregation of financial instruments and funds belonging to clients. Accordingly, a branch of a third country firm which holds financial instruments belonging to clients must have

[80] The Commission, on the basis of draft implementing technical standards submitted to it by ESMA, published implementing technical standards specifying the format in which this information is to be reported. See Commission Implementing Regulation (EU) 2022/1220 of 14 July 2022.

[81] Art. 41(3)(h) MiFID II.

[82] Art. 41(2) MiFID II. The list is available on ESMA's website: https://www.esma.europa.eu/publications-and-data/databases-and-registers (last accessed on 4 January 2024).

[83] Specifically, Arts. 16 to 20, 23, 24, 25, 27, 28(1), 30, 31 and 32 MiFID II and Arts. 3 to 26 MiFIR and the measures adopted pursuant thereto.

adequate arrangements to safeguard the ownership rights of clients and to prevent the use of a client's financial instruments on own account except with the client's express consent.[84] Similarly, when holding funds belonging to clients, the branch must make adequate arrangements to safeguard the rights of clients and, except in the case of banks, prevent the use of client funds for its own account.[85]

Importantly, Member States may not impose any additional requirements on the organisation and operation of the branch in respect of the matters covered by MiFID II nor may they treat any branch of third country firms more favourably than Union firms.[86]

Compliance with the relevant requirements under MiFID II and MiFIR is supervised by the competent authority in the Member State where the authorisation was granted.[87] If the branch is part of a group which also has other entities in the EU, the competent authority of the branch must cooperate closely with the competent authorities of other group entities or branches and ESMA and EBA to ensure comprehensive, consistent and effective supervision in accordance with MiFID II/ MiFIR, CRD/CRR and IFD/IFR.[88]

3.2.3.1 Application of (Prudential) Requirements not Based on MiFID II/MiFIR As discussed above, the branch of the third country firm must comply with a number of requirements under MiFID II and MiFIR. These acts, however, do not include prudential requirements beyond the condition that the branch must dispose of sufficient initial capital.[89] Indeed, MiFID II and MiFIR, in general, do not stipulate prudential requirements for investment firms. These requirements are instead provided by the dedicated prudential framework for investment firms under IFD and IFR, or (for systemic investment firms) CRD and CRR.

This prompts the question whether a Member State may impose prudential requirements on a branch of a third country firm, for instance, by submitting such a branch to IFR and IFD. MiFID II provides that the Member States may not impose any additional requirements on the organisation and operation of the branch in respect of the matters covered by MiFID II.[90] However, in our view, this provision does not preclude a Member State from imposing prudential requirements on a branch of a third country firm since prudential requirements (such as solvency and liquidity requirements) are not a matter covered by MiFID II. In fact, it may be recalled that MiFID II requires Member States to not treat branches of third country firms more favourably than Union firms.[91]

[84] See Art. 16(8) MiFID II, as further elaborated in Arts. 2 to 8 of Commission Delegated Directive (EU) 2017/593 of 7 April 2016.
[85] See Art. 16(9) MiFID II, as further elaborated in Arts. 2 to 8 of Commission Delegated Directive (EU) 2017/593 of 7 April 2016.
[86] Art. 41(2) MiFID II.
[87] Ibid.
[88] Art. 41(5) MiFID II.
[89] Art. 39(2), sub (c) MiFID II.
[90] Art. 41(2) MiFID II.
[91] Ibid.

3.2.3.2 Difficulties in the Supervision of a Branch From the above it follows that a branch of a third country firm authorised on the basis of MiFID II must comply with numerous requirements under MiFID II and MIFIR and possibly prudential requirements under national law. Such authorisation and ongoing requirements at the level of a third country branch are in stark contrast to intra-EU situations where the requirements imposed on a branch are, based on the premise of mutual recognition, rather limited. Indeed, the substantial requirements imposed on a branch of a third country firm render the use of a branch to gain market access somewhat similar to a situation where a third country firm establishes a subsidiary with full authorisation in the EU.

However, there are (and remain) some key differences between a branch and a subsidiary. Most notably, a branch, in contrast to a subsidiary, does not have legal personality. Instead, it is part of the third country firm. It is therefore difficult to apply requirements solely at the level of the branch.[92] After all, it is the legal entity – established in the third country – that determines and is responsible for the behaviour of the branch. For the same reasons, a branch will not issue capital instruments and will most likely not hold separate capital or liquidity at branch level.

3.2.3.3 CRD6 Proposal In light of these difficulties, it is of interest to note the CRD6 reforms as regards market access for third country banks, as recently proposed by the Commission.[93] As discussed in Sect. 2.3.1, under the CRD6 proposal, the provision of core banking services in the Union requires, with a few exceptions, a third country bank to establish a physical presence in a Member State through a branch or a subsidiary. According to the Commission such physical presence is required as a prerequisite for effective prudential regulation and supervision in the Union.[94] However, as set out in Sect. 2.3.1, the third country regime under the CRD6 proposal does not apply to a third country bank when it provides investment services and activities in the Union and any accommodating ancillary services such as related deposit taking, granting credit or loans. Consequently, for such third country banks, the third country regime under MiFID II and MIFIR remains relevant. Yet, it is of interest to briefly discuss the new regime under the CRD6 proposal as it provides more extensive (prudential) requirements at branch level, potentially inspiring similar developments within the MiFID II optional branch regime.

Under the CRD6 proposal, the establishment of a third country branch is subject to prior authorisation in accordance with the minimum conditions provided by the CRD6 proposal.[95] The minimum requirements regarding third country branches are

[92] The European Banking Authority (EBA) observed as regards the banking sector: 'Admittedly, since the [third country branch] is not a separate legal entity from the [third country bank], more robust and autonomous forms of risk capitalisation (CRR-like) may prove difficult/impossible to determine and implement at the [third country branch] level. For loss absorption purposes, the majority of [competent authorities] ultimately rely on the [third country bank]'s capital position, coupled with effective supervision and cooperation with the [third country home authority].' In our view, the same applies *mutatis mutandis* to EU branches of third country investment firms. See EBA (2021), p 62.

[93] Binder (2024).

[94] See Explanatory Memorandum to the CRD6 proposal, p 13.

[95] Art. 48c CRD6 proposal.

relative to the risk that they pose to the financial stability and market integrity of the Union and the Member States. Consequently, third country branches are categorised as either class 1, where they are deemed riskier, or, otherwise, as class 2, where they are small and non-complex and do not pose a significant financial stability risk.[96] Third country branches will classify as class 1 if they meet any of the following conditions:

- The total value of the assets booked or originated by the third country branch in the Member State is equal to or higher than EUR 5 billion;[97]
- The third country branch's authorised activities include taking deposits or other repayable funds from retail customers, provided that the amount of such deposits and other repayable funds is equal to or higher than 5% of the total liabilities of the third country branch or the amount of such deposits and other repayable funds exceeds EUR 50 million;[98] or
- The third country branch is not a qualifying third country branch.

Third country branches that do not meet any of these conditions are classified as class 2 branches.[99]

Class 1 branches must maintain a minimum capital endowment that is at least equal to 2.5% of the branch's average liabilities or, for newly authorised third country branches, of the branch's liabilities at the time of authorisation, subject to a minimum of EUR 10 million.[100] Class 2 third country branches must maintain 0.5% of the branch's average liabilities, or, for newly authorised third country branches, of the branch's liabilities at the time of authorisation, subject to a minimum of EUR 5 million.[101] Third country branches must fulfil the minimum capital endowment requirement with assets in the form of cash or cash assimilated instruments, debt securities issued by central governments or central banks of Member States, or any other instrument that is available to the third country branch for unrestricted and immediate use to cover risks or losses as soon as those occur.[102] The branch is required to deposit the capital endowment instruments in an escrow account with a

[96] Recital (23) CRD6 proposal.

[97] Art. 48a(1)(a) CRD6 proposal.

[98] Art. 48a(1)(b) CRD6 proposal.

[99] A branch is a 'qualifying third country branch' if:

- the head undertaking of the branch is established in a country that applies prudential standards and a supervisory oversight that are at least equivalent to CRD and CRR;
- the supervisory authorities of the branch's head undertaking are subject to confidentiality requirements that are at least equivalent to CRD; and
- the country where the third country branch's head undertaking is established is not listed as a high-risk third country that has strategic deficiencies in its regime on anti-money laundering and counter terrorist financing, in accordance with Art. 9 of Directive (EU) 2015/849 of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (Fourth AML Directive). See Arts. 48a(1)(c) and 48b CRD6 proposal.

[100] Art. 48e(1)(a) CRD6 proposal.

[101] Art. 48e(1)(b) CRD6 proposal.

[102] Art. 48e(2) CRD6 proposal.

bank in the Member State where the branch is authorised and that is not part of its head undertaking's group or, where permitted under national law, with the central bank of the Member State.[103] The capital endowment instruments deposited in an escrow account must be available for use for the purposes of the resolution of the branch as provided under Article 96 BRRD[104] in the case of resolution of the third country branch and for the purposes of the winding-up of the third country branch in accordance with the national law of the Member State.[105]

Third country branches are also subject to minimum liquidity requirements. They must maintain at all times a volume of unencumbered and liquid assets sufficient to cover liquidity outflows over a minimum period of 30 days.[106] Class 1 third country branches must comply with the liquidity coverage requirement laid down in Part Six, Title I CRR, and LCR.[107,108] The third country branches must deposit these liquid assets in an account held in the Member State where the branch is authorised with a bank that is not part of its head undertaking's group or, where permitted under national law, with the central bank of the Member State.[109]

Besides the minimum capital endowment and the liquidity requirements, the CRD6 proposal introduces a number of additional prudential requirements for third country branches. These include internal governance and risk controls at branch level,[110] along with the requirement that the branch must have at least two persons in the relevant Member State effectively directing its business.[111] The competent authorities must conduct a supervisory review and evaluation ('SREP'), with a frequency and intensity proportionate to the classification of the branch and other relevant criteria, such as the nature, scale and complexity of its activities.[112] Finally, the CRD6 proposal requires that the competent authorities possess a minimum list of supervisory measures and powers.[113] These may be used to ensure that the third country branches comply with the requirements under CRD6 and national law, and to ensure that the material risks that the third country branches are exposed to are covered and managed in a sound and sufficient manner and that those branches remain viable.[114]

103 See Art. 48e(3) CRD6 proposal.

104 Directive 2014/59/EU of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms.

105 See Art. 48e(3) CRD6 proposal.

106 See Art. 48f(1) CRD6 proposal.

107 Commission Delegated Regulation (EU) 2015/61 of 10 October 2014 to supplement Regulation (EU) No 575/2013 of the European Parliament and the Council with regard to liquidity coverage requirement for Credit Institutions.

108 See Art. 48f(2) CRD6 proposal.

109 See Art. 48f(3) CRD6 proposal.

110 See for class 1 branches Art. 48h(2) and for class 2 branches Art. 48h(3) CRD6 proposal.

111 Those persons must be of good repute and possess sufficient knowledge, skills and experience and commit sufficient time to the performance of their duties, and are subject to prior approval by the competent authorities. Art. 48h(1) CRD6 proposal.

112 Art. 48o CRD6 proposal.

113 Art. 48p(2) CRD6 proposal.

114 Art. 48p(1) CRD6 proposal.

While these new prudential requirements under CRD6 may alleviate some concerns connected with the imposition of prudential requirements at branch level, questions remain regarding their effectiveness.[115] It is therefore of interest to note that the CRD6 proposal empowers competent authorities to require, on a case-by-case basis, third country branches that pose a significant risk to the financial stability of the Union or of the Member State to apply for a full bank authorisation.[116] This effectively implies that the third country bank must establish a subsidiary authorised with a banking license under CRD to continue conducting banking activities in the Member State and the EU.

3.3 The Equivalence Regime

The equivalence regime for third country firms was introduced in Articles 46–49 MiFIR, following which it was updated quite significantly as part of the new prudential regime for investment firms set out in IFR. This section discusses the most important updates of the equivalence regime. However, it should be noted that despite this updated version, the regime is still not active, since the Commission has not taken any equivalence decisions yet. As a result, the market access and supervision of third country firms providing services to professional clients is still a national matter. [117]The following discussion of the equivalence regime is therefore only theoretical as there is no practical experience with the regime yet.

[115] Binder (2024).

[116] Competent authorities have the power to require third country branches to apply for authorisation, at least where:

- the third country branch has engaged in the past or is currently engaged in the performance of core banking activities—with the exception of intragroup funding transactions concluded with other third country branches of the same head undertaking and transactions entered into on a reverse solicitation basis—with customers or counterparties in other Member States.
- the third country branch meets the systemic importance indicators for ‘other systemically important institutions (or ‘O-SII’)’ as referred to in Art. 131(3) CRD or is assessed as being of systemic importance in accordance with Art. 48k(3) CRD and poses significant financial stability risks in the Union or the Member state where it is established; or
- the aggregate amount of the assets of all third country branches in the Union which belong to the same third country group is equal to or higher than EUR 40 billion or the amount of the third country branch assets on their book in the Member State where it is established is equal to or higher than EUR 10 billion.

However, before the competent authority may use this power, it must first assess the systemic importance and consider imposing requirements to address identified risks of the third country branch (Art. 48k CRD6 proposal), or make use of supervisory measures or powers (Art. 48p CRD6 proposal), as appropriate. Alternatively, the competent authority must be able to justify, based on grounds other than those listed under the three bullets above, that such measures would be insufficient to address the material supervisory concerns. Before requiring a branch to apply for authorisation, the competent authorities must consult EBA and other competent authorities where the third country group has established other branches or subsidiary institutions. See Art. 48j CRD6 proposal.

[117] See also Recital (41) MiFIR.

3.3.1 The Equivalence Assessment 2.0

Article 47 MiFIR contains the framework for the equivalence assessment by the Commission. This framework has been updated in several respects. First, the Commission can now also restrict its equivalence decision to certain services. [118] As a result, when a third country is considered equivalent by the Commission, it may still not be possible to obtain an ESMA registration for a third country firm established in this country if the equivalence decision does not cover the services provided by that firm.

In addition, the scope of the EU framework that is taken into account by the Commission to establish equivalence has been widened. The Commission now also assesses whether third country firms comply with legally binding prudential, organisational and business conduct requirements which have equivalent effect to the requirements set out in CRR, IFR and IFD, in addition to CRD IV, MiFID II and MiFIR. Considering that IFR and IFD include the new prudential regime for investment firms, it is logical that these acts have been added. It is not clear why CRR was not included in the original text of Article 47 MiFIR. It may be that it was considered to be too extensive or burdensome at that time to check whether a third country regime has equivalent effect to CRR. In our view it is good that CRR has been added, since it contains core elements of prudential supervision, albeit that the relevance of CRR for investment firms became more limited due to the introduction of IFR. Another new element is that the Commission considers not only the prudential and business conduct requirements, but also the *organisational* requirements set out in these legislative acts.[119]

In addition to considering the equivalent effect of the third country framework, the Commission now also assesses whether third country firms are subject to effective supervision and enforcement ensuring compliance with the applicable legally binding prudential, organisational and business conduct requirements. [120] As a result of this extension of the equivalence assessment, it is now checked three times whether a third country firm is subject to effective supervision and enforcement. Article 47(1b) MiFIR requires that a third country framework may only be considered to have equivalent effect, as meant in Article 47(1)(a) MiFIR, where that framework fulfils a number of conditions, including that third country firms are subject to authorisation and to effective supervision and enforcement on an ongoing basis. In addition, ESMA can only register a third country firm when the firm is authorised and is subject to effective supervision and enforcement ensuring full compliance with the requirements applicable in that third country.[121] It is not entirely clear whether this actually means that three different tests are being done. Although the wording of the three tests is slightly different, we would be very surprised if the three tests could have a different outcome.

[118] Art. 46(4), last paragraph MiFIR.
[119] Art. 47(1), under (a) MiFIR.
[120] Art. 47(1), under (b) MiFIR.
[121] Art. 46(2), under (b) MiFIR.

Furthermore, the Commission should now also take into account, when adopting the equivalence decision, whether the third country is identified as a non-cooperative jurisdiction for tax purposes under the relevant Union policy or as a high-risk third country pursuant to Article 9(2) Fourth AML Directive. This is not part of the equivalence assessment itself. It therefore seems that the Commission may still adopt an equivalence decision, even if the third country is identified as a non-cooperative jurisdiction or a high-risk third country.[122] Whether that is desirable is another question of course.

Lastly, when considering the equivalent effect of the third country framework, the Commission should specifically consider in relation to third country firms that deal on own account or conduct placement activities on a firm commitment basis whether they are subject to *comparable* capital requirements to those that would apply if they were established in the Union. For third country firms providing other services, the Commission should only consider whether they are subject to *sufficient* capital requirements. Also, the Commission should now generally consider whether third country firms are subject to adequate business conduct and organisational requirements, where in the previous framework this was restricted to conduct of business rules and organisational requirements *in the area of internal control functions*.[123]

3.3.2 Systemic Importance

Another new aspect is the strengthened regime in case the scale and scope of the services provided by third country firms in the Union following the adoption of an equivalence decision are likely to be of systemic importance for the Union. In that case, the legally binding prudential, organisational and business conduct requirements may only be considered by the Commission to have equivalent effect *after a detailed and granular assessment*.[124] To that end, the Commission should also assess and take into account the supervisory convergence between the third country concerned and the Union. Apparently, this is not something that the Commission has to do when conducting the assessment in relation to a third country where the scale and scope of the services are *not* likely to be of systemic importance. This makes the assessment of whether such scale and scope are likely to be of systemic importance very relevant. The Commission is empowered to adopt delegated acts further specifying the circumstances under which such scale and scope of the services are likely to be of systemic importance to the Union.[125] Currently, it is not known yet for which countries this may be the case. One could however expect that the UK, the US and China may be amongst these countries.

Where the scale and scope of the services are likely to be of systemic importance for the EU, the Commission *may* attach specific operational conditions to equivalence decisions so as to ensure that ESMA and national competent authorities have the necessary tools to prevent regulatory arbitrage and monitor the activities

[122] Art. 47(1a), last paragraph MiFIR.
[123] Art. 47(1b) MiFIR.
[124] Art. 47(1), last paragraph MiFIR. See also Recital (45) IFR.
[125] Art. 47(1a) MiFIR.

of third country firms registered by ESMA in respect of services provided in the Union. These specific operational conditions may entail that those firms comply with certain requirements relating to post-trade disclosure, reporting and trading obligations.[126]

3.3.3 The Application for an ESMA Registration

In relation to the ESMA registration following the adoption of an equivalence decision, there have also been some updates. First, the conditions for registration have been extended. In order to be able to be registered, the third country firm now also has to have established the necessary arrangements and procedures to report certain information to ESMA (see Sect. 3.3.4).[127] In addition, the specifics of the cooperation arrangements that ESMA enters into with the relevant competent authorities of third countries that are considered equivalent have been updated. These cooperation arrangements should now also specify, where relevant, the arrangements for the onward sharing by ESMA of information with competent authorities of the Member States (see Sect. 3.3.5). In addition, the requirements set in relation to the procedures concerning the coordination of supervisory activities are more extensive. Lastly, the cooperation arrangements should also provide for procedures concerning a request for information that ESMA may submit to a registered third country firm.[128]

Most importantly, however, the scope of information that has to be provided with the application for an ESMA registration will be much more extensive. Currently, Article 1 of Commission Delegated Regulation (EU) 2016/2022 of 14 July 2016 sets out the information necessary for the registration. This basically includes contact details, information on the supervision in the home country and information on which services will be provided in the Union. From the final report published by ESMA on 28 September 2020[129] it can however be deduced that ESMA proposed a new delegated regulation in which the information to be provided for the registration application will be much more extensive. ESMA considers this necessary taking into account its increased responsibilities after registration (see Sect. 3.3.5) and the list of information that third country firms have to provide on an annual basis after registration (see Sect. 3.3.4).[130] Commission Delegated Regulation (EU) 2016/2022 has not been repealed yet.

3.3.4 Obligations After ESMA Registration

The obligations for third country firms registered by ESMA following an equivalence decision by the Commission were strengthened.[131] A new annual reporting obligation was introduced on the basis of which registered third country firms need

126 Arts. 47(1a), second paragraph, and 47(1b), last paragraph MiFIR.
127 Art. 46(2), under (d) MiFIR.
128 Art. 47(2) MiFIR.
129 ESMA (2020), Annex I.
130 Ibid., point 18, p 9.
131 Recital (43) IFR.

to inform ESMA on, *inter alia*, the scale and scope of the services provided in the Union, the turnover and aggregated value of the assets, whether investor protection arrangements have been taken, the risk management policy and arrangements, the governance arrangements and any other information necessary to enable ESMA or the competent authorities to carry out their tasks in accordance with MiFIR.[132] In addition, third country firms should keep, at the disposal of ESMA, the data relating to all orders and all transactions in the EU in financial instruments which they have carried out, whether on own account or on behalf of a client, for a period of 5 years.[133]

What has not changed is Article 46(5) MiFIR, which requires that third country firms providing services in accordance with Article 46 shall inform clients established in the Union, in writing and in a prominent way, before the provision of any services that they are not allowed to provide services to clients other than professional clients and that they are not subject to supervision in the Union. They also have to indicate the name and address of the competent authority responsible for supervision in the third country. It is not clear what happens when third country firms do not comply with this information requirement. Potentially, ESMA could consider this to be acting in a manner which is clearly prejudicial to the interests of investors or the orderly functioning of markets (see further Sect. 3.3.5). In addition, it is still not entirely clear whether this requirement only applies when investment firms act under an ESMA registration, or also when they act under a national regime in accordance with Article 46(4), last paragraph MiFIR.

3.3.5 New Responsibilities and Powers for ESMA and National Competent Authorities

ESMA's new responsibility under the updated equivalence regime entails that it shall monitor the regulatory and supervisory developments, the enforcement practices and other relevant market developments in third countries for which equivalence decisions have been adopted by the Commission in order to verify that the conditions on the basis of which those decisions have been taken are still fulfilled. It will submit a confidential report on its findings to the Commission on an annual basis. The Commission will subsequently submit a report to the European Parliament and the Council at least on an annual basis.[134]

In addition, ESMA has new powers. It may conduct on-site inspections.[135] Furthermore, it may temporarily prohibit or restrict a third country firm from providing services where the third country firm has failed to comply with any product intervention measures taken by ESMA, EBA or a national competent authority, where it has failed to comply with an information request from ESMA in due time and a proper manner, or where it does not cooperate with an investigation or an on-site

132 Art. 46(6a) MiFIR.
133 Art. 46(6b) MiFIR.
134 Art. 47(5) MiFIR.
135 Art. 47(2) MiFIR.

inspection.[136] In addition, ESMA has to withdraw the registration of a third country firm where ESMA has referred the matter to the competent authority of the third country, and that competent authority has (i) not taken the appropriate measures needed to protect investors or the proper functioning of the markets in the Union, or (ii) failed to demonstrate that the third country firm complies with the requirements applicable to it in the third country or, (iii) with the conditions under which a decision in accordance with Article 47(1) MiFIR has been adopted. However, ESMA may only take such a withdrawal decision where it has well-founded reasons to believe that the third country firm *either* is acting in a manner which is clearly prejudicial to the interests of investors or the orderly functioning of markets, *or* has seriously infringed the provisions which are applicable to it in the third country and which are relevant for the equivalence assessment.[137]

Another interesting aspect of the updated equivalence regime is the new role of national competent authorities. One would think that there is no such role, since the registration is done with ESMA and after registration Member States shall not impose any additional requirements on the third country firm in respect of matters covered by MiFIR or MiFID II.[138] However, this is not the case. They cooperate with ESMA in investigations and on-site inspections. National competent authorities—of the Member States in which the third country firms are active—also get access to the information that ESMA receives from the third country firms. They may also request ESMA to ask third country firms to provide any further information in respect of their operations. ESMA should also access the relevant data kept at its disposal, and make such data available to a national competent authority upon its request.[139] Lastly, national competent authorities may prohibit or restrict (i) the marketing, distribution or sale of certain financial instruments or structured deposits or financial instruments or structured deposits with certain specified features, or (ii) a type of financial activity or practice by a registered third country firm.[140]

4 Equivalence Is Dead, Long Live Equivalence?

The third country regime under MiFID II/MiFIR can hardly be called successful. No third country has been considered equivalent yet by the Commission. Therefore, third country firms cannot make use of an ESMA registration to provide services to professional clients throughout the EU. This is despite the high hopes that the regime

> should harmonise the existing fragmented framework, ensure certainty and uniform treatment of third-country firms accessing the Union, ensure that an assessment of effective equivalence has been carried out by the Commission in relation to the prudential and business conduct framework of third countries,

[136] Arts. 49(1) and 46(6c) MiFIR.
[137] Arts. 49(2) MiFIR and 46(6c) MiFIR.
[138] Art. 46(3) MiFIR.
[139] Art. 46(6a) and (6b) MiFIR.
[140] Arts. 1(4a) and 42 MiFIR.

> and should provide for a comparable level of protection to clients in the Union receiving services by third-country firms.[141]

In addition, only around 50 third country firms, most of which are banks, have established an authorised branch in the EU to provide services to retail clients under the MiFID II optional branch regime.

The updated version of the third country regime for the provision of services to professional clients makes it even more difficult to establish equivalence and less attractive to apply for an ESMA registration. One might even wonder what the value of equivalence still is, since the application for the registration and the subsequent ongoing obligations are increasingly comparable to having an EU subsidiary. In addition, in respect of the third country regime for the provision of services to retail clients, the optional branch regime under MiFID II does not include or consider any (potential) equivalence determinations. Instead, the optional branch regime is much akin to a full license requirement, albeit with notable difficulties when it comes to supervising and enforcing the substantial requirements at branch level. At the time of writing this article, we do not anticipate any change in the foreseeable future.[142] It is however noteworthy that the new CRD 6 proposal provides quite an extensive harmonisation of the market access criteria for third country banks that wish to provide core banking activities in a Member State. This framework, however, is not applicable to third country banks that provide investment services or activities in the EU and accommodating ancillary services. Nevertheless, it may serve as inspiration for potential future harmonisation of the MiFID II optional branch regime.

As it stands, the conditions governing access to the European market for third country firms remain for a large part provided by national law, with one exception, i.e., where Member States have chosen to apply the optional regime for the provision of services to retail clients.[143] A Member State may therefore provide market access based on (national) equivalence—but it may also subject third country firms to full authorisation, exempt them from authorisation and other requirements, or provide no market access at all.[144] Hence, while the equivalence regime in MiFIR seems to be dead,[145] equivalence granted at Member State level may be the viable option.

[141] Recital (41) MiFIR.

[142] On 25 November 2021, two proposals were published for review of MiFID II and MiFIR. At the time of writing this article, these proposals are still awaiting Parliament's position in first reading. https://oeil.secure.europarl.europa.eu/oeil/popups/ficheprocedure.do?reference=2021/0384(COD)&l=en and https://oeil.secure.europarl.europa.eu/oeil/popups/ficheprocedure.do?reference=2021/0385(COD)&l=en (last accessed on 4 January 2024). They do not provide for any changes of the third country regime.

[143] Art. 39 MiFID II.

[144] E.g., the Netherlands exempts third country firms established in Australia, the USA and Switzerland from the authorisation requirement. This regime applies to the provision of investment services to professional clients and to the investment activity of dealing on own account (Art. 10 Exemption Regulation AFS). Luxembourg provides market access to third country firms that are subject to supervision and authorisation rules that the *Commission de Surveillance du Secteur Financier* (CSSF) deems equivalent to those laid down in the Law on the Financial Sector (CSSF (2020)). Germany, which has not exercised the Member State option of Art. 39 MiFID II, provides for an exemption from German licensing and other requirements for third country firms 'as long as the undertaking, due to the nature of business it conducts, does not require supervision in this regard' (Pitz and Nemeczek (2021), p 60).

[145] Pennesi (2022), p 140.

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