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Briefing note

International Regulatory Update

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- Government Accountability Office reports on expectations of support for large bank holding companies
- Recent Clifford Chance Briefings: EMIR implementation timeline; Japanese Companies Act Reform; and more. Follow this link to the briefings section.

EU Commission reports on operation of European System of Financial Supervision

The EU Commission has published its review reports on the European System of Financial Supervision (ESFS), consisting of a report on the operation of the European Supervisory Authorities (ESAs) – the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA), and the European Securities and Markets Authority (ESMA) – and a report on the mission and organisation of the European Systemic Risk Board (ESRB). These two reports set out the findings of a review of the functioning of the new supervisory architecture, which was put in place in 2011 as part of the EU's response to the financial crisis.

The ESAs report identifies several areas for improvement which can be implemented by the ESAs and the Commission in the short term and would not require legislative action. In particular, the report states that the ESAs should give a higher profile to issues related to consumer/investor protection, and strengthen the focus on supervisory convergence, amongst other things by making better use of peer reviews.

The report also identifies other areas for consideration in the longer term, which would imply changes to the legislative framework for the ESAs. These include:

- the governance of the ESAs, in particular to further improve the capacity of the Board of Supervisors to take decisions in the interest of the EU as a whole; and
- a revision of the existing funding arrangements so that the ESAs could fulfil their broad range of tasks, taking into account the EU and national budgetary constraints.

The ESRB report indicates that certain improvements to the ESRB framework in the short-and medium term could enhance the efficiency of macro-prudential oversight at EU level.

EBA publishes final technical standards on treatment of equity exposures under IRB approach

The EBA has published its final draft Regulatory Technical Standards (RTS) specifying the treatment of equity exposures under the internal ratings-based (IRB) approach. The RTS establish that competent authorities are allowed to grant institutions a temporary exemption from the IRB treatment for certain equity exposures provided such exemption was being applied on the last day of application of the Capital Requirements Directive I (CRD I), i.e. 31 December 2007. This exemption, which was already introduced in the CRD I to partly relieve institutions' capital requirements for equity exposures under the IRB approach, will end on 31 December 2017 and the EBA expects it to have immaterial impact on most institutions.

MiFIR: EBA consults on criteria for intervention powers concerning structured deposits

The EBA has launched a consultation on its technical advice to the EU Commission on the criteria and factors to be taken into account when exercising intervention powers on structured deposits under the Markets in Financial Instruments Regulation (MiFIR).

The EBA is responsible for monitoring the market for structured deposits across the EU. Under certain specific circumstances the EBA can also temporarily prohibit or restrict the marketing, distribution or sale of certain structured deposits. The EU Commission recently requested the EBA to provide technical advice on the criteria and factors to be taken into account when exercising these powers.

The EBA proposes a set of criteria and factors and includes explanatory notes to provide the rationale for each deviation from the criteria published by ESMA. The EBA considered that some of those criteria were not applicable to structured deposits, while others needed to be adapted and in some cases, new criteria had to be introduced, so as to take into account characteristics that are specific to structured deposits.

The deadline for comments is 5 October 2014.

EMIR: ESMA issues guidelines on implementation of CPSS-IOSCO principles for market infrastructures in respect of CCPs

ESMA has issued guidelines and recommendations regarding the implementation of the CPSS-IOSCO Principles for Financial Market Infrastructures by competent authorities as part of the exercise of their duties resulting

from the European Market Infrastructure Regulation (EMIR) for the authorisation and supervision of central counterparties (CCPs) under Article 22(1).

ESMA has also updated its list of CCPs that have been authorised to offer services and activities in the EU in accordance EMIR. With the authorisation of CME Clearing Europe Ltd, there are now ten CCPs authorised under EMIR.

AIFMD: ESMA publishes official translations of guidelines on reporting obligations

ESMA has published the official translations of the Guidelines on reporting obligations under Articles 3(3)(d) and 24(1), (2), and (4) of the Alternative Investment Fund Managers Directive (AIFMD). These guidelines provide clarifications on the information that alternative investment fund managers (AIFMs) must report to national competent authorities (NCAs), the timing of such reporting together with the procedures to be followed when AIFMs move from one reporting obligation to another.

The publication of the translations triggers a period of two months within which national supervisors have to declare to ESMA whether they intend to comply with the guidelines or otherwise explain the reasons for non-compliance. The guidelines will apply from the end of this notification period.

UK Government consults on proposals to create two new criminal offences for abuse of wholesale energy market

The UK Government has launched a consultation on proposals to create two new criminal offences of energy market manipulation and insider trading. The aim is to safeguard consumers from any unfair practices. The proposed offences would give UK regulators new powers to prosecute people suspected of abusing the wholesale electricity and gas markets.

Under the new laws, it would be a criminal offence to fix the price of energy at an artificial level or use insider information to buy or sell energy on the wholesale market. It would also be an offence to make misleading claims or conceal facts about wholesale energy prices to manipulate the market – especially if it could affect competition in the energy market. Anyone found guilty of rigging wholesale gas and electricity prices could face up to two years in jail.

The deadline for responses to the consultation is 30 September 2014. Pending the consultation and Parliamentary process, the proposed new criminal sanctions could come into force in spring 2015.

Bank Recovery and Resolution Directive: FCA consults on implementation

The Financial Conduct Authority (FCA) has published a consultation paper (CP14/15) setting out proposed changes to its Handbook that are required to transpose the Bank Recovery and Resolution Directive (BRRD) into the UK regulatory regime for the investment firms and certain group entities that the FCA regulates prudentially and that fall within the scope of the Directive.

Comments on CP14/15 are due by 1 October 2014. The BRRD must be transposed into national law by 31 December 2014 and applied from 1 January 2015.

FCA consults on proposed guidance on loan to income ratios in residential mortgage lending

The FCA has published for consultation its proposed guidance on the Financial Policy Committee's recommendation on loan to income ratios in mortgage lending. In particular, the proposed guidance sets out:

- how the FCA expects firms to act in light of the FPC's recommendation;
- how the FCA will determine which firms should apply the LTI limit when the guidance comes into effect;
- how the FCA will determine which firms should apply the LTI limit on an on-going basis; and
- how the FCA will monitor if a firm's mortgage lending is consistent with its expectations on the LTI limit and what supervisory action may be taken.

Comments on the proposed guidance are due by 7 September 2014.

FCA restricts distribution of CoCos to retail investors

The FCA has made temporary product intervention rules which will restrict firms from distributing contingent convertible instruments (CoCos) to retail investors. The rules will come into effect on 1 October 2014 and lapse on 1 October 2015.

The FCA regards CoCos as posing particular risks of inappropriate distribution to ordinary retail customers (i.e. retail clients who are neither sophisticated nor high net worth or who do not meet any of the other permitted criteria). The restrictions will limit the ability of firms to distribute CoCos to retail customers by requiring firms to check that the customer falls within one of the permitted categories.

The FCA is planning to publish a consultation paper on proposed permanent rules on CoCos in September 2014.

Following consideration of feedback, it aims to publish a policy statement in Q2 2015, with final rules to take effect on 1 October 2015 when the temporary product intervention rules expire.

FCA sets out its approach to financial promotions in social media

The FCA has launched a consultation on proposed guidance which is intended to clarify the FCA's approach to the supervision of financial promotions in social media, including its character-limited forms.

Comments on the proposed guidance are due by 6 November 2014.

Ring-fenced bodies: FSMA (Excluded Activities and Prohibitions) Order 2014 published

The Financial Services and Markets Act 2000 (Excluded Activities and Prohibitions) Order 2014 (SI 2014/2080) has been published.

Section 4 of the Financial Services (Banking Reform) Act 2013 inserts a new Part 9B into the Financial Services and Markets Act 2000 (FSMA) providing for ring-fencing. Those UK institutions which carry on one or more core activities (defined in new section 142B of FSMA as the regulated activity of accepting deposits, subject to any exceptions provided for by the Treasury by Order) will be ring-fenced bodies. As such they will not be permitted to carry on excluded activities, defined in new section 142D of FSMA, or to do anything prohibited by the Treasury under section 142E. Section 142D defines a single excluded activity: the regulated activity of dealing in investments as principal, except in circumstances specified by the Treasury. SI 2014/2080 provides for a number of cases in which ring-fenced bodies are to be permitted to deal in investments in principal, and imposes a number of prohibitions (subject to exceptions) on what ring-fenced bodies may do.

Greater London Authority report sets out economic case for reforming EU

The Mayor of London's chief economic advisor, Dr Gerard Lyons, has published a report which considers how London's economy would be affected by four different scenarios based on the UK's relationship with Europe in 20 years' time.

The report indicates that the best economic scenario for London would be for the UK to remain part of a reformed European Union. However, it also indicates that a scenario where the UK leaves the EU but continues to conduct outward looking and positive economic policies with the EU and the wider world offers nearly the same level of benefits. According to the report, a third scenario where the UK remains in an unreformed EU offers far less opportunity for economic growth and a worst case scenario where the UK leaves the EU and operates isolationist economic policies would cost London's economy more than one million jobs.

The report emphasises that reform is as much in the long term interest of the EU as of the UK and London.

According to the report, the reforms that are needed include:

- accepting the case for economic reform;
- halting the process towards ever closer union;
- a clear timetable for reform;
- reforming the relationship between the eurozone and non-eurozone;
- completing the Single Market; and
- non economic areas for reform.

The Netherlands implements CRD 4 and CRR

The Netherlands has implemented the Capital Requirements Directive (CRD 4). The requirements of CRD 4 have been implemented in the Financial Supervision Act and its implementing decrees, and relate to e.g. the management of banks and investment firms, their risk management, their capital buffers and transparency requirements. The competent regulators have also been given additional supervisory tools. Sanctions for breaches of the provisions have been increased. Finally, relevant provisions of Dutch law have been made consistent with the Capital Requirements Regulation (CRR) which itself already applied as of 1 January 2014.

Dutch Central Bank issues revised version of regulation on sound remuneration policies

The Dutch Central Bank (DCB) has issued a revised version of its Regulation on Sound Remuneration Policies (Regeling beheerst beloningsbeleid). The 2014 Regulation replaces a similar regulation which was issued in 2011. The 2014 Regulation updates the 2011 Regulation and is now based on CRD 4. Only limited amendments have been made. Just like the 2011 Regulation, the 2014 Regulation is applicable to more financial undertakings than banks and investment firms, e.g. to securities clearing members, entities for risk-acceptance, premium pension institutions and insurers. The 100% bonus cap from CRD 4, however, only applies to banks and investment firms

(pending new legislation which, once adopted, would lower the bonus cap for all financial sector entities to 20%).

The 2014 Regulation includes rules on:

- the manner in which the remuneration policy is established, adopted, implemented, evaluated and amended;
- the different forms of remuneration components and structures, and the management of related risks; and
- the content and manner in which transparency on a firm's remuneration policy is given.

The most important amendments compared to the 2011 Regulation are an elaboration of the prohibition on guaranteed bonuses, and the malus and clawback provisions.

The 2014 Regulation entered into force on 1 August 2014.

EMIR: Dutch Central Bank publishes 'points for attention'

Following interviews with institutions supervised by the Dutch Central Bank and a round table with market participants, the Dutch Central Bank has published a document setting out 'points for attention' relating to the implementation of the European Market Infrastructure Regulation (EMIR) for banks, pension funds, insurance companies and general clearing members. These points for attention can be evaluated in the future during discussions between the Dutch Central Bank and institutions subject to its supervision.

The main points for attention are:

- scarcity of collateral;
- increase in contingent liquidity risk due to new margin obligations;
- access to central clearing; and
- communication risk.

According to the Dutch Central Bank, the overview does not purport to be exhaustive. Neither the impact of EMIR on reporting obligations nor the supervision of central counterparties is included in the overview. The overview also does not specifically address the impact of changes to the supervision of central counterparties on clearing of non-OTC derivatives, nor does it include a possible concurrence between EMIR and rules for non-EU jurisdictions in international (non-EU) OTC derivatives transactions.

SAFE issues circular to reform settlement of foreign capital by foreign-invested enterprises in certain areas

The State Administration of Foreign Exchange (SAFE) has issued a circular on issues concerning the pilot reform of the settlement of foreign capital by foreign-invested enterprises in certain areas to carry out a pilot programme of discretionary settlement of foreign capital by foreign-invested enterprises (FIEs) in selected industrial parks and pilot zones in Zhongguancun, Tianjin, Shenyang, Guangzhou, Wenzhou, Qianhai, etc. (but excluding the Shanghai Free Trade Zone).

Amongst other things, the circular states that:

- an FIE is allowed to settle its foreign currency capital on a discretionary basis and the RMB funds obtained from such settlement shall be deposited in a special discretionary settlement account opened at the same bank where it opens the capital account;
- RMB funds obtained from discretionary settlement shall not be used for activities beyond the FIE's approved business scope, securities investment, extending entrustment loan, or purchasing non-self-used real estate (except for real estate FIEs); and
- a common FIE may use the RMB funds obtained from discretionary settlement for making equity investment onshore, provided that the target company shall go through relevant procedures to open a special account for receiving the RMB funds.

The circular came into force on 4 August 2014. In the event of any discrepancy between the circular and the existing provisions, the circular shall prevail. For the time being, the 'Circular on Issues concerning the Improvement of Business Operations with Respect to the Administration of Payment and Settlement of Foreign Capital of Foreign-invested Enterprises' (Hui Zong Fa [2008] No.142) and the 'Supplementary Circular on Issues concerning the Improvement of Business Operations with Respect to the Administration of Payment and Settlement of Foreign Capital of Foreign-Invested Enterprises' (Hui Zong Fa [2011] No.88) previously issued by SAFE will not apply within the pilot areas covered by the circular.

MAS and SGX respond to feedback on proposed review of securities market structure and practices

The Monetary Authority of Singapore (MAS) and the Singapore Exchange (SGX) have issued their response to feedback on their February 2014 joint consultation on the review of the securities market structure and practices. The

MAS and SGX have confirmed that they have taken into account the feedback received and decided to proceed with all five proposals in the original consultation paper.

Further, in order to improve retail investors' access to a broader range of listed securities, particularly blue-chip stocks, the SGX will reduce the board lot size for securities listed on the SGX from the existing 1,000 shares to 100 shares in January 2015. The SGX will announce details of this initiative by the end of August 2014.

The MAS has indicated that the implementation of the initiatives will be phased in over the next 24 months. The MAS and SGX will work with the industry on the implementation details and will undertake further consultations on the relevant regulatory requirements or operational rules, where applicable.

MAS publishes responses to first consultation and launches second consultation on implementation of Basel III liquidity coverage ratio

The MAS has published its second consultation paper on the implementation of the Basel III liquidity coverage ratio (LCR) rules in Singapore, along with the responses to the feedback it received on its first consultation, which was published in August 2013. The August 2013 consultation proposed to require all banks, merchant banks and finance companies in Singapore to comply with the Basel III LCR requirements.

Considering the feedback received on its August 2013 consultation, the MAS has decided, amongst other things:

- to adopt a two-tier liquidity requirement framework under which banks and related entities assessed by the MAS to be systemically important in Singapore will be required to adopt the LCR framework and the smaller institutions will be given a choice to comply with either the LCR or a modified minimum liquid assets (MLA) framework;
- not to impose a separate US dollar liquidity requirement but to monitor whether institutions manage prudently their liquidity risks by currency on a supervisory basis;
- to extend the netting treatment to the full 30-day period over which the LCR requirement is calculated; and
- to align the definition of Level 2B HQLA with that in the Basel rules text, so as to avoid unnecessary friction for global banks' reporting systems.

In addition, the MAS has decided to revise the all-currency liquidity requirement and the implementation timelines for new liquidity requirements for various classes of institutions. The details of the revised arrangements are set out in the response section of the consultation paper.

The second consultation sets out a draft Notice and the corresponding reporting forms to implement the proposed LCR framework for banks in Singapore. The draft Notice and forms are appended in Annexes A and B of the consultation paper respectively.

Comments on the consultation paper are due by 5 September 2014.

MAS consults on leverage ratio disclosure requirements for banks incorporated in Singapore

The MAS has launched a public consultation on leverage ratio disclosure requirements for banks incorporated in Singapore. The proposed requirements are based on the Basel Committee on Banking Supervision's (BCBS') requirements for disclosure of the leverage ratio published in January 2014. The BCBS publication sets out a common disclosure framework, including a common set of templates, for banks to publicly disclose their leverage ratios.

The consultation paper sets out the MAS' proposed amendments to Parts II, IV, XI and XII of MAS Notice 637 on Risk Based Capital Adequacy Requirements for Banks Incorporated in Singapore, to implement leverage ratio disclosure requirements for Singapore-incorporated banks that are consistent with the requirements issued by the BCBS. The proposed disclosure requirements are intended to enhance the transparency and comparability of disclosures relating to the composition of the leverage ratio across banks. The draft amendments to the MAS Notice 637 are appended in Annex 1 of the consultation paper.

The MAS has indicated that the proposed amendments will take effect from 1 January 2015.

Comments on the consultation paper are due by 5 September 2014.

SEC allows primary listing and dual offering of foreign companies in Thailand

The Capital Market Supervisory Board has approved in principle a new set of regulations which will allow foreign companies to list on the Stock Exchange of Thailand (SET) whether by way of a primary listing or a dual offering whereby the foreign company lists in Thailand and another country simultaneously or within a proximate period. These regulations will become effective in August 2014.

Foreign companies must comply with approval criteria, disclosure standards and other relevant rules which are similar to those which Thai companies must comply with. Some additional rules and conditions also apply, for example:

- equity offerings must comply with the laws and regulations of the home jurisdictions;
- their laws and regulations on shareholder protection should be equivalent to those in Thailand,;
- the capital market regulators of the countries where the issuing companies are incorporated should have authority to collaborate with the SEC in terms of enforcement and exchange of information on violations of relevant laws and regulations;
- at least two directors must be Thai nationals and residents, of which at least one director must be an independent director and audit committee member;
- the financial statements must be prepared in accordance with Thai accounting standards or International Financial Reporting Standards (IFRS); and
- the auditor and financial advisor (who must serve for three years) must be on the SEC's approved list.

If a Thai holding company with its core business overseas has non-Thai major shareholders, it will be required to comply with the regulations applicable to a primary listing by a foreign company in addition to the regulations applicable to Thai companies if it plans to list in Thailand. However, foreign companies with more than 50% of their shares held by Thai shareholders or controlled by Thai shareholders will be subject to the regulations applicable to Thai companies.

Government Accountability Office reports on expectations of support for large bank holding companies

The US Government Accountability Office (GAO) has published a report entitled 'Large Bank Holding Companies: Expectations of Government Support'. In creating the report, the GAO reviewed relevant statutes and rules, and interviewed regulators, bank holding companies, rating agencies, investment firms, and corporate customers of banks. The GAO also conducted quantitative analyses to assess potential 'too-big-to-fail' funding cost advantages.

According to the GAO, while views varied among market participants, many believed that recent regulatory reforms have reduced but not eliminated the likelihood that the federal government would prevent the failure of one of the largest bank holding companies. The report also notes that recent reforms provide regulators with new authority to resolve a large failing bank holding company in an orderly process and require the largest bank holding companies to meet stricter capital and other standards, increasing costs and reducing risks for these firms.

In response to reforms, two of three major rating agencies have reduced or removed the assumed government support they incorporated into some large bank holding companies' overall credit ratings. Credit rating agencies and large investors cited the new Orderly Liquidation Authority as a key factor influencing their views. While several large investors viewed the resolution process as credible, others cited potential challenges, such as the risk that multiple failures of large firms could destabilize markets.

RECENT CLIFFORD CHANCE BRIEFINGS

EMIR – illustrative implementation timeline and expected developments

The last stages of the EU's derivatives reforms are now in sight. Many of the obligations under the EU regulation on OTC derivatives, central counterparties and trade repositories (EMIR) have already come into force and the European Supervisory Authorities are developing the last major regulatory technical standards required to implement EMIR – on margin for uncleared OTC derivatives and the first clearing obligations. However, there are still a number of steps that need to be taken before EMIR is fully in place and the EU authorities' attention is already turning to the 2015 review of EMIR and possible future amendments.

This briefing sets out an updated illustrative implementation timeline for EMIR and a list of some expected developments under EMIR, as well as highlighting some other recent developments.

http://www.cliffordchance.com/briefings/2014/08/emir_illustrativeimplementationtimelinean.html

EMIR – Calculation of counterparty limits by UCITS for cleared derivatives transactions

The EU UCITS Directive allows UCITS to invest in both exchange traded and over the counter (OTC) derivatives, subject to eligibility criteria and, in the case of OTC derivatives, exposure limits. EMIR will impose obligations on UCITS to clear certain OTC derivatives transactions, which will raise a number of issues for UCITS, in particular, as to how the exposure limits apply when UCITS post initial and variation margin on their cleared OTC derivative positions. The European Securities and Markets Authority

(ESMA) has recently published a discussion paper on the calculation of counterparty risk by UCITS for OTC financial derivative transactions subject to clearing obligations, which may lead to changes to the UCITS Directive with implications for both OTC and exchange traded derivatives.

This briefing discusses the impact of EMIR on UCITS.

http://www.cliffordchance.com/briefings/2014/08/emir_calculationofcounterpartylimitsbyucit.html

European Commission reconsiders insurance sector exemption from antitrust laws

The European Commission has launched a consultation on the functioning and future of the Insurance Block Exemption Regulation (IBER). The IBER exempts from prohibition under EU antitrust law certain agreements between companies in the insurance sector. The current version of the IBER came into effect in 2010 and is due to expire in March 2017.

The EC will consider whether any parts of the IBER merit renewal, i.e. whether the insurance sector is still sufficiently exceptional to require an industry-specific exemption from competition law. Abolishing or narrowing the scope of the IBER could increase the burden on insurers and reinsurers to self-assess the compliance of certain activity with EU antitrust law.

This briefing discusses this consultation.

http://www.cliffordchance.com/briefings/2014/08/european_commissionreconsidersinsurancesecto.html

Companies Act Reform – Organisation Restructuring/M&A (Share Purchase Demand, Injunction against Organisation Restructuring and Corporate Split)

This briefing explains the amendment to the Japanese Companies Act and other related laws, which was enacted on 20 June 2014, focusing on:

- share purchase demands, which are demands by shareholders that the company purchase their shares, in relation to business transfers and organisation restructuring (collectively, 'Organisation Restructuring');
- requests for injunctions against Organisation Restructuring and;
- corporate splits.

The reform extensively amends the provisions of the current share purchase demand system with the aim of preventing the abusive exercise of share purchase demands. Moreover, the reform entrenches requests for injunctions against Organisation Restructurings in statute and sets out provisions to protect creditors from fraudulent company splits. The reform is expected to come into force by 1 April 2015.

http://www.cliffordchance.com/briefings/2014/08/companies_act_reformorganisatio0.html

Saudi Arabia plans to open its stock market to allow foreign investment

On 22 July 2014, the Capital Market Authority of Saudi Arabia (the CMA) announced that the Saudi Arabian Council of Ministers had granted authority to the CMA to permit foreign financial institutions to buy and sell shares in companies listed on the Saudi Arabian Stock Exchange and to prescribe the rules that will govern their access to the market.

This briefing discusses this development.

http://www.cliffordchance.com/briefings/2014/07/saudi_arabia_planstoopenitsstockmarkett0.html

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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