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Briefing note

International Regulatory Update

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UK and EU authorities react to outcome of referendum

The Presidents of the EU Council, Parliament, and Commission and the Prime Minister of the Netherlands as holder of the rotating Presidency of the Council of the EU have published a joint statement following a meeting in Brussels in response to the outcome of the UK referendum on EU membership. Among other things, the statement sets out:

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- an expectation that the UK Government give effect to the decision under Article 50 of the Treaty on European Union as soon as possible;
- the New Settlement for the UK within the EU, agreed at the European Council in February 2016, will now not take effect and ceases to exist; and
- any agreement which will be concluded with the UK as a third country will have to reflect the interests of both sides and be balanced in terms of rights and obligations.

The EU Commission has also published a Q&A on the role the Commission will play in the Article 50 process. The College of Commissions is expected to meet on 27 June to assess the situation and prepare for the European Council on 28-29 June 2016.

The UK Prime Minister made a statement on the outcome of the referendum and will attend the European Council to explain the decision. However, the Prime Minister also set out his intention to stand down by October and announced that the decision about when to trigger Article 50 should be taken by the new Prime Minister.

The Governor of the Bank of England gave a statement that highlighted that HM Treasury and the Bank have engaged in contingency planning and the Bank intends to take additional measures as required, including readiness to provide additional funds through normal facilities and liquidity in foreign currency, if required. The Bank intends to assess economic conditions and will consider any additional policy responses.

The Financial Conduct Authority (FCA) and Payment Systems Regulator (PSR) also published statements on the referendum result and highlighted, among other things, that firms must abide by their obligations under UK law, including those derived from EU law, and continue implementation plans for legislation that is still to come into effect.

Banking Union: EU Council publishes conclusions on roadmap towards completion and ECON publishes working document on EDIS

The EU Council has published conclusions on a roadmap to complete the Banking Union, which sets out the Council's view of the importance of work being carried out by institutions at Banking Union, EU28 and international level. Among other things the Roadmap underlines certain key steps, including the Council's intention to:

- begin technical work with a view to swift implementation of measures to be put forward by the EU Commission on banking, including implementation of the Total Loss Absorbing Capacity (TLAC) and reviewing the minimum requirement for own funds and eligible liabilities (MREL);
- await the outcomes of the Basel Committee on the regulatory treatment of sovereign exposures;
- continue constructive work at a technical level on the European Deposit Insurance Scheme (EDIS), on which the Council notes the intention of Member States to have recourse to an intergovernmental agreement (IGA) when political negotiations begin; and
- annually assess progress made towards completing the Banking Union.

On the Single Resolution Fund (SRF), the Council has also noted the intention by Member States to begin work in September 2016 once all participating Member States have fully transposed the Bank Recovery and Resolution Directive (BRRD).

Separately on 16 June, the EU Parliament Committee on Economic and Monetary Affairs (ECON) published a working document on the legislative proposal for EDIS and the Commission's communication entitled 'Towards the Completion of the Banking Union'. The working document examines both documents as a single package, despite their difference in legal nature, and sets out linkages between the EDIS proposal and certain other legislative texts and structures, discusses relevant key elements in the debate about risk reduction and determines a number of key questions for the future handling of the package to complete the Banking Union.

SSM: ECB reports on governance and risk appetite

The European Central Bank (ECB) has published a Single Supervisory Mechanism (SSM) supervisory statement on governance and risk appetite. The statement follows a thematic review of significant institutions' (SIs') management bodies in charge of supervisory and management functions and their risk appetite framework (RAF).

The statement sets out lessons learnt from the thematic review and describes some good practices observed across the SIs, but is not intended to provide exhaustive guidance on effective governance and RAFs. The statement sets out certain supervisory expectations regarding a bank's board and RAF.

Overall, the ECB has identified that major improvements have been made but most SIs fall short of international best practices. The ECB intends to continue to foster dialogue and interaction with management bodies in order to promote adequate and sound governance arrangements.

BRRD: ITS on identification and transmission of information by authorities to EBA publishes in Official Journal

A Commission Implementing Regulation (2016/962) laying down implementing technical standards (ITS) with regard to uniform formats, templates and definitions for the identification and transmission of information by competent authorities and resolution authorities to the European Banking Authority (EBA) under the Bank Recovery and Resolution Directive (BRRD) has been published in the Official Journal.

The Regulation will enter into force on 7 July 2016.

MiFID: ESMA publishes document on waivers from pre-trade transparency

The European Securities and Markets Authority (ESMA) has published a document setting out waivers from pre-trade transparency under MiFID, relating to ESMA's predecessor, the Committee of European Securities Regulators (CESR), positions and ESMA opinions on functionalities subject to the waiver process.

Under MiFID, operators of regulated markets (RMs) and multilateral trading facilities (MTFs) must make public the current bid and offer prices and the depth of trading interests in respect of shares admitted to trading on a regulated market unless exemptions apply. MiFID allows competent authorities to grant four types of waivers which are contained in Articles 18 and 20 of the MiFID Implementing Regulation (1287/2006), in relation to:

- reference price systems;
- negotiated trade systems;
- order management facilities; and
- large-in-scale transactions.

ESMA's waivers document includes a table of waivers granted by national competent authorities and is aimed at competent authorities with the intention to ensure convergence of supervisory activities in accordance with ESMA's opinions and also provide firms with clarity as to the content of the MiFID requirements without creating an extra layer of requirements and to assist firms when they intend to develop new trading functionalities.

EBA publishes 2016 consumer trends report

The European Banking Authority (EBA) has published its fifth annual consumer trends report. The report sets out the trends the EBA has observed in 2016 and any issues that may arise or have arisen for consumers. The report aims to provide early indicators as to the areas in which the EBA may take action, and also summarises measures taken by the EBA to address issues identified in the previous year's report.

Eight different consumer trends, including selling practices, alternative financial services providers, virtual currencies, indebtedness and banking fees and costs, have been highlighted in this year's report. The EBA has started to address some of these trends and will use the findings of the report as input when developing and publishing its work programme for 2017.

FSB consults on policy recommendations to address structural vulnerabilities from asset management activities

The Financial Stability Board (FSB) has launched a consultation on its proposed policy recommendations to address structural vulnerabilities from asset management activities. The 14 recommendations proposed by the FSB address four structural vulnerabilities the FSB believes could potentially present financial stability risks:

- liquidity mismatch between fund investments and redemption terms and conditions for fund units;
- leverage within investment funds;
- operational risk and challenges in transferring investment mandates in stressed conditions; and
- securities lending activities of asset managers and funds.

Issues associated with liquidity mismatch and leverage are considered key vulnerabilities by the FSB. The recommendations are intended to provide authorities and asset management entities with the tools and data to effectively detect and address the identified risks. The FSB intends to finalise the policy recommendations by the end of 2016, many of which will be operationalised by the International Organization of Securities Commissions (IOSCO) in its work to address data gaps related to funds.

Comments to the consultation close 21 September 2016.

HKEX and KRX sign non-binding letter of intent for exploring cross-listing of equity derivatives

Hong Kong Exchanges and Clearing Limited (HKEX) and the Korea Exchange (KRX) have announced that they have signed a non-binding letter of intent to explore the cross-listing of their equity derivatives in each other's markets. The equity derivatives under consideration include, but are not limited to, stock index futures and options and single stock futures and options offered in local currency.

The HKEX expects the cross-listing between KRX and HKEX to open up significant opportunities as the trading hours largely overlap. Investors will be able to trade cross-listed products in the same way that they transact local products.

SFC and HKEX launch joint consultation on listing regulation

The Securities and Futures Commission (SFC) and HKEX have jointly launched a consultation on proposed enhancements to the Stock Exchange of Hong Kong Limited's (SEHK's) decision-making and governance structure for listing regulation.

Under the proposals:

- two new Exchange Committees on which the SFC and the SEHK are equally represented will be established – the Listing Policy Committee, which will initiate, steer and decide listing policy with participation by representatives of the HKEX Board and the Takeovers and Mergers Panel, and the Listing Regulatory Committee, which will decide on initial public offer (IPO) and post-IPO matters that have suitability concerns or broader policy implications;
- the Listing Committee will provide a non-binding view to both the Listing Policy Committee and the Listing Regulatory Committee on their decisions;
- the listing function will remain within the SEHK, which will continue to be the frontline regulator for listing matters;
- the Listing Committee, together with the Listing Department, will continue to decide a large majority of initial listing applications and post-listing matters; and
- the SFC's powers and functions in relation to listing matters will remain unchanged, but the ways in which those powers and functions are exercised and performed will be enhanced.

The enhancements are intended to:

- achieve, through the Listing Policy Committee, closer coordination and cooperation between the SFC and the SEHK on listing policy formation and provide the SFC with earlier and more direct input on listing policy matters and listing regulation;
- streamline, through the Listing Regulatory Committee, the processes for important or difficult listing decisions that raise suitability issues or have broader policy implications;
- simplify the process for initial listing applications so that they can be vetted and approved more efficiently – as part of the proposals, the SFC will no longer as a matter of routine issue a separate set of comments on draft IPO prospectuses under the dual filing regime; and
- establish clearer accountability for decision-making in listing regulation and for oversight of the administration of the listing rules.

Comments on the consultation are due by 19 September 2016.

SFC invites intermediaries and their affiliated corporations to participate in OTC derivatives activities survey 2016

The SFC has issued a circular inviting intermediaries and their affiliated corporations to take part in its survey on activities in relation to OTC derivative products or transactions. The survey is to be completed by all intermediaries and their affiliated corporations. In particular, the SFC wishes to draw the survey to the attention of intermediaries and their affiliated corporations that are likely to be affected by the regulatory regime governing the OTC derivatives market in Hong Kong provided for under the Securities and Futures (Amendment) Ordinance 2014 (i.e. those currently engaged in or planning to engage in the business of providing automated trading services for, or managing portfolios of, OTC derivative products, dealing in or advising on OTC derivative products, and/or providing client clearing services for OTC derivative transactions in Hong Kong).

Intermediaries and their affiliated corporations should return the completed survey to the SFC on or before 15 July 2016.

FSC to apply foreign currency liquidity coverage ratio to banks from 2017

The Financial Services Commission (FSC) has announced that it will introduce a foreign currency liquidity coverage

ratio (LCR) rule starting from 2017. The rule will require commercial banks to hold 60% of their foreign exchange debt in high-quality liquid assets (HQLA) to withstand a 30-day net cash outflow in systemic risks. The FSC/Financial Supervisory Service (FSS) adopted the foreign currency LCR in 2015 as a guideline to monitor banks' foreign exchange liquidity risks, in accordance with the Basel III recommendation. Since then, commercial banks have been advised to maintain a foreign currency LCR of at least 40% in 2015 and 50% in 2016.

The foreign currency LCR rule will apply to all banks with the exception of:

- commercial banks with foreign exchange debt of less than 5% of their total debt and USD 500 million or less in foreign exchange debt;
- Export-Import Bank of Korea (KEXIM); and
- branches of foreign banks operating in Korea.

The foreign currency LCR for commercial banks will be set at 60% in 2017, and increased gradually to 70% in 2018 and 80% in 2019. Banks will be required to calculate their foreign currency LCR each business day and maintain a monthly average of the ratios above the minimum requirement. Overlapping regulations – e.g. seven-day and one-month maturity mismatch ratio requirements, three-month foreign exchange liquidity requirement – will be abolished or replaced by the foreign currency LCR.

For the next six months, the FSC has indicated that it will gather opinions from the banking sector about the proposed rule and amend relevant rules including the Regulation on Supervision of Banking Business.

MAS issues notices on financial market infrastructure standards for central securities depositories, licensed trade repositories and approved clearing houses

The Monetary Authority of Singapore (MAS) has issued two Notices:

- Notice (SFA 03AA-N01) on Financial Market Infrastructure Standards for central securities depositories (CSDs); and
- Notice (SFA 02A/03-N01) on Financial Market Infrastructure Standards for licensed trade repositories and approved clearing houses.

Amongst other things, Notice SFA 03AA-N01 sets out the principles in the CPMI-IOSCO Principles for Financial Market Infrastructures (PFMI) that regulated CSDs have to comply with, relating to the following:

- legal risk management;
- governance arrangements;
- framework for the comprehensive management of risks;
- physical deliveries;
- participant default rules and procedures;
- general business risk;
- custody and investment risks;
- communication procedures and standards; and
- disclosure of rules, key procedures and market data.

Some of the principles in the PFMI applicable to licensed trade repositories and approved clearing houses are set out in the Securities and Futures Act and its subsidiary legislation. Amongst other things, Notice SFA 02A/03-N01 sets out the remaining principles in the PFMI that licensed trade repositories and approved clearing houses have to comply with, relating to the following:

- credit risk management;
- collateral;
- margin;
- liquidity risk;
- money settlement;
- segregation and portability; and
- disclosure of market data.

Both Notices were effected on 16 June 2016.

ASIC reports on compliance review of retail OTC derivatives sector

The Australian Securities and Investment Commission (ASIC) has released its 'Report 482 – Compliance review of the retail OTC derivatives sector', following a review of 55 licensees against 7 key compliance risks.

The report is relevant to Australian Financial Services (AFS) licensees and entities that provide them support, such as legal and/or compliance services providers.

ASIC notes that there has been a material increase in aggressive marketing by issuers of retail OTC derivatives, particularly through cold calling and unsolicited emails.

In the review, ASIC observed that a significantly high number of smaller, foreign owned or foreign controlled AFS licensees either lacked awareness of their Australian regulatory obligations or were reluctant to invest in resources to meet their Australian compliance obligations. Often, these overseas AFS licensees were subject to very little or no regulatory oversight in their home jurisdictions.

As a result, ASIC will increase monitoring of AFS licensee compliance and continue to monitor the industry.

The review led to over 150 regulatory outcomes for ASIC, including the cancellation of two AFS licences and a further two suspended licenses. ASIC has also ordered some AFS licensees to hold more capital, improve disclosure and financial reporting.

CLIFFORD CHANCE BRIEFINGS

Clifford Chance Comment: New lease accounting standard IFRS 16 – all change for lessees

Lease accounting is being overhauled for companies accounting under full International Financial Reporting Standards (IFRS), resulting in on-balance sheet treatment for operating leases for the first time. The change will impact most companies using IFRS in some way, but groups operating in sectors with traditionally large operating lease portfolios, such as retail, transport and communications will be particularly affected.

This briefing paper summarises the accounting change and its key impact on English law financing agreements.

https://www.cliffordchance.com/briefings/2016/06/new_lease_accountingstandardifrs16al.html

Clifford Chance Comment: The tax impact of Brexit – what steps should UK and EU businesses take now?

On 23 June 2016 the UK voted to leave the European Union. Whilst many of the terms of exit are hard to anticipate, there are a number of predictable adverse effects for which preparations can be made.

This briefing paper outlines some mitigating steps that UK and EU businesses can take now.

https://www.cliffordchance.com/briefings/2016/06/the_tax_impact_ofbrexitwhatstepsshouldu.html

Clifford Chance Comment: The Employment law implications of 'Brexit'

At first glance, it would appear that the 'Brexit' vote will have substantial implications for UK employment law, and the immigration system in the UK. In reality the extent to which current employment legislation will be affected (repealed, revised, and interpreted) will be dictated by the nature of the 'Brexit' which has not yet been determined.

There is no immediate change to employment legislation as a consequence of the vote. The UK remains a member of the EU and will have two years to negotiate the terms of its exit.

This briefing paper explores some of the key questions that arise in relation to employment law issues.

https://www.cliffordchance.com/briefings/2016/06/client_briefing_brexit.html

Clifford Chance Comment: US Supreme Court holds RICO statute has extraterritorial reach, but does not apply to injuries outside the United States

The US Supreme Court has held in RJR Nabisco, Inc. v. The European Community that the Racketeer Influenced and Corrupt Organizations Act (RICO) may apply to conduct that occurs outside the United States, but in a significant move the Court has imposed a 'domestic injury' requirement for private civil RICO claims. The RICO statute was originally intended to combat organized crime, but has become a potent tool for civil plaintiffs in all manner of business disputes and fraud cases in US courts, principally because of the possibility of recovering treble damages. The Supreme Court's decision in RJR Nabisco significantly limits the extent to which this tool can be used in private civil litigation involving conduct that occurs outside the United States, and overrules the decisions of some lower courts holding that the statute does not require a domestic injury. This decision continues an important trend in the Supreme Court of limiting the reach of US courts in civil actions to matters with a significant relationship to the United States. Notably, by anchoring its ruling in the 'private civil action' provision of Section 1964(c), the Supreme Court restricted private civil actions while leaving for another day the ability of US prosecutors to continue to bring criminal RICO cases for offshore conduct.

This briefing discusses the decision.

https://www.cliffordchance.com/briefings/2016/06/u_s_supreme_courtholdsricostatuteha.html