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International Regulatory Update

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EU contract law: European Parliament adopts resolution and Commissioner Reding outlines next steps

The European Parliament has adopted a resolution on policy options for progress towards a European Contract Law in a plenary session. The resolution follows the EU Commission's July 2010 Green Paper, which launched a public consultation to gather views from relevant stakeholders regarding possible policy options in the field of European Contract Law. Amongst other things, the resolution favours the option of setting up an optional European Contract Law by means of a regulation, complemented by a 'toolbox' that could be endorsed by means of an interinstitutional agreement.

In addition, Viviane Reding, EU Commissioner for Justice, recently gave a speech on the Commission's work on an EU contract law instrument, in which she indicated that she does not favour full harmonisation or a compulsory European Code. Instead, Ms. Reding argued that the twin aims of enhancing the single market for businesses and consumers while respecting Europe's legal diversity and the principle of subsidiarity can be achieved by proposing a legal instrument on European contract law that is voluntary and optional, can be chosen by businesses and consumers and then serve as basis for their transactions, and does not replace existing national contract law, but exists alongside it.

Ms. Reding noted that the Commission will need to decide whether the optional instrument should be made available for cross-border transactions only, or whether it should also apply to domestic transactions if chosen by the parties to the contract. She suggested that the best solution might be to limit the scope of the optional instrument to cross-border contracts, but to allow Member States to extend the application of the optional instrument also to domestic contracts.

Credit rating agencies: European Parliament plenary session adopts resolution

The European Parliament's plenary session in Strasbourg has adopted a resolution on credit rating agencies (CRAs). The resolution is based on a non-legislative report prepared by the Parliament's ECON Committee.

Amongst other things, the resolution calls on the European Commission to carry out a detailed impact and viability assessment for a fully-independent European credit rating foundation, with funding from the financial services industry made available for the first five years at most. It also proposes that market participants who are unable to carry out risk analyses in house should not be able to invest in structured products, or else should be able to do so only at the highest risk weighting.

In addition, the resolution calls for special attention to sovereign debt ratings and, in particular, increased transparency in relation to how CRAs arrive at their sovereign ratings – the resolution further states that CRAs should explain their methodologies and why their ratings deviate from the forecasts of the main international financial institutions. Finally, it suggests that CRAs' exposure to civil liability in the event of gross negligence or misconduct be defined on a consistent basis across the EU and that the Commission should identify ways for such civil liability to be anchored in Member States' civil law.

Consumer Rights Directive: European Parliament and Council reach provisional agreement

The European Parliament has announced that it has reached a provisional agreement with the Council and the European Commission on the proposed Consumer Rights Directive.

The agreement still needs to be formally approved by the Parliament's plenary session and by the Council. The Parliament is expected to vote on the agreement at its June or July plenary session.

OTC derivatives and market infrastructures: Hungarian EU Presidency publishes compromise proposal

The Hungarian EU Council Presidency has published a compromise text for the proposed regulation on OTC derivatives and market infrastructures.

European Payments Council consults on SEPA cards standardisation requirements

The European Payments Council and the Cards Stakeholders Group have published the latest version of the 'SEPA Cards Standardisation Volume – Book of Requirements' for public consultation. The SEPA Cards Standardisation Volume defines the functional and security standards requirements needed to achieve interoperability based on open and free standards within the Single Euro Payments Area (SEPA) cards market. The latest version includes updates with regard to security requirements, payment with cashback, dynamic currency conversion, mobile contactless payments, payment with aggregated amount and surcharging.

Comments are due by 29 July 2011.

OECD consults on draft recommendation on regulatory policy and governance

The OECD has published a draft recommendation on regulatory policy and governance for public consultation, which includes an explanatory text and questions to guide the consultation process. The draft recommendation updates existing OECD instruments on regulatory reform and management adopted since 1995. The OECD intends to produce a recommendation that covers regulatory policy, management and governance as a whole-of-government instrument to be applied by sectoral ministries and regulatory agencies. Comments both on the specific recommendations as well as the explanatory notes are due by 1 July 2011.

Following this round of consultation, a further revised draft will be prepared for the consideration of the Regulatory Policy Committee at its next meeting on 3 and 4 November 2011, at which the Committee also intends to discuss the impact of the new recommendation on its future work programme, including reviews, thematic studies and indicators, and measures to promote the widest possible communication of the recommendation in 2012.

IMF staff discussion paper on 'too important to fail' published

The IMF has published a staff discussion paper which argues that, amongst other things, the policy framework to deal with the 'too important to fail' problem should contain more stringent capital (and possibly liquidity) requirements to limit contribution to systemic risk. The paper also calls for intensive supervision consistent with the complexity and riskiness of systemically important financial institutions.

UK government consults on changes to Money Laundering Regulations 2007

The UK government has published its response to the review of the Money Laundering Regulations 2007 and launched a consultation on its proposals to amend the regulations. The review found that the regulations and their implementation are broadly effective and proportionate, but that improvements could be made. Amongst other things, the government has invited views on the proposed removal of over two dozen criminal penalties for businesses which fail to have the appropriate systems and controls in place to combat money laundering. According to the government, this would allow businesses to implement a fully risk-based approach, where businesses make their own assessment of the risks they face and implement appropriate systems and controls. Civil penalties will remain and the government will be consulting on whether regulators should have the power to impose additional penalties. The government is also proposing a general exclusion for very small businesses (for example those with below GBP 13,000 VAT-exclusive turnover per annum), or a reduction in the requirements placed on such businesses.

The government has stressed that its consultation will not affect the criminal penalties for money laundering under the Proceeds of Crime Act 2002 or the obligations of firms to report suspicious activity to SOCA. The government has also published a pre-consultation impact assessment on the costs and benefits of its proposals.

The consultation period ends on 30 August 2011.

Pre-consultation impact assessment

FSA issues Quarterly Consultation No. 29

The FSA has published its Quarterly Consultation (No. 29) (CP11/11), in which it invites comments on miscellaneous amendments to the Handbook. Amongst other things, the consultation paper proposes amendments to: (1) extend the list of appropriate qualifications for individual advisers and add bodies to the list for accredited body status; (2) provide guidance on certain descriptions firms should use to promote financial products; and (3) clarify how consumers may be able to cancel ongoing adviser charges for services relating to a financial product without being required to withdraw his or her investments.

Comments on chapter 3 of CP11/11 are due by 6 July 2011 and on all other chapters by 6 August 2011.

AMF and ACP set out legal framework for rolling spot forex

The Autorité des marchés financiers (AMF) and the Autorité de contrôle prudential (ACP) have issued a position statement defining the legal framework for rolling spot forex. According to the AMF and the ACP, it has become necessary to clarify the legal framework for financial contracts and rolling spot forex in light of an increase in the number of offers aimed at individuals on the internet, and because intermediaries do not always have the necessary authorisation to do business in France.

Following work carried out by a joint AMF/ACP working group, and taking into account current practices in the EU, the AMF and the ACP have concluded that foreign exchange contracts with a maturity date at the end of the day qualify as financial instruments (and, more specifically, as financial contracts) when they provide for, or effectively allow for, a tacit extension of positions.

Q&As

CRD 3: BaFin consults on draft implementing regulation

The Federal Financial Supervisory Authority (BaFin) has published a consultation paper on a draft regulation (CRD 3-ÄnderungsVO) implementing the revised Capital Requirements Directive (CRD 3, as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies) in Germany.

The CRD 3-ÄnderungsVO mainly covers amendments to the Solvability Regulation (SolvV) and the Large Exposure Regulation (GroMiKV) due to the implementation of CRD 3. The amendments to the SolvV include extended capital requirements in the banking book and for securitisations, as well as stricter disclosure requirements.

Comments are due by 15 July 2011.

BaFin consults on draft updated guidance note on notification of non-German UCITS funds for public distribution in Germany

The Federal Financial Supervisory Authority (BaFin) has issued a consultation paper on a draft updated guidance note on the notification of non-German UCITS funds for public distribution in Germany. The amendments to the guidance note reflect amendments to the German Investment Act (InvG) due to the implementation of UCITS IV.

In particular, the guidance note covers: (1) the procedure for notifying the intention of public distribution of non-German UCITS in Germany; (2) the requirements that have to be considered for public distribution; and (3) the procedure for submitting notifications of changes and for termination of public distribution of non-German UCITS.

Comments are due by 15 June 2011.

BaFin consults on updated guidance note on interest rate risks in banking book

The Federal Financial Supervisory Authority (BaFin) has published a consultation paper (10/2011) on an updated guidance note on interest rate risks in the banking book. The updated guidance note replaces guidance note 7/2007 (BA) of 6 November 2007. Under section 10 para 1b of the German Banking Act (KWG), BaFin is authorised to react to certain risks which are not covered by the Solvability Regulation (SolvV) by increasing capital requirements. Moreover, based on section 125 para 5 of the Capital Requirements Directive (CRD 1), reviews and evaluations performed by BaFin shall include the exposure of credit institutions to the interest rate risk arising from non-trading activities.

Amongst other things, the updated guidance note covers: (1) calculation of sudden and unexpected changes in interest rates; (2) evaluation of changes in interest rates scenarios; and (3) supervisory information requirements and further procedures.

Comments are due by 1 July 2011. A hearing on the updated guidance note will take place on 8 July 2011.

Dutch Ministry of Finance submits legislative proposal to Parliament to extend major holdings disclosure regime to cash settled instruments

The Dutch government has submitted a legislative proposal to Parliament which would, once enacted, extend the obligation to disclose major holdings and capital interests in listed companies (laid down in the Dutch Financial Supervision Act) to include certain cash-settled derivative instruments and other instruments that may lead to a sudden, previously undisclosed change of control over a listed company.

In particular, in connection with the requirement to disclose major holdings, a person will be deemed to possess shares in a relevant listed company if he/she: (1) holds a financial instrument of which the value rise depends, in whole or in part, on the value rise of shares or related distributions, and which does not give a direct right to settle in shares (e.g. contracts for differences and total return equity swaps); (2) may be required to acquire shares as a result of having sold a put option; or (3) has concluded another contract with a similar economic effect to holding shares. The Dutch government has decided to extend the current major holdings disclosure regime to cover such

instruments as well, as they may be used to secretly accumulate substantial economic positions in listed companies.

The explanatory notes to the current bill state that the new disclosure requirements would be similar to those in the UK and France, and that the Dutch government prefers, for the time being, to refrain from introducing a general requirement to disclose gross short positions in listed companies, and to await relevant developments at the EU level. The bill also provides that market participants should make an initial notification within four weeks following enactment if their stake in a listed company exceeds 3% at such time, provided that such stake has not previously been disclosed or if the enactment of the bill results in a different calculation. This 3% threshold is in line with another bill, which is currently pending, which proposes a change to the current first threshold from 5% to 3%. The new rules are expected to become law by 1 January 2012.

Code of conduct for persons licensed by or registered with SFC issued

The Securities and Futures Commission (SFC) has issued a 'Code of Conduct for Persons Licensed by or Registered with the SFC'. The SFC has indicated that it will be guided by the code in considering whether a licensed or registered person satisfies the requirement of being fit and proper to remain licensed or registered, along with the general principles in this context.

The SFC has also published a set of FAQs on the new conduct requirements. The additional FAQs are intended to help intermediaries implement the investor characterisation requirement under the code of conduct.

SGX consults on proposed listing rule changes on general meetings

The Singapore Exchange (SGX) has issued a consultation paper setting out proposed amendments to the listing rules intended to enhance shareholder engagement, encourage participation at general meetings and increase disclosure of voting outcomes.

Amongst other things, the SGX has proposed: (1) for all primary-listed companies to hold their general meetings in Singapore unless prohibited by relevant laws and regulations in the jurisdiction of its incorporation; (2) for all listed companies to adopt voting by poll, for which the SGX will provide sufficient time for administrative and logistics preparation in anticipation of the proposed rule amendments; and (3) a new rule for issuers to make prompt disclosure of the results of the polls, including details such as the number of votes for and against each resolution, as well as the number of proxy votes cast.

The SGX intends to apply the proposed amendments to both Mainboard and Catalist companies. Comments are due by 17 June 2011.

SGX consults on proposed improvements to pre-opening and pre-closing routines of securities market

The Singapore Exchange (SGX) has issued a consultation paper on its proposals to improve the pre-opening and pre-closing routines of the securities market. The proposals, which are intended to enhance the price discovery process and to strengthen market transparency, include, amongst other things: (1) the publication of real-time Indicative Equilibrium Prices throughout the pre-open and pre-close phases, so that market participants are better able to assess market demand and supply conditions and adjust their orders accordingly; and (2) the introduction of a random end to the pre-close phase of the closing routine to protect the integrity of the closing price against the impact of sudden large entry and withdrawal orders.

Comments are due by 15 June 2011.

ASIC consults on credit rating agencies' compliance reporting

The Australian Securities and Investments Commission (ASIC) has published a consultation paper (CP 160) on proposals for the form and content of annual compliance reporting by licensed credit rating agencies (CRAs) under their AFS licence conditions. In particular, CP 160 proposes implementing reporting requirements for CRAs concerning their compliance with obligations on matters such as the quality and integrity of their ratings process, conflicts of interest management and the transparency and timeliness of ratings disclosure.

Comments are due by 13 July 2011.

US Federal agencies consult on proposed stress-testing guidance

The Board of Governors of the Federal Reserve System (FRB), the Office of the Comptroller of the Currency (OCC), and the Federal Deposit Insurance Corporation (FDIC) have invited comments on proposed supervisory

guidance regarding stress-testing practices at banking organizations with total consolidated assets of more than USD 10 billion.

The proposed guidance outlines general principles for a satisfactory stress testing framework and describes how stress testing should be used at various levels within an organization. The guidance also discusses the importance of stress testing in capital and liquidity planning, and the importance of strong internal governance and controls in an effective stress-testing framework.

Comments are due by 29 July 2011.

US Federal agencies extend comment period on risk retention proposed rulemaking

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the Federal Housing Finance Agency, the Department of Housing and Urban Development, the Office of the Comptroller of the Currency (OCC) and the Securities and Exchange Commission (SEC) have announced an extension of the comment period on the proposed rules to implement the credit risk retention requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Comments were originally due by 10 June 2011, but the comment period has now been extended until 1 August 2011.

US Federal agencies issue guidance on the advanced measurement approaches for operational risk

The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision, have issued guidance on the advanced measurement approaches (AMA) for operational risk. The interagency guidance discusses a number of common implementation issues, challenges and considerations for addressing these challenges in order to implement a satisfactory AMA framework. The guidance primarily focuses on the combination and use of the four required AMA data elements – internal operational loss event data, external operational loss event data, business environment and internal control factors, and scenario analysis.

The OCC has emphasized that the guidance addresses certain aspects of the minimum risk-based capital requirements for operational risk, and is not intended to address the treatment of operational risk in a bank's internal capital adequacy assessment process.

FRB Governor Tarullo discusses regulation of systemically important financial institutions

Federal Reserve Board Governor Daniel K. Tarullo has given a speech on the requirement in the Dodd-Frank Wall Street Reform and Consumer Protection Act that the Federal Reserve Board (FRB) establish new prudential standards to address the risk of disorderly failure of systemically important financial institutions. Mr. Tarullo focused on the additional capital requirements that would be imposed on systemically important financial institutions beyond the minimum requirements established by Basel III.

He noted that the Dodd-Frank Act does not specify the form of enhanced capital requirements for systemically important financial institutions and suggested certain desirable characteristics of the supplemental capital requirements, including: (1) calculating the capital requirement using a transparent and replicable metric based on the impact of a firm's failure on the financial system as a whole; (2) being progressive in nature, i.e., increasing in stringency with the estimated systemic significance of the firm; (3) building in constructive incentive effects to discourage systemically consequential growth or mergers; (4) meeting an enhanced requirement with high-quality capital; and (5) being congruent with international standards.

Mr. Tarullo also noted that the FRB will in any case apply the enhanced capital standards to foreign banking organizations operating in the United States.

In addition, Mr. Tarullo suggested that the FRB is likely to focus primarily on the 'expected impact' approach to determine how much additional capital would be needed to reduce the probability of failure of a systemically important financial institutions sufficiently to equalize the expected impact on the financial system of the failure of a systemically important financial institutions and the failure of a banking firm that is not systemically important. He noted that the enhanced capital requirement implied by this methodology can range between about 20% to more than 100% over the Basel III requirements, depending on the choice made among plausible assumptions.

RECENT CLIFFORD CHANCE BRIEFINGS

State guarantees and State aid – some hope for lenders

An Advocate General to the European Court of Justice has issued an opinion that EU law does not require that State guarantees conferring unlawful State aid on a borrower are void and unenforceable.

In her opinion of 26 May 2011, Advocate General (AG) Kokott re-examined statements in the previous case law of the EU Courts that had been widely construed as endorsing the unenforceability of such guarantees, and the duty of lenders to verify for themselves the lawfulness of the State guarantees against which they lend. She concluded that those statements should not, in fact, bear that interpretation. In particular, the AG opined that a lender's duty of due diligence extends only so far as confirming that a guarantee will not confer unlawful State aid on it, the lender, and that there is no such requirement to investigate whether the borrower will receive such State aid as a result of the guarantee.

If the ECJ does follow AG Kokott's opinion, it will considerably mitigate (but not eliminate) the risks for lenders in lending against a State guarantee, in particular in those countries, such as the UK, that do not have any national legislation expressly providing for invalidity of any contractual measure through which unlawful State aid is granted.

This briefing discusses the AG's opinion.

http://www.cliffordchance.com/publicationviews/publications/2011/06/state_guaranteesandstateaidsomehopefo.html

Contentious Commentary – a review for litigators

This newsletter provides a summary of recent developments in litigation. The newsletter is produced by lawyers in the litigation and dispute resolution practice at Clifford Chance.

http://www.cliffordchance.com/publicationviews/publications/2011/06/contentious_commentaryareviewforlitigators.html

UK Credit Guarantee Scheme – opening the door to buybacks of guaranteed debt

On 8 June 2011, HM Treasury announced amendments to the rules of the UK Government's Credit Guarantee Scheme, permitting eligible institutions to repurchase UK Government guaranteed debt in certain circumstances. As well as providing UK banks and financial institutions with a welcome opportunity to manage their liability profiles, it also signals the continued restoration of confidence in the UK banking sector.

This briefing discusses the changes.

http://www.cliffordchance.com/publicationviews/publications/2011/06/uk_credit_guaranteeschemeopeningthedoort.html

Broadening the Equator Principles beyond Project Finance – New Proposals

A review of the Equator Principles has made recommendations to change a number of aspects of the Equator Principles framework and these could have a significant impact on finance transactions. In particular, use of the Equator Principles could extend beyond pure project finance to corporate loans where the majority of funds are used to finance a single asset. These suggested changes to the Equator Principles framework will need to go through the formal Equator Principles institutions' deliberation process before the Equator Principles can be changed and this will take several months. Signatories and non-signatories to the Equator Principles alike should start to assess now the impact that the proposed changes could have on finance transactions and consider taking part in the update process.

This briefing discusses the recommendations.

http://www.cliffordchance.com/publicationviews/publications/2011/06/broadening_the_equatorprinciplesbeyondprojec.html

CSSF Circular 11/512 dated 30 May 2011 UCITS Risk Management

The Luxembourg Commission de Surveillance du Secteur Financier (CSSF) has issued a new circular (Circular 11/512) that provides an overview of the main changes to the regulatory framework relating to UCITS risk

management in light of CSSF Regulation 10-4 and the publication by ESMA of a number of documents on risk management. In particular, Circular 11/512 provides details regarding the rules on risk management provided for in these documents, identifies the content and format of the risk management process to be communicated to the CSSF, and includes a template to be followed by UCITS management companies and self-managed UCITS for the description of this risk management process.

This briefing sets out the key points of the circular and the implications for UCITS management companies and self-managed UCITS falling within the scope of the circular.

http://www.cliffordchance.com/publicationviews/publications/2011/06/cssf_circular_11512dated30may2011ucitsris.html

SFC launches consultation on Securities and Futures (Short Position Reporting) Rules implementing new reporting regime

The Securities and Futures Commission (SFC) has issued a consultation paper on the proposed Securities and Futures (Short Position Reporting) Rules, implementing a new reporting regime for short positions. The proposed rules largely follow the results of a first consultation launched by the SFC in 2009 on the introduction of such a reporting regime, which were published by the SFC in March 2010.

This briefing summarises the key features of the proposed rules and highlighting the modifications introduced by the SFC compared to the first consultation conclusions.

http://www.cliffordchance.com/publicationviews/publications/2011/06/sfc_launches_consultationonsecuritiesan.html

The Industrial Revitalisation Law amendment

An amendment in respect of the Law on Special Measures for Industrial Revitalisation and Innovation was passed by the Diet on 18 May 2011 and promulgated on 25 May 2011. The amendment is mainly aimed at accelerating strategic industrial reorganisation to strengthen the global competitiveness of Japanese industries. The amendment contains certain new special measures which may influence M&A transactions.

This briefing summarises the main points.

English version
http://www.cliffordchance.com/publicationviews/publications/2011/06/the_industrial_revitalisationlawamendment.html

Japanese version
http://www.cliffordchance.com/publicationviews/publications/2011/06/the_industrial_revitalisationlawamendmen.html

E-meetings for Indian companies

India has permitted directors and shareholders of Indian companies to participate in board and shareholders' meetings, through videoconferencing. This will not only help in improving governance of widely held Indian public companies but will also be of particular benefit to non-resident directors of Indian companies.

This briefing discusses the new rules.

http://www.cliffordchance.com/publicationviews/publications/2011/06/e-meetings_for_indiancompanies.html

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