CLIFFORD CHANCE

Briefing note

International Regulatory Update

6 – 10 January 2014

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Greek EU Council Presidency unveils work programme

On 1 January 2014, Greece took over the EU Council's six-month rotating Presidency. The Greek EU Council Presidency has now published its work programme, which sets out the items on the EU Council's agenda in the first half of 2014 and which of them will be priorities for the Greek Presidency.

Amongst other things, the Greek Presidency will strive to reach agreement with the EU Parliament on the Single Resolution Mechanism (SRM) within the current parliamentary term.

The Greek Presidency will also focus on:

- the revision of the legal framework for payment services (PSD 2);
- the proposal for a directive on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features;
- reaching an agreement within the Council on the updated framework for combating money laundering and terrorist financing;
- the completion of work on the Markets in Financial Instruments Regulation and Directive (MiFIR/MiFID 2); and
- discussions on the benchmarking legislative proposal.

CRR/CRD 4: EU Commission publishes draft ITS on supervisory reporting

The EU Commission's Directorate General for the Internal Market and Services has published a draft version of its forthcoming Implementing Technical Standards (ITS) with regard to supervisory reporting of institutions under the Capital Requirements Regulation (CRR) in order to help all interested parties to begin to prepare for the new requirements for supervisory reporting under the CRR/CRD 4 framework.

Within the next couple of months, once all language versions are available, the Commission services intend to submit this draft standard to the College of the Commission for adoption. The Commission has emphasised that only the Implementing Regulation on Supervisory Reporting by institutions as finally adopted by the Commission and published in the Official Journal of the European Union will be legally binding.

SEPA: EU Commission proposes additional transition period of six months

The EU Commission has adopted a proposal for a regulation amending Regulation (EU) 260/2012 as regards the migration to EU-wide credit transfers and direct debits to give an extra transition period of six months during which payments which differ from the Single Euro Payments Area (SEPA) format can still be accepted. The proposal is intended to minimise any possible risk of disruption to payments for consumers and businesses. The proposal does not change the formal deadline for migration of 1 February 2014, but the introduction of a transitional period of six months, until 1 August 2014, means that banks and payment institutions will be able to agree with their clients to process payments that differ from the SEPA standard until then. After 1 August 2014, there will be no further transitional period.

Taking into account the urgency of the situation, the Commission has urged the EU Council and Parliament to take up and agree this proposal rapidly so as to ensure legal clarity for all stakeholders. The Commission has also called upon Member States to ensure that, should the proposal still be in the process of adoption on 1 February 2014, banks and payment services providers will not be penalised for continuing to process legacy payments in parallel with SEPA payments. The Commission has indicated that for this reason the proposal, if adopted after 1 February 2014 by the Council and Parliament, will have a retroactive effect as from 31 January 2014.

The Eurosystem has issued a statement stressing that the SEPA migration end date of 1 February 2014 remains and urging all market participants to complete the transition of all credit transfer and direct debit transactions to the SEPA standards by this date.

Market abuse review: ECON Committee votes on proposed directive on criminal sanctions

The EU Parliament's Committee on Economic and Monetary Affairs (ECON) has voted on the EU Commission's proposal for a directive on criminal sanctions for insider dealing and market manipulation, backing an agreement on the proposal reached with the EU Council in December 2013.

The directive will oblige Member States to provide in their national legislation for criminal penalties in respect of insider dealing, market manipulation and unlawful disclosure of inside information. The directive will be applied taking into account the legal framework established by the Market Abuse Regulation (MAR) and will amend and replace Directive 2003/6/EC.

The agreement means that:

- there will be common EU definitions of market abuse offences such as insider dealing, unlawful disclosure of information and market manipulation;
- there will be a common set of criminal sanctions including fines and imprisonment with a maximum sanction of at least four years for insider dealing/market manipulation and of two years for unlawful disclosure of inside information;
- legal persons will be held liable for market abuses;
- Member States need to establish jurisdiction for these offences if they occur in their country or the offender is a national; and
- Member States need to ensure that judicial and law enforcement authorities dealing with these cases are well trained.

The agreement is now expected to be confirmed by the EU Parliament in plenary in February 2014.

PSD 2: EU Parliament Legal Affairs Committee publishes opinion

The EU Parliament's Committee on Legal Affairs has published an opinion for the ECON Committee on the proposed new Payment Services Directive (PSD 2).

EU Parliament Legal Affairs Committee publishes opinions on proposed regulation on information accompanying transfers of funds and new Anti-Money Laundering Directive

The EU Parliament's Committee on Legal Affairs has published its opinions, both dated 4 December 2013, on the proposed regulation on information accompanying transfers of funds and the proposed directive on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

MiFID: ESMA publishes draft technical standards on assessment of acquisitions and increases in qualifying holdings in investment firms

The European Securities and Markets Authority (ESMA) has published its final draft technical standards, dated 17 December 2013, on the assessment of acquisitions and increases in qualifying holdings in investment firms under Article 10a(8) of Markets in Financial Instruments Directive (MiFID).

Article 10b(4) of MiFID requires Member States to make publicly available the information necessary to carry out the assessment of a proposed acquirer of an investment firm. The information must be provided by the proposed acquirer at the time of the initial notification and is aimed at ensuring that competent authorities are provided with adequate and proportionate information in order to assess the acquisition. Article 10a of MiFID, as amended by Article 6(4) of the Omnibus II Directive, requires ESMA to draft:

- regulatory technical standards (RTS) to establish an exhaustive list of information referred to in Article 10b(4) of MiFID; and
- implementing technical standards (ITS) to determine standard forms, templates and procedures for the cooperation and exchange of information between the relevant competent authorities as referred to in Article 10(4) of MiFID.

ESMA has submitted the draft RTS and ITS to the EU Commission. The Commission has three months to decide whether to endorse ESMA's draft technical standards.

Omnibus II: ESMA urges Commission to allow sufficient time for drafting RTS on prospectus related issues

ESMA has published a letter, dated 16 December 2013, in which its Chair urges the EU Commission to ensure that ESMA has sufficient time to draft the regulatory technical standards on prospectus related issues it is required to prepare under the proposed Omnibus II Directive.

The original proposal foresaw the drafting of four RTS by ESMA together with the establishment of a system for receipt of final terms to be communicated to ESMA by issuers. The RTS concern:

- information to be incorporated by reference;
- procedures for the approval of a prospectus and the conditions in accordance with which time limits may be adjusted;

- provisions relating to the publication of prospectuses; and
- dissemination of advertisements prior to a prospectus being made available to the public or before the opening of subscription.

The deadline for the submission of each of these draft RTS to the Commission was set in the Omnibus II proposal at 1 January 2014. However, the EU Parliament is currently not expected to vote on the proposal until March 2014 and the deadline will need to be changed.

ESMA considers that in order to complete all required steps for high quality technical standards a minimum of one year is needed for the draft RTS and the establishment of a technical solution for receipt of final terms. The letter therefore urges the Commission to include in the Omnibus II Directive a generic reference for ESMA to submit the draft RTS within one year from the publication of the directive in the Official Journal.

IOSCO and FSB consult on assessment methodologies for identifying non-bank non-insurer global systemically important financial institutions

The International Organization of Securities Commissions (IOSCO) and the Financial Stability Board (FSB) have jointly published a consultation paper on assessment methodologies for identifying non-bank non-insurer global systemically important financial institutions (NBNI G-SIFIs). The assessment methodologies for identifying NBNI G-SIFIs complement the methodologies that currently cover banks and insurers.

The FSB and IOSCO based their work in developing the methodologies on the following two principles:

- the objective in developing the methodologies is to identify NBNI financial entities whose distress or failure would cause significant disruption to the global financial system and economic activity across jurisdictions; and
- the general framework should be broadly consistent with methodologies for identifying global systemically important banks and insurers (G-SIBs and G-SIIs).

Comments are due by 7 April 2014.

Law on limited purpose loans for socially responsible projects published

A new law on limited purpose loans for socially responsible projects has been published in the Moniteur Belge / Belgisch Staatsblad. The law creates a legal framework for the collection by credit institutions of long-term savings from retail investors, and the use of those funds for socially responsible projects. The law provides for a reduction of the withholding tax rate on interest received by retail investors on these instruments.

Ministerial Order on prudential regime for financing companies published

A Ministerial Order on the prudential regime for financing companies (sociétés de financement), dated 23 December 2013, has been published in the Journal Officiel. The Order determines the prudential regime for financing companies, which is intended to be comparable to that for credit institutions in terms of its robustness.

Unless otherwise provided, financing companies have to comply with the following rules applicable to credit institutions:

- the EU Capital Requirements Regulation (CRR);
- Regulation no. 91-05 of the French Banking and Financial Regulation Committee (Comité de la réglementation bancaire et financière – CRBF) of 15 February 1991 relating to the solvency ratio;
- Regulation no. 97-02 of the CRBF of 21 February 1997 relating to internal control in credit institutions; and
- the Ministerial Order (arrêté ministériel) of 5 May 2009 regarding identification, measure, management and monitoring liquidity risk.

The Order adjusts certain of the above rules to financing companies. In this respect, the Order states that, amongst other things:

- financing companies are exempted from the liquidity and leverage requirements (in particular, ratios) provided for in the CRR;
- for the purposes of article 119 para 1 and article 129 para 1(a) of the CRR, financing companies are deemed to be subject to prudential requirements comparable to those applied to credit institutions in terms of robustness;
- assets and off-balance sheet liabilities provided by the financing company to its managers and main shareholders must be deducted from the financing company’s own funds – for this purpose, the Order provides for a specific definition of managers and main shareholders;
- unless otherwise provided, the EU Commission’s delegated and implementing regulations related to the CRR do not apply to financing companies;

- provisions relating to financial holding companies must be applicable to a financing company's parent undertaking and to financing companies controlled by it; and
- the reporting requirements of the financing company under the CRR will be specified by a relevant instruction of the Autorité de contrôle prudentiel et de résolution.

Securities Association of China amends norms for direct investment business of securities companies

The Securities Association of China (SAC) has amended the 'Norms for Direct Investment Business of Securities Companies' in order to encourage innovation of securities companies' direct investment business and support small and micro enterprises. The amended Norms have been filed with the China Securities Regulatory Commission (CSRC) and took effect from 3 January 2014.

Amongst other things, the amendments include the following:

- direct investment funds set up by direct investment subsidiaries of securities companies are additionally allowed to invest in target enterprises through debt instruments, which was previously permitted only when associated with equity investment – direct investment subsidiaries can now also provide financial advisory services in relation to debt instrument investments;
- it has been clarified that direct investment subsidiaries are not allowed to carry out any business that is within the statutory business scope of securities companies;
- commercial papers (that are registered with the National Association of Financial Market Institutional Investors) and reverse bond repurchase agreements are added to the permissible proprietary investment scope of direct investment subsidiaries, affiliates controlled by direct investment subsidiaries and direct investment funds (direct investment entities);
- securities companies can now provide security for their direct investment entities;
- direct investment entities may apply leverage strategy through incurring indebtedness, but non-wholly-owned affiliates controlled by direct investment subsidiaries and direct investment funds may not incur debt with a tenor of more than 12 months or which exceeds 30% of the registered capital / paid-in capital contribution;
- individuals are now eligible for investing in direct investment funds; and
- interests of direct investment funds can be subscribed and transferred through the OTC market of securities companies, inter-institution quotation and transfer system of SAC and other trading facilities recognised by the CSRC.

Government consults on establishing an effective resolution regime for financial institutions in Hong Kong

The Hong Kong government and the financial regulators, namely the Hong Kong Monetary Authority (HKMA), the Securities and Futures Commission (SFC) and the Insurance Authority (IA), have jointly launched the first stage of a public consultation on establishing an effective resolution regime for financial institutions in Hong Kong.

The government believes that the establishment of an effective resolution regime for financial institutions in Hong Kong is required to meet the latest international standards for the regulation and supervision of financial institutions. An effective resolution regime is intended to provide the authorities with powers to resolve non-viable financial institutions without severe systemic disruption whilst protecting taxpayers.

The proposed resolution regime for financial institutions in Hong Kong seeks to meet the standards set out in the 'Key Attributes of Effective Resolution Regimes for Financial Institutions' issued by the Financial Stability Board (FSB) in November 2011.

The consultation is intended to seek views from the public and the financial services industry on initial thinking and some proposals for establishing a resolution regime in Hong Kong. The government will analyse the views and comments received to further develop the proposals for the second stage of the public consultation. The government aims to conduct the second stage of the public consultation later in 2014 on the more specific details and operation of the resolution regime. Subject to the outcome of the public consultation, the government will seek to introduce legislative proposals into the Legislative Council in 2015.

Comments are due by 6 April 2014.

HKMA issues circular on risks associated with virtual commodities

The HKMA has issued a circular to remind all authorised institutions of the need to exercise prudent risk management regarding the money laundering and terrorist financing risks associated with virtual commodities. The circular follows recent global attention on virtual commodities such as Bitcoin and their associated money laundering and terrorist financing risks.

Under the 'Guideline on Anti-Money Laundering and Counter-Terrorist Financing', authorised institutions are advised to assess the extent to which their services are vulnerable to money laundering and terrorist financing abuse. The circular notes that this is especially relevant where emerging technological developments may facilitate anonymity. According to the HKMA, virtual commodities that are transacted or held on the basis of anonymity fall into this category and pose significantly higher inherent money laundering and terrorist financing risks, including risks associated with potential or existing customers that may use authorised institutions' accounts or other services for any activities relating to virtual commodities. Authorised institutions are therefore advised to ensure an escalated level of vigilance commensurate with these risks when considering whether to establish or maintain business relationships with customers who are operators of schemes related to virtual commodities.

As in the case of any new business development, the HKMA expects authorised institutions to conduct comprehensive risk identification and assessment, taking into account potential regulatory requirements locally and overseas, when considering whether to offer any new banking or investment products relating to virtual commodities. Specifically, before an authorised institution offers any product to customers that involves or is linked to any virtual commodity it should notify and discuss this with the HKMA.

RBI issues circular in relation to FDI instruments with optionality clauses

The Reserve Bank of India (RBI) has issued a circular on its decision to allow optionality clauses in equity shares and compulsorily and mandatorily convertible preference shares/debentures to be issued to a person resident outside India under the foreign direct investment (FDI) scheme. The optionality clause will oblige the buy-back of securities from the investor at the price prevailing/value determined at the time of exercise of the optionality so as to enable the investor to exit without any assured return. The provision of optionality clause will be subject to the following conditions:

- there is a minimum lock-in period of one year or a minimum lock-in period as prescribed under FDI regulations, whichever is higher;
- after the lock-in period, the non-resident investor exercising option/right will be eligible to exit without any assured return as per the following norms:
  - in case of a listed company, the non-resident investor will be eligible to exit at the market price prevailing at the recognised stock exchanges; and
  - in case of unlisted company, the non-resident investor will be eligible to exit from the investment in equity shares of the investee company at a price not exceeding that arrived at on the basis of Return on Equity (RoE) (RoE shall mean Profit After Tax / Net Worth; Net Worth would include all free reserves and paid up capital) as per the latest audited balance sheet; and
- investments in compulsorily convertible debentures (CCDs) and compulsorily convertible preference shares (CCPS) of an investee company may be transferred at a price worked out as per any internationally accepted pricing methodology at the time of exit duly certified by a chartered accountant or a Securities and Exchange Board of India (SEBI) registered merchant banker.

Japanese Bankers Association sets out plan for reform of JBA TIBOR

The Japanese Bankers Association (JBA) has published a report outlining a plan for the reform of JBA TIBOR administration systems as well as the Code of Conduct for reference banks. In response to incidents occurring a few years ago, the JBA has been exploring measures to maintain and enhance the credibility of JBA TIBOR and to bring it in line with LIBOR and IOSCO's 'Principles for Financial Benchmarks', published on 17 July 2013.

The report sets out proposed measures to enhance the governance systems of the benchmark administrator and of reference banks. The JBA will establish a new entity to which it will transfer its TIBOR calculation and publication operations. The new entity will establish a governance system, which focuses on aligning the fairness and transparency of benchmark administrations with the IOSCO's 'Principles for Financial Benchmarks'. The JBA will replace the 'JBA TIBOR Publication Rules', which currently provide for TIBOR publication processes and other matters, with the Code of Conduct. The Code of Conduct provides the rules which reference banks should comply with and the internal systems which they should have in place in connection with rate submissions.

The JBA aims to implement the measures described above as soon as possible although the effective date is yet to be determined.

FSA consults on draft amended guidelines for supervision of major banks and inspection manual for credit institutions

The Financial Services Agency of Japan (FSA) has published the draft amended 'Comprehensive Guidelines for Supervision of Major Banks' and 'Inspection Manual for Credit Institutions' for public comment.

The draft guidelines set out a number of points the FSA should consider as part of its supervisory function of statutory auditors (e.g. whether the statutory auditor has sufficient knowledge and experience to independently audit directors' execution of their duties so as to ensure sound and appropriate operation of the relevant bank). This builds upon the amended Banking Act which was passed by the Diet on 12 June 2013 and introduced the fit-and-proper requirements for statutory auditors of licensed banks.

The draft guidelines also clarify issues that the FSA should have regard to when supervising branch offices of foreign banks operating in Japan that accept deposits (e.g. whether the branch office transfers most of the funds deposited by residents of Japan outside Japan).

Comments are due by 14 February 2014.

FSA seeks public comment on draft amended Ordinance for Enforcement of Banking Act

The FSA has published a draft amended Ordinance for Enforcement of the Banking Act for public comment.

Under the current regulatory framework, a bank licensed under the Banking Act of Japan may act as an agent or intermediary for a foreign bank which is, among others things, a subsidiary or parent company of a licensed bank. The draft Ordinance allows a licensed bank to act as an agent or intermediary for a foreign bank which is not a subsidiary, as long as the agency or intermediary activities are conducted outside of Japan.

The draft Ordinance also details issues the regulator should consider when reviewing an application for a banking business licence submitted by a foreign bank (e.g., whether the assets of a foreign bank branch in Japan are sufficient for the branch to carry out its banking business soundly and efficiently).

Comments are due by 27 January 2014.

Ministry of Strategy and Finance revises tax code to stimulate venture capital

The Ministry of Strategy and Finance (MOSF) has announced the government's plan to promote the creation of a 'try again' culture by supporting angel investment and venture capital through the tax code. Incentives under the tax code will be created to stimulate business growth by supporting technology mergers and acquisitions (M&As) and strategic partnerships in order to promote technological innovation.

According to the MOSF, tax incentives will be offered to venture capital investments according to the stage of the investment cycle. At the creation stage, venture financing will have its emphasis shift from loan-centered financing to investment centered financing, and tax deductions for investing in startups will be increased. Investments of up to 50 million won will be eligible for a 50% income tax deduction, and any amount exceeding the first 50 million won will be eligible for a 30% deduction. This deduction will not be included in the total income tax deduction limit. In addition, direct investment in Korea New Exchange (KONEX)-listed businesses will be exempt from both the corporate tax for income from dividends and capital gains, and the securities transaction tax.

At the growth and remittance stage, a tax credit (10% tax deduction for the amount that the technology is valued at) will be instituted to stimulate technology M&As. Tax postponement systems will be created to support venture businesses that engage in strategic partnerships. To this end, taxes on the exchange of shares between businesses that engage in strategic partnerships will be deferred until those shares are sold.

At the reinvestment stage, tax postponement systems will be created in order to promote reinvestment by venture startups. In this regard, taxes on the sale of ventures shares, where the money is reinvested in another startup or venture, will be deferred until the reinvested shares are sold.

FINRA announces 2014 regulatory and exam priorities

The Financial Industry Regulatory Authority (FINRA) has published its 2014 Regulatory and Examination Priorities Letter, which breaks down according to business conduct, fraud, and financial and operational priorities.

Areas specifically addressed by the Priorities Letter include:

- suitability issues, including those related to complex structured products, private real estate investment trusts, 'frontier funds' (i.e., funds focused on what investment managers consider to be the next emerging markets), and interest rate sensitive securities products;

- offerings, including initial public offerings and FINRA's anti-spinning rules, private placements involving general solicitation under new SEC Rule 506(d), and private placement due diligence practices;
- fraud in microcap and low-priced over-the-counter securities, insider trading, and manipulative practices in algorithmic and high frequency trading;
- funding and liquidity risks including risk control and assessment documentation required to be maintained by certain firms under recent amendments to Rule 17a-3 of the US Securities Exchange Act of 1934;
- anti-money laundering controls in connection with firms executing large volumes of low-priced securities on a DVP/RVP (Delivery Versus Payment/Receipt Versus Payment) basis without examining such transactions for suspicious activity and filing suspicious activity reports (SARs) if necessary; and
- customer identification practices due to a perceived 'misconception' at some executing broker-dealers that their Customer Identification Program (CIP) requirements do not apply to DVP/RVP customers (who are not otherwise exempt), and/or that the prime broker is responsible for CIP on those customers.

A cover letter accompanying the Priorities Letter also emphasizes FINRA's plan to use technology to gather more and different data to identify and prioritize risks, and to better protect investors and monitor securities markets. For example, FINRA intends for its proposed Comprehensive Automated Risk Data System (CARDS) to enable it to regularly and automatically collect and analyze standardized account information, account activity, and securities holdings maintained by firms as part of their books and records.

RECENT CLIFFORD CHANCE BRIEFINGS

2013 Review – US Federal Courts Address Jurisdiction Over Cases Involving Alleged Human Rights Abuses Committed Abroad

The US Supreme Court's 2013 decision in Kiobel v. Royal Dutch Petroleum Co. limiting the extraterritorial reach of the Alien Tort Statute (ATS) dominated the year's news for human rights litigation. In 2014, plaintiffs and defendants will continue to fight in the lower courts to define the scope of the Supreme Court's ruling. In the meantime, a pending Supreme Court decision promises to further address the extraterritorial reach of US law.

This briefing discusses the Kiobel decision.

http://www.cliffordchance.com/publicationviews/publications/2014/01/2013_review_us_federalcourtsaddres.html