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International Regulatory Update

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Lord Turner considers challenges beyond Basel III

Lord Turner, the FSA Chairman, has given a speech entitled 'Leverage, Maturity Transformation and Financial Stability – Challenges Beyond Basel III', in which he argued that neither Basel III nor fixing 'too big to fail' through improved resolvability are sufficient to ensure financial stability.

Amongst other things, he noted that: (1) in an ideal world, equity ratios would be set significantly above Basel III standards – he indicated a figure

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closer to 15% to 20% of risk-weighted assets; (2) the ability to resolve large systemically important banks is not sufficient to address risks of systemic instability; and (3) potential risks in shadow banking need to be addressed, avoiding too exclusive focus on individual banks or even on the whole banking system.

Lord Turner suggested four policy implications: (1) still higher capital standards, in particular for systemically important firms; (2) macro-prudential oversight of a continually mutating system; (3) policy responses which are discretionary and varied through the cycle; and (4) appropriately robust policies for financial stability that reflect an assessment of the economic value added of increased financial intensity and innovation.

Slides

EBA publishes details of stress test scenarios and methodology

EBA has published documents explaining the scenarios and methodology for its 2011 EU-wide stress test, which will be applied on a wide sample of European banks covering over 60% of total EU banking assets. EBA is coordinating the stress test with the national supervisory authorities, the European Systemic Risk Board, the European Central Bank and the European Commission.

The exercise is being run between March and June 2011, and the results will be published on a bank-by-bank basis in mid June.

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ESMA consults on guidelines on application of endorsement regime under Article 4(3) of Credit Rating Regulation 1060/2009

ESMA has published a consultation paper on its guidelines on the application of the endorsement regime under Article 4(3) of the EU Credit Rating Regulation 1060/2009. The consultation paper presents ESMA's interpretation of Article 4(3) of the Regulation, providing reasons in support of the interpretation that third country regulations must contain enforceable rules that are 'as stringent as' the one in the EU regulation. The consultation paper also asks market participants to provide comments on the content of Annex I by considering the Cost-Benefit analysis in Annex II.

Comments are due by 31 March 2011. ESMA will consider the feedback in April 2011 in order to adopt and publish final guidelines on endorsement by 7 June 2011.

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

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

Credit rating agencies: ECON Committee votes on resolution

The European Parliament's ECON Committee has voted on an own-initiative resolution, drafted by Wolf Klinz, on credit rating agencies (CRAs). The resolution did not find unanimous support in the Committee, with Socialists choosing to abstain from the vote with a view to amending the resolution before the Parliament's plenary session votes on it. The Committee has indicated that the key areas of disagreement included methods for rating sovereign debt and the structure of the proposed European credit rating foundation.

Basel Committee and CPSS to issue guidance on foreign exchange settlement risk

The Basel Committee on Banking Supervision and the Committee on Payment and Settlement Systems (CPSS) have announced that they are establishing a joint working group to revise the Basel Committee's 2000 supervisory guidance for managing settlement risk in foreign exchange transactions. A report entitled 'Progress in reducing foreign exchange settlement risk', published in May 2008, found that, through mechanisms such as CLS Bank, the financial services industry has made substantial progress in reducing FX settlement risk. The report noted, however, that part of the market still settles in a manner that does not mitigate FX settlement risk and that some bilateral settlement exposures are large in relation to capital, and recommended further action by individual institutions, industry groups and central banks.

The guidance issued by the Basel Committee in 2000 was before CLS Bank and other payment versus payment (PVP) settlement systems were operational. The two committees note that, as a result, it does not fully reflect advances in the market and differences between trades that settle through sound PVP arrangements and those that settle bilaterally through correspondent banking relationships. They have indicated that the revised guidance will address these and other developments with respect to FX settlement risk management.

The committees plan to issue revised guidance for public comment by the end of 2011.

IOSCO survey of client assets regimes published

IOSCO has published the results of a survey of regimes for the protection, distribution and/or transfer of client assets. IOSCO notes that regulators considering cross-border financial activity need to understand the methods for, and scope of, protection afforded to client assets in other jurisdictions, both to fulfil their own responsibilities and to achieve effective cross-border coordination, and that market participants need similar information in considering where to do business. The survey report is intended to increase access to information concerning the protections that participating regimes offer to client assets. The report covers both the pre- and post-insolvency treatment of client assets.

FSA publishes Prudential Risk Outlook

The FSA has published its Prudential Risk Outlook (PRO), which sets out its assessment of macro-economic and financial trends as a context for its micro-prudential regulation and supervision of firms. The PRO describes still important risks to financial stability and it highlights in particular: (1) incomplete progress in deleveraging required to create a less vulnerable system; (2) progress towards improved global capital and liquidity standards and the need, as that progress is achieved, to understand possible risk transfers and migrations to other parts of the financial system; (3) a number of important areas of credit risk, relating in particular to vulnerable euro-zone countries, to commercial real estate, and potentially, in emerging markets facing rapid property price inflation; and (4) the risks created by a sustained period of low interest rates which could crystallise as and when interest rates return to more normal levels.

The PRO is one of two parallel documents. Its sister publication is the Retail Conduct Risk Outlook, which was published in February 2011. The FSA's Business Plan, which is expected to be published the week of 21 March 2011, describes those priorities and the resulting resource requirements.

Prospectus Directive: HM Treasury consults on early implementation of amendments

On 24 November 2010, the European Parliament and Council adopted a Directive which amends the Prospectus Directive and the Transparency Directive. Member States have until 1 July 2012 to adopt and publish their measures to transpose the Amending Directive into national law. HM Treasury has issued a consultation paper on introducing two of the measures from the Amending Directive in the UK ahead of the implementation deadline: (1) increasing the total consideration of the offer for which the Directive does not apply from EUR 2.5 million to EUR 5 million; and (2) increasing the minimum number of investors for which a prospectus is required from 100 to 150 investors.

A draft of the proposed Statutory Instrument implementing two measures of the Amending Directive is set out at Annex A of the consultation document. A draft impact assessment is set out at Annex B.

Consultation responses are due by 9 June 2011. The Government will consult separately on proposals for implementation in the UK of the remaining elements of the Amending Directive.

UK government consults on changes to competition regime

The Department for Business, Innovation and Skills (BIS) has published a consultation paper on possible changes to the UK's competition regime. In particular, the paper sets out proposals to create a single Competition and Markets Authority (CMA) by merging the competition functions of the Office of Fair Trading with the Competition Commission.

Amongst other things, the consultation paper also seeks views on: (1) ways to improve the voluntary merger notification scheme and the alternative of the mandatory pre-notification of mergers; (2) the introduction of more (and tighter) statutory deadlines in merger and market cases, coupled with appropriate information powers; and (3) streamlining the handling of antitrust cases.

Comments are due by 13 June 2011.

AMF amends Book IV of general regulation on collective investment products

The ministerial order of 22 February 2011 approving amendments to Book IV of the French Financial Markets Authority's (AMF's) General Regulation has been published in the Official Journal. The AMF has decided to extend the format of the Key Investor Information Document (KIID) to non-UCITS funds and real estate collective investment schemes (organismes de placement collectif dans l'immobilier – OPCI) available to the public at large. In addition, the AIMF is offering the option, only for non-UCITS funds and OPCIs available to the public at large, to replace the simplified prospectus (or information statement) with the KIID ahead of schedule. The requirement to use the KIID (in place of the simplified prospectus) will enter into force on 1st July 2011.

In addition, the AMF has decided to eliminate the simplified prospectus for leveraged and unleveraged funds with streamlined investment rules (OPCVM ARIA 1 and ARIA 2) and leveraged real estate collective investment schemes with streamlined operating rules (OPCI RFA EL).

Proposal to limit liability of Dutch financial regulatory authorities announced

The Minister of Finance has sent a letter to Dutch Parliament with a recommendation to limit the liability of the Dutch Central Bank (DCB) and the Netherlands Authority for the Financial Markets (AFM). The Minister considers a limitation of liability desirable as this would allow financial regulators to display critical supervision more openly. The limitation of liability will be implemented in the Dutch Financial Supervision Act (FSA) and will therefore only affect liability claims concerning the performance of supervision by virtue of the FSA. It is still under consideration whether the limitation of liability should also extend to supervision that is performed pursuant to other Acts.

This limitation of liability was also proposed in the De Wit Report 'Lost Credit', an investigative report about the financial crisis, and was recommended by the Basel Committee on Banking Supervision. In addition, the proposed rule would align the Dutch regime for claims on financial regulators with the regimes in the UK, Ireland, Luxembourg and France.

The Minister expects that a legislative proposal will be sent to the Dutch Parliament in August 2011.

Dutch Minister of Finance comments on new framework for management of state participations in financial institutions

Following discussion in the lower chamber of Parliament about the pending legislative proposal to create a separate holding company for state participations in financial institutions, the Dutch Minister of Finance has issued further comments on the proposal. Upon enactment, the proposal would bring certain state participations under the management of a new foundation, which would in turn issue corresponding participations to the Dutch state. The aim of the proposed Act is to limit the influence of the Minister of Finance, as a shareholder, on the state participations in certain financial institutions which the state obtained during the financial market turmoil in 2008. This limitation is deemed necessary to facilitate a transparent weighing of interests, a credible exit strategy, and a commercial and not politically motivated management.

The Minister intends to include certain provisions in the foundation's articles of association, including an approval authority for the Minister of Finance with regard to the foundation's budget and its directors, as well as a requirement for the foundation to include a conflict of interest policy in its articles. The proposal is expected to be enacted by 1 July 2011.

SFC issues checklist to facilitate readiness for listed renminbi securities business

The Securities and Futures Commission (SFC) has issued a checklist to facilitate the Stock Exchange of Hong Kong Limited (SEHK) and the Central Clearing and Settlement System (CCASS) participants' review of their readiness to conduct listed renminbi (RMB) securities business. The checklist recaps the key areas the participants should consider during their readiness review.

HKMA enhances regulatory requirements for selling of investment-linked assurance scheme products

The Hong Kong Monetary Authority (HKMA) has issued a circular to enhance the regulatory requirements for the sale of investment-linked assurance scheme products by authorised institutions. The circular requires authorised institutions to ensure compliance with the relevant regulatory requirements when selling investment-linked assurance scheme products, particularly the control measures set out in the Annex of the circular. The HKMA has indicated that most of these measures are existing regulatory requirements or practices generally adopted by the industry that are now being formalised as regulatory requirements to ensure their consistent application by all authorised institutions to enhance investor protection.

The circular calls on authorised institutions to review their existing control procedures and practices in the sale of investment-linked assurance scheme products to ensure that they comply with the relevant regulatory requirements.

MAS publishes explanatory brief on Deposit Insurance and Policy Owners' Protection Schemes Bill and Insurance (Amendment) Bill

The Monetary Authority of Singapore (MAS) has published an explanatory brief on the Deposit Insurance and Policy Owners' Protection Schemes Bill and the Insurance (Amendment) Bill. The amendments in the Bill provide for enhanced deposit insurance and policy owners' protection schemes, and are intended to strengthen the protection of depositors and policy owners. In addition, by amending the Insurance Act, the MAS intends to strengthen the insurance regulatory framework to allow it to act swiftly when dealing with distressed insurers.

The amendments in the Deposit Insurance and Policy Owners' Protection Schemes Bill include: (1) raising the coverage limit from SGD 20,000 to SGD 50,000 per depositor per deposit insurance scheme member and expanding coverage from insuring only individuals and charities to insuring all non-bank depositors; (2) in the event of a payout, paying the gross amount of depositors' insured deposits up to the deposit insurance coverage limit, without first netting off their liabilities to the scheme member; and (3) enhancing the powers of the Singapore Deposit Insurance Corporation (SDIC) to administer the policy owners' protection scheme as well as the deposit insurance scheme.

The amendments in the Insurance (Amendment) Bill include: (1) granting powers to the MAS to take control of a distressed insurer and to determine the sale or transfer of assets and liabilities, or ownership, of the insurer; and (2) allowing the MAS to approve the appointment of a liquidator for an insurer in liquidation.

Key provisions in Deposit Insurance and Policy Owners' Protection Schemes Bill
Key provisions in Insurance (Amendment) Bill

FSC announces amendment to Depositor Protection Act

The Financial Services Commission (FSC) has announced that the National Assembly has approved an amendment to the Depositor Protection Act, which creates a special purpose account within the deposit insurance fund that will only be used for the restructuring of savings banks. The special fund for savings banks will be financed by part of the deposit insurance fees and government contributions.

Amongst other things, under the amended Depositor Protection Act: (1) the special account will be run temporarily until troubled savings banks are stabilised – taking into account the period of repayment, the special account will remain valid until 31 December 2026; (2) the Korea Deposit Insurance Corporation (KDIC) is required annually to report plans on how to manage the special fund and the results to the Standing Committee of the National Assembly, and publish a white paper on the operation of the special fund; and (3) when the special account is liquidated, the government contributions out of the remaining balance will belong to the national treasury.

The amended Depositor Protection Act will enter into force on 1 April 2011.

FDIC consults on proposed rule to set claims process under Dodd-Frank Act orderly liquidation authority

The Board of Directors of the Federal Deposit Insurance Corporation (FDIC) has issued a notice of proposed rulemaking which is intended to clarify the application of the orderly liquidation authority contained in Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The notice of proposed rulemaking establishes a framework for the priority payment of creditors and for the procedures for filing a claim with the receiver and, if dissatisfied, pursuing the claim in court. In addition, it clarifies certain other issues relating to the implementation of the orderly liquidation authority, including how compensation will be recouped from senior executives and directors who are substantially responsible for the failure of a firm.

Comments on the proposed rule will be accepted for 60 days after publication in the Federal Register.

RECENT CLIFFORD CHANCE BRIEFINGS

Claims against banks – the facts win again

Facts usually determine the outcome of litigation. So it was with a recent claim brought against a bank. The claimant failed because it could not prove the facts upon which its claim relied, a fate that has befallen a number

of similar claims against banks. In this case, the buyer of a structured note incorporating a CDO2 failed to show that the bank selling the note had made an implied representation that the CDO2 had a very low risk of default. Banks have responsibilities, but that does not mean that they guarantee investors' returns.

This briefing discusses the case.

http://www.cliffordchance.com/publicationviews/publications/2011/03/claims_against_banksthefactswinagain.html

Eurosail Appeal – more navigating troubled financial waters

The case of BNY Corporate Trustee Services Ltd v Eurosail is the first time that the Court of Appeal has analysed the meaning of balance sheet insolvency under section 123(2) Insolvency Act 1986 since the introduction of that section some 25 years ago. The case has been much anticipated by those operating in the structured finance market as it concerned the interpretation of some of the key aspects of a traditional securitisation structure: the balance sheet insolvency test as an event of default and the effects of a post enforcement call option. However, the decision has much wider ramifications than solely for the asset-backed market, and is of importance for any financial transactions which utilise the section 123(2) test for triggering an event of default as well as for general corporate solvency situations.

This briefing explores the reasoning behind the Court of Appeal decision and its implications for the asset-backed market and a wider range of financial transactions. Although the court has made the test for balance sheet insolvency more complex and more subjective, the decision should bring greater stability to financial transactions in the future.

http://www.cliffordchance.com/publicationviews/publications/2011/03/eurosail_appeal_amorenavigatingtrouble.html

Contentious Commentary – a review for litigators

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

http://www.cliffordchance.com/publicationviews/publications/2011/03/contentious_commentaryareviewforlitigators.html

Anti-money laundering system of the Netherlands evaluated by the Financial Action Task Force

Recently, the Financial Action Task Force (FATF) published the report of the mutual evaluation of the Netherlands, assessing its level of compliance with the FATF requirements for anti-money laundering and combating the financing of terrorism. It describes and analyses these measures and provides recommendations on how to strengthen certain aspects of the system.

This briefing lists the main conclusions of the FATF relevant for financial institutions, including the reaction of the Dutch government regarding this evaluation.

http://www.cliffordchance.com/publicationviews/publications/2011/03/anti-money_launderingsystemofthenetherland.html

Polish Legislation Newsletter

The Polish Legislation Newsletter summarises selected recent changes to Polish law. The February 2011 edition contains information on, amongst other things: (1) an Act Amending the Act on Commercialisation and Privatisation and Certain Other Acts; (2) an Act Amending the Act on the Special Terms of Consumer Sales and Amending the Civil Code; and (3) an Ordinance of the Minister of Finance Amending the Ordinance on the Calculation of Default Interest and a Prolongation Fee and the Scope of Information to be Contained in the Accounts.

http://www.cliffordchance.com/publicationviews/publications/2011/03/polish_legislationnewsletterfebruary2011.html

India's New Merger Control Regime in Force from 1 June

India's merger control regime will come into force from 1 June 2011, following the notification on 4 March 2011 of the Government of India of Sections 5 and 6 of Competition Act, 2002, after nine years of deliberation. Assuming there are no further delays, all mergers, acquisitions and joint ventures that are 'put into effect' after this date, and which meet certain turnover or asset thresholds, will be subject to mandatory notification to the Competition

Commission of India (CCI) and a 'standstill obligation' prohibiting completion until the CCI has issued a clearance decision.

This briefing provides an overview of the new regime and highlights a number of worrying aspects.

Please contact Barbara Kahn by email at barbara.kahn@cliffordchance.com for a copy of this briefing.