MFSA

MALTA FINANCIAL SERVICES AUTHORITY

CIRCULAR ON MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE ('MIFID II') AND MARKETS IN FINANCIAL INSTRUMENTS REGULATIONS ('MIFIR')

Spots and Foreign Exchange (FX) Forward Contracts and their scope in MiFID II

1.0 Introduction

Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing MiFID II, Directive 2014/65/EU of the European Parliament and of the Council (the 'Delegated Regulation') clarifies the scope and includes definitions in relation to the circumstances under which derivative contracts relating to currencies should be considered financial instruments as well as the meaning of spot contracts for currencies.

2.0 Spots and Forward Contracts - MiFID II

Derivative contracts relating to currencies are only excluded from application of MiFID II if they meet all the criteria provided in Article 10(1) of the Delegated Regulation. Accordingly, in assessing whether the dealings in foreign exchange would fall under the MiFID II regime, a company should analyse whether the instruments it deals with satisfy the requirements of the aforementioned article, namely:-

Derivative contracts relating to a currency shall not be a financial instrument where the contract is a spot contract or a means of payment that:

i. must be settled physically otherwise than by reason of a default or other termination event;
ii. is entered into by at least a person which is not a financial counterparty within the meaning of Article 2(8) of Regulation (EU) No 648/2012 of the European Parliament and of the Council ('EMIR');
iii. is entered into in order to facilitate payment for identifiable goods, services or direct investment; and
iv. is not traded on a trading venue.

In terms of Article 10(2) of the Delegated Regulation, a spot contract shall be a contract for the exchange of one currency against another currency, under the terms of which delivery is scheduled to be made within the longer of the following periods:

a. 2 trading days in respect of any pair of the major currencies set out in Article 10(3) of the Delegated Regulation;

b. for any pair of currencies where at least one currency is not a major currency, the longer of 2 trading days or the period generally accepted in the market for that currency pair as the standard delivery period;

c. where the contract for the exchange of those currencies is used for the main purpose of the sale or purchase of a transferable security or a unit in a collective investment undertaking, the period generally accepted in the market for the settlement of that transferable security or a unit in a collective investment undertaking as the standard delivery period or 5 trading days, whichever is shorter.

The Delegated Regulation states that a contract shall not be considered a spot contract where, irrespective of its explicit terms, there is an understanding between the parties to the contract that delivery of the currency is to be postponed and not to be performed within the period set out in the first subparagraph of Article 10(2).

3.0 Way Forward

Please note that those derivative contracts that do not satisfy the requirements of Article 10(1) of the Delegated Regulation, qualify as 'financial instrument' in terms of Section C (4) of Annex I of MiFID II.

Consequently companies trading in such transactions will either have to provide a representation that all their FX transactions fall within the exclusion contained in Article 10(1) of the Delegated Regulation, or comply with EMIR and MiFID II obligations, as the case may be.

Contacts

Should you have any queries relating to the above please contact the Authority on MarketInfrastructures@mfsa.com.mt

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