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- **Recent Clifford Chance briefings: financing mechanisms for listed Spanish companies and US financial regulatory questions for decentralized finance. Follow this link to the briefings section.**

Capital Markets Union: ECON Committee adopts report calling for targeted changes and additional legislative measures

The EU Parliament's Committee on Economic and Monetary Affairs (ECON) has adopted a non-binding report calling for the development of the Capital Markets Union (CMU) project to be accelerated.

In an accompanying press release, MEPs have proposed simplified rules and new provisions designed to help SMEs to tap into financial markets and reduce their reliance on bank lending.

Among other things, the MEPs call for:

- targeted changes aligning and simplifying the existing provisions, including those concerning capital requirements, reporting frameworks, and IPO listing requirements for SMEs;
- an acceleration of the development of the EU venture capital and private equity markets to increase transparency and reduce fragmentation;
- adequate prudential rules for loss absorption capacity;
- new legislative measures, including proposals on European secured notes (ESNs) and a European single access point for financial and non-financial information with respect to listed and unlisted EU companies; and
- a more harmonised approach to consumer and investor protection in EU financial services legislation, adapted to the green and digital transformation, in order to ensure effective and consistent levels of protection across all financial products and providers.

ECON Committee adopts report on digital finance recommendations

ECON has adopted a report with recommendations for the EU Commission on digital finance. The report contains a motion for an EU Parliament resolution aimed at addressing the fragmentation of existing regulation and providing a comprehensive regulatory framework for the treatment of cryptoassets, cyber resilience, digital onboarding and the use of data. In particular, the proposals call for:

- the creation of a pan-European cryptoasset taxonomy and a common monitoring and supervisory framework;
- the closure of gaps in EU anti-money laundering legislation;
- the amendment of legislation in the area of ICT and cyber security requirements for the financial sector to address inconsistencies and gaps, with a focus on modernisation, reporting of incidents, resilience testing and third-party providers; and
- the careful monitoring and governance of cross-border data flows, including to and from third countries.

The Committee also welcomes the EU Commission's announcement that it will finalise its Fintech Action Plan by the third quarter of 2020. It emphasises that any EU-level measures should allow market participants to innovate, be proportional and technologically neutral, and ensure a high level of protection for consumers and investors. It calls for a common European model with a central role for the European Supervisory Authorities (ESAs) and international cooperation for standards setting.

EBA calls on EU Commission to establish single rulebook on AML/CFT

The European Banking Authority (EBA) has responded to the EU Commission's call for advice on how to strengthen the EU legal framework on anti-money laundering and countering the financing of terrorism (AML/CFT).

The EBA's advice sets out how the framework should be strengthened to tackle vulnerabilities linked to divergent national approaches and gaps in the EU defences against money laundering and terrorist financing (ML/TF). The EBA has recommended that the Commission establish a single rulebook to:

- harmonise the EU legal framework in a directly applicable Regulation;
- strengthen aspects of the current AML/CFT Directive where existing provisions are insufficiently robust or specific, for example in relation to competent authorities' supervision powers in this area;
- review the list of obliged entities currently within the scope of the EU's AML/CFT regime; and
- clarify provisions in sectoral financial services legislation to ensure their compatibility with the EU's AML/CFT objectives.

ESMA allows postponements to application of annual transparency calculations for non-equity instruments

The European Securities and Markets Authority (ESMA) has decided that trading venues and investment firms may postpone the application of the annual transparency calculations for non-equity instruments other than bonds to 21 September 2020.

This decision also applies to the quarterly calculations for the purpose of the systematic internaliser (SI) regime for non-equity instruments other than bonds. Investment firms that apply the transparency calculations on 21 September may also perform the SI-test by 21 September 2020.

Since ESMA's publication on 15 July 2020 of the results of the liquidity assessment for non-equity instruments other than bonds, it has been approached by stakeholders raising concerns that the application of the non-equity transparency calculations coincides with the quarterly expiry week of many equity derivatives, a week characterised by high trading volumes and a higher level of volatility due to the rolling over of many contracts.

In order to avoid technical issues that might be exacerbated by high market volatility during the current sensitive period, ESMA has agreed that trading venues and investment firms may apply the non-equity transparency calculations from 21 September instead of 15 September 2020.

FSB announces extensions to implementation timelines for SFTs

The Financial Stability Board (FSB) has announced extensions to the implementation timelines for minimum haircut standards for non-centrally cleared securities financing transactions (SFTs).

The FSB framework for numerical haircut floors for bank-to-non-bank transactions is expected to be implemented through the Basel III framework in many jurisdictions. Following the decision to defer the implementation of the Basel III framework by one year to January 2023, the FSB has decided to also extend the implementation dates for its policy recommendations related to minimum haircut standards for non-centrally cleared SFTs by one year.

The extended timelines are:

- January 2023 for bank-to-non-bank transactions; and
- January 2025 for non-bank-to-non-bank transactions.

The extension aims to give market participants more time to prepare for the implementation of the framework and is in line with the reprioritisation of the FSB's work due to the COVID-19 pandemic.

Working Group on Sterling Risk-Free Reference Rates publishes papers on LIBOR transition for loans, bonds and cash market products

The Working Group on Sterling Risk-Free Reference Rates has published a number of papers intended to support firms in the transition of their existing sterling LIBOR-linked contracts, including:

- a paper on the active transition of legacy loan products;
- a paper on how issuers might consider converting existing bonds and securitisations, including the process of consent solicitation; and
- a recommendation on the appropriate 'credit adjustment spread' to be used in fallbacks for sterling cash market products referencing sterling LIBOR.

The statement of recommendation follows a consultation launched in December 2019, which identified a strong consensus in favour of the historical five-year median spread adjustment methodology as the preferred methodology for credit adjustment spread calculations across both cessation and pre-cessation triggers for cash products maturing beyond end-2021. This maintains consistency with ISDA's approach for derivatives.

FCA publishes Quarterly Consultation No. 29

The Financial Conduct Authority (FCA) has published its quarterly consultation paper (CP20/18) on miscellaneous amendments to its handbook. This quarter, the FCA is proposing:

- consequential changes to the listing rules (Chapter 8) to align with provisions for exempted documents under the Prospectus Regulation;
- changes to Article 34 of the UK-RTS; and

- onshoring changes to the FCA handbook for legislative provisions and/or relevant technical changes needed to its rules as a result of onshoring over the transition period for EU withdrawal.

Comments on Chapters 2 and 4 are due by 4 November 2020, while comments on the Fees (Credit Rating Agencies, Trade Repositories and Securitisation Regulation) Instrument 2020 and on Chapter 3 are due by 5 October 2020.

BaFin clarifies that installation of crypto-ATM requires BaFin license

The German Federal Financial Supervisory Authority (BaFin) has clarified that the public installation of machines where crypto currencies (e.g. Bitcoin, DASH, Litecoin, Ether) can be sold or purchased constitutes dealing on own account under section 1 para 1a sentence 2 no. 4c of the German Banking Act (KWG) (i.e. a financial service) or potentially also principal broking business (Finanzkommissionsgeschäft) under section 1 para 1 sentence 1 no. 4 KWG (i.e. banking business) and thus requires a prior license from BaFin pursuant to section 32 para 1 sentence 1 KWG.

Operators of such crypto-ATM would commit a criminal offence under section 54 para 1 no. 2 KWG if they acted without the required license.

Independent of criminal liability, BaFin also enforces its measures, if necessary, by way of administrative enforcement, such as sealing business premises and machines as part of a freezing order pursuant to section 44c para 4 KWG after a prohibition order has been issued.

Persons or companies that provide such operators of crypto-ATM with premises, electricity or internet connections are involved in their illegal business and may themselves become addressees of administrative measures. Lessors should therefore always assure themselves that operators have a BaFin license as a business registration alone is not sufficient.

BaFin consults on draft circular on determination of tranche maturity

BaFin has launched a consultation on a draft circular regarding the EBA guidelines on the determination of the weighted average maturity (WAM) of the contractual payments due under a tranche in accordance with point (a) of Article 257(1) of the Capital Requirements Regulation (CRR), which BaFin intends to adopt in its administrative practice with effect from 1 October 2020.

The EBA has already carried out a consultation on the guidelines. BaFin will accept written comments on its draft circular until 25 September 2020.

BaFin plans storage obligation for virtual IBAN

BaFin has announced that it intends, by way of a general administrative act (Allgemeinverfügung), to oblige credit institutions to store International Bank Account Numbers (IBAN) issued to payment service providers in a file system pursuant to section 24c para 1 of the German Banking Act (KWG). In particular, credit institutions will have to specify the names of the payment service providers' end customers to whom the virtual IBAN is passed on.

A virtual IBAN constitutes an account within the meaning of section 154 para 1 of the German Tax Code (Abgabenordnung). The management of such an account is attributed to the credit institution that has issued the respective

IBAN, and whose bank identifier code is encrypted in it. Credit institutions are therefore obliged to store data concerning the use of such virtual IBAN in a file system pursuant to section 24c para 1 KWG. BaFin notes that indicators that virtual IBAN are being abused in a large number of cases, for purposes such as fraud, have recently increased and that it impedes the combatting and prosecution of such criminal actions if information related to the users of virtual IBAN is not stored pursuant to section 24c para 1 KWG.

BaFin will accept written comments on the draft general administrative act until 2 October 2020.

Transaction reporting: Consob publishes operational guidelines

The Commissione Nazionale per le Società e la Borsa (Consob) has published operational guidelines on transaction reporting. The aim of the guidance is to manage reporting requirements relating to transactions in financial instruments carried out by investment firms, as governed by Article 26 of MiFIR. Investment firms identified in the guidance are required to report details of such transactions to Consob as promptly as possible and by the end of the following business day at the latest. EU authorities, in accordance with Article 85 of MiFID2, must coordinate in order to ensure that the competent authority receives the required set of information and shall make available to ESMA, upon request, all information communicated in accordance with Article 26 of MiFIR.

The guidance is addressed to investment firms, managers of trading venues and authorised reporting mechanisms (ARM), as defined under MiFID 2.

CSSF publishes 2019 annual report

The Luxembourg financial sector supervisory authority, the Commission de surveillance du secteur financier (CSSF), has published its annual report for 2019. Amongst other things, the report contains an overview of the CSSF's organisation and priority action areas (consumer and investor protection, financial innovation and digitalisation, the fight against money laundering and terrorist financing, the review of business models and the management of risks associated with virtual currencies). It also provides an insight into the CSSF's work and activities in relation to the main legal and regulatory developments of 2019 and the CSSF's activities at national and international level, as well as an analysis of the evolution of the different sectors that are under the supervision of the CSSF. Attention is drawn to the various ongoing challenges faced by the CSSF as well as by other supervisory authorities (a potential hard Brexit scenario, the digital transition of the financial system, and the growing importance of sustainable finance).

China consults on new rules for foreign investment in Chinese bond market

The People's Bank of China (PBoC), the China Securities Regulatory Commission (CSRC) and the State Administration of Foreign Exchange (SAFE) have jointly released the 'Bulletin on Matters Concerning Investment by Overseas Institutional Investors in the China Bond Market (Consultation Draft)'. Amongst other things, the consultation draft clarifies the following matters for an overseas institutional investor (OII) seeking to invest in the Chinese bond market:

- market access – the consultation draft clarifies the types of eligible OIIs and the corresponding application processes. For commercial entities, the access application can be made online;
- investment scope and method – OIIs that have obtained access to the China interbank bond market (CIBM) may invest in exchange-traded bonds directly or through access programmes. An OII may conduct non-trade transfer of bonds between different accounts opened by the same OII under the (Renminbi) Qualified Investment Foreign Investor regime and the regime proposed by the consultation draft. The investment scope of OIIs remains consistent with the current regimes; and
- custody and settlement – OIIs that invest in the CIBM may appoint a PRC bank as its custodian (nominee holder) through a multi-layer custody arrangement.

Comments are due by 1 October 2020.

SAFE issues new guidelines for current account foreign exchange businesses

The State Administration of Foreign Exchange (SAFE) has issued the 'Guidelines for Current Account Foreign Exchange Businesses (2020 Version)'. The guidelines are effective upon issuance and twenty-nine SAFE regulations have been repealed at the same time.

The guidelines are intended to integrate the existing foreign exchange regulations for current account items, streamline the relevant foreign exchange procedures and simplify the materials required. The guidelines do not introduce substantial changes or major adjustments to existing policies. Current account matters covered in the guidelines include trade in goods, trade in services, individual current account businesses, foreign currency cash businesses, current account businesses of insurance institutions and payment institutions and other current account businesses, such as pilot programmes of current account payments, donations, duty-free goods, representation offices and offshore accounts.

HKMA issues circular on enhanced disclosure measures in respect of digital platforms for application of unsecured loan and credit card products

The Hong Kong Monetary Authority (HKMA) has issued a circular to set out enhanced disclosure measures in respect of digital platforms for the application of unsecured loan and credit card products. The measures have been developed after taking into account feedback from the banking industry and references from the 'Updated Effective Approaches for Financial Consumer Protection in the Digital Age' issued by the Organisation for Economic Co-operation and Development (OECD). Amongst other things, the HKMA:

- requires authorised institutions (AIs) to take proactive steps to ensure that their relevant digital application processes are designed in a manner which, in promotion of responsible business conduct and responsible borrowing, help prospective borrowers to understand the key product features as well as the terms and conditions of the credit products, and provide the prospective borrowers with an adequate chance to consider

the implications of their repayment obligations in order to enable them to make informed borrowing decisions;

- encourages AIs to test digital disclosure approaches to ensure their effectiveness from customers' perspectives; and
- expects all AIs to extend the enhanced measures to those digital platforms which allow retail individual and small and medium-sized enterprises (SME) customers to apply for unsecured loan and/or credit card products even if they do not adopt the 'new personal-lending portfolio' arrangement.

The HKMA expects AIs to adopt, from 1 December 2020, the enhanced measures for all of their new digital platforms which allow retail individual and SME customers to apply for unsecured loan and/or credit card products. For the existing relevant digital platforms and those implemented prior to 1 December 2020, AIs have been advised to enhance their relevant systems to put in place the enhanced measures within 12 months from the issuance date of the circular (i.e. by 3 September 2021). Meanwhile, the HKMA expect AIs to take proactive steps to ensure that system enhancement will be completed as soon as practicable.

SFC issues circular on implementation of changes to open-ended fund companies regime

The Securities and Futures Commission (SFC) has issued a circular to set out further details on its implementation of changes to the open-ended fund companies (OFC) regime, which came into effect on 11 September 2020.

The circular notes that the amendments to the Code on OFCs (OFC Code) have been gazetted to implement the changes to the OFC regime which include the removal of the investment restrictions and expansion of the custodian eligibility requirements for private OFCs. A six-month transition period (i.e. from 11 September 2020 to 10 March 2021) will be given for existing private OFC custodians to make necessary adjustments in order to comply with the new safekeeping requirements set out in the new appendix A to the OFC Code.

Moreover, to implement and provide further guidance in relation to the enhancements to the OFC regime, the SFC has updated the following frequently asked questions (FAQs), information checklists and template:

- FAQs relating to OFCs;
- information checklist for application for authorisation of unit trusts and mutual funds under the revamped process;
- information checklist for (i) a change of director of a public OFC, or (ii) a change of name of a public OFC or a publicly offered sub-fund of an OFC;
- information checklist for application for registration of a private OFC or establishment of a privately offered sub-fund of an OFC;
- information checklist for application for approval of appointment of director, custodian or investment manager of a private OFC; and
- template of instrument of incorporation for umbrella private OFC.

These FAQs, information checklists and template have also been updated to reflect certain enhancements to the application process for the registration of OFCs, establishment of OFC sub-funds and other OFC approvals in order to

facilitate electronic submission of documents to alleviate any administrative burden.

MAS consults on draft notices on competency requirements for representatives conducting regulated activities under FAA and SFA

The Monetary Authority of Singapore (MAS) has launched a public consultation on draft notices on the competency requirements for representatives conducting regulated activities under the Financial Advisers Act (FAA) and Securities and Futures Act (SFA).

On 12 December 2016, the MAS published a consultation paper on a review of competency requirements for representatives conducting regulated activities under the SFA and the FAA. The December 2016 consultation proposed changes to the Capital Markets and Financial Advisory Services Examinations (CMFAS Examination) to raise the competency of appointed representatives, build a culture of high ethical standards in the financial industry, and offer greater customisation and flexibility to appointed representatives to fulfil the competency requirements.

The MAS is now consulting on the legal amendments to the 'Notice on Minimum Entry and Examination Requirements for Representatives of Licensed Financial Advisers and Exempt Financial Advisers' (FAA-N13) and the 'Notice on Minimum Entry and Examination Requirements for Representatives of Holders of Capital Markets Services Licence and Exempt Financial Institutions' (SFA 04-N09) to implement the changes set out in the December 2016 consultation paper, to the CMFAS Examination. In particular, the MAS will be making the following key changes to the CMFAS Examination:

- introduce ethics and skills content into the existing rules and regulations modules to form the rules, ethics and skills (RES) modules;
- tailor the RES modules for appointed representatives trading on the respective securities and derivatives exchanges; and
- provide appointed representatives with the option to take new combined product knowledge modules.

The MAS has indicated that it will work with the Institute of Banking and Finance (IBF) and the Singapore College of Insurance (SCI) to implement the revised CMFAS Examination in the first quarter of 2021 (T-date). On T-date, IBF and SCI will cease to offer the existing CMFAS Examination and will only offer the revised CMFAS Examination.

Comments on the consultation are due by 5 October 2020.

MAS responds to consultation and publishes notices and guidelines regarding best execution requirements

Following the responses to the MAS' November 2017 public consultation on its proposal to formalise expectations for 'capital market intermediaries' to have in place policies and procedures to place and/or execute customers' orders on the best available terms, as well as on the proposed enhancement to the existing business conduct requirement relating to handling of customers' orders, the MAS has published the following notice and guidelines to implement the 'best execution' requirements set out in the consultation paper:

- Notice on Execution of Customer's Orders (SFA 04-N16) – this Notice applies to capital markets intermediaries carrying on business in dealing in capital markets products, fund management or real estate investment trust management, and sets out requirements for these intermediaries to establish and implement written policies and procedures to place and/or execute: (i) customers' orders on the best available terms; and (ii) comparable customers' orders in accordance with the time of receipt of such orders. The Notice is effective from 3 March 2022; and
- Guidelines to Notice SFA04-N16 on Execution of Customers' Orders – these Guidelines apply to capital markets intermediaries (as defined in the Notice) and are intended to set out guidance on the requirements set out in the MAS Notice SFA04-N16. In particular, the MAS requires capital markets intermediaries to establish and implement best execution policies and procedures, taking into account a range of factors, including price, costs, speed, likelihood of execution and settlement, size and nature of the order, or any other considerations relevant to the placement and/or execution of the order.

The MAS has also published a new Notice on Execution of Orders by Market Operators (SFA 02-N03), which came into effect on 4 September 2020. The Notice SFA 02-N03 requires a locally-incorporated market operator, which may exercise discretion in placing and/or executing orders on its organised market, to establish and implement written policies and procedures (that are commensurate with the nature, scale and complexity of its business) to place and/or execute: (i) orders on the best available terms; and (ii) comparable orders in accordance with the time of receipt of such orders.

MAS sets out supervisory expectations regarding effective AML/CFT controls in private banking industry

The MAS has published a guidance paper to set out its supervisory expectations regarding effective anti-money laundering and countering the financing of terrorism (AML/CFT) controls in the private banking industry. The guidance paper summarises the key findings from the MAS' thematic inspections of private banks between 2019 to 2020 on the effectiveness of their AML/CFT risk management and controls, and supplements its Guidance on Private Banking Controls issued in 2014.

Private banks are advised to assess the effectiveness of their controls against the MAS' inspection findings and the good practices highlighted in the guidance paper, and to take appropriate steps to address any gaps. In particular, the MAS has identified the following key control areas for improvement:

- there should be robust corroboration of clients' source of wealth and funds;
- private banks should continue to be alert to evolving risk and typologies, and ensure that effective controls are in place to detect and mitigate these risk concerns. Particular attention should be placed on tax and corruption-related ML risks;
- private banks should subject commercial / third party transaction flows to necessary scrutiny and set clear follow-up actions;
- management should exercise strong oversight and set a strong AML/CFT right risk culture; and

- the performance management framework should provide an adequate balance of incentives and penalties to drive the right risk culture and staff behaviour.

The MAS has clarified that, while the guidance paper is derived from the inspections of private banks, the takeaways are applicable and relevant to other types of financial institutions (FIs), with the appropriate calibrations. All FIs should therefore study and incorporate learning points from the guidance paper in a risk-based and proportionate manner. The findings and examples highlighted are non-exhaustive, and FIs should continue to implement appropriate AML/CFT controls that are commensurate with the nature and complexity of their business.

RECENT CLIFFORD CHANCE BRIEFINGS

Towards a new regime for share capital increases and convertible bonds for listed companies

Among the measures developed in different countries to help address the economic consequences of the COVID-19 pandemic, many are designed to facilitate the financing mechanisms of companies, in light of the perception that many of them will face the need to raise capital in the coming months. The Spanish legislator has jumped on that bandwagon and the draft Bill approved by Spain's Government on 14 July 2020 to implement Directive (EU) 2017/828 on long-term shareholder engagement includes, together with other changes such as the new 'loyalty shares', several measures to make the regime governing the issuance of shares and convertible bonds by listed companies more flexible.

This briefing discusses these measures.

https://www.cliffordchance.com/briefings/2020/09/towards-a-new-regime-for-share-capital-increases-and-convertible.html

As DeFi matures, US financial regulatory questions loom large

The decentralized finance or 'DeFi' movement aspires to create a global peer-to-peer alternative to traditional financial services using permissionless distributed ledger or blockchain technology. DeFi companies have reportedly taken in billions in cryptocurrency over recent months, with some estimates placing the total amount currently 'locked' in DeFi-related platforms at almost USD 8 billion. But financial services offered by global DeFi platforms could be subject to relevant local laws and regulations that may, if not adhered to, present regulatory enforcement risks for DeFi providers.

In the US, the US Securities and Exchange Commission (SEC) and US Commodity Futures Trading Commission (CFTC) recently took enforcement action for violations of the US securities laws and the Commodity Exchange Act against entities doing business as 'Abra' which developed a blockchain-based smart contracts app advertised as a DeFi platform that provided users with synthetic investment exposure to various assets through swap contracts. DeFi platforms may also attract scrutiny from the US Treasury's Financial Crimes Enforcement Network (FinCEN), because many allow users to transmit and/or exchange virtual currencies. FinCEN has made statements this year about ensuring compliance with its registration and other regulatory

requirements – particularly with respect to non-US platforms on which US persons can transact in virtual currencies. Although to date, nascent DeFi platforms seem to have avoided publicized US regulatory scrutiny, this may change if platforms continue attracting significant capital, particularly from retail users.

This briefing explores what DeFi is, reviews the recent SEC and CFTC actions against Abra, explores some of the red flags that DeFi platforms should be aware of and discusses steps that platforms can take to avoid inadvertently violating US regulatory requirements.

https://www.cliffordchance.com/briefings/2020/09/as-defi-matures--us-financial-regulatory-questions-loom-large.html

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