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Briefing note

International Regulatory Update

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EBA publishes opinion on lending-based crowdfunding

The European Banking Authority (EBA) has published an opinion on lending-based crowdfunding across the EU. In the opinion, the EBA recommends that EU legislators converge the supervision practices of crowdfunding to avoid regulatory arbitrage and to ensure a level playing field across the EU Single Market.

The EBA has looked into the type of regulation that would be required in order to drive confidence in crowdfunding. The opinion reviews present business models in the sector and considered the extent to which the identified risks are already addressed in existing EU directives and regulations and national regulatory frameworks.

The EBA has identified the Payment Services Directive (Directive 2007/64/EC), which can cover payment-related aspects of crowdfunding activities, as the most readily applicable EU legislative text to lending-based crowdfunding. However, the EBA notes that since crowdfunding platforms would not typically fall within the perimeter of credit institutions, as they are defined under EU law, lending-related aspects are not covered by EU law. The opinion warns that this situation leaves several lending-related risks unlikely to be addressed and suggests a set of options to mitigate these.

CRR: EBA publishes opinion and report on CVA risk

The EBA has published an opinion addressed to the EU Commission on aspects related to the calculation of own funds requirements for Credit Valuation Adjustment (CVA) risk. The sixteen policy recommendations in the opinion build on a technical analysis conducted by the EBA which has been published in the form of a report and a review.

The CVA data collection exercise conducted by the EBA on a sample of 32 banks across 11 jurisdictions highlighted:

- the materiality of the CVA risks that are currently not covered by EU legislation due to some exemptions provided for in the Capital Requirements Regulation (CRR); and
- that EU exemptions on the application of CVA charges should be reconsidered or removed, since they leave potential risks uncaptured (the EBA has emphasised that any action in this regard should be taken only after a Basel review of the CVA framework as part of the fundamental review of the trading book).

The EBA is proposing policy recommendations that can be implemented in the short-term, which will aim to provide clarification and convergence in the implementation of the current CVA framework in the EU. In order to partially address the risks generated by the current EU exemptions, the EBA recommends monitoring the impact of the transactions exempted from the CVA risk charge, and defining potential situations of excessive CVA risks, which could be taken into account as part of banks' Supervisory Review and Evaluation Process (SREP).

EMIR: ESMA and Japanese Financial Services Agency publish memorandum of cooperation regarding CCPs

The European Securities and Markets Authority (ESMA) and the Financial Services Agency of Japan (JFSA) have entered into a memorandum of cooperation regarding central counterparties established in Japan and licensed or approved by the JFSA that have applied to ESMA for recognition as central counterparties (CCPs) under the European Market Infrastructure Regulation (EMIR). The memorandum of cooperation confirms the fulfilment of the condition set out in Article 25(2)(c) of EMIR, i.e. that cooperation arrangements have been established as regards the covered CCPs, and expresses the two authorities' willingness to consult, cooperate and exchange information in the interest of fulfilling responsibilities and mandates of each authority over the covered CCPs.

MiFID: ESMA publishes peer review on best execution supervisory practices

ESMA has published the findings of a peer review study on supervisory practices in relation to best execution, the obligation to execute orders on terms most favourable to the client, under Article 21 of MiFID. The review was conducted by the ESMA Review Panel under a mandate from the ESMA Board of Supervisors and comprised a self-assessment questionnaire for 29 national competent authorities (NCAs) represented on the ESMA Review Panel and a peer review of each Member's self-assessment. The assessments were complemented by on-site visits to NCAs in France, Liechtenstein, Luxembourg, Malta, Poland and Spain.

The peer review considered supervision and enforcement of best execution and identified that:

- oversight of best execution is often carried out as part of general conduct of business supervision;
- best execution is often viewed primarily in terms of best price;
- execution venues are often highly concentrated in the main domestic market;
- there are difficulties for NCAs having comprehensive oversight of what constitutes best execution across all venues;
- best execution monitoring often does not cover non-equity and less liquid markets; and
- low levels of complaints have resulted in few enforcement actions, which may relate to a lack of investor understanding on the issue.

The report highlights a number of recommendations that assessors felt may ensure better implementation, enforcement and supervision if developed by competent authorities and ESMA. The recommendations include:

- developing guidance on national implementation of MiFID rules;
- an assessment of NCAs resources on best execution and whether these are adequate;
- establishing whether obstacles exist to developing alternative execution venues;
- a customer education programme; and
- examining the possible use of proportionate sanctions to ensure a credible deterrent against future breaches.

ECON Committee publishes report on Multilateral Interchange Fees Regulation

The EU Parliament Committee on Economic and Monetary Affairs (ECON) has published a supplementary report on the proposed Regulation on interchange fees for card-based payment transactions (MIF Regulation) following its vote on the proposal on 27 January 2015.

The report has been tabled for vote at a forthcoming Parliament plenary session.

IOSCO reviews implementation of financial benchmark principles

The International Organization of Securities Commission (IOSCO) has published a review of the implementation of its principles for financial benchmarks.

The review provides:

- an overview of the reported level of implementation of the principles, including any stated application by administrators of the concept of proportionality; and
- high level information about the extent of the voluntary market adoption of the principles, with a view to understanding what administrators have done and what remains to be done, to implement the principles.

IOSCO reports on prudential standards in the securities sector

IOSCO has published a final report on prudential standards in the securities sector. The report seeks to highlight similarities, differences and gaps among the different frameworks and aims to update IOSCO's 1989 Capital Standards Report based on the issued identified in this final report. The report's comparative analysis focuses on the net capital rule (NCR) approach, in particular the US approaches, and the Capital Requirements Directive, although the report also recognises relevant national variations.

The report highlights prudential regulatory and supervisory areas that might be considered in an update of the 1989 report, particularly:

- identifying opportunities for regulatory capital arbitrage that might have (or actually have) materialised from differences in prudential regulations across jurisdictions; and
- accounting for the increasing use of internal models and the commensurate increase in infrastructure, systems and controls that are necessary to help ensure that firms are not undercapitalised compared to the risks posed by their positions and activities.

CPMI and IOSCO assess implementation of Principles for Financial Market Infrastructures

The Committee on Payments and Market Infrastructures (CPMI) and IOSCO have published their latest implementation monitoring assessment of the principles for financial market infrastructures (PFMIs) in the EU, Japan and the United States. The PFMIs are intended to set expectations for the design and operation of key financial market infrastructures to enhance their safety and efficiency and, more broadly, to limit systemic risk and foster transparency and financial stability.

The CPMI and IOSCO decided to monitor the implementation of the PFMIs in the 28 member jurisdictions by way of a three level monitoring framework. These

reports are the level two assessments, which examine the completeness of the legal and regulatory or oversight frameworks applied to systemically important CCPs and trade repositories (TRs) in each jurisdiction and the consistency of these frameworks with the PFMIs. The reports summarise the legal and regulatory frameworks, the key findings of the assessments and, where appropriate, make recommendations to support the progress of the implementation. The reports identify that overall progress on CCPs has been good, whereas progress on TRs has been more varied.

CPMI and IOSCO publish standards on public quantitative disclosure for CCPs

The CPMI and IOSCO have published public quantitative disclosure standards for CCPs, which set out the disclosure standards that CCPs are expected to meet under the principles for financial market infrastructures. The standards complement the disclosure framework published by CPSS and IOSCO in December 2012, prior to CPSS (the Committee on Payment and Settlement Systems) changing its name to CPMI in September 2014.

The standards are intended to assist stakeholders, including authorities, participants and the public, to assess the risks associated with CCPs including risk controls, the possible impact of their systemic risk and risk of participating in a CCP either directly or indirectly. The standards and disclosure framework jointly set out the minimum standards that CCPs are expected to meet in their disclosures, which must be completed by 1 January 2016 at the latest and updated according the frequencies set out in the standards.

ISDA publishes key principles for improving regulatory transparency and derivatives trade reporting

The International Swaps and Derivatives Association (ISDA) has published a paper that outlines a number of key principles and initiatives for regulators, market participants and industry service providers in order to improve regulatory transparency of derivatives activity.

The key principles outlined in the paper suggest that:

- regulatory reporting requirements for derivatives transactions should be harmonised within and across jurisdictions;
- policy-makers should embrace and adopt the use of standards, such as legal entity identifiers (LEIs), unique trade identifiers (UTIs), unique product identifiers (UPIs) and Financial products Markup Language (FpML), with the aim to drive improved quality and consistency in meeting reporting requirements;
- where global standards do not yet exist, market participants and regulators should collaborate and secure agreement on common solutions to improve consistency and cross-border harmonisation;
- regulations that prevent policy-makers from appropriately accessing and sharing data across jurisdictions must be amended or repealed; and
- reporting progress should be benchmarked.

PRA and FCA consult on senior managers regime, approach to non-executive directors, presumption of responsibility and formalised whistleblowing arrangements

The Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) have published a joint consultation paper (FCA CP/15/5 and PRA CP7/15) on the Senior Managers Regime (SMR) for relevant authorised persons. The proposals set out:

- the Senior Insurance Manager's Regime (SIMR), which is aligned to the banking regime but not identical, and takes into account measures relating to governance, fitness and propriety of individuals under Solvency II;
- the regulators' revised approach to non-executive directors in UK banks, building societies, credit unions, PRA-designated investment firms and Solvency II firms following feedback received from a previous consultation in July 2014; and
- how the PRA intends to exercise 'the presumption of responsibility', which was introduced by the Banking Reform Act 2013 and enables the PRA and FCA to impose regulatory sanctions on individual senior managers when a bank breaches a regulatory requirement if the senior manager responsible for the area where the breach occurred cannot demonstrate taking reasonable steps to avoid or stop it. The FCA will consult on its proposed guidance separately.

On non-executive directors, the proposals would require the Chairperson, Senior Independent Directors (SIDs) and the Chairs of the risk, audit, remuneration and nomination committees to be subject to approval and inclusion in the SMR. The regulators propose that standard non-executive directors will not be included in the combined SMR under the proposals or be subject to pre-approval by regulators.

The consultation paper also sets out the approach to non-executive directors in the approval and individual

accountability regime for Solvency II firms, which the PRA and FCA propose to align to the scope of the SMR for relevant authorised persons as far as their functions are concerned and the PRA's proposed requirements on propriety for non-executive directors in relevant authorised firms who will not be in the scope of the SMR. The consultation paper also sets out FCA guidance on the role and responsibility of non-executive directors. Comments on the consultation are due by 24 April 2015.

The SMR proposals incorporate measures arising from recommendations from the Parliamentary Commission for Banking Standards (PCBS) in June 2013, which also made recommendations with regard to whistleblowing arrangements at firms. The PRA and FCA are consulting separately on measures to formalise whistleblowing procedures in deposit taking firms, PRA-designated investment firms and insurers based on current good practice that has been observed and which relate to:

- internal whistleblowing arrangements;
- protection for whistleblowers; and
- the allocation of responsibility under the SMR and SIMR to a certain individual to oversee internal whistleblowing arrangements.

Small credit unions with GBP 25 million or less in assets would not be included in the new regime. Comments on the consultation on whistleblowing are due by May 2015.

FCA publishes occasional paper on consumer vulnerability

The FCA has published an occasional paper (No. 8) on consumer vulnerability. The paper states that a vulnerable consumer is someone who, due to their personal circumstances, is especially susceptible to detriment, particularly when a firm is not acting with appropriate levels of care and identifies this as an area where firms can take action and create good outcomes for consumers.

The occasional paper is intended to broaden understanding and elicit debate on consumer vulnerability, provide some examples of good practice and provide practical resources to help firms develop and implement a vulnerability strategy. It identifies problem areas relating to policy, systems, products and implementation. The FCA commissioned research amongst a range of consumers in potentially vulnerable circumstances and has published the findings of that study alongside the occasional paper. A practitioners' pack has also been published.

FCA consults on consumer credit regime policy changes

The FCA has published a consultation paper (CP15/6) outlining proposed policy changes to its consumer credit regime. The changes are intended to address potential areas of harm to consumers that the FCA has observed in the market and include clarifications and amendments to ensure FCA rules clearly reflect policy intention and deal with issues raised by firms and other stakeholders.

The key proposals are to:

- consult on whether to retain the rules made in the FCA's policy statement on credit broking and fees (PS14/18);
- require firms to provide explanations to guarantors, assess their creditworthiness and treat them with forbearance;
- remove the exemption from the requirement for firms to include a risk warning in financial promotions regarding high-cost short-term credit;
- amend FCA rules regarding the relative prominence and representative APRs, and to make current guidance on the clear, fair and not-misleading principle a rule;
- correct an anomaly and allow firms to introduce continuous payment authority to collect repayments where a customer is in arrears or default and the lender is exercising forbearance; and
- consult on consequential changes to FCA rules in relation to the implementation of the Mortgage Credit Directive and the transfer of second charge mortgage regulation.

Comments are due by 6 May 2015.

PRA consults on rules and powers over external auditors and actuaries

The PRA has published a consultation paper (CP8/15) introducing two proposals on the interaction between the PRA and external auditors and actuaries.

The consultation is relevant to large banks, building societies and insurers and also to the auditors and actuaries of all PRA-authorised firms and aims to further enhance the benefits derived from the auditor-supervisor dialogue.

The proposals include:

- requiring external auditors of the largest UK-headquartered deposit-taking institutions that are not

subsidiaries of non-UK firms to provide written reports to the PRA as part of the statutory audit cycle; and

- PRA intentions relating to the HM Treasury regulations which will commence the PRA's disciplinary powers over actuaries and auditors under s 345A of Financial Services and Markets Act 2000 (FSMA), including how the PRA will cooperate with other regulators.

Comments are due by 27 May 2015.

CMA publishes final report on payday lending market

The Competition and Markets Authority (CMA) has published its final report on its investigation into the payday lending market. The report follows provisional findings published in June 2014 and proposed remedies to issues identified in October 2014.

In the final report the CMA announces that it will order online lenders to publish details of their products on at least one FCA-authorised price comparison website that should provide clear and comparable information to consumers, in particular the total amount payable on a loan. The CMA believes that one or more price comparison websites will emerge to be authorised by the FCA but has decided that lenders will be obliged to set up an FCA-authorised website if this does not occur. Both online and high-street payday lenders will also be ordered to provide existing customers with a summary of their cost of borrowing to indicate:

- the total cost of their most recent loan;
- the cumulative cost of their borrowing in the past twelve months; and
- the impact of late repayment on their cost of borrowing.

The CMA has also made recommendations to the FCA in relation to:

- the content of an FCA-authorised price comparison website;
- improvements in disclosure of charges including late fees;
- enhancing customers' ability to shop around without unduly affecting their access to credit;
- the development of real-time data sharing between lenders and credit reference agencies; and
- lead-generator transparency, to help customers understand how they operate.

The CMA will publish an order within six months to establish its rules on price comparison websites and borrowing summaries. The CMA will work with the FCA to implement its recommendations; it is expected that the FCA will consult on measures relating to the recommendations in summer 2015.

Financial Markets and Insolvency (Settlement Finality) (Amendment) Regulations 2015 published

The Financial Markets and Insolvency (Settlement Finality) (Amendment) Regulations 2015 (SI 2015/347) have been published. The Regulations implement Article 70 of the Central Securities Depositories Regulation (CSDR), which amends the definition of 'system' in Directive 98/26/EC on settlement finality in payment securities settlement systems (the SFD) to require notice of designation of SFD systems to be given to ESMA rather than the EU Commission. The Regulations make corresponding amendments to the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (SI 1999/2979) and include such notification requirements for UK designating authorities, which are the FCA and Bank of England.

The Regulations will enter into force on 18 March 2015.

FSMA 2000 (Over the Counter Derivatives, Central Counterparties and Trade Repositories) (Amendment) Regulations 2015 published

The Financial Services and Markets Act 2000 (Over the Counter Derivatives, Central Counterparties and Trade Repositories) (Amendment) Regulations 2015 (SI 2015/348) have been published. The Regulations amend transitional provisions included in the Financial Services and Markets Act 2000 (Over the Counter Derivatives, Central Counterparties and Trade Repositories) Regulations 2013 (SI 2013/504) in order that the special resolution regime under Part 1 of the Banking Act 2009 be applied to any clearing house incorporated in, or formed under the law of, any part of the UK that immediately before 15 March 2013 was recognised under Part 18 of the Financial Services and Markets Act 2000 and provided clearing services as a central counterparty during the period in which its application for authorisation under EMIR was being determined. The Regulations also correct a minor typographical error in Regulation 36.

The Regulations come into force on 18 March 2015.

Benchmarks: FSMA 2000 (Regulated Activities) (Amendment) Order 2015 published

The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2015 (SI 2015/369) has been published. The Order amends the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544) to bring seven additional financial benchmarks

within the regulatory regime put in place for LIBOR following recommendations from the Fair and Effective Markets Review (FEMR), a joint initiative between HM Treasury, the Bank of England and FCA.

The benchmarks brought under the regime are all major UK-based financial benchmarks in the fixed income, commodity and currency (FICC) markets and comprise:

- the Sterling Overnight Index Average (SONIA);
- the Repurchase Overnight Index Average (RONIA);
- ISDAFIX;
- WM/Reuters (WMR) London 4pm Closing Spot Rate;
- London Gold Fixing (to be replaced by LBMA Gold Price);
- LBMA Silver Price; and
- ICE Brent.

The Order also makes amendments to the Financial Services Act 2012 (Misleading Statements and Impressions) Order 2013 (SI 2013/637), which specifies relevant activities, investments and benchmarks for the purposes of criminal offences under the Financial Services Act 2012, in order that the additional benchmarks are brought into this regime.

The Order will come into force on 1 April 2015.

BaFin proposes draft circular on implementation of EBA guidelines on disclosure of encumbered and unencumbered assets

The German Federal Financial Supervisory Authority (BaFin) has launched a consultation on a draft circular on the implementation of the EBA guidelines on the disclosure of encumbered and unencumbered assets (EBA/GL/2014/03) issued on 27 June 2014. The circular applies to institutions subject to the disclosure regime in Part 8 of the CRR.

The consultation period ends on 27 March 2015.

CSSF issues circular on publication requirements for information on unencumbered assets

The Luxembourg financial sector supervisory authority, the Commission de Surveillance du Secteur Financier (CSSF), has issued circular 15/605 dated 20 February 2015 on the publication requirements for information on unencumbered assets. The circular is addressed to credit institutions subject to disclosure requirements in Part 8 of the CRR.

The circular implements the EBA guidelines on the disclosure of encumbered and unencumbered assets into the Luxembourg regulatory framework. Credit institutions will have to disclose information on their encumbered and unencumbered assets as well as collateral received in accordance with the three disclosure templates set out in the EBA guidelines.

The EBA guidelines are the first step in the disclosure framework of asset encumbrance. They will be reviewed after one year and will form the basis of the binding technical standards on more extensive disclosure that the EBA will have to develop and submit to the EU Commission by 1 January 2016.

The circular entered into force with immediate effect and applies until the EBA guidelines have been replaced by the regulatory technical standards to be developed by the EBA and endorsed by the Commission.

CRR/CRD 4: CSSF issues circular providing clarifications for investment firms

The CSSF has issued circular 15/606 concerning clarifications for investment firms in the framework of the implementation into Luxembourg law of the Capital Requirements Directive (CRD 4) and the entry into force of the CRR.

The purpose of the circular is to provide investment firms with certain clarifications in relation to their categorisation following the entry into force of the CRR and the submission of the CRD 4 implementing Bill 6660 to the Luxembourg Parliament.

One of the innovations of the Bill is to introduce the new sub-category of CRR investment firms into the law of 5 April 1993 on the financial sector, as amended (FSL).

The circular provides guidance on which types of Luxembourg investment firms will and which will not fall within the new category of CRR investment firms subject to the CRR. The circular further explains that each investment firm holding client assets (funds or securities) is required to be licensed for the ancillary service of safekeeping and administration of financial instruments for the account of clients, including custodianship and related services such as cash/collateral management and will therefore be considered as CRR investment firm being subject to the CRR. Moreover, the circular specifies the meaning of holding client assets and reminds all investment firms of their client asset protection obligations.

To enable it to categorise investment firms, the CSSF has requested, as part of any new application file for an investment firm or in the context of an extension of an

existing licence, to be provided with the completed questionnaire attached to the circular.

HKMA announces refinement to renminbi liquidity facility

The Hong Kong Monetary Authority (HKMA) has announced adjustments to the calculations of interest rates on the renminbi (RMB) intraday and overnight funds provided under the RMB liquidity facility to authorised institutions participating in RMB business in Hong Kong.

Instead of referencing the CNH HIBOR fixing on a single day, the new calculations will be based on 3-day moving averages of the fixing. The adjustments are intended to reduce the volatility of the applicable repo rates and fine tune the charging arrangement for intraday repo converted into overnight repo.

The HKMA welcomes participating AIs to use the facility to meet their liquidity needs. Nonetheless, participating AIs are advised to plan their funding ahead of time and avoid over-dependence on the RMB liquidity facility. The HKMA has indicated that it will review the terms and conditions of the facility in the light of actual operating experience.

RECENT CLIFFORD CHANCE BRIEFINGS

Setting a new benchmark

The Council of the EU has reached political agreement on the EU Benchmark Regulation. The legislation will impose controls on a range of financial market activity that uses interest rate, currency, commodity and other indices to set prices and contract values. Although not yet finalised the new rules are expected to be published later this year and apply in 2016. The Regulation is expansive in scope, covering not only indices such as LIBOR and the DAX but also many other less obvious 'benchmarks'. The new rules could lead to the transformation or even disappearance of some benchmarks, presenting a significant implementation challenge. The compliance burden for firms that administer, use and contribute to financial benchmarks will also be substantial and the Regulation will pose special challenges for EU market participants that rely on non-EU benchmarks.

This briefing discusses the scope and impact of the EU Benchmark Regulation.

http://www.cliffordchance.com/briefings/2015/02/setting_a_new_benchmark.html