C L I F F O R D
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Briefing note

International Regulatory Update

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IN THIS WEEK'S NEWS

- Ratings agencies: EU Commission publishes equivalence decisions on Argentina, Brazil, Hong Kong, Mexico, and Singapore
- EBA publishes action plan for colleges of supervisors
- EBA publishes methodology and scenarios for 2014 EU-wide stress test
- EBA launches data collection exercise on credit valuation adjustment
- CRD 4: European Systemic Risk Board responds to call for advice on macro-prudential rules
- Joint Forum publishes final report on point of sale disclosure
- BoE publishes details of UK stress test
- CRD 4: PRA publishes capital buffers framework
- BaFin publishes minimum requirements for drawing up recovery plans
- German Federal Government publishes draft act to reduce dependence on ratings
- New royal decree on disclosure obligations of listed issuers published
- CSSF signs multilateral memorandum of understanding with ESMA
- DNB imposes systemic risk buffer requirement on Dutch systemic banks
- SAFE issues pilot rules on multi-national companies' foreign exchange cash pooling
- Shenzhen Stock Exchange updates trading rules for QFIIs and RQFIIs
- Shanghai Stock Exchange consults on implementing rules for Shanghai-Hong Kong Stock Connect
- HKMA issues circular on implementation of new large exposures framework for banks
- APRA proposes simplified prudential framework for securitisation
- Australia and US sign FATCA intergovernmental agreement

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- Recent Clifford Chance Briefings: UCITS V; The UK's challenge to the FTT; and more. Follow this link to the briefing section.

Ratings agencies: EU Commission publishes equivalence decisions on Argentina, Brazil, Hong Kong, Mexico, and Singapore

The EU Commission has adopted five implementing decisions which confirm that the rules on credit rating agencies (CRAs) in place in Argentina, Brazil, Hong Kong, Mexico, and Singapore are equivalent to those in the EU. The adoption of these decisions follows the positive technical assessment of the regulatory environments in these jurisdictions by the European Securities and Markets Authority (ESMA), the EU supervisor for credit rating agencies. The equivalence decisions allow smaller CRAs in these countries to apply for certification in the EU with the result that their ratings can be used by EU financial institutions for regulatory purposes.

EBA publishes action plan for colleges of supervisors

The European Banking Authority (EBA) has published its 2014 action plan for colleges of supervisors of European Economic Area (EEA) banks. The plan identifies key activities necessary for the effective oversight of Europe's cross border banking groups in 2014, and is issued alongside a report providing an assessment on the colleges functioning during 2013.

The 2014 action plan takes into account the latest regulatory and institutional developments that will impact the functioning of colleges in 2014. Key points include:

- a common methodology for the supervisory review and evaluation process (SREP) in pillar 2 capital requirements which aims for higher consistency in the outcome of capital joint decisions by colleges of supervisors;
- the need to reach a joint decision on liquidity, under the Capital Requirements Directive (CRD 4) which will be supported by technical standards, and common templates issued by the EBA as well as a common methodology for the assessment of liquidity under SREP; and
- ensuring effective communication and coordination between national supervisors of cross-border banking groups during the 2014 AQRs and EU-wide stress test exercise.

EBA publishes methodology and scenarios for 2014 EU-wide stress test

The EBA has released its methodology and scenarios for the 2014 EU-wide stress test. The test is designed to assess banks' resilience to hypothetical external shocks, identify remaining vulnerabilities in the EU banking sector, and provide a high level of transparency into EU banks' exposures. The methodology will be used by all EU supervisory authorities to ensure that the main EU banks are all assessed against common assumptions, definitions and approaches. The EBA has also released the macroeconomic scenarios, developed by the European Systemic Risk Board (ESRB), which will be used to assess the impact that changes in the economic environment have on EU banks.

EBA launches data collection exercise on credit valuation adjustment

The EBA has launched a data collection exercise in order to inform recommendations to the EU Commission on Credit Valuation Adjustment (CVA) risk in accordance with the Capital Requirements Regulation and advise the Commission on appropriate amendments to the CVA framework. The data will additionally be used to inform international discussions on CVA risk. Participation in the exercise will be voluntary, but banks with relatively substantial portfolios of OTC derivatives are expected to participate regardless of whether they use the advanced or the standardised method for CVA risk.

CRD 4: European Systemic Risk Board responds to call for advice on macro-prudential rules

The European Systemic Risk Board (ESRB) has published its response to the EU Commission's call for advice on the sufficiency of macro-prudential provisions in the EU capital requirements framework to mitigate systemic risks in EU sectors, regions and Member States. The ESRB states that the CRD 4 package consists of many of the components for a sound macro-prudential framework in the EU, but suggests specific alterations to the regime to improve its effectiveness and coverage.

Joint Forum publishes final report on point of sale disclosure

The Joint Forum, which comprises the Basel Committee on Banking Supervision (BCBS), the International Association of Insurance Supervisors (IAIS) and the International Organization of Securities Commissions (IOSCO), has published its final report on point of sale (POS) disclosure.

The report identifies and assesses differences and gaps in regulatory approaches to POS disclosure for investment and savings products across the insurance, banking and securities sectors, and considers whether the approaches need to be further aligned across sectors.

It sets out recommendations, for use mainly by policymakers and supervisors to assist them with POS disclosure regulations, and advises that jurisdictions should consider implementing a concise written or electronic POS disclosure document for the product sample identified in the report, taking into account the jurisdiction's regulatory regime. It recommends that the POS disclosure documents should:

- be provided to consumers free of charge, before the time of purchase;
- be clear, fair, not misleading and written in a plain language designed to be understandable by the consumer;
- include the same type of information to facilitate comparison of competing products; and
- be concise, set out key information about a product and make it clear that it does not provide exhaustive information.

Jurisdictions considering POS disclosure should consider:

- requiring that a POS disclosure document disclose key characteristics including costs, risks and financial benefits or other features of a given product and any underlying or referenced assets, investments or indices, irrespective of the financial sector from which the products are derived;
- allocating and clearly establishing responsibility for preparing, making available and/or delivering the POS disclosure document and identifying which entity is responsible for its content; and
- how to use its capabilities and powers to implement these POS recommendations.

BoE publishes details of UK stress test

The Bank of England (BoE) has published details of the scenario for stress tests that eight major UK banks and building societies will undertake in 2014. The UK stress test will be built on and run alongside the EBA's EU-wide exercise, but will add a number of additional UK layers which explore particular vulnerabilities facing the UK banking system. The BoE intends to publish the results towards the end of 2014. The publication of the stress test scenario follows a discussion paper published by the BoE in October 2013 setting out proposals for annual and concurrent stress testing in the UK.

CRD 4: PRA publishes capital buffers framework

The Prudential Regulation Authority (PRA) has published its policy and supervisory statements to implement the CRD 4 capital buffers framework. The statements provide the final rules and set out the expectations of the PRA on CRD 4 capital buffers for UK banks, building societies and PRA designated investment firms covered by the framework.

BaFin publishes minimum requirements for drawing up recovery plans

The German Federal Financial Supervisory Authority (BaFin) has published its minimum requirements for drawing up recovery plans. The requirements apply to German credit institutions that have been identified by BaFin as potentially systemically important.

German Federal Government publishes draft act to reduce dependence on ratings

The German Federal Government has published a draft act to reduce reliance on ratings. The act is intended to implement recently enacted EU legislation on the regulation of rating agencies and the supervision of institutions for occupational retirement provision, undertakings for collective investment in transferable securities and alternative investment funds managers in respect of over-reliance on credit ratings. The draft act was published shortly after the publication of the German action plan to reduce overreliance on CRA ratings.

New royal decree on disclosure obligations of listed issuers published

A royal decree of 26 March 2014, amending certain disclosure obligations of issuers whose shares are listed on a regulated market, has been published in the Moniteur Belge. The new royal decree implements certain provisions of the amended Transparency Directive (2013/50/EU) into Belgian law. The royal decree relaxes certain disclosure requirements for issuers whose shares are listed on a regulated market, and in particular provides that such issuers no longer need to publish quarterly financial reports.

The Financial Services and Markets Authority has updated its circular (FSMA/2012_01) on disclosure requirements for listed companies in order to reflect the provisions of the royal decree.

CSSF signs multilateral memorandum of understanding with ESMA

The Luxembourg financial sector supervisory authority, the Commission de Surveillance du Secteur Financier (CSSF), has signed a multilateral memorandum of understanding (MMoU) which provides a legal framework for cooperation arrangements and information exchange among competent authorities and ESMA.

The MMoU updates and replaces the existing CESR MMoU. The update was necessary in order to take into account developments in European law and to incorporate other cooperation procedures that have been agreed between competent authorities with the assistance of ESMA. The new MMoU is intended to cover all competent authorities of the EU, the EEA, the EFTA and ESMA.

The MMoU will enter into force on 27 May 2014.

DNB imposes systemic risk buffer requirement on Dutch systemic banks

The Dutch Central Bank (DNB) has announced that it intends to impose a systemic risk capital buffer requirement on the four systemic banks in the Netherlands. The new buffer requirement, to be phased in between 2016 and 2019, is based on the European Capital Requirements Directive (2013/36/EU or CRD 4). In the context of systemic buffer requirements, CRD 4 distinguishes between the buffer requirement for systemically important institutions and the systemic risk buffer, with the higher of the two being the applicable buffer. The buffer requirement for systemically important institutions has already been implemented in Dutch legislation, while the systemic risk buffer is included in the draft Act implementing CRD 4, which is expected to enter into force mid-2014 upon adoption by the Upper House of Parliament. The new systemic risk buffer requirement, which will be between 1-3% of risk weighted assets, relates to risks resulting from non-cyclical long-term system risks or non-cyclical macro-prudential long-term risks.

The DNB has launched a public consultation on a new supervisory regulation concerning the systemic risk buffer. The consultation period ends on 1 June 2014.

The DNB has commented that systemic buffers increase the resilience of systemic banks, thereby reducing the risk of such banks failing, and that it has developed, in line with international agreements, a method to identify systemic banks. To determine which banks are systemically important, and which additional buffer requirement will apply to these banks, the DNB assesses banks against a number of criteria. These criteria include the size of a bank relative to Dutch gross domestic product (GDP), a bank's interconnectedness with other financial institutions and the substitutability of certain crucial functions performed by a bank. This is elaborated in a DNBulletin entitled 'Additional buffer requirement enhances resilience of Dutch systemic banks'.

SAFE issues pilot rules on multi-national companies' foreign exchange cash pooling

The State Administration of Foreign Exchange (SAFE) has issued the 'Pilot Rules on Foreign Currency Cash Pooling of Multi-national Companies', which are intended to facilitate the cross-border treasury management of multi-national companies.

Under the pilot rules, multi-national companies (MNCs) may apply to open a domestic foreign exchange master account (Domestic FX Master Account) to pool foreign currency positions from onshore participating group members under both current account and capital account, and an international foreign exchange master account (International FX Master Account) to pool positions from offshore participating group members. Funds can be freely transferred between the International FX Master Account and offshore accounts. Movement of funds from the International FX Master Account to the Domestic FX Master Account and the other way around are subject to an aggregate foreign debt quota and outbound lending quota respectively.

An eligible MNC must meet certain requirements including:

- having more than USD 100 million of foreign currency receipt/payment in the preceding year;
- sufficient internal systems to operate cash pooling;
- no material violation against the SAFE regulations in the last three years; and
- onshore participating companies are 'Category A' enterprises under foreign exchange administration regime of trade of goods.

The MNC should also develop a business plan with its account bank in advance for SAFE's deliberation.

SAFE will take a 'negative list' approach to regulating the foreign currency conversion of pooled capital funds and foreign debts, which means foreign currencies can be converted into RMB and transferred to special RMB deposit accounts first, and then be paid out after the bank's confirmation of lawful use and authenticity.

The Domestic FX Master Account can be used for processing all participating companies' cross-border payment and receipts under current account transactions on a netting basis, subject to reporting obligations to SAFE.

The pilot rules will take effect as of 1 June 2014.

Shenzhen Stock Exchange updates trading rules for QFIIs and RQFIIs

The Shenzhen Stock Exchange (SZSE) has issued the 'Implementing Rules on Securities Trading of Qualified Foreign Institutional Investors and Renminbi Qualified Foreign Institutional Investors on the Shenzhen Stock Exchange'. The rules, which became effective immediately, supersede all the previous trading rules applicable to Qualified Foreign Institutional Investors (QFIIs) issued by SZSE and apply to the Renminbi Qualified Foreign Institutional Investors (RQFIIs) as well.

Amongst other things, the rules include the following changes:

- the alert shareholding threshold for all QFIIs and RQFIIs in a single listed company has been raised to 26% (from 16%), which is consistent with the relevant change on foreign ownership limit under the relevant QFII and RQFII rules issued by the China Securities Regulatory Commission;
- the rules further specify the permissible securities that a QFII or RQFII may invest on the SZSE, which include certainly newly-introduced products such as preferred stocks, policy financial bonds, asset-backed securities, when-issued treasury bonds, etc.;
- for the disclosure of interest by any QFII, RQFII or its underlying investor, it should aggregate both onshore and offshore listed shares of a listed company held by it;
- where a QFII or RQFII opens multiple securities accounts on the SZSE for securities trading, each account has to be opened via a separate securities company; and
- to the extent SZSE spots any unusual trading activity, the SZSE is entitled to order a QFII or RQFII to report the securities transactions and positions of its underlying investors on a timely basis.

The rules are substantially consistent with the 'Implementing Rules on Securities Trading of Qualified Foreign Institutional Investors and Renminbi Qualified Foreign Institutional Investors on the Shanghai Stock Exchange' issued by the Shanghai Stock Exchange in March 2014.

Shanghai Stock Exchange consults on implementing rules for Shanghai-Hong Kong Stock Connect

Further to the policy announcement of the Shanghai-Hong Kong Stock Connect scheme, the Shanghai Stock Exchange (SSE) has issued a consultation draft of the 'Implementing Rules for the Shanghai-Hong Kong Stock Connect Pilot Scheme' for public comment. Besides setting out the rules on the operational level for the Shanghai-Hong Kong Stock Connect, the consultation draft sets out the following proposed rules:

- for Hong Kong investors trading A-shares on SSE (i.e. the Northbound Trade Link), SSE's current trading rules should be complied with – however, block trading, market price order, securities lending and margin trading or short selling is not allowed;
- for an investor with an SSE account trading shares on the Stock Exchange of Hong Kong (i.e. the Southbound Trade Link), the investor must appoint one securities house as the sole broker and deposit the cash with a third party custodian bank – similarly, brokers may not provide securities lending and margin trading services in this regard and no short selling is allowed;
- under either the Northbound or Southbound Trade Links, if the daily trading quota is fully used, buy orders will be rejected until the next trading day, while sell orders will not be affected – if the outstanding amount of total quota at the end of a trading day is less than the daily trading quota, buy orders will be rejected on the next trading day (while sell orders will not be affected) until the outstanding amount of total quota recovers to be more than the daily trading quota;
- under the Northbound Trade Link, investors are subject to the foreign shareholding limits, information disclosure requirements and relevant disposal requirements where the holding limit is breached which are applicable to qualified foreign institutional investors (QFIIs) and Renminbi qualified foreign institutional investors (RQFIIs); and
- SSE reserves the right to adopt emergency measures to deal with abnormal trading conditions.

The consultation period will end on 16 May 2014.

HKMA issues circular on implementation of new large exposures framework for banks

The Hong Kong Monetary Authority (HKMA) has issued a circular to all locally incorporated authorised institutions on the implementation of the new supervisory framework for measuring and controlling large exposures of banks. The new framework, issued by the Basel Committee on Banking Supervision (BCBS) on 15 April 2014, is scheduled to take effect from 1 January 2019 and it will supersede the BCBS large exposures guidance from 1991 which forms the basis `of the current large exposures rules in many jurisdictions, including Hong Kong.

The new large exposure standard includes a general limit applied to all of a bank's exposures to a single counterparty, which is set at 25% of a bank's Tier 1 capital. This limit also applies to a bank's exposure to identified groups of connected counterparties (i.e. counterparties that are interdependent and likely to fail simultaneously). A tighter limit, set at 15% of Tier 1 capital, will apply to exposures between banks that have been designated as global systemically important banks (G-SIBs).

The HKMA intends to implement the new standard in accordance with the BCBS timetable and will consult the industry on its implementation proposals for Hong Kong in due course. In the meantime, the HKMA has recommended that authorised institutions familiarise themselves with the new framework and carefully consider the implications on their business activities.

APRA proposes simplified prudential framework for securitisation

The Australian Prudential Regulation Authority (APRA) has released for consultation a discussion paper on its proposals to simplify the prudential framework for securitisation for authorised deposit-taking institutions (ADIs). In APRA's view, the prudential framework for securitisation needs to be clear and simple for stakeholders to understand. APRA's proposed approach to securitisation includes the following features:

- a set of key principles that apply to securitisation, rather than an expanded set of prudential requirements;
- a simple two credit class structure, which reduces the likelihood of opaque risk transfer and enhances benefits for system stability;
- explicit recognition of funding-only securitisation, with a simple but robust prudential regime that also allows for revolving securitisations or master trusts;
- simpler requirements for capital relief, matching risk to the amount of regulatory capital held;
- better integration of securitisation with the ADI liquidity regime; and
- clarification of the treatment of warehouses and similar structures.

APRA's proposed reform of the prudential framework for securitisation is intended to assist in the further recovery of this market in Australia.

APRA has invited written submissions on the proposals by 31 July 2014. Thereafter, APRA intends to release a second consultation package in 2015 that will include APRA's response to submissions as well as a draft prudential standard, prudential practice guide and associated reporting requirements.

Australia and US sign FATCA intergovernmental agreement

The Australian Treasury has, on behalf of the Australian government, signed an intergovernmental agreement (IGA) with the government of the United States. The IGA is intended to improve international tax compliance and implement the Foreign Account Tax Compliance Act (FATCA) as well as reduce the burden on Australian financial institutions in complying with FATCA.

FATCA was enacted by the US Congress in March 2010 as an information-reporting regime to detect US taxpayers who use accounts with offshore financial institutions to conceal income from the US Internal Revenue Service (IRS). FATCA will commence on 1 July 2014 and will affect a large part of the Australian financial services sector.

The Australian government has developed draft legislation to give effect to Australia's obligations under the IGA.

With effect from 1 July 2014, the amendments will require Australian financial institutions to collect information about their customers who are likely to be taxpayers in the US and to provide that information to the Commissioner of Taxation, who will in turn provide that information to the IRS.

The draft legislation together with the explanatory memorandum is subject to public consultation and submissions are due to close on 9 May 2014 before legislation is enacted.

RECENT CLIFFORD CHANCE BRIEFINGS

Legal regime of the depositaries under UCITS V

On 15 April 2014, the EU Parliament in a plenary session gave its final approval to the UCITS V Directive. Once it enters into force, Member States will have 18 months to transpose it into national law; however, depositories will have a longer transition period – 42 months – to comply with the requirements.

UCITS V focuses mainly on three areas: the legal regime of the depositaries, the sanctions regime and lastly, the remuneration policy of management companies.

This briefing discusses the impact of the new directive on depositories.

http://www.cliffordchance.com/content/cliffordchance/briefings/2014/04/legal_regime_of_thedepositariesunderucitsv.html

Remuneration policy of management companies under UCITS V

This briefing discusses the new remuneration policy of management companies under UCITS V.

http://www.cliffordchance.com/briefings/2014/04/remuneration_policyofmanagementcompaniesunde.html

European Court throws out the UK's challenge to the FTT

The European Court has rejected the UK's legal challenge to the proposed EU financial transaction tax on procedural grounds. A substantive challenge may follow if the FTT's proponents proceed with the more ambitious proposals currently on the table. In our view such a substantive challenge would likely succeed.

This briefing discusses the Court's decision and what happens next.

http://www.cliffordchance.com/briefings/2014/04/european_court_throwsouttheukschallengetotheftt.html

Belgium and US sign FATCA Intergovernmental Agreement

On 23 April 2014, the Belgian and US governments signed an Intergovernmental Agreement (IGA) intended to implement the Foreign Account Tax Compliance Act (FATCA) in Belgium.

This briefing discusses the signature of the IGA.

http://www.cliffordchance.com/content/cliffordchance/briefings/2014/04/belgium_and_us_signfatcaintergovernmenta.html

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