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Briefing note

International Regulatory Update

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- Recent Clifford Chance Briefings: ESMA publishes details of New Disclosure Regime for Structured Finance Instruments; and more. Follow this link to the briefings section.

EU Council agrees position on European long-term investment funds

The Permanent Representatives Committee, on behalf of the EU Council, has agreed its position on a proposed regulation on European long-term investment funds. The regulation aims to increase the pool of capital available for long-term investment into the EU economy by creating a new form of fund vehicle. The Committee has invited the incoming Italian Council Presidency to start negotiations with the EU Parliament to enable adoption of the text at first reading.

CRD 4: Implementing Regulation on information disclosure by competent authorities published in Official Journal

Commission Implementing Regulation (EU) No 650/2014 laying down implementing technical standards with regard to the format, structure, contents list and annual publication date of the information to be disclosed by competent authorities under the Capital Requirements Directive (CRD 4) has been published in the Official Journal.

The Implementing Regulation will enter into force on 15 July 2014.

AIFMD: Delegated Regulation determining types of alternative investment fund managers published in Official Journal

Commission Delegated Regulation (EU) No 694/2014 of 17 December 2013 supplementing the Alternative Investment Fund Managers Directive (AIFMD) with regard to regulatory technical standards determining types of alternative investment fund managers has been published in the Official Journal.

The Delegated Regulation will enter into force on 14 July 2014.

AIFMD: ESMA publishes model MoU guidelines compliance table

The European Securities and Markets Authority (ESMA) has published a table showing which national regulatory authorities comply or intend to comply with ESMA's guidelines on the model memorandum of understanding (MoU) concerning consultation, cooperation and the exchange of information related to the supervision of AIFMD entities.

The table shows that all Member States have complied or intend to comply, with the exception of Slovenia. As a consequence of late transposition of the AIFMD, the guidelines are not applicable to Slovenia as no competent authority has been designated under Article 44 of the AIFMD.

The table also shows that Gibraltar, a European territory for whose external relations the UK is responsible, has not responded to ESMA.

Rating agencies: ESMA publishes draft RTS on transparency requirements

ESMA has published its final report on draft Regulatory Technical Standards (RTS) required under the Credit Rating Agencies (CRA3) Regulation. The draft RTS cover:

- disclosure requirements on structured finance instruments;
- the European Rating Platform; and
- periodic reporting fees charged by credit rating agencies.

The EU Commission has three months to decide whether to endorse the draft RTS.

EBA publishes final draft RTS on professional indemnity insurance for mortgage credit intermediaries

The European Banking Authority (EBA) has published its final draft RTS on the minimum monetary amount of the professional indemnity insurance (PII) or comparable guarantee for mortgage credit intermediaries under the Mortgage Credit Directive (MCD). The RTS specify the minimum amount for each claim and an aggregate annual amount for all claims based on seven consultation responses that identified an average amount set by Member States currently requiring PII, or a comparable guarantee, for mortgage credit intermediaries.

The EBA will review the RTS by 21 March 2018 and biannually thereafter.

EBA consults on RTS on use of internal ratings based approach

The EBA has launched a consultation on draft RTS on the sequential implementation of the Internal Ratings Based (IRB) approach and permanent partial use of the Standardised Approach (SA) under the Capital Requirements Regulation (CRR). Under the CRR, institutions must implement the IRB Approach for all exposures unless a competent authority gives permission to permanently use the SA. The RTS specify conditions for the permanent and temporary use of the SA by institutions that have received permission to use the IRB Approach, including:

- criteria to be used by institutions when applying the SA for the calculation of the capital requirements for credit risk;
- conditions on which competent authorities may allow institutions to use the SA permanently;
- the definition of a minimum level of exposure to be treated under the IRB approach; and
- the definition of maximum levels of exposure permanently allowed under the SA for certain classes.

EBA reports on impact of pension plans in capital

The EBA has published a report on the impact on volatility of own funds of revised International Accounting Standard for employee benefits (IAS 19) and the deduction of defined benefit pension assets from own funds in accordance with the CRR.

The report sets out:

- the accounting and regulatory changes relevant to the assessment;
- a quantitative assessment of the impact on the volatility of own funds during a specific time period; and
- additional considerations about variables in relation to defined benefit pension funds that could impact on the volatility of own funds in the future.

The report has been prepared under a mandate in the CRR and the EU Commission will take it into account when reporting to the EU Parliament and EU Council about this issue by 31 December 2014.

Basel Committee consults on revisions to Pillar 3 disclosure requirements

The Basel Committee on Banking Supervision has published a consultation paper on Pillar 3 disclosure requirements and intends to replace the existing Pillar 3 framework once the proposed new standard has been finalised. The review responds to perceived inadequacies in the existing framework, in particular those requirements related to risk-weighted assets (RWA), and the proposed framework is intended to enable market participants to compare banks' disclosures of the capital ratio's denominator and to assess more effectively a bank's overall capital adequacy.

Comments are due by 26 September 2014. The consultation is the first phase of the Committee's review of disclosure requirements. A second phase will consider standards and additional disclosure requirements.

Basel Committee publishes revised principles for supervisory colleges

The Basel Committee on Banking Supervision has published revised principles for effective supervisory colleges, which discuss expectations in relation to the colleges of supervisors among the authorities responsible for supervision of cross-border banking groups. The principles set out objectives, governance, communication issues and potential areas for collaboration and information-sharing among home and host supervisors: a cross-border entity's home supervisor and the supervisors of jurisdictions hosting branches. The Committee published its 'Good Practice Principles on Supervisory Colleges' in 2010 and the revised principles retain the key features of those principles but draw on consultations with supervisors and internationally active banks to clarify the relationship between home and host supervisors.

The key changes to the principles include:

- a greater emphasis on collaboration and information-sharing among college members and between home and host supervisors;
- the inclusion of a new expectation regarding the need to balance core college effectiveness with host involvement;
- encouragement for greater consistency in providing feedback to banks;
- differentiation between colleges and crisis-management groups (CMGs) for banks that are subject to both structures; and
- alignment across the principles on how macro-prudential information is shared and used.

IOSCO reports on risk identification for securities regulators

The International Organization of Securities Commission (IOSCO) has published a report on risk identification and assessment methodologies for securities regulators. The paper provides a practical overview of the different methods that IOSCO and national regulators have developed and implemented through concrete examples of the methods currently employed by members of the Committee on Emerging Risks (CER). In particular, the paper discusses:

- commonly used definitions of systemic risk;
- IOSCO risk identification methods;
- the range of methods implemented at the national level by CER members; and
- an analytical framework for assessing whether or not a risk, trend or vulnerability is systemic.

FCA seeks views on recovering costs of processing applications for authorisation through fees

The Financial Conduct Authority (FCA) has published a discussion paper on how it recovers the costs of administering the regulatory gateway through application fees. The existing fee structure was set by the Financial Services Authority (FSA), which was succeeded by the FCA and Prudential Regulation Authority (PRA) on 1 April 2013. The FSA policy has not changed since 2000 and application rates remain largely unchanged since 2001, meaning that fees have decreased by 36% as they have not been adjusted for inflation.

The discussion paper seeks views among the 18,500 firms that constitute the FCA's 'A' fee-block on:

- operating the regulatory gateway;
- distributing the recovery of authorisation costs between different fee-payers; and
- suggestions for revising application fees.

Comments on the discussion paper are due by 22 August 2014.

Following this engagement with stakeholders, the FCA intends to consult on proposals to be introduced from 1 April 2015. When proposals are prepared for consultation, the FCA will consider whether there are implications for other types of firm not included in this exercise, including payment services providers, electronic money issuers, issuers and sponsors of securities and mutual societies. The PRA is engaging in this FCA exercise and also intends to consult on application fees in October 2014.

PRA consults on implementation of loan-to-income ratio limit for mortgage lending

The PRA has published a consultation paper (CP11/14) on proposed rules to implement the Financial Policy Committee's recommendation on loan to income ratios in mortgage lending. The recommendation is addressed to the PRA and the Financial Conduct Authority and asks them to ensure that mortgage lenders limit the number of mortgage loans made at or greater than 4.5 times LTI to no more than 15% of their overall number of mortgage loans.

Comments are due by 31 August 2014 and final rules will come into effect on 1 October 2014.

Bank ring-fencing: Draft statutory instruments on core and excluded activities published

The draft Financial Services and Markets Act 2000 (Ring-fenced Bodies and Core Activities) Order 2014 and draft Financial Services and Markets Act 2000 (Excluded Activities and Prohibitions) Order 2014 have been published.

The Ring-fenced Bodies and Core Activities Order will define the circumstances under which a UK institution accepting a deposit is not carrying out a core activity under the Financial Services and Markets Act 2000 (FSMA), which specifies that UK institutions carrying out one or more core activities are ring-fenced bodies. This will enable some deposits to be held by banks that are not ring-fenced bodies and will exempt certain banks from the definition of 'ring-fenced body' under FSMA.

FSMA specifies the regulated activity of dealing in investments as principal as an excluded activity that a ring-fenced body is not permitted to carry out, except in circumstances specified by the Treasury. The Excluded Activities and Prohibitions Order specifies a number of cases in which ring-fenced bodies will be permitted to deal in investments in principal, and imposes a number of prohibitions (subject to exceptions) on what ring-fenced bodies may do.

German Federal Parliament enacts amendments to German Capital Investment Act

The German Federal Parliament (Bundestag) has approved the Financial Market Adaptation Law (Finanzmarktanpassungsgesetz). Amongst other things, the Financial Market Adaptation Law amends the German Capital Investment Act (Kapitalanlagegesetzbuch, KAGB), which implemented the AIFMD into German law.

The main topic of the KAGB amendment is to adjust and supplement definitions for open-ended and closed-ended AIFs to the respective specifications of the EU Commission as laid down in its Delegated Regulation (EU) 694/2014 of 17 December 2013 with regard to regulatory technical standards determining types of alternative investment fund managers. In deviation of the previous terminology of the KAGB and in order to comply with the terminology of the Delegated Regulation, an AIF will only be considered to be a closed-ended AIF if it does not allow for redemption or repurchase of the shares in the respective AIF prior to its liquidation phase or wind-down. Therefore in the future, a considerably higher amount of AIFs will qualify as open-ended AIF under the KAGB. With regard to grandfathered AIFs which have not conducted any additional investments after 22 July 2013, the grandfathering status will remain, if potential redemption rights are not exercisable after an initial period of at least 5 years. The Delegated Regulation will enter into force on 14 July 2014.

Another important topic of the KAGB amendment is that portfolio management, investment advice, fund related custody and administration services and investment brokerage may be conducted under the EU passport.

The amendments to the KAGB will enter into force after publication of the Financial Market Adaptation Law in the Federal Law Gazette (Bundesgesetzblatt).

AIFMD: Bank of Italy and CONSOB publish draft second-level regulation for implementation in Italy

The Bank of Italy and CONSOB have launched a consultation on draft regulations intended to align the existing second level regulations to Legislative Decree no. 58/1998 (Italian Financial Act), as amended by Legislative Decree no. 44/2014, which implemented the AIFMD in Italy. Once enacted, the draft regulations will amend the Bank of Italy Regulation on collective asset management dated 8 May 2012, the Bank of Italy Joint Regulation dated 29 October 2007, the CONSOB Regulation on issuers dated 14 May 1999 and the CONSOB Regulation on intermediaries dated 29 October 2007, currently in force.

Comments are due within 60 days of the date of publication of the consultation document (26 June 2014).

CSRC issues opinions to promote development of fund industry

In order to further promote the development of the fund management industry, the China Securities Regulatory Commission (CSRC) has issued the 'Opinions on Promoting Innovation and the Development of the Securities Investment Fund Industry', which set out the high-level strategies and policies to facilitate the growth of fund managers, support the innovation of fund products and reform the regulatory framework for funds.

Amongst other things, the opinions set out the following key initiatives:

- foreign investment shareholding restrictions on CSRC licensed fund management companies will be further relaxed when appropriate;
- mutual fund recognition with overseas securities markets (such as Hong Kong) will be promoted step by step;
- cross-listed fund products in domestic and overseas stock exchanges will be supported; and
- the Qualified Foreign Institutional Investors and Renminbi Qualified Foreign Institutional Investors programmes will be further expanded in terms of qualified applicants and investment scope.

MOFCOM issues notice to relax administration on foreign invested enterprises

The Ministry of Commerce (MOFCOM) has issued the 'Notice on Improving Foreign Investment Approval Administration', which is intended to apply the earlier State Council circular on reforming registered capital system and the amendments in the PRC Company Law to foreign invested enterprises (FIEs). In particular, the Notice provides that:

- restrictions on FIEs' initial capital contribution, capital contribution timeline, cash contribution, etc. will be removed;

- the minimum registered capital requirement will be removed except for those sectors specified by laws, regulations or the State Council;
- paid-in capital will no longer be verified by MOFCOM except for those sectors specified by the State Council;
- percentage requirements on total investment and registered capital will still apply; and
- all the FIEs approved prior to 1 March 2014 should follow the capital contribution under their original bylaws/contracts unless the investors apply with the competent MOFCOM authority for changes.

In addition, the Notice also provides for certain requirements on foreign investment statistics work.

CBRC issues circular to further relax approval requirements and pursue streamlined market access regime

The China Banking Regulatory Commission (CBRC) has issued the 'Circular on Certain Issues related to Promoting Relaxation of the Approval Process and Improving the Market Access Regime', as part of its efforts to relax existing approval requirements and improve efficiency of administrative procedures in the financial industry. Amongst other things, the Circular provides for the following:

- prior approvals for certain events (including extension of preparation period for setting up new institutions, delay in and business opening, institution downgrade, business suspension, QFII/RQFII custody business by Chinese funded commercial banks and rural commercial banks, etc.);
- the approval authority level for certain matters (such as establishment of provincial branches by certain type of commercial banks and qualification of chairmen/general managers of consumer finance companies, etc.) is downgraded to local CBRC agencies; and
- unified standards and procedures are emphasised for the market access regime.

HKMA issues new supervisory policy manual on recovery planning

Following consultation with industry associations, the Hong Kong Monetary Authority (HKMA) has issued a new supervisory policy manual (SPM) module on recovery planning as statutory guidance, by notice in the Gazette, under the Banking Ordinance. The SPM is based on the Financial Stability Board's 'Key Attributes of Effective Resolution Regimes for Financial Institutions', issued in November 2011, which include standards relating to the development of recovery and resolution plans for, at a minimum, financial institutions that could be systemically significant or critical if they were to fail.

The SPM provides guidance to authorised institutions on the key elements of effective recovery planning, and sets out the HKMA's approach to, and expectations in, reviewing authorised institutions' recovery plans. The guidance on resolution planning will be developed in the form of a new separate module for the SPM in due course.

The HKMA has indicated that it will adopt a phased approach to the implementation of recovery planning for authorised institutions, with priority given to those authorised institutions that are assessed to be more systemically significant or critical in Hong Kong. Those authorised institutions identified by the HKMA for inclusion in the 'first wave' of authorised institutions to generate recovery plans for review by the HKMA will be notified shortly and will be expected to submit a recovery plan within six months of that notification. Other authorised institutions will be informed of the subsequent 'waves' to which they have been ascribed and the timetable for submitting their recovery plans in due course.

SFC proposes greater flexibility for dissemination of prices and net asset values by authorised funds

The Securities and Futures Commission (SFC) has published proposals to amend its Code on Unit Trusts and Mutual Funds (UT Code) relating to the publication of offer and redemption prices or net asset values (NAVs), and notices of dealing suspension of collective investment schemes authorised by the SFC under the UT Code.

The SFC is proposing to:

- remove the requirement mandating the use of newspapers to publish prices or NAVs – instead the SFC will allow schemes to use any appropriate means to make public their prices or NAVs;
- require schemes to make public their prices or NAVs on every dealing day; and
- remove the requirement in the UT Code that mandates the use of a newspaper to publish a dealing suspension notice – instead, schemes can use any appropriate means to do this (the frequency of publication however will remain unchanged).

Subject to the comments received, the proposals above will apply to new collective investment schemes which are authorised by the SFC on and from the date such changes are published in the government gazette. A 6-month transitional period will apply to collective investment schemes which have been authorised by the SFC prior to the effective date and remain authorised on that date. They will be required to comply with the amendments within six months from the effective date.

The SFC has invited comments on the proposals by 23 July 2014.

FSA publishes amendment to clearing requirements for OTC derivatives transactions

The Financial Services Agency (FSA) has published an amendment to the ordinance and the administrative notice under the Financial Instruments and Exchange Act regarding the clearing requirements for OTC derivative transactions. The amendment follows a public consultation procedure based on a draft amendment published on 2 May 2014. The FSA has also published its responses to comments and questions received from the public on the draft.

In all material respects, the content of the finalised amendment is essentially the same as the draft. With the requirements currently applicable to certain credit default swaps and interest rate swaps (IRS), the amendment broadens the scope of application of the requirements for IRS in two ways.

Currently, only IRS on 3-month or 6-month JPY-LIBOR are subject to the requirements. The amendment adds, from 1 July 2014, 3-month and 6-month Euro-yen TIBOR (with maximum 5 and 10 years' duration, respectively).

The requirements generally apply to locally licensed Financial Instruments Business Operators (i.e. securities houses, investment managers and investment advisors) and Registered Financial Institutions (i.e. banks and other financial institutions). Currently, if the parties to a transaction (or their parents or subsidiaries) are not, on reasonable grounds, members of the same Central Counterparty Clearing House, then such parties are exempt from the requirements.

The draft amendment changes, from 1 December 2014, the eligibility criteria to receive an exemption from the requirements as follows:

- one party is not a Type I Financial Instruments Business Operator (i.e. securities house), a bank which is a Registered Financial Institution, DBJ, Shoko Chukin Bank, Shinkin Central Bank, or Nochu Bank; or
- the average outstanding notional amount of one party is, from 1 December 2014, less than JPY 1 trillion and, from 1 December 2015, less than JPY 300 billion.

Applicants who exceeded or ceased to exceed the above threshold must report the same to the FSA during a period between 1 April and 31 May each year. The first report is due by 19 August 2014 for applicants who exceeded the JPY 1 trillion threshold. The FSA will publish a list of those applicants whose notional reaches the threshold.

MAS consults on proposed framework for systemically important banks in Singapore

The Monetary Authority of Singapore (MAS) has launched a public consultation on the proposed framework for systemically important banks in Singapore. The MAS has proposed a framework to identify domestic systemically important banks (D-SIBs) in Singapore and address the risks they pose.

The consultation paper sets out the proposals for the D-SIB framework, including an outline of the methodology to be employed to assess the systemic importance of banks in Singapore and a range of policy measures that may apply to D-SIBs.

Comments on the consultation paper are due by 25 July 2014.

SEC adopts rules and guidance on cross-border application of its forthcoming regulations to govern security-based swap activity

The Securities Exchange Commission (SEC) has adopted rules and guidance on the cross-border application of regulations governing security-based swap activity, which the SEC has proposed pursuant to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act but has not yet finalized.

This rulemaking and guidance establishes criteria for determining whether an entity is a 'US person' and whether a cross-border securities-based swap transaction should be counted by a financial institution in calculating whether they exceed a specified threshold that would require registration with the SEC as a 'security-based swap dealer' or a 'major security-based swap participant.'

The SEC has also adopted a procedural framework to permit market participants subject to more than one set of comparable regulations across different jurisdictions to apply to the SEC for 'substituted compliance' relief. If the SEC were to grant a request for substituted compliance (after a public comment process), market participants would be permitted to satisfy specified US requirements by complying with the comparable non-US rules identified in the application.

This rulemaking implements a portion of the SEC's 2013 crossborder rulemaking proposal and represents the first in a series. Additional related rulemaking is expected in the near-term.

RECENT CLIFFORD CHANCE BRIEFINGS

ESMA publishes details of New Disclosure Regime for Structured Finance Instruments

On 24 June 2014, the European Securities and Markets Authority (ESMA) published its long-awaited final draft of the regulatory technical standards implementing the disclosure requirements imposed under Article 8b of the Credit Rating Agencies Regulation. These disclosure requirements apply to so-called 'structured finance instruments', which are defined to include any financial assets resulting from a securitisation, regardless of whether they are unrated, private, bilateral, intragroup or indeed not even a 'security' for regulatory purposes.

This briefing highlights the main changes to the RTS since the draft originally published for consultation and a few areas of concern that remain.

http://www.cliffordchance.com/briefings/2014/06/esma_publishes_detailsofnewdisclosureregim.html

When it's so broke, you can't fix it – The decision not to do business in highly corrupt countries

The collapse on 24 April 2013, of the garment factory in the Rana Plaza complex in Dhaka, Bangladesh, resulted in the death of more than 1,120 workers. A few months later, Nike Inc. announced its decision to sever ties with its key garment suppliers in Bangladesh, '[i]n effect, conced[ing] that problems outsourcing production to the country couldn't be easily fixed.' Transparency International described the challenge as 'a global garment supply chain bedeviled by endemic corruption.' But this problem is not unique to Bangladesh or the garment industry. There are countries and industries where corruption is so rampant and corporate compliance such a challenge that companies decide to exit the country or not enter it at all. So the question becomes, when does a company like Nike reach the point of knowing that 'it's so broke it can't be fixed?'

This briefing sets out a number of key factors for companies to consider when determining whether to enter or exit a market plagued with corruption.

http://www.cliffordchance.com/briefings/2014/06/when_it_s_so_brokeyoucantfixitth.html

Bribery risks for companies investing in Africa

Bribery risks in Africa are not necessarily different in kind from bribery risks in other jurisdictions, but there is a perception that bribery is more prevalent in many African countries.

As investors are increasingly drawn to the continent by a range of attractive opportunities – particularly in natural resources – they can also face challenges in the form of political unrest, security issues and corruption. The last ten years have also shown that prosecutors and regulators (particularly in the US) are not deterred from tackling investigations of conduct in Africa, by the challenges of investigating there and further, that they are not prepared to accept claims that 'that is how business is done here'.

This briefing discusses the issues surrounding investment in Africa.

http://www.cliffordchance.com/briefings/2014/06/bribery_risks_forcompaniesinvestinginafrica.html

Private Equity / leveraged buy-outs – Significant new changes deriving from the recent Draft Bill on the tax reform

The Draft Bill of the tax reform introduces significant limitations on the tax deductibility of interest deriving from acquisition debt. Said limitations will apply to scenarios in which a tax group is created, as well as to mergers taking place subsequent to the buyout.

This briefing comments on this new bill.

http://www.cliffordchance.com/briefings/2014/06/private_equity_leveragedbuy-outssignifican.html

FATCA – Russian Response

On 20 June 2014, the State Duma (the lower chamber of the Russian Parliament) adopted Federal Law 'On Specifics of Carrying Out Financial Transactions with Foreign Citizens and Legal Entities, on amendments to the Code of Administrative Offences and on Abolishment of Certain Legislative Acts of the Russian Federation' (FTFP Law). The FTFP Law seeks to address some of the FATCA compliance issues that have been faced by Russian financial institutions after the unilateral withdrawal of the US from signing the otherwise agreed Intergovernmental Agreement with Russia. The FTFP Law still needs to be approved by the Federation Council, signed into the law by the President and officially published, but it is likely that all these steps will be accomplished within the next few days.

This briefing sets out the key provisions of the FTFP Law.

http://www.cliffordchance.com/briefings/2014/06/fatca_russian_response.html

Singapore High Court finds that parties are presumed to have chosen the law of the seat as the proper law of the arbitration agreement

The Singapore High Court recently found in FirstLink Investments Corp Ltd v GT Payment Pte Ltd and others [2014] SGHCR 12 that where there is no express choice of law, the proper law of the arbitration agreement is generally the law of the seat (typically chosen out of a desire for neutrality), rather than the law of the substantive contract.

This briefing discusses this case.

http://www.cliffordchance.com/briefings/2014/06/singapore_high_courtfindsthatpartiesar.html

Sovereign pari passu clauses – NML Capital 2, Argentina 0

The US Supreme Court has declined to hear Argentina's appeal against a lower court's judgment on the effect of a pari passu clause in Argentina's bonds. This leaves in place the decision that if Argentina pays current interest on its restructured bonds, it must also pay its holdout creditors in full. This points the spotlight directly at Argentina. Argentina has so far flatly refused to pay the holdouts. Will it now default on the restructured bonds, try to negotiate a settlement with holdouts or does it have a plan to circumvent the US courts? The decision also has wider implications for other sovereign borrowers. The US court rulings make sovereign payment default even more unattractive than it would otherwise be, but careful drafting of sovereign bonds could mitigate the risk of a similar fate for other sovereign borrowers.

This briefing discusses both the immediate and long term effects of this decision.

http://www.cliffordchance.com/briefings/2014/06/sovereign_pari_passuclausesnmlcapital20.html