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27 June - 1 July 2011

International Regulatory Update

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FSA consults on Financial Conduct Authority's approach to regulation

The FSA has published a document setting out its initial thinking on how the Financial Conduct Authority (FCA), which is expected to be established by end-2012, will approach the delivery of its objectives. The document sets out: (1) the scope of the FCA; (2) the FCA's objectives and powers, as proposed by the government; (3) the regulatory approach which the FCA expects to follow in discharging its responsibilities; (4) how the FCA plans to discharge its various functions, including supervision, policy making, authorisation, and

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enforcement; (5) the FCA's plans to coordinate with other regulatory authorities, in the UK and internationally; and (6) the next steps in implementing the FCA's operating model.

Comments are due by 1 September 2011.

In addition, the FSA held a conference to mark the launch of the consultation at which both Hector Sants, FSA Chief Executive, and Margaret Cole, Interim Managing Director of the conduct business unit, gave speeches.

Hector Sants argued that the FCA needs to: (1) deliver a more proactive style of regulation than its predecessor, at the core of which will be early intervention both in respect of products and selling processes; (2) deliver meaningful choice and effective competition; (3) deliver a credible deterrence agenda; (4) deliver a more effective redress process; (5) ensure consumers have the right information to make informed judgements; and (6) act in a more transparent and accountable manner. However, Mr. Sants acknowledged that a mandate of this nature will require the FCA to have more resources and powers than the FSA. He also acknowledged that an approach of early intervention will necessarily run the risk of reducing innovation and constraining individual freedom of choice.

Margaret Cole emphasised the need for close co-ordination between the FCA and the other new regulatory bodies, including the Prudential Regulation Authority (PRA), particularly where a firm is dual-regulated. She also stressed that the FCA will need to engage effectively at an early stage in EU negotiations to influence the outcomes.

Ms. Cole highlighted the FCA's new powers in product intervention, including the power to direct firms to withdraw or amend misleading financial promotions with immediate effect, and to publish the fact that a warning notice in relation to a disciplinary matter has been issued. She also stated that the FCA will require firms to publish more information on their activities to improve market discipline. Finally, she noted that the FCA will need to consider the interactions and linkages across the financial value chain where risks are transmitted between wholesale and retail customers. In particular, she indicated that the FCA will look at intervention further up the value chain, targeted at product governance.

Group of Central Bank Governors and Heads of Supervision agrees measures for global systemically important banks

The Group of Central Bank Governors and Heads of Supervision, the oversight body of the Basel Committee on Banking Supervision, has agreed on a consultative document setting out measures for global systemically important banks. These measures include the methodology for assessing systemic importance, the additional required capital and the arrangements by which they will be phased in. The measures are intended to strengthen the resilience of global systemically important banks and create strong incentives for them to reduce their systemic importance over time.

The assessment methodology for global systemically important banks is based on an indicator-based approach and comprises five broad categories: (1) size; (2) interconnectedness; (3) lack of substitutability; (4) global (cross-jurisdictional) activity; and (5) complexity. The additional loss absorbency requirements are to be met with a progressive Common Equity Tier 1 capital requirement ranging from 1% to 2.5%, depending on a bank's systemic importance. To provide a disincentive for banks facing the highest charge to increase materially their global systemic importance in the future, an additional 1% surcharge would be applied in such circumstances.

The higher loss absorbency requirements will be introduced in parallel with the Basel III capital conservation and countercyclical buffers, between 1 January 2016 and year end 2018, becoming fully effective on 1 January 2019.

The Group of Central Bank Governors and Heads of Supervision and the Basel Committee have indicated that they will continue to review contingent capital, and support the use of contingent capital to meet higher national loss absorbency requirements than the global minimum.

The Group of Central Bank Governors and Heads of Supervision is submitting the consultative document to the Financial Stability Board (FSB), which is coordinating the overall set of measures to reduce the moral hazard posed by global systemically important financial institutions. This package of measures is due to be issued for consultation around the end of July 2011.

AIFMD published in Official Journal

The Alternative Investment Fund Managers (AIFM) Directive has been published in the Official Journal and will enter into force on 21 July 2011.

Poland commences EU Council Presidency

Poland has taken over the EU Council's six-month rotating Presidency. In relation to the financial services sector, the Polish Presidency's six-month work programme states that the Presidency will support and promote the early adoption of proposals to improve financial market regulation and oversight and to develop crisis management rules, and that special emphasis will be placed on the implementation of measures to increase the integrity and transparency of the financial sector, reducing systemic risks and excessive risk-taking.

The work programme also indicates that the ECOFIN Council will monitor the operation of the new macro- and micro-prudential oversight framework, closely collaborating with the European Systemic Risk Board (ESRB) and the newly established supervisory agencies. In addition, the Polish Presidency will continue work on financial sector taxation.

Work relating to the establishment of the European Stability Mechanism will also be continued to enable its entry into force in accordance with the timetable set by the European Council in December 2010.

Basel Committee issues Pillar 3 disclosure requirements on remuneration

The Basel Committee on Banking Supervision has issued its final Pillar 3 disclosure requirements for remuneration. The Pillar 3 disclosure requirements on remuneration are designed to add greater specificity to the disclosure guidance on this topic that was included in the supplemental Pillar 2 guidance issued by the Basel Committee in July 2009.

In particular, banks will be requested to disclose qualitative and quantitative information about their remuneration practices and policies covering the following areas: (1) governance/committee structures; (2) the design/operation of the remuneration structure, and frequency of review; (3) the independence of remuneration for risk/compliance staff; (4) risk adjustment methodologies; (5) the link between remuneration and performance; (6) long-term performance measures (deferral, malus, clawback); and (7) types of remuneration (cash/equity, fixed/variable).

Basel Committee publishes guidance on operational risk

The Basel Committee on Banking Supervision has published the following two papers on operational risk:

- 'Principles for the Sound Management of Operational Risk'; and
- 'Operational Risk – Supervisory Guidelines for the Advanced Measurement Approaches'.

'Principles for the Sound Management of Operational Risk' updates the Committee's 2003 paper on this topic. The updated version highlights the evolution of operational risk management since 2003. The principles outlined in the report are based on best industry practice and supervisory experience and cover three overarching themes – governance, risk management and disclosure.

'Operational Risk – Supervisory Guidelines for the Advanced Measurement Approaches' seeks to promote convergence towards a narrower band of effective risk management and measurement practices by setting out supervisory guidelines relating to governance, data and modelling.

BBA annual conference: regulators share views on future of regulation and capital requirements

The BBA has held its annual international banking conference, at which Andrea Enria, EBA Chairman, Paul Tucker, Bank of England Deputy Governor for Financial Stability, Hector Sants, FSA Chief Executive, and Mark Hoban, Financial Secretary to HM Treasury, all gave speeches.

Andrea Enria emphasised the need for consistency in the implementation of global reforms and of the single rulebook in the European Union. However, he also acknowledged that there are good reasons for leaving some room for flexibility at the national level. In particular, he noted that macro-prudential supervision may require that certain prudential requirements are adjusted having regard to the stability of the system as a whole. According to Mr. Enria, macro-prudential tools should be operated within a framework of constrained discretion, under ex ante guidance and ex post review by the European Systemic Risk Board (ESRB).

Paul Tucker reviewed progress in constructing what he described as the new 'social contract' for banking. He indicated that this would involve rapid payouts from deposit insurance; liquidity provision against wider collateral; constraints on shadow banking to limit regulatory arbitrage; simplification of systemically important financial institutions' internal structures and practices to aid resolvability; powers for resolution agencies to reconstruct the capital structure of a distressed bank or dealer, to avoid the disorder of orthodox liquidation; a capital surcharge

for systemically important financial institutions; and the UK's new Financial Policy Committee (FPC) temporarily raising capital or liquidity requirements in the face of threats to stability.

Hector Sants focused on the changing shape of banking regulation in the UK. He provided an overview of the new Prudential Regulation Authority's (PRA's) and the Financial Conduct Authority's (FCA's) objectives and the approach that they will take to banking regulation. He emphasised that the reforms should lead to a change in the behaviours and the processes of banks and regulators alike.

Mark Hoban argued, amongst other things, that Basel III should be implemented as the minimum standard across the EU, not the maximum, and that jurisdictions should retain the right to apply higher levels of regulation to ensure financial stability. He added that maximum harmonisation would limit the ability of national regulators to impose requirements to reflect the unique risks and characteristics of their home markets, and would also undermine the ability of national regulators to tackle macro risks unique to their markets.

Ministry of Justice issues circular on Bribery Act 2010

The Ministry of Justice has published a circular about the Bribery Act 2010, which provides a brief explanation and commentary on key provisions. The Bribery Act replaces the offences at common law and under the Public Bodies Corrupt Practices Act 1889, the Prevention of Corruption Act 1906 and the Prevention of Corruption Act 1916 (known collectively as the Prevention of Corruption Acts 1889 to 1916) with a new consolidated scheme of bribery offences.

Amongst other things, the circular covers: (1) consent to prosecution; (2) liability of individuals; (3) corporate liability; and (4) defence for certain bribery offences.

The Bribery Act 2010 will enter into force on 1 July 2011.

BaFin issues circular on other illegal acts under KWG in connection with anti-money laundering

The Federal Financial Supervisory Authority (BaFin) has published Circular 7/2011 (GW) regarding other illegal acts under section 25c para 1 and 9 of the German Banking Act (KWG). Section 25c of the KWG was amended by the German 'Act on the Implementation of Directive 2009/110/EC of the European Parliament and of the Council of 16 September 2009 on the taking up, pursuit and prudential supervision of the business of electronic money institutions amending Directives 2005/60/EC and 2006/48/EC and repealing Directive 2000/46/EC', which entered into force on 30 April 2011. It covers internal procedures designed to prevent money-laundering and other illegal acts.

The circular provides rules for interpretation and application as regards the legal requirements for preventing other legal acts within the meaning of section 25c of the KWG.

Rules for interpretation and application

Belgian Constitutional Court annuls bank levy

The Constitutional Court has annulled the bank levy adopted in response to the financial crisis in 2009. The levy consists of an annual fee of 0.15% payable by banks on the amount of their deposits covered by the retail deposit guarantee scheme. The court held that this fee is discriminatory because its calculation does not take into account the degree of insolvency risk of each particular bank, and bears disproportionately on those institutions that fund themselves mainly from retail deposits, compared to those that fund themselves mainly on the capital markets. The annulment does not affect the fees payable in 2011, and takes effect from 2012.

Judgment (French)
Judgment (Dutch)
Judgment (German)

Dutch authority publishes new standard language and signs for exemption warning

The Netherlands Authority for the Financial Markets (AFM) has published a new exemption warning, which has been nicknamed the 'Wild West Sign' (wildwestbordje), to be included in all offering materials when offering to Dutch investors. The Wild West Sign will have to be included by exempted issuers, collective investment schemes and offerors of 'investment objects' (beleggingsobjecten) that are exempt from prospectus or license requirements.

While the inclusion of such a warning is already obligatory for some securities, as of 1 January 2012 the warning will need to have a prescribed form to be determined by the AFM. The sign will have to cover at least 10% of the front page of all written offering materials (including a prospectus approved in another Member State but not passported into the Netherlands) and websites. Only issuers offering solely to qualified investors are exempt from the requirement to include the Wild West Sign.

The Wild West Sign consists of a picture of a worrying man, a euro sign, a question mark and the following phrase (in either Dutch or English): 'Attention! This investment falls outside AFM supervision. No license/ prospectus required for this activity.' The AFM has also provided a voice message to be included in radio advertisements.

SFC publishes consultation conclusions on proposals to expand scope of conflicts of interest requirements governing research analysts

The Securities and Futures Commission (SFC) has published its consultation conclusions on proposals to expand the scope of conflicts of interest requirements governing research analysts, which were published on 30 September 2010. The SFC will proceed to extend to real estate investment trusts (REITs) and listing applicants the requirements governing analyst conduct in preparing investment research reports. The SFC will also extend the conflicts of interest requirements to analysts conducting research for business operations that are constituted in a form other than a corporation or a REIT. One of the new requirements stipulates that sponsors of listing applicants are required to take reasonable steps to ensure that all material information, including material forward looking information, disclosed to analysts is contained in prospectuses or listing documents.

The SFC intends to implement the new requirements with effect from 1 September 2011 except for the requirements in relation to new listings. In the case of a new listing applicant, the new requirements will apply to any new listing where the listing application (i.e. the A1 Form) is submitted to the Stock Exchange of Hong Kong Ltd on or after 1 August 2011.

Japanese FSA consults on draft legislation concerning short selling connected to public offerings

The Financial Services Agency (FSA) has published drafts of the amended Order for Enforcement of the Financial Instruments and Exchange Law and the amended Ordinance on Financial Instruments Business, etc. for public comment. The amendments provide that an investor who accrues a short selling position of shares in a company after the company has announced a public offering of those shares shall not settle his short selling position with the shares acquired under the public offering. The implementation dates for the amendments are not yet available.

Comments are due by 25 July 2011.

Singapore authority strengthens capital requirements for Singapore-incorporated banks

The Monetary Authority of Singapore (MAS) has announced that it will require Singapore-incorporated banks to meet capital adequacy requirements that are higher than the Basel III global capital standards.

From 1 January 2015, Singapore-incorporated banks will be required to meet a minimum Common Equity Tier 1 (CET1) capital adequacy ratio (CAR) of 6.5%, Tier 1 CAR of 8% and total CAR of 10%, which are higher than the Basel III minimum requirements of 4.5%, 6% and 8% for CET1 CAR, Tier 1 CAR and total CAR, respectively. In addition, the MAS will require Singapore-incorporated banks to meet the Basel III minimum capital adequacy requirements from 1 January 2013, two years ahead of the Basel Committee on Banking Supervision's 2015 timeline. This means that, from 1 January 2013, Singapore-incorporated banks will meet a minimum CET1 CAR of 4.5% and Tier 1 CAR of 6%. The MAS' existing requirement for total CAR will remain unchanged at 10%.

The MAS believes that capital requirements on Singapore-incorporated banks need to be set higher than the Basel III minimum requirements because each of the Singapore-incorporated banks is systemically important in Singapore and has a substantial retail presence. The MAS plans to adopt these standards and intends to consult on the text of its rules later in 2011.

Korean authorities issues guidelines on issuance of covered bonds

The Financial Services Commission (FSC) and Financial Supervisory Service (FSS) have issued guidelines on the issuance of covered bonds by banks, as one of the follow-up measures to implement their comprehensive policy measures on household debt. The guidelines are intended to provide a framework for covered bond issuances to diversify banks' financing of instruments and encourage them to offer more long-term and fixed-rate mortgage loans instead of short-term and floating-rate ones.

SEC consults on proposed business conduct standards for security-based swap dealers and major security-based swap participants

The SEC has requested public comment on proposed business conduct standards for security-based swap dealers and major security-based swap participants. Amongst other things, the proposed rules would require security-based swap dealers and major security-based swap participants to disclose conflicts of interest and material incentives to potential counterparties. Additional restrictions would apply when dealing with special entities like municipalities, pension plans, and endowments.

Comments are due by 29 August 2011.

RECENT CLIFFORD CHANCE BRIEFINGS

A better schematic for regulating securitisation in Europe

Securitisation regulation in Europe must be overhauled to differentiate between the products that are essential to financing economic growth and the more notorious transactions that have become associated with the financial crisis. The present one-size-fits-all regulatory definition of securitisation, based on that put forward by the Basel II Accord which has, in essence, been adopted by the European Commission in the Capital Requirements Directive, suggests that securitisation is a single definable product. Yet, in reality, there are a wide variety of securitisation product types ranging from secured corporate debt through to exotic derivative trades and it is wrong to suggest that they can be categorised together because they share an abstract 'unifying' set of characteristics.

This article proposes a new approach to defining and categorising transactions, which will help to distinguish the products and assist in delivering regulatory approaches which fit the demands of the particular product type. This proposed approach which assesses securitisations by reference to skills sets will provide a sounder basis for deciding whether a transaction is a 'good' securitisation or a 'bad' one and so whether it deserves encouragement as an essential part of the solution for funding the recovery of the real economy in many jurisdictions, or prohibited in some way as a cause of the global credit crisis.

http://www.cliffordchance.com/publicationviews/publications/2011/06/a_better_schematicforregulatingsecuritisatio.html

OTC derivatives reforms – Impact on cross-border business

The reforms of OTC derivatives markets threaten the ability of international banking groups to centralise the risk management of their cross-border derivatives business. The resulting more regionalised booking models are likely to reduce client choice and competition, increase clients' risk management costs, distort market behaviour and create new risks to financial stability. International banking groups currently use a number of different structures to book cross-border OTC derivatives transactions, providing important benefits to the firm and its clients/counterparties: good risk management and capital efficiency, compliance with licensing laws, maximising netting, meeting client/counterparty preferences and compliance with tax rules. These structures also improve the overall efficiency and resilience of the financial system.

This briefing reviews the possible impact of the OTC derivatives reforms on cross-border transactions and banks' booking structures and proposing possible solutions.

http://www.cliffordchance.com/publicationviews/publications/2011/06/otc_derivatives_reformsimpactoncross-borde.html

Sense and Suitability

The FSA's 'Dear CEO' letter addressed to firms in the wealth management industry signals a definitive turning point in its attitude towards the regulation of the sector. The letter reports on 'significant' and 'widespread' failings following its review of client portfolio suitability and will have come as a rather unwelcome surprise for those firms not involved in the review, many of which will need to take immediate steps to assess suitability. Those firms which were the subject of the review will have received even less pleasant news, as the FSA's letter reports that it is involved in ongoing regulatory action with them as a result of its findings.

This briefing discusses the implications of the 'Dear CEO' letter.

http://www.cliffordchance.com/publicationviews/publications/2011/06/sense_and_suitability.html

Applying the lessons from Springwell and other mis-selling cases

Recent cases of alleged mis-selling offer useful insights into what banks and other financial institutions can expect from the English courts. Journalist Chuck Grieve listened as Clifford Chance experts outlined lessons that can be learned.

http://www.cliffordchance.com/publicationviews/publications/2011/06/applying_the_lessonsfromspringwellandothe.html

New Luxembourg licence requirement for non-EU/EEA finance professionals

The Luxembourg legislator has introduced a new license requirement for banks, investment firms and other professionals which are incorporated in a non-EU/EEA country and which are not established in Luxembourg, but which come occasionally and temporarily to Luxembourg, notably to collect deposits or other repayable funds from the public and to provide any other services within the scope of Luxembourg financial sector legislation in Luxembourg. The new licence requirement for non-EU/EEA professionals was introduced by a law dated 28 April 2011 that has come into force on 9 May 2011. It has been further explained by the recent Circular 11/515 dated 14 June 2011 issued by the Luxembourg financial sector regulator Commission de Surveillance du Secteur Financier (CSSF).

This briefing discusses the new licence requirement rules.

http://www.cliffordchance.com/publicationviews/publications/2011/06/new_luxembourg_licencerequirementfornon-euee.html

New Dutch regulation may discourage cross-border securities offerings into the Netherlands

The mandatory use of a new Dutch standardised exemption warning on offering materials could prove to have a considerable impact on exempt offerings of securities in the Netherlands. Despite widespread market concerns, the Dutch Financial Markets Amendment Act introduces the requirement to include a 'health warning' dubbed 'Wild West Sign' in marketing material and prospectuses for offerings of securities which are exempt from prospectus requirements under the EU Prospectus Directive. If the prospectus is approved by the Dutch securities markets regulatory authority (AFM) or another EU competent authority and passported into the Netherlands, this requirement does not apply. In addition, the Amendment Act will raise the minimum denomination threshold for certain non-regulated investment products from EUR 50,000 to EUR 100,000. The above changes take effect on 1 January 2012.

This briefing discusses the changes.

http://www.cliffordchance.com/publicationviews/publications/2011/06/new_dutch_regulationmaydiscouragecross-borde.html

Codification of price sensitive information disclosure requirement

The Hong Kong Government is introducing the Securities and Futures (Amendment) Bill 2011 to codify the price sensitive information disclosure requirement to the Legislative Council on 29 June 2011. Under the Bill, a listed corporation is required to disclose price sensitive information as soon as reasonably practicable after it has become aware of the information unless the information falls within the Safe Harbours as provided in the Securities and Futures Ordinance (SFO).

This briefing highlights the key proposals made under the Bill and summarises the key points of the Securities and Futures Commission (SFC)'s revised guidelines on disclosure of inside information.

http://www.cliffordchance.com/publicationviews/publications/2011/06/codification_of_pricesensitiveinformatio.html

Casting a wide net – SEC significantly expands regulation of non-US investment advisers, adopts final rules under Dodd-Frank

On 22 June 2011, almost five months after the close of the formal public comment period, the SEC adopted final rules relating to provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act that modify the US Investment Advisers Act of 1940, as amended. These provisions expand the Advisers Act's coverage to include many formerly-exempt investment advisers to private equity and hedge funds. From the standpoint of non-US investment advisers, the final rules are identical to the proposed rules in nearly all material respects. Two SEC releases, Rules Implementing Amendments to the Investment Advisers Act of 1940, Release No. IA-

3221 (the 'Implementing Adopting Release') and Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than USD 150 Million in Assets Under Management, and Foreign Private Advisers, Release No. IA-3222 (the 'Exemptions Adopting Release'), contain the published text of the final rules.

As predicted, the SEC officially postponed the compliance date for the expanded registration requirements. An investment adviser that becomes subject to registration under the Advisers Act due to the elimination of the 'private adviser' exemption will not need to register with the SEC (or report information if an 'exempt reporting adviser') until 30 March 2012. Investment advisers required to register with the SEC should plan to file their completed Form ADV (Parts 1 and 2) no later than 14 February 2012 to ensure compliance by the deadline.

This briefing reviews the aspects of the Exemptions Adopting Release most relevant to investment advisers who are organized and have their principal place of business outside the United States.

http://www.cliffordchance.com/publicationviews/publications/2011/06/casting_a_wide_netsecsignificantlyexpand.html

Turkish delight – revocable trusts and settlors' creditors

If a settlor of a trust retains the power to revoke the trust, judgment creditors of the settlor may be able to enforce their judgments against the assets secreted in the trust. This can be achieved by the court appointing a receiver over the settlor's power of revocation, and the receiver then exercising that power. Once the trust has been revoked and the trust assets put back in the hands of the settlor, those assets are fair game for the settlor's creditors. Many will consider this to be obviously the right result, but the Privy Council decision that reached it only did so by reversing the decision of the lower courts and by revisiting some basic trust principles.

This briefing discusses the decision in Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank & Trust Company (Cayman) Ltd.

http://www.cliffordchance.com/publicationviews/publications/2011/06/turkish_delight_revocabletrustsandsettlors.html