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Briefing note

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International Regulatory Group Contacts

Chris Bates +44 (0)20 7006 1041

Nick O'Neill +1 212 878 3119

Marc Benzler +49 69 7199 3304

Steven Gatti +1 202 912 5095

Paul Landless +65 6410 2235

Mark Shipman + 852 2826 8992

Donna Wacker +852 2826 3478

International Regulatory Update Editor

Joachim Richter +44 (0)20 7006 2503

To email one of the above, please use firstname.lastname@cliffordchance.com

Clifford Chance LLP, 10 Upper Bank Street, London, E14 5JJ, UK
www.cliffordchance.com

MiFID2/MiFIR: ESMA clarifies concept of 'traded on a trading venue

The European Securities and Markets Authority (ESMA) has published an opinion clarifying the concept of 'traded on a trading venue' (TOTV) in respect of over-the-counter (OTC) derivatives under MiFID2 and MiFIR. The concept of TOTV is particularly relevant for:

- pre-trade and post-trade transparency requirements on market operators and investments firms operating a trading venue, and for investment firms (including systematic internalisers) operating OTC; and
- transaction reporting obligations.

The opinion sets out which transactions in derivatives concluded outside of trading venues are subject to transaction reporting and transparency requirements, and specifies that only OTC-derivatives sharing the same reference data details as the derivatives traded on a trading venue should be considered to be TOTV, and therefore subject to the transparency and reporting requirements of MiFIR.

MMF Regulation: ESMA consults on draft technical advice, ITS and guidelines

ESMA has published a consultation paper on draft technical advice, implementing technical standards (ITS) and guidelines under the Money Market Funds (MMF) Regulation.

The draft technical advice relates to the liquidity and credit quality requirements applicable to assets received as part of a reverse repurchase agreement and criteria for:

- the validation of the credit quality assessment methodologies;
- quantification of the credit risk and the relative risk of default of an issuer and of the instrument in which the MMF invests; and
- establishing qualitative indicators on the issuer of the instrument.

The draft ITS relate to development of a reporting template for managers of MMFs to send to competent authorities and the guidelines are intended to set out common reference parameters of the scenarios to be included in the stress tests that managers are required to conduct.

Comments on the consultation are due by 7 August 2017.

CRR: EBA consults on scope of draft guidelines on connected clients

The European Banking Authority (EBA) has launched a consultation on the scope of its draft guidelines on connected clients. The EBA already sought feedback on these draft guidelines in July 2016, but following comments from respondents it has decided to launch a second consultation on proposals to extend the scope of the guidelines.

The draft guidelines provide guidance on two types of interconnection (control relationships and economic dependencies), which lead to the formation of groups of connected clients. In the first consultation the EBA proposed the guidelines applied only in the context of the large exposures regime. However the concept of a 'group of connected clients' is relevant to other areas of the Capital Requirements Regulation (CRR), such as the categorisation of clients in the retail exposure class for the purposes of credit risk, the development and application of rating systems and the application of the SME supporting factor. The concept is also relevant to the EBA technical standards and other EBA guidelines.

This second consultation therefore seeks feedback on extending the scope of the draft guidelines to include all aspects of the CRR, the EBA technical standards and the EBA guidelines where the concept of a group of connected clients is relevant.

Comments are due by 26 June 2017.

CRR review: EBA publishes opinion on own funds

The EBA has published an opinion on own funds in the context of the review of the CRR and Capital Requirements Directive (CRD 4), proposals on which were published by the EU Commission in November 2016, and the consultation on the operation of the European Supervisory Authorities (ESAs).

Under the CRR, the EBA monitors the quality of own funds instruments issued by institutions and, since 2013, the EBA has continuously been monitoring the quality of Common Equity Tier 1 (CET1) instruments and Additional Tier 1 (AT1) instruments in the EU. The opinion sets out the EBA's view on possible reinforcement of the EBA's role in terms of the evaluation of the compliance of CET1 instruments to ensure the enforceability of the CRR and provisions in the regulatory technical standards (RTS) for CET1 instruments for all institutions in the EU.

The opinion also elaborates on:

- restrictions of distributions with regard to the Maximum Distributable Amount (MDA) and its definition;
- the reduction, redemption and repurchase of capital instruments;
- the introduction of an anti-circumvention principle; and
- a point of non-viability criterion.

The opinion is addressed to the EU Commission, EU Parliament and EU Council.

BRRD: EBA publishes RTS on valuation in resolution

The EBA has published a final report on regulatory technical standards (RTS) on valuation in resolution under the Bank Recovery and Resolution Directive (BRRD). The RTS are intended to promote the consistent application of methodologies for valuations in relation to the principles upon which an independent valuer must apply their own judgment and expertise to valuations. The final report sets out two sets of RTS, one covering valuations before resolution and the other covering valuations after resolution.

To conduct a valuation before resolution, the independent valuer is empowered to challenge banks' management assumptions, data, methodologies and judgements on which the institutions prepare their financial statements. After resolution, valuation is important to establish whether the no-creditor-worse-off (NCWO) safeguard has been breached by the resolution action and whether any compensation has to be paid to creditors and shareholders by the resolution fund.

The two sets of RTS complete the EBA's regulatory activity on valuation for the purposes of resolution and will be submitted to the EU Commission for endorsement. The EU Commission has previously endorsed RTS on the independent valuer and RTS on the valuation of derivatives for the purposes of resolution, which have both already entered into force.

BRRD: Delegated Regulation on classes of arrangement to be protected in partial property transfer published in Official Journal

A Commission Delegated Regulation (2017/867) on classes of arrangement to be protected in a partial property transfer under Article 76 of the BRRD has been published in the Official Journal.

The various classes of arrangements set out in Article 76(2) of the BRRD are detailed to varying degrees, and some classes refer to one type of contractual relationship and liability or to a limited set of contractual relationships and liabilities, while others cover a greater number and an open range of contractual liabilities, transactions and relationships. The Delegated Regulation further specifies the classes of protected arrangements in relation to security arrangements, set-off and netting arrangements and structured finance arrangements. The Delegated Regulation is not intended to prevent resolution authorities from further specifying in partial transfers those types of set-off and netting arrangements to be protected in individual partial transfers, where those arrangements are recognised for risk mitigation purposes under the applicable prudential rules, and the protection, in particular by non-separability, is a condition for that recognition.

The Regulation will enter into force on 9 June 2017.

EU Council Presidency publishes compromise text on proposed amendment to BRRD as regards insolvency hierarchy

The EU Council Presidency has published a compromise text, dated 30 March 2017, on the proposal for a Directive to amend the BRRD as regards the ranking of unsecured debt instruments in insolvency hierarchy.

Brexit: EU27 adopt negotiating directives

The EU Council, meeting in EU27 format, has adopted a decision authorising the opening of Brexit negotiations with the UK and negotiating directives for the talks.

The negotiating directives are intended to guide the EU Commission for the first phase of the negotiations, in line with the aims established by the European Council. The negotiating directives prioritise some matters which, at this stage, have been identified as necessary to ensure an orderly withdrawal of the UK from the EU, including:

- citizens' rights;
- the financial settlement; and
- the situation of Ireland.

The negotiating directives also cover certain other issues to be addressed in order to reduce uncertainty and avoid a legal vacuum, including arrangements for procedures based on EU law and goods already on the market.

The negotiating directives may be amended and supplemented during the negotiations and other matters not covered by this set of negotiating directives, such as services, will be part of subsequent sets of negotiating directives.

Global Foreign Exchange Committee launches global FX code

The FX global code has been launched, comprising a set of global principles of good practice in the foreign exchange market developed to promote the integrity and effective functioning of the wholesale foreign exchange (FX) market. Publication of the code is the culmination of two years of work by members of the central bank Foreign Exchange Working Group (FXWG), in close cooperation with a Market Participant Group (MPG), representing firms from both the buy-side and sell-side. The FXWG was directed to be established by the Bank for International Settlements (BIS) Governors in May 2015.

The voluntary code contains 55 principles organised around six leading principles:

- ethical behaviour to promote the fairness and integrity of the FX market;
- sound and effective governance;
- exercising care when negotiating and executing transactions in order to promote a robust, fair, open, liquid, and appropriately transparent FX market;
- information sharing, including accuracy of communications and protecting confidential information;
- robust risk management and compliance; and
- putting in place robust, efficient, transparent, and risk-mitigating post-trade processes to promote the predictable, smooth, and timely settlement of transactions in the FX market.

The Global Code, while not rules or regulation, is intended to serve as a supplement to any and all local laws, rules, and regulation by identifying global good practices and processes. The Global Code will be maintained and reviewed by a new Global Foreign Exchange Committee, a global association of FX committees. The Committees have separately published a statement on the Global Code.

The FXWG has also produced a report on adherence, which sets out a framework to promote awareness, incentivise adherence to the Global Code's standards and ensure that the principles remain up to date.

Italian Council of Ministers approves draft legislative decree implementing AMLD 4

The Italian Council of Ministers has approved, in final examination, a legislative decree implementing Directive 2015/849/EU on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (AMLD 4), establishing stricter provisions concerning the fight against money laundering and terrorist financing.

The category of 'politically exposed person' has been extended in order also to capture mayors of municipalities with more than 15,000 inhabitants and the top management of companies these municipalities invest in.

Amongst other things, the following has been introduced:

- the role of the Anti-mafia and Antiterrorism Direction (Direzione antimafia e antiterrorismo) has been strengthened;
- the administrative sanctions regime has been reorganised into a system of effective, proportionate and dissuasive measures to be applied to natural and legal persons directly responsible for the violations;
- a register of beneficial owners of legal persons and trusts (Registro dei titolari effettivi di persone giuridiche e trust) has been established in order to increase transparency;
- suspicious transactions must not be carried out until the related report has been submitted to the authority;
- excessive formalities and technicalities concerning the ways of retaining documents and data have been eliminated; and
- an adequate control system of the operators used by money transfers has been introduced.

EMIR: Consob issues communication on reporting requirements

The Commissione Nazionale per le Società e la Borsa (Consob) has issued Communication n.0069306, publishing the results of a review on reports submitted by a number of financial and non-financial counterparties.

The review, conducted in 2016, was intended to verify to what extent the reports were exhaustive and correct, and in compliance with the provisions of the European Market Infrastructure Regulation (EMIR) and relevant implementing regulations, as well as the guidance contained in the European Securities and Markets Authority's (ESMA's) Q&A on the implementation of EMIR.

In particular, Consob notes that:

- even when counterparties delegate reporting to third parties (EMIR art. 9, par. 4), they must always supervise the accuracy of the information submitted on their behalf. The delegation agreement must comply with this requirement;

- in a number of instances, validation of submitted trades failed due to counterparties omitting certain information or using wrong UTI codes. Counterparties are required to follow ESMA's validation rules and constantly monitor the reports' outcomes in order promptly to correct any mistakes;
- counterparties are required always to make use of the LEI (Legal Entity Identifier) code and UTI (Unique Trade Identifier) code when making submissions, so as to ensure the positive result of both the pairing phase and the matching phase; and
- non-financial counterparties sometimes fail properly to complete field no. 15 of the submission form regarding whether the relevant trade is directly linked to commercial activity or treasury financing.

Consob has emphasised that it expects counterparties to pay greater attention to the above aspects in future.

Polish President submits draft Act on Payment Services to Sejm

The President of the Republic of Poland has submitted to the Sejm a legislative initiative concerning the draft amendment of the Act on Payment Services and certain other Acts. The draft is intended to facilitate the effective recalling of the amounts of payment transactions executed using incorrect payment account numbers, which the parties ordering a credit transfer were unable to recover as a result of the actions taken by their payment services providers.

The draft envisages, among other things, an exemption from the obligation to maintain banking secrecy. If the payee does not voluntarily return the funds, the payment services provider, after calling on the payee to return the funds and informing the payee of the consequences of the failure to do so, will provide the payee's particulars to the party ordering the credit transfer so that he will be able to initiate court proceedings.

MAS consults on proposed amendments to regulatory requirements in relation to credit loss provisioning

The Monetary Authority of Singapore (MAS) has launched a consultation on proposed amendments to MAS Notices 612, 1005, 637 and 1111 relating to the changes in the recognition and measurement of allowance for credit losses introduced in International Financial Reporting Standard (IFRS) 9 Financial Instruments and Singapore Financial Reporting Standard (SFRS) 109 Financial Instruments.

The Singapore Accounting Standards Council has adopted IFRS 9 and has issued the standard as SFRS 109. SFRS 109 will replace SFRS 39 Financial Instruments: Recognition and Measurement, and will be effective for annual periods beginning on or after 1 January 2018. Banks in Singapore are required to apply SFRS 109 or IFRS 9 (for locally-incorporated banks that are listed on the Singapore Exchange) when preparing their financial statements for reporting periods beginning on or after 1 January 2018.

SFRS 109 introduces a new approach for the estimation of allowance for credit losses based on the Expected Credit Loss model. As the accounting estimates of allowance for credit losses closely interact with a bank's prudential provisioning and regulatory capital computation, there is a need to review the relevant regulatory requirements.

Amongst other things, the MAS seeks comments on the following proposals:

- the removal of regulatory requirements on minimum impairment provisions for credit impaired exposures;
- locally-incorporated domestic systemically important banks to maintain minimum loss allowances for non-credit impaired exposures of 1% of exposures, net of collaterals and to disclose the expected credit losses estimated under SFRS 109 in their financial statements;
- foreign bank branches and merchant banks to be permitted to maintain loss allowances of 1% of non-credit impaired exposures, net of collaterals, if it results in higher loss allowances than the expected credit losses estimated under SFRS 109;
- the approaches that banks may be required to adopt to comply with the minimum regulatory loss allowance;
- retaining the option for banks incorporated outside Singapore to record their loss allowances for non-credit impaired exposures at the bank's head office, and the related reporting template;
- a transitional arrangement of up to two years; and
- the interim regulatory treatment of loan loss allowances under the ECL model.

Comments on the consultation paper are due by 12 June 2017.

Enhanced position limit regime to take effect in Hong Kong on 1 June 2017

The Securities and Futures Commission (SFC) has announced that the enhancements to the position limit regime, including the introduction of various excess position

limits and the raising of the statutory position limit for stock options contracts, will come into operation on 1 June 2017, the commencement date of amendments to the Securities and Futures (Contracts Limits and Reportable Positions) Rules.

The enhancements include a 300% cap on the excess position limit that may be authorised by the SFC, a statutory position limit of 150,000 contracts for stock options as well as new excess position limits for index arbitrage activities, asset managers and market makers of exchange-traded funds.

In light of market responses, the minimum 'assets under management' requirement applicable to asset managers will also be lowered from HKD 100 billion to HKD 80 billion.

HKMA issues circular on consequential amendments to Banking (Capital) Rules arising out of Financial Institutions (Resolution) Ordinance

The Hong Kong Monetary Authority (HKMA) has issued a circular to authorised institutions drawing their attention to two consequential amendments introduced in the Financial Institutions (Resolution) Ordinance. The amendments relate to the qualifying criteria for capital instruments issued by authorised institutions incorporated in Hong Kong under the Banking (Capital) Rules (BCR).

The Financial Institutions (Resolution) Ordinance (Commencement) Notice 2017 was gazetted on 12 May 2017. Under the Commencement Notice, the Ordinance (except Part 8, section 192 and Division 10 of Part 15) will come into operation on 7 July 2017. This covers, among other things, two consequential amendments to the BCR requiring that for any capital instrument to be qualified as Additional Tier 1 capital of an authorised institution under Schedule 4B of the BCR or Tier 2 capital of an authorised institution under Schedule 4C of the BCR, the terms and conditions of the instrument must contain a provision to the effect that the holder of the instrument:

- acknowledges that the instrument is subject to being written off, cancelled, converted or modified, or to having its form changed, in the exercise of powers under the Ordinance;
- agrees to be bound by any such write off, cancellation, conversion, modification or form change; and
- acknowledges that the rights of the holder are subject to anything done in the exercise of those powers.

The Commencement Notice was tabled before the Legislative Council on 17 May 2017 for negative vetting.

To qualify as Additional Tier 1 capital or Tier 2 capital of an authorised institution under the BCR, any instrument issued on or after the commencement date of the Ordinance (i.e. 7 July 2017 subject to negative vetting by the Legislative Council) will be required to meet the additional criterion described in the circular.

ASIC reports on conduct in wholesale spot foreign exchange market

The Australian Securities & Investments Commission (ASIC) has released a report setting out its observations on key behavioural drivers of conduct arising from recent ASIC investigations into the wholesale spot foreign exchange (FX) businesses of the major Australian financial institutions.

The report illustrates the behavioural drivers of conduct that, in ASIC's view, are likely to lead to poor conduct if not adequately managed. The report also describes a number of good practice principles for managing these drivers to more effectively prevent, detect and respond to inappropriate practices.

ASIC notes that it will use the report as a reference point for its surveillance of the FX markets and, where appropriate, the broader wholesale over-the-counter markets. The release of ASIC's report coincides with the release of Phase Two of the FX Global Code of Conduct.

RECENT CLIFFORD CHANCE BRIEFINGS

What does the Singapore FTA Decision mean for the EU's FTAs and Brexit?

On 16 May 2017 the Court of Justice of the European Union ruled that the EU could not conclude the proposed Free Trade Agreement with Singapore alone, but that it would also have to be ratified by the EU's Member States in order for it to come into force.

This long-awaited ruling will shape the EU's trade policy for years to come, and sets a precedent for future trade negotiations between the EU and third countries, including any free trade agreement that the UK may look to conclude with the EU once it has left.

This briefing paper summarises the opinion of the CJEU, and asks what it means for the EU's trade policy, and whether it is good or bad news for the UK.

https://www.cliffordchance.com/briefings/2017/05/what_does_the_singaporeftadecisionmeanforth.html

Law Creating a Two-tier Banking System to Take Effect on 1 June 2017

The Russian President has put his signature to a law that separates banks into credit institutions with universal and basic licences depending on the amount of their capital. It is contemplated that this differentiation will help ease the regulatory burden on banks that hold a basic licence. At the same time, the law limits the transactions such banks can perform with foreign entities and individuals.

This briefing paper discusses the law.

https://www.cliffordchance.com/briefings/2017/05/law_creating_a_two-tierbankingsystemtotak0.html