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Governance, Regulation & Compliance

Regulatory Radar

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Newsletter on banking and financial regulation

In this issue

In March the European Commission published its Green paper on Shadow Banking. Shadow banking is the system of credit intermediation that involves entities and activities that are outside the regular banking system, and thus are not regulated like banks. The Green Paper sets out how EU measures already address some shadow banking activities and what still needs to be done given the evolving nature of the shadow banking system.

Several important draft reports from the Committee on Economic and Monetary Affairs were also published in March i.e. the draft reports on the proposals for EMIR, MiFID II and MiFIR and MAD II. The rapporteurs identify a number of key issues and suggest important changes to the draft texts.

In the area of investment management, ESMA issued its final Guidelines on risk measurement and the calculation of global exposure for certain types of structured UCITS as well as a Discussion Paper, entitled "An overview of the Proxy Advisory Industry. Considerations on Possible Policy Options". The aim of the Discussion Paper is to give an overview of ESMA's understanding of the functioning of the proxy advisory industry in Europe and to gain evidence on the extent to which market failures may exist in practice that are related to the activities of proxy advisors in Europe.

With regard to tax, the European Commission published a report on the results of the European Savings Taxation Directive. The report covers the period 2005-2010 and provides for practical suggestions to make the current system even more transparent in the future. It also identifies a number of loopholes in the current Savings Tax Directive.

On a Belgian level the Royal Decree of 12 March 2012 approving the Regulation of the FSMA on the approval of compliance officers was published in the Official Journal. The Regulation introduces a mandatory approval process in order to ensure that compliance officers have the required knowledge, experience and training with regard to conduct of business rules.

We hope you enjoy the reading.

The Editorial Board.

Normative documents

Official Journal of Belgium (BS/MB)

On 26 March, the Royal Decree of 12 March 2012 approving the Regulation of the Financial Services and Markets Authority on the approval of compliance officers was published in the Official Journal. In order to ensure that compliance officers have the required knowledge, experience and training with regard to conduct of business rules, the Regulation introduces a mandatory approval process. Anyone wishing to obtain the FSMA's approval as a compliance officer must fulfill the following requirements:

- Have a Master's degree or equivalent experience;
- Pass an exam that tests their knowledge of conduct of business rules;
- Be fit and proper;
- Be covered by a legal protection insurance policy.

In addition to the above, the Regulation also requires approved compliance officers to participate regularly in continuing education.

Mandatory approval is only required for heads of the compliance function within a financial institution, who report directly to the institution's senior management. Compliance officers who already held the position before 1 April 2011 do not need to pass an exam, but they must meet the other criteria for approval.

Official Journal of the European Union (OJ)

AML/CFT and sanctions

In March, the following documents related to AML/CTF and sanctions measures were published in the Official Journal:

- Commission Implementing Regulation (EU) No 177/2012 of 1 March 2012 amending for the 165th time Council Regulation (EC) No 881/2002 imposing certain specific restrictive measures directed against certain persons and entities associated with the Al-Qaida network in OJ L 61 of 2 March;
- Council Implementing Regulation (EU) No 193/2012 of 8 March 2012 implementing Regulation (EC) No 560/2005 imposing certain specific restrictive measures directed against certain persons and entities in view of the situation in Côte d'Ivoire in OJ L 71 of 9 March;
- Council Implementing Decision 2012/144/CFSP of 8 March 2012 implementing Decision 2010/656/CFSP renewing the restrictive measures against Côte d'Ivoire in OJ L 71 of 9 March;

- Council Implementing Regulation (EU) No 213/2012 of 13 March 2012 amending Implementing Regulation (EU) No 1375/2011 implementing Article 2(3) of Regulation (EC) No 2580/2001 on specific restrictive measures directed against certain persons and entities with a view to combating terrorism in OJ L 74 of 14 March;
- Commission Implementing Regulation (EU) No 215/2012 of 13 March 2012 amending for the 166th time Council Regulation (EC) No 881/2002 imposing certain specific restrictive measures directed against certain persons and entities associated with the Al Qaida network in OJ L 74 of 14 March 2012;
- Council Decision 2012/149/CFSP of 13 March 2012 amending Decision 2010/638/CFSP concerning restrictive measures against the Republic of Guinea in OJ L 74 of 14 March;
- Council Decision 2012/150/CFSP of 13 March 2012 amending Decision 2011/872/CFSP updating the list of persons, groups and entities subject to Articles 2, 3 and 4 of Common Position 2001/931/CFSP on the application of specific measures to combat terrorism in OJ L 74 of 14 March;
- Council Decision 2012/152/CFSP of 15 March 2012 amending Decision 2010/413/CFSP concerning restrictive measures against Iran in OJ L 77 of 16 March;
- Council Decision 2012/158/CFSP of 19 March 2012 amending Decision 2011/173/CFSP concerning restrictive measures in view of the situation in Bosnia and Herzegovina in OJ L 80 of 20 March;
- Council Decision 2012/159/CFSP of 19 March 2012 amending Decision 2011/172/CFSP concerning restrictive measures directed against certain persons, entities and bodies in view of the situation in Egypt in OJ L 80 of 20 March;
- Commission Implementing Regulation (EU) No 253/2012 of 22 March 2012 amending for the 167th time Council Regulation (EC) No 881/2002 imposing certain specific restrictive measures directed against certain persons and entities associated with the Al Qaida network in OJ L 84 of 23 March;
- Council Implementing Regulation (EU) No 263/2012 of 23 March 2012 implementing Article 11(1) of Regulation (EU) No 753/2011 concerning restrictive measures directed against certain individuals, groups, undertakings and entities in view of the situation in Afghanistan in OJ L 87 of 24 March;
- Council Regulation (EU) No 264/2012 of 23 March 2012 amending Regulation (EU) No 359/2011 concerning restrictive measures directed against certain persons, entities and bodies in view of the situation in Iran in OJ L 87 of 24 March;
- Council Implementing Regulation (EU) No 265/2012 of 23 March 2012 implementing Article 8a(1) of Regulation (EC) No 765/2006 concerning restrictive measures in respect of Belarus in OJ L 87 of 24 March;
- Council Implementing Regulation (EU) No 266/2012

of 23 March 2012 implementing Article 32(1) of Regulation (EU) No 36/2012 concerning restrictive measures in view of the situation in Syria in OJ L 87 of 24 March;

- Council Implementing Decision 2012/167/CFSP of 23 March 2012 implementing Decision 2011/486/CFSP concerning restrictive measures directed against certain individuals, groups, undertakings and entities in view of the situation in Afghanistan in OJ L 87 of 24 March;
- Council Decision 2012/168/CFSP of 23 March 2012 amending Decision 2011/235/CFSP concerning restrictive measures directed against certain persons and entities in view of the situation in Iran in OJ L 87 of 24 March;
- Council Decision 2012/169/CFSP of 23 March 2012 amending Decision 2010/413/CFSP concerning restrictive measures directed against Iran in OJ L 87 of 24 March;
- Council Decision 2012/170/CFSP of 23 March 2012 amending Decision 2010/573/CFSP concerning restrictive measures against the leadership of the Transnistrian region of the Republic of Moldova in OJ L 87 of 24 March;
- Council Implementing Decision 2012/171/CFSP of 23 March 2012 implementing Decision 2010/639/CFSP concerning restrictive measures against Belarus in OJ L 87 of 24 March.
- Council Implementing Decision 2012/172/CFSP of 23 March 2012 implementing Decision 2011/782/CFSP concerning restrictive measures against Syria in OJ L 87 of 24 March;
- Council Regulation (EU) No 267/2012 of 23 March 2012 concerning restrictive measures against Iran and repealing Regulation (EU) No 961/2010 in OJ L 88 of 24 March.

Technical and business requirements for credit transfers and direct debits in euro

On 30 March, the Regulation (EU) No 260/2012 of the European Parliament and of the Council of 14 March 2012 establishing technical and business requirements for credit transfers and direct debits in euro and amending Regulation (EC) No 924/2009 was published in OJ L 94. The Regulation lays down rules for credit transfer and direct debit transactions denominated in euro within the EU where both the payer's payment service provider and the payee's payment service provider are located in the Union, or where the sole payment service provider (PSP) involved in the payment transaction is located in the EU.

Financial Services and Markets Authorities (FSMA)

Periodic financial statements

On 29 March, the FSMA published Circular FSMA_2012_05 on the periodic financial statements of management companies of undertakings for collective investment and of

portfolio management and investment advice companies (in ➲Dutch and in ➲French). The Circular supersedes Circular CBFA_2010_10 and includes the following changes to the reporting tables:

- A new table, table 14 "activities", is added. This table should contain an overview of:
  - per type of client, the assets under management and assets related to the reception and transmission of orders
  - the total number of clients per activity
- Table 13 "provisions" is modified to align section "a. Fees for management services" with section "b. Fees for advisory services"
- Table 11 "written options" is removed as it is not relevant for UCI management companies and portfolio management and investment advice companies
- Table 9 "investment portfolio" is removed to avoid overlap with tables 5 and 7
- In table 5 "Notes and other fixed income instruments" a line is added for the market value of unlisted securities.

The new tables will come into force on 30 June 2012. As of then it will also no longer be required to download the file "reporting on assets under management" via eCorporate every three months as the information will be covered by table 14 "activities". Furthermore, the FSMA indicates that the Circular will be supplemented by a Regulation in the near future.

Consultative or informative documents

Eurofinas

Data protection

On 16 February, Eurofinas published ➲its comments on the ➲European Commission's proposal for a Regulation of the European Parliament and of the Council on the protection of individuals with regard to the processing of personal data and on the free movement of such data.

European Central Bank (ECB)

Oversight expectations for links between retail payment systems

On 23 March, the ECB published ➲its draft Oversight expectations for links between retail payment systems.

As part of its oversight function, the Eurosystem established the "Oversight standards for euro retail payment systems" in 2003. However the Eurosystem has recognized that these standards have not been designed to adequately cover the additional risks associated with links between retail payment systems (RPS). It has therefore established a harmonized single set of expectations for RPSs to comply with, specifically for risks that may arise

when one RPS establishes a link with another. The national central banks (NCBs) responsible will, as part of their respective oversight functions, assess the compliance of an RPS for any links it may have. The goal is to ensure that the risks stemming from the establishment of links between RPSs are properly managed. The expectations cover risks related to legal, financial and operational arrangements, as well as issues related to governance, access and efficiency. With a view towards ensuring consistency in the implementation of expectations, the Eurosystem will draw up a single methodology to be applied by the NCBs.

Comments on the draft Oversight expectations can be submitted until 18 May.

Composite indicator of systemic stress

On 12 March, the ECB published ➲a working paper, entitled "CISS - a composite indicator of systemic stress in the financial system". The paper introduces a new indicator of contemporaneous stress in the financial system named Composite Indicator of Systemic Stress (CISS). Its specific statistical design is shaped according to standard definitions of systemic risk. The main methodological innovation of the CISS is the application of basic portfolio theory to the aggregation of five market-specific sub-indices created from a total of 15 individual financial stress measures. The aggregation accordingly takes into account the time-varying cross-correlations between the sub-indices. As a result, the CISS puts relatively more weight on situations in which stress prevails in several market segments at the same time, capturing the idea that financial stress is more systemic and thus more dangerous for the economy as a whole if financial instability spreads more widely across the whole financial system. Applied to euro area data, the paper determines within a threshold VAR model a systemic crisis-level of the CISS at which financial stress tends to depress real economic activity.

European Commission

Credit rating agencies

On 21 March, the European Commission endorsed the following technical standards:

- ➲ regulatory technical standards on information for registration and certification of credit rating agencies. The Regulation lays down the rules which determine the information to be provided to ESMA by a credit rating agency in its application for registration, or certification and for the assessment of its systemic importance to the financial stability or integrity of financial markets.
- ➲ regulatory technical standards for the presentation of the information that credit rating agencies shall make available in a central repository established by the European Securities and Markets Authority.
- ➲ regulatory technical standards on the content and format of ratings data periodic reporting to be submitted to the European Securities and Markets

Authority by credit rating agencies. The regulation sets out the structure, format, method and period of reporting of Credit Rating Agencies to ESMA's central repository (CEREP).

Freezing and confiscation of crime proceeds

On 12 March, the European Commission published a ➲proposal for a Directive of the European Parliament and of the Council on the freezing and confiscation of proceeds of crime in the European Union. The Proposal aims to simplify existing rules and fill gaps which have benefitted criminals until now. It will, in particular:

- Lay down clearer and more efficient rules on the confiscation of assets which are not directly linked to a specific crime, but which clearly result from similar criminal activities committed by the convicted person (extended confiscation).
- Strengthen rules on confiscation where assets have been transferred from the suspect to a third party who should have realised that they were illegal or the fact that they were transferred in order to avoid confiscation (third-party confiscation).
- Allow confiscation of criminal assets where a criminal conviction is not possible because the suspect is deceased, permanently ill or has fled (limited non-conviction based confiscation).
- Ensure that competent authorities, such as prosecutors, can temporarily freeze assets that risk disappearing if no action is taken, subject to confirmation by a court as soon as possible (precautionary freezing).
- Allow financial investigations on a person's assets to be continued for years after a criminal conviction in order to fully execute a previously issued confiscation order (effective execution).
- Require Member States to manage frozen or confiscated assets so that they do not lose economic value (asset management).
- Require Member States to regularly collect data on confiscation and asset recovery (statistics).

The Proposal was accompanied by ➲a memo outlining the background and key aspects of the Proposal.

European Securities and Markets Authority (ESMA)

Joint Committee medium term strategy

On 23 March, ESMA published a ➲note setting out the Medium term strategy for the Joint Committee (consisting of ESMA, EIOPA and EBA).
The note sets out following areas where the Joint Committee will strive to deliver over the medium term:

1. Risk Assessment: Drafting of policy focused risk reports for the Economic and Financial Committee–Financial Stability Committee meetings in March and September each calendar year. These reports shall include preliminary policy conclusions, and provide a cross sectoral assessment which shall be fed into

each of the ESAs sector systemic risk assessment work;

2. Regulatory work: Developing Technical Standards and Guidelines in relation to legislative proposals which have cross sectoral ramifications, such as for the Financial Conglomerates Directive (FICOD), European Markets Infrastructure Regulation (EMIR), Third Money Laundering Directive, and the proposed Audit Regulation. The Joint Committee shall also prepare responses to request for Calls for Advice, and/or provide input to the European Commission in relation to its forthcoming reviews of legislation, which have cross sectoral ramifications, such as for the FICOD, the Third Money Laundering Directive, the Payment Services Directive and the 2nd E-money Directive.
3. Consumer Protection:
    a. Developing by 2014, some high level principles to be applied by Member States' Competent Authorities requiring the boards of financial institutions ensure that due consideration and analysis of the risks to consumers is performed, before a new financial product is launched;
    b. Considering appropriate cross sector consistent measures in light of the EC's legislative proposals on Packaged Retail Investment Products (PRIPs) due to be published in 2012 The Joint Committee shall also undertake further consideration of any cross sectoral issues relating to PRIPs stemming from developments in relation to the Markets in Financial Instruments Directive (MiFID) and the Insurance Mediation Directive (IMD), where appropriate.
4. Supervisory Practice:
    a. Developing guidelines aimed at the convergence of supervisory practices with regard to Mixed Financial Holding Companies, 3rd Country Equivalence, and supervisory coordination arrangements under the FICOD;
    b. Assessing AML supervisory practices and risk based approaches, with a view to producing an AML supervisory tool kit so as to promote common supervisory approaches and practice;
    c. Ensure cross sector exchange of views on a regular basis in order to promote consistent IFRS application.

The note was accompanied by an ➲overview of the Work Programme 2012 deliverables.

Credit rating agencies

On 22 March, ESMA published its first ➲Report on the Supervision of Credit Rating Agencies. This report provides an overview of ESMA's supervisory activity on Credit Rating Agencies (CRAs) registered in the European Union and summarizes the results of ESMA's first examination of the

three groups of registered CRAs (Fitch Ratings, Moody's Investors Services, and Standard & Poor's Rating Services). ESMA's main remarks and observations relate to the following topics:

- Internal processes: Certain parts of CRAs' internal processes (i.e. Rating Committees and other key internal meetings) were not sufficiently recorded. Some core elements of the rating process do not appear to be appropriately or systematically recorded. Furthermore, Rating Committees attendees were sometimes given insufficient time to analyse the documentation which would be discussed in the meetings.
- Analytical Resources: A high staff turnover in one or more CRAs, notably in specific lines of business was noted. According to ESMA the quality of the output of the credit rating activity, could be undermined both by the limited number of resources and by the fact that new employees need time to acquire the proper knowledge of the CRAs internal process and of the peculiarities of specific asset classes.;
- Governance and control functions: One or more CRAs need to improve the role and tasks of the internal control functions and the Independent Directors, to enhance the effectiveness of their activities;
- Disclosure of methodologies and presentation of ratings: One or more CRAs disclose the methodologies underlying credit rating decisions for some other products in multiple documents, published in different periods and not easily identifiable on the CRAs web pages. This could prevent the user of the credit ratings from a clear understanding of the rationale of the relevant methodology and the key rating assumptions underlying the credit ratings. Moreover, ESMA found that the methodologies published by one or more CRAs on the rating categories in the selected sample, not always provide a clear and exhaustive overview of the criteria. and models used and how these criteria contribute to the eventual rating decision.
- IT systems: One or more CRAs are currently facing a number of challenges with respect their IT infrastructure such as the transition to new systems, integration of systems and replacement of old systems. Additionally, ESAM noted that the use of companies' web sites as the main vehicles for the dissemination of ratings and the provision of other services has greatly increased the critical nature of such means.

Endorsement credit ratings issued in the US, Canada, Hong Kong and Singapore

In a ➲press release of 15 March, ESMA announced that it considers the regulatory frameworks for credit rating agencies (CRAs) of the United States of America, Canada, Hong Kong and Singapore to be in line with European rules. This allows European financial institutions to continue using for regulatory purposes credit ratings issued in these

countries after 30 April 2012. The equivalence decision also allows EU CRAs to endorse the ratings issued by CRAs that are registered or licensed and are subject to supervision in those countries.

Financial Action Task Force (FATF)

National cooperation and coordination

On 7 March, the FATF published a ➲Best Practices Paper on FATFRecommendation 2: Sharing among domestic competent authorities information related to the financing of proliferation.

Financial Law Institute

Takeover Directive

On 23 March, the Financial Law Institute published ➲a working paper, entitled "A New Look at the Debate about the Takeover Directive". With a view of the projected revision of the takeover directive, the paper calls attention to some items that would usefully be revised. Attention is drawn to the mandatory bid rule, the scope of which should restricted to share acquisitions and not apply to other control changes, while company law in general should strictly regulate conflicted transactions, thereby eliminating control premia, and hence the need to proceed to a mandatory bid. Multistate takeover should be reregulated, taking into account the new supervisory structure, esp. ESMA. Also some of the blanks should be filled e.g. on squeeze outs, sell outs, and other specific requirements like "acting in concert". As to the most controversial item of defensive techniques, a fundamental revision seems unlikely, but one could be considered to allow these techniques, but subject their effectiveness to a qualified vote in the general meeting, the shareholders voting according to the rules applicable before the bid.

Financial Stability Board (FSB)

Financial Institution Risk Disclosures

In a ➲press release of 20 March, the FSB announced that it is taking the following steps to improve risk disclosures by financial institutions:

- Facilitate the formation of a task force to develop principles for improved disclosures based on current market conditions and risks, including ways to enhance the comparability of disclosures: The task force will involve investors, financial institutions, and external auditors and will be requested to develop proposed principles later this year for implementation in connection with end-year 2012 annual reports;
- Encourage the task force to have dialogue with international standard-setting bodies at key stages as it develops its recommendations and to report to

the FSB.

- identify leading practice risk disclosures presented in annual reports for end-year 2011 based on broad risk areas such as those identified in the summary of the roundtable. The task force would be asked to report on these leading practice disclosures to the FSB in 2012;
- Consider holding another international roundtable in late 2012 to facilitate further discussion by investors, financial institutions, auditors, standard setters, regulators and supervisors on market conditions and risks at that time and the progress toward improving the transparency of risks and risk management through relevant disclosures.

Contribution of external audit to financial stability

In a ➲press release of 15 March, the FSB indicated that further work should be conducted in the following areas to improve the role that external audits play in providing information to prudential supervisors and regulators of financial institutions, and to reinforce the effectiveness of the regulation of external audits:

- Improving the information that external audits provide to prudential supervisors and regulators of financial institutions, including systemically important financial institutions (SIFIs).
- Reinforcing the effectiveness of audit regulation, particularly for external audits of financial institutions, to improve audit quality:
    - The FSB is requesting the International Forum of Independent Audit Regulators (IFIAR) to report on (i) challenges and problems that its members have identified in their inspection programmes relating to external audits of financial institutions, including audits of SIFIs; (ii) responses by IFIAR members to those issues, including follow-up with external audit firms; and (iii) member recommendations concerning steps that could be taken by audit regulators and auditors to further strengthen external audits of financial institutions.
    - The FSB encourages the continued efforts of the International Audit and Assurance Standards Board (IAASB), internationally, and other audit standard setters in their national contexts to improve the standards on information that external audits provide to investors and other financial report users. The approaches set forth in various consultative documents differ across jurisdictions, and it will be important to seek high quality standards that enhance audit practices, and to the extent possible, improved international consistency. IOSCO has agreed to monitor developments in this area and provide updates to the FSB on progress.
    - The FSB will ask IOSCO to report to the FSB on authorities' experiences with the

considerations in IOSCO's 2008 report on audit contingency planning.
- The FSB will ask FSB members and other key bodies such as the IAASB, to provide input to the World Bank's review of how to enhance its Accounting and Auditing Reports on Standards and Codes (ROSCs).

Legal Entity Identifiers

On 7 March, the FSB published a ➲Notice on Technical Features of the Legal Entity Identifier (LEI). In the notice, the Board provides an update with respect to the LEI initiative. It indicates that the FSB LEI Expert Group has made significant progress in identifying the key issues and developing framework solutions to be presented in the report to the FSB Plenary, to enable the Board to meet the G-20 mandate provided at the Cannes Summit. Work is proceeding intensively under five workstreams: 1) governance, 2) operational model, 3) scope, confidentiality and access; 4) funding; and 5) implementation and phasing. The FSB also provides provide early clarity on two technical points, namely the format of the global LEI code and the minimum set of reference data.

Insurance Europe

Supervision of Financial Conglomerates

On 20 March, Insurance Europe published ➲its comments and ➲the comments of the International Network of Insurance Associations on ➲consultative paper on "Principles for the supervision of financial conglomerates".

Organization for Economic Co-operation and Development (OECD)

Financial Literacy

On 15 March, the OECD published ➲a working paper, entitled "Measuring Financial Literacy: Results of the OECD/International Network on Financial Education (INFE) Pilot Study".
This paper presents the findings from an OECD International Network on Financial Education pilot study undertaken in 14 countries. The analysis focuses on variations in financial knowledge, behaviour and attitude across countries and within countries by socio-demographics. The results highlight reasons for concern. It appears that most people have some very basic financial knowledge, but understanding of other, everyday financial concepts such as compound interest and diversification is lacking amongst sizeable proportions of the population in every country. There is also some indication that certain respondents are over-confident, in that they have given incorrect responses rather than admitting that they do not know the answer. Furthermore, some countries need to work particularly hard to ensure that women are not left

behind. Analysis of the relationship between financial behaviour and knowledge suggests a positive association in every country: when knowledge increases so does behaviour. This does not prove causation, and much more research is needed to understand the relationship between these variables.
In the working paper is also indicated that inequality in opportunities may be preventing individuals from being more financially literate.

Credit institutions and investment firms

Normative documents

Official Journal of Belgium (BS/MB)

Capital Requirements

On 27 March, the Royal Decree of 19 March 2012 approving the Regulation of the National Bank of Belgium on own funds of credit institutions and investment firms was published in the Official Journal (➲in Dutch and ➲in French). This Regulation transposes the capital requirements set out in Directive 2010/76/EU of the European Parliament and of the Council of 24 November 2010 amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-securitizations, and the supervisory review of remuneration policies into Belgian law.

Consultative or informative documents

European Association of Public Banks (EAPB)

Internal audit function

On 2 March, the EAPB published ➲its comments on the ➲Basel Committee's consultation on banks' internal audit function.

European Banking Federation (EBF)

Supervisory reporting requirements

On 26 March, the EBF published ➲its comments on ➲EBA's consultation paper on draft Implementing Technical Standards (ITS) on supervisory reporting requirements for institutions.

European Central Bank (ECB)

Classification system between the reporting frameworks of the ECB and the EBA

In a ➲press release of 23 March, the ECB together with EBA announced the publication of the second version of the classification system between their respective reporting frameworks. The first version of the classification system was published in February 2010. This second edition includes further enhancements and updates a series of reconciliation proposals which are in the process of being implemented.

The effect of the monetary policy on bank risk

On 15 March, the ECB published ➲a working paper, entitled "Do bank characteristics influence the effect of monetary policy on bank risk?". Unusually low levels of short-term interest rates have often been named as one of the factors contributing to risk-taking by banks. The link between low interest rates and banks' risk-taking, points to a different dimension of the monetary transmission mechanism, the so-called risk-taking channel. This channel may operate in at least two ways. First, low interest rates impact valuations, incomes and cash flows, which in turn can modify how banks measure estimated risks. Second, low returns on investments, such as government securities, coupled with the lower cost of obtaining new debt for borrowers may increase incentives for investors (including banks) and borrowers to take on more risks. If banks' incentives are at the centre of the workings of the risk-taking channel, it would be expected that individual bank characteristics would have a major impact on how the risk-taking channel operates. As such the working paper analyzes whether the impact of monetary policy on bank risk depends upon bank characteristics. It relates the materialization of bank risk during the financial crisis to differences in the monetary policy stance and bank characteristics in the pre-crisis period for a large sample of listed banks operating in the European Union and the United States. For each country, a measure of monetary policy looseness is constructed, which is interacted with certain bank characteristics (o.a. liquidity, capital, market value, securitization intensity, traditional lending activity). These interactions show whether bank specific characteristics lead to heterogeneity in bank risk related to monetary policy. It is found that banks that were well-capitalized and highly liquid prior to the crisis suffered a lower level of erosion of their solvency during the 2007-2009 financial crisis. However, the insulation effects produced by capital and liquidity buffers were lower in those countries that, prior to the crisis, experienced a particularly prolonged period of low interest rates.

European Commission

Shadow banking

On 19 March, the European Commission published a

➲Green Paper on Shadow Banking. Shadow banking is the system of credit intermediation that involves entities and activities that are outside the regular banking system, and thus are not regulated like banks. Possible shadow banking entities and activities include:

- Special purpose entities which perform liquidity and/or maturity transformation
- Money Market Funds (MMFs) and other types of investment funds or products with deposit-like characteristics
- Investment funds, including Exchange Traded Funds (ETFs), that provide credit or are leveraged;
- Finance companies and securities entities providing credit or credit guarantees, or performing liquidity and/or maturity transformation without being regulated like a bank;
- Insurance and reinsurance undertakings which issue or guarantee credit products;
- Securitisation and securities lending and repurchase agreement (repo) transactions.

The Green Paper sets out how EU measures already address some shadow banking activities and what still needs to be done given the evolving nature of the shadow banking system. In this context, there are five key areas where the Commission is further investigating options and next steps, namely:

- Banking regulation:
    1. Consolidation rules for shadow banking entities are being examined to ensure that bank-sponsored entities are appropriately consolidated for prudential purposes and therefore fully subject to the comprehensive Basel III framework;
    2. As regards bank exposure to shadow banking entities, there are several issues that need to be investigated further: (i) whether the large exposure regime in the current banking legislation is stringent enough to properly address all shadow banking exposures, individually as well as globally; (ii) how to account effectively for leverage in shadow banking entities such as investment funds, including in particular whether to extend the so-called look-through approach currently being applied by some banks; (iii) whether to apply the CRD II treatment of liquidity lines and credit exposures for securitization vehicles to all other shadow banking entities; and, (iv) a review of the implementation of the national supervisory treatment for implicit support
    3. It is being considered to enlarge the scope of financial institutions and activities covered by the current banking legislation. The Commission is currently studying the merits of extending certain provisions of CRD IV to non deposit-taking finance companies not covered by the definition in the Capital Requirements Regulation (CRR).
- Asset management regulation:

1. As far as ETFs are concerned, the current regulatory debate focuses on possible liquidity disruptions; the quality of collateral provided in cases of securities lending and derivatives (swap) transactions between ETF providers and their counterparties; and, conflicts of interest where counterparties in these transactions belong to the same corporate group. In addition, ESMA is currently carrying out a review of the UCITS framework in general and in particular as regards the potential application to ETFs, with a view to adopting new guidelines this year.
2. In relation to MMFs, the main concerns identified relate to the risks of runs.

- Securities lending and repurchase agreements: With respect to securities lending and repurchase agreements, the issues to be covered could include: prudent collateral management; reinvestment practices of cash received against collateralised securities; re-use of collateral (rehypothecation); ways to improve transparency both in the markets and for supervisory authorities, and, the role of market infrastructure. Finally, bankruptcy laws and their impact on collateral should also be reviewed with a view to increasing international consistency along with the accounting practices of such transactions.
- Securitization: With respect to securitization, it needs to be examined whether the measures relating to securitization in the context of the CRD and Solvency II have been effective in addressing shadow banking concerns.
- Other shadow banking entities: Additional work on other shadow banking entities is also underway within the FSB and the EU in order to: (i) list the entities that could be covered; (ii) map the existing regulatory and supervisory regimes in place; (iii) identify gaps in these regimes; and, (iv) suggest additional prudential measures for these entities, where necessary. Finally, the Commission considers that further analysis should be carried out to monitor whether the new Solvency II Framework will be fully effective in addressing any issues raised by insurance and reinsurance undertakings performing activities similar to shadow banking activities.

Comments on the Green Paper can be submitted until 1 June.

Bank accounts

On 20 March, the European Commission launched a ➲consultation on bank accounts. The object of the consultation is to assess the need for action at EU level and, if so, what measures could be taken in relation to one or all of the following issues:

- The transparency and comparability of bank account fees;
- Bank account switching; and

- Access to a basic bank account.

Responses to the consultation can be submitted until 12 June.

European Credit Research Institute (ECRI)

Credit reporting

On 13 March, ECRI published ➲a commentary, entitled "Credit reporting: Towards better access to credit and protection for consumers". It analyses the contribution of credit to better access and the protection for consumers. According to the commentary, Credit reporting addresses the fundamental problem of credit markets: information asymmetry between borrowers and lenders. By providing an efficient mechanism for evaluating risk, accurate credit information enables credit markets to function more effectively and at a lower cost than would otherwise be possible. Regulators and financial market actors therefore increasingly recognize the value of credit-reporting systems for the improved management of credit risk and as a tool to enhance access to credit, thereby contributing to sustainable economic growth and financial sector stability. The commentary indicates that the level of credit reporting differs substantially among EU member states, creating varying needs for reform. In some countries the absence of a credit-reporting system significantly impedes financial inclusion, while in other countries the inadequate sharing of credit information hinders consumer mobility and choice, also inhibiting technological innovations. Different layers of information are relevant in different countries, but the overall playing field and level of protection should be equal throughout the EU to facilitate integrated, European credit markets. This calls for a cross-sectional analysis of the functioning of national credit reporting systems. In this respect the commentary emphasizes that when assessing the need for regulations or amendments, regulators should carefully weigh the intended benefits against the potential negative consequences that such new rules may have on the credit-reporting system as a whole. Excessive regulation should be carefully avoided to prevent disruption of the information networks that are at the heart of efficient credit-reporting systems.

European Savings Banks Group (ESBG)

Basic payment account

On 6 March, the ESBG published the ➲European Banking Industry Committee observations on the ➲European Commission's Recommendation on access to a basic payment account and the ➲IMCO Working Document.

International Capital Market Association (ICMA)

Shadow banking

On 20 March, the ICMA published a ➲paper, entitled "Shadow banking and repo". The paper explores concerns raised by regulators about "shadow banking", particularly in the context of the European repo market and is intended to the "securities lending and repo" workstream set up by the Financial Stability Board within its shadow banking project and the ➲European Commission's green paper on shadow banking.

Investment products and asset management

Normative documents

Official Journal of the European Union (OJ)

Short selling and Credit Default Swaps

On 24 March, ➲Regulation (EU) No 236/2012 of the European Parliament and of the Council of 14 March 2012 on short selling and certain aspects of credit default swaps was published in OJ L 86. The regulation sets outs a common regulatory framework with regard to the requirements and powers relating to short selling and credit default swaps and to ensure greater coordination and consistency between Member States where measures have to be taken in exceptional circumstances. The regulation covers all types of financial instruments but provides for a response proportionate to the potential risks posed by the short selling of different instruments. In particular, for shares of companies listed in the EU, it creates a two-tier model for the disclosure of significant net short positions: While at a lower threshold, notification of a position must be made privately to the regulator, at a higher threshold, positions must be disclosed to the market. For sovereign debt, on the other hand, significant net short positions relating to issuers in the EU would always require private disclosure to regulators. The Regulation also provides for notification of significant positions in credit default swaps that relate to EU sovereign debt issuers. To tackle the increased risks posed by uncovered short sales, the Regulation requires that anyone entering into a short sale must at the time of the sale have borrowed the instruments, entered into an agreement to borrow them or made other arrangements to ensure they can be borrowed in time to settle the deal. However, these restrictions don't apply to the short selling of sovereign debt if the transaction serves to hedge a long position in debt instruments of an issuer. Moreover, if the liquidity of sovereign debt falls below a specified threshold, the restrictions on uncovered short selling may be temporarily suspended by the competent authority. With respect to sovereign credit default swaps, the Regulation stipulates that persons may only enter into sovereign credit default swaps transactions where that transaction does not lead to an uncovered position. In exceptional situations that

threaten financial stability or market confidence in a member state or the EU, the regulation provides that competent authorities should have temporary powers to require greater transparency or to impose restrictions on short selling and credit default swap transactions or to limit individuals from entering into derivative transactions. In such a situation, ESMA is given a key coordination role, to ensure consistency between competent authorities and to guarantee that such measures are only taken where they are necessary and proportionate. ESMA is also given the power to take measures where the situation has cross-border implications.

Consultative or informative documents

Bank of International Settlement (BIS)

Collateral requirements for mandatory central clearing of over-the-counter derivatives

On the same day, the BIS also published ➲a working paper, entitled "Collateral requirements for mandatory central clearing of over-the-counter derivatives". Pursuant to the G20 Recommendation for strengthening financial stability, all standardised OTC derivatives should be cleared with central counterparties (CCPs) by the end of 2012. This would place CCPs between the counterparties of all such bilateral transactions, so they would become sellers to every buyer and buyers to every seller, and thus take on the counterparty credit risk of the bilateral trades. The working paper estimates the amount of collateral that prudent CCPs would require to clear Interest Rates Swaps (IRS) and credit default swaps (CDS) portfolios that are representative of those of the major derivatives dealers. It finds that major dealers already have sufficient unencumbered assets to meet initial margin requirements, but that some of them may need to increase their cash holdings to meet variation margin calls. Default funds worth only a small fraction of dealers' equity appear sufficient to protect CCPs against almost all possible losses that could arise from the default of one or more dealers, especially if initial margin requirements take into account the tail risks and time variation in risk of cleared portfolios. Finally, the papers find that concentrating clearing of OTC derivatives in a single CCP could economize on collateral requirements without undermining the robustness of central clearing.

European Association of Co-operative Banks (EACB)

OTC Derivatives, CCPs and Trade Repositories

On 19 March, the EACB published its ➲comments on Joint ESMA, EBA and EIOPA Discussion Paper on Draft Regulatory Technical Standards on risk mitigation techniques for OTC derivatives not cleared by a CCP under the Regulation on OTC derivatives, CCPs and Trade Repositories

European Association of Public Banks (EAPB)

EMIR

On 20 March, the EAPB published ➲its comments on ➲ESMA's discussion paper on Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories.

MiFID Compliance Function Requirements

On the same day, the EAPB also published ➲its comments on ➲ESMA's consultation paper on "Guidelines on certain aspects of the MiFID compliance function requirements".

European Banking Authority (EBA)

Capital requirements for CCPs

On 6 March, EBA published a ➲discussion paper on Draft Regulatory Technical Standards on the capital requirements for CCPs foreseen by the EMIR. The discussion paper expresses the EBA's preliminary views with respect to capital requirements for CCPs. EBA is of the view that a CCP should hold capital, including retained earnings and reserves, that is at all times at least equal to the higher of the following two amounts: (i) its operational expenses during an appropriate time span for winding-down or restructuring its activities, and (ii) the sum of the capital requirements for the overall operational risk and for credit, counterparty and market risks stemming from "non-clearing activities" it carries out. It is EBA's preliminary view that the operational expenses for winding down or restructuring should be calculated as a CCP's ongoing annual expenses divided by 12 and multiplied by the estimated number of months necessary to ensure winding-down or restructuring of its activities. EBA considers that a CCP should estimate the number of months necessary to ensure winding-down or restructuring of its activities taking into account the complexity of its business. In line with the recommendations provided by CPSS-IOSCO the time period used for the calculation of the operational expenses for winding-down or restructuring should be the longer of the two: (i) internally estimated time period; and (ii) [6-12] months. The Authority further views that, in order to calculate the ongoing operational expenses, a CCP should also consider projected or expected events, such as new business lines or activities the CCP is about to undertake. Nevertheless, in the EBA's view, the operational expenses should be not lower than those incurred in the most recent period. Furthermore, EBA is of the view that the capital requirements for operational risk and risk exposures, EBA has indicated that they could be calculated using approaches set out for banks by the Capital Requirements Directive. In addition to the above, EBA considers that a CCP should have procedures in place to identify all sources of risks that may impact on its on-going functions and should consider the likelihood of potential adverse effects on its revenues, expenses and level of capital. A CCP

should also monitor the compliance with the capital requirements on an ongoing basis and should report it to the relevant competent authority at least on quarterly basis. Finally, EBA indicates that it considering the possibility of establishing a notification threshold equal to [105%-110%] of the capital requirements. In that case, when the level of capital falls below such threshold, a CCP should immediately inform the competent authority and explain which actions it intends to take to ensure compliance with the capital requirements. In order to allow a CCP to be better prepared for dealing with the situation of capital shortage, the EBA contemplates that a CCP should develop a general capital plan, specifying the measures it intends to take when the level of capital falls below the notification threshold.

European Banking Federation (EBF)

OTC Derivatives, CCPs and Trade Repositories

On 21 March, the EBF published ➲its comments on ➲ESMA's discussion paper on Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories.

Short selling and Credit Default Swaps

On 13 March, the EBF published ➲its comments on ➲ESMA's consultation paper on draft technical advice on possible Delegated Acts concerning the regulation on short selling and certain aspects of credit default swaps ((EC) No XX/2012).

Venture Capital Funds

On 2 March, the EBF published ➲the letter it sent to Mr. Lamberts, the lead ECON Rapporteur for the ➲proposed Regulation on Venture Capital Funds. In the letter, the Federation sets out its comments with respect to the aforementioned Regulation.

European Commission

Prospectus Directive

On 30 March, the European Commission published the proposed ➲Commission Delegated Regulation (EU) amending Regulation (EC) No 809/2004 as regards the format and the content of the prospectus, the base prospectus, the summary and the final terms and as regards the disclosure requirements. The Regulation sets out new requirements with respect to:

- The format of the final terms to the base prospectus: The Delegated Regulation categorizes the different items of the applicable Prospectus Regulation Annexes to determine which information should be included in the base prospectus, at the time of approval, and which information should be included in the final terms, at the time of an

individual issue. Some additional information may be inserted in the final terms, on a voluntary basis, but this information is limited to ensure the harmonization and readability of final terms. The Regulation also emphasises that Final Terms must not amend or replace any information in the base prospectus. Instead a supplement or new prospectus must be approved.

- The format and detailed content of the key information to be included in the summary of the prospectus: The Delegated Regulation introduces five sections setting out the mandatory key information to be included in the summary. The order of the sections and of the items within each section is mandatory, thus ensuring equivalent information always appears in the same position, facilitating comparability with other summaries. The mandatory disclosure requirements for summaries are based on the component annexes from which individual prospectuses are constructed ensuring maximum correlation between a summary and the main body of its prospectus. The standardization of the format and content of the summary increases investor protection, consumer confidence and legal certainty. Investors will receive a clearer document and find it easier to compare the summary with that of other similar investment products, thus significantly helping them make investment decisions.

The delegated Regulation also introduces proportionate disclosure regimes for:

- Rights issues: When there is a pre-emptive offer of equity securities and shares of the same class are already admitted to trading on a regulated market or traded on a multilateral trading facility (MTF), issuers will be able to make use of proportionate schedules. To ensure a harmonized approach in relation to the proportionate disclosure regime for rights issues for regulated markets and for multilateral trading facilities, minimum disclosure requirements which multilateral trading facilities need to impose on issuers are also defined;
- SMEs and issuers with reduced market capitalization: SMEs and issuers with reduced market capitalization can make use of proportionate schedules. They can also opt for a full disclosure regime on a voluntary basis or take advantage of the regime introduced for rights issues;
- Credit institutions issuing non-equity securities: Credit institutions issuing credit institutions issuing non-equity securities that draw up a prospectus may choose to include in their prospectus historical financial information covering only the last financial year, or such shorter period that the issuer has been in operation.

Securities settlement and central securities depositories (CSDs)

On 7 March, the European Commission published ➲its

proposal for a Regulation on improving securities settlement in the European Union and on central securities depositories (CSDs) and amending Directive 98/26/EC. The proposal aims to harmonize both the timing and conduct of securities settlement in Europe and the rules governing Central Securities Depositories (CSDs) which operate the infrastructures enabling settlement. The key elements of the proposal are:

- The settlement period will be harmonized and set at a maximum of two days after the trading day for the securities traded on stock exchanges or other regulated markets (currently two to three days are necessary for most securities transactions in Europe);
- Market participants that fail to deliver their securities on the agreed settlement date will be subject to penalties, and will have to buy those securities in the market and deliver them to their counterparties;
- Most securities will have to be recorded electronically, in book-entry form through a CSD, at least from the moment they are traded via an organized trading facility (i.e. non OTC market) or posted as collateral;
- CSDs will have to comply with strict organizational, conduct of business and prudential requirements to ensure their viability and the protection of their users. They will also have to be authorized and supervised by their national competent authorities;
- Authorized CSDs will be granted a 'passport' to provide their services in other Member States;
- Users will be able to choose between all 30 CSDs in Europe;
- CSDs in the EU will have access to any other CSDs or other market infrastructures such as trading venues or Central Counterparties (CCPs), whichever country they are based in.

The proposal has accompanied by a ➲Frequently Asked Questions.

European Covered Bond Council (ECBC)

OTC Derivatives, CCPs and Trade Repositories

On 19 March, the ECBC published ➲its comments on ➲ESMA's discussion paper on Draft Technical Standards for the Regulation on OTC Derivatives, CCPs and Trade Repositories

European Parliament

OTC Derivatives, CCPs and Trade Repositories

In a ➲press release of 29 March, the European Parliament announced the adoption in first reading of ➲the Regulation of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories. In negotiations, Members of Parliament secured a requirement that all derivative contracts (not only OTC derivatives), would have to be reported to central data

centers or "trade repositories", which would have to publish aggregate positions by class of derivatives, thereby offering market players a clearer view of the market. Parliament's negotiators strengthened ESMA's role by making it easier for it to block the authorization of a CCP to operate on the EU's internal market. They also provided for binding mediation by ESMA in disputes among national authorities over the authorization of CCPs. Furthermore, the Parliament secured a "light touch" regime for pension schemes with regard to the clearing obligation. For these schemes, the obligation would not apply for three years, extendable by another two years plus one, subject to proper justification. Finally, the Council and Commission agreed to a proposal by Parliament to have the implementation of the legislation evaluated by the Commission. This evaluation would assess how effectively CCPs are supervised, including supervisory colleges' voting arrangements and the ESMA's role in the process of authorizing CCPs. The Commission will present a report, if necessary accompanied by proposals to Parliament and Council, no later than three years after the regulation's entry into force.

MiFID

On 27 March, the Committee on Economic and Monetary Affairs published ➲the draft report on the proposal for a regulation of the European Parliament and of the Council on markets in financial instruments and amending Regulation [EMIR] on OTC derivatives, central counterparties and trade repositories (MiFIR). The key points and proposals of the rapporteur are:

- The rapporteur proposes to define “bilateral” and “multilateral” system more clearly in order to achieve a precise distinction between bilateral and multilateral trading.
- He believes that the provisions concerning access to market infrastructure could give rise to problems through liquidity fragmentation or if interoperability were involved. Supervisors need to be able to intervene to prevent these problems from occurring.
- He supports the measures which increase transparency and supported the MiFIR requirements extending pre- and post-trade transparency to equity like products and non-equities.
- He welcomes the proposed obligations in relation to transaction reporting which included a new requirement for Regulated Markets (RMs), Multilateral Trading Facilities (MTFs) and OTFs to keep data on orders so that it is accessible to supervisors for at least 5 years.
- He notes that competent authorities could set permanent bans or restrictions on financial products or activities or practices coordinated by ESMA. In addition ESMA can temporarily ban or restrict products, practices and services. However, the rapporteur questions whether the possibility to ban products or services only ex-post is enough to ensure financial market stability or investor protection and therefore proposes two additions.

First, ESMA or competent authorities should not only monitor financial instruments but additionally investment products which also include structured deposits. Second, in addition to the possibility to impose bans or restrictions on products which have already been marketed, ESMA or competent authorities should also be able to impose restrictions or prohibitions on a precautionary basis before an investment product or financial instrument is placed on the market. Furthermore, ESMA and competent authorities should give notice if they intend to ban an investment product or financial instrument on a precautionary basis so that changes to the respective instrument or product can be made within a certain time limit.

On 16 March, the Committee on Economic and Monetary Affairs published the ➲draft report on the proposal for a directive of the European Parliament and of the Council on markets in financial instruments repealing Directive 2004/39/EC of the European Parliament and of the Council. The key points and proposals of the rapporteur are:

- The rapporteur supports the European Commission's proposal to extend the scope of MiFID and limit the exemptions. To ensure that the exemptions are not misused, he proposes a reporting obligation for persons to explain why their activity is ancillary to their main business;
- He proposes to remove the obligation for firms to specify whether investment advice is independent and if it is based on a broad or a more restricted analysis of the market. Instead investment firms should inform clients before investment advice is given if there have been third party payments and if the advice is given on a limited number of instruments. The rapporteur also proposes to that firms providing investment advice should be required to only indicate whether they will provide clients with a periodical assessment of the suitability of the financial instruments instead of a ongoing assessment;
- He proposes the introduction of the requirement for firms providing investment advice on a fee-paying basis to inform clients whether the financial instruments recommended will be limited to financial instruments issued or provided by entities having close links with the investment firm;
- He proposes removal of the prohibition for firms providing portfolio management to receive inducement. The rapporteur is of the opinion that it will be sufficient that clients are informed of expected scale of inducements, prior to signing the portfolio management agreement. any acceptance of an inducement should be fully transparent;
- He proposes the introduction of the obligation that investment firms must, when designing a new product, specify a target group within the retail or professional client category and ensure that the product is designed to meet those customers' needs and marketed to clients within the target group. The information which has to be obtained about clients

should also contain information about the clients' risk tolerance;
- He questions whether the creation of a new category of organised execution venue, the Organised Trading Facility (OTF), is the right way to capture organised venues which are not caught by the existing categories. To avoid loopholes, he propose to limit to OTF category to non-equities, and consequently adjusting the review clause to ensure that the need for, and effect of, this new category is reviewed.
- He proposes a more differentiated approach approach to algorithmic trading, which involves distinguishing between different types of high frequency trading and direct electronic access.
- He proposes the introduction of a requirement that all orders be valid for at least 500 milliseconds to slow down trading;
- He proposes to strengthen the rules for management bodies of trading venues by requiring that one person should not be able to hold more than one executive or two non-executive directorships at the same time, although the ability to combine executive and non-executive directorships within the same group is retained;
- He proposes the introduction of the requirement to put in place parameter for halting trading on trading venues. The parameters should be reported to competent authorities and the European Securities and Markets Authority
- He proposes the introduction of the requirement for require trading venues to ensure their fee structures contain higher fees for placing an order which is cancelled than for an order which is executed and higher fees for market participants who place a high ratio of cancelled orders.
- He proposes to reduce of the number of delegated and implementing acts and specify the periods for ESMA to draft the requested regulatory standards.

Market Abuse

On 26 March, the Committee on Economic and Monetary Affairs published the following two draft rapporteur reports on the European Commission's proposals to revise the Market Abuse Directive:

- Draft report on the proposal for a directive of the European Parliament and of the Council on criminal sanctions for insider dealing and market manipulation. In the report, the rapporteur proposes to shorten the implementing period for the directive to 12 months instead of 24 months. The Committee would also like that the European Commission reports to the European Parliament and the Council on the application of the Directive two years after entry into force of this Directive instead of 4 years.
- Draft report on the proposal for a regulation of the European Parliament and of the Council on insider dealing and market manipulation (market abuse). The report proposes a number of amendments to the Commission text to create a more robust and strong market abuse framework such as a

clarification of the definition of inside information, introduction of the concept of a "trading window" which prohibits managers from conducting any transactions on their own account during certain periods, removal of the threshold for reporting of managers' transactions over 20,000 Euros and strengthening the protection of whistleblowers.

European Securities and Markets Authority (ESMA)

Shortselling and credit default swaps

On 30 March, ESMA published ➲its final report on the draft technical standards on the Regulation (EU) No 236/2012 of the European Parliament and of the Council on short selling and certain aspects of credit default swaps. The document sets out a summary of the responses received by ESMA and describes any material changes to the proposed technical standards. It also includes in a cost-benefit analysis. Finally, it contains the final draft Regulatory Technical Standards and Implementing Technical Standards to be submitted to the European Commission.

The Regulatory technical standards set out:

- The details of the information on net short positions to be provided to the competent authorities and disclosed to the public by a natural or legal person;
- The details of the information to be provided to ESMA by the competent authority;
- The method for calculation of turnover to determine the principal venue for the trading of a share.

The Implementing technical standards specify:

- The means by which information on net short positions may be disclosed to the public by natural or legal person as well as the format of information to be provided to ESMA by competent authority;
- The types of agreements, arrangements and measures that adequately ensure that the shares will be available for settlement and the types of agreements or arrangements that adequately ensure that the sovereign debt will be available for settlement;
- The date and period for principal trading venue calculations, notification to ESMA and the effectiveness of the relevant list;

The draft RTS and ITS were submitted to the European Commission on 31 March 2012. The Commission has three months to decide whether to endorse them.

Risk measurement and the calculation of global exposure for certain types of structured UCITS

On 28 March, ESMA published the final ➲Guidelines on risk measurement and the calculation of global exposure for certain types of structured UCITS. The guidelines set out, for certain types of structured UCITS, an optional regime for the calculation of the global exposure and supplement the requirements on calculation of global exposure relating

to derivative instruments in Article 51(3) of the UCITS Directive and Articles 40 to 42 of Commission Directive 2010/43/EU. The calculation method put forward by the guidelines is the commitment approach as defined in the ➲General Guidelines but adjusted in the following way:

- The formula-based investment strategy for each predefined payoff is broken down into individual payoff scenarios.
- The financial derivative instruments implied in each scenario are assessed to establish whether the derivative may be excluded from the calculation of global exposure under the provisions of Box 3 or Box 4 of the General Guidelines.
- Finally the UCITS calculates the global exposure of the individual scenarios to assess compliance with the global exposure limit of 100% of NAV.

To be able to use the aforementioned method, UCITS must comply with the following criteria:

- The UCITS is passively managed and structured to achieve at maturity the pre-defined payoff and holds at all times the assets needed to ensure that this pre-defined payoff will be met;
- The UCITS is formula based and the pre-defined payoff can be divided into a limited number of separate scenarios which are dependent on the value of the underlying assets and which offer investors different payoffs;
- The investor can only be exposed to one payoff profile at any time during the life of the UCITS;
- The use of the commitment approach as defined in the General Guidelines to calculate global exposure for the individual scenarios is appropriate taking into account the requirements of Box 1 of the General Guidelines;
- The UCITS has a final maturity not exceeding 9 years;
- The UCITS does not accept new subscriptions from the public after the initial marketing period;
- The maximum loss the UCITS can suffer when the portfolio switches from one payoff profile to another must be limited to 100% of the initial offer price; and
- The impact of the performance of a single underlying asset on the payoff profile when the UCITS switches from one scenario to another complies with the diversification requirements of the UCITS Directive based on the initial net asset value of the UCITS.

Waivers from Pre-trade Transparency

On 26 March, ESMA published a ➲revision of its waiver document regarding pre-trade transparency. The revised document extends the scope of the previous version to pre-existing systems by including many of EU operating systems and functionalities where an order, which is sent to a Regulated Market or a Multilateral Trading Facility, is not subject to any pre-trade transparency, even where such a situation was not supported by an explicit waiver. A total of 19 additional functionalities are now covered by the

document. However, not all revised pre-existing cases of limited pre-trade transparency were considered by ESMA as MiFID-compliant. In particular, two preexisting functionalities were added to the list as "non-MiFID compliant" systems. ESMA expects firms to adjust these non-MiFID compliant systems to ensure future compliance. In addition, the document includes a new entry about a proposal for a reference price system considered as non-MiFID compliant (i.e. not being an operating functionality).

Proxy advisors

On 22 March 2012, ESMA published a discussion paper, entitled "An overview of the Proxy Advisory Industry. Considerations on Possible Policy Options". The aim of the Discussion Paper is to give an overview of ESMA's understanding of the functioning of the proxy advisory industry in Europe and to gain evidence on the extent to which market failures may exist in practice that are related to the activities of proxy advisors in Europe. The focus of the Discussion Paper is, therefore, on the state and structure of the proxy advisors market in Europe, the methodologies used by proxy advisors, and on discussing the main concerns that have been expressed. The paper mainly focuses on the following key issues related to the proxy advisory market which may have an impact on the proper functioning of the voting process:

- Factors influencing the accuracy, independence and reliability of the proxy advice such as such as the potential for conflicts of interest to play a role, proxy advisors' methodology and their dialogue with issuers; and
- Degree of transparency on management of conflicts of interest, dialogue with issuers, the voting policies and guidelines, the voting recommendations, and the procedures for elaborating a voting recommendation report.

Furthermore, the paper sets out a range of policy options in relation to the key issues mentioned above. They include:

- Recommending to the European Commission to take no further action at EU-level on proxy advisors, at least at this stage;
- Encouraging Members States and/or industry to develop standards (i.e. by promoting some form of informal engagement between the European Authorities, Member States, and/or industry to develop standards);
- Developing quasi-binding EU regulatory instruments (e.g. through ESMA guidelines or recommendations);
- Introducing binding EU legislation.

Responses to the Discussion Paper can be submitted until 25 June.

Risk mitigation techniques for OTC derivatives not cleared by a CCP

On 6 March, ESMA published a ➲Joint ESMA, EBA and

EIOPA Discussion Paper on Draft Regulatory Technical Standards on risk mitigation techniques for OTC derivatives not cleared by a CCP under the Regulation on OTC derivatives, CCPs and Trade Repositories. The discussion paper expresses the ESAs' preliminary views on requirements on risk mitigation techniques for OTC derivative contracts not cleared by a Central Counter Party (CCP) and aims at gathering the stakeholders' opinions at an early stage of the process. The Regulation on OTC derivatives, central counterparties and trade repositories ("EMIR") requires that Financial Counterparties (FC) and Non Financial Counterparties (NFC), to exchange appropriate collateral for OTC derivative contracts not cleared by a CCP. Financial Counterparties are also required to hold appropriate capital for risks not covered by the exchange of collateral. Regarding the collateral requirements, it is the ESAs' view that, in order to comply with the requirements set forth in EMIR, there should be at least an exchange of variation margin collateral by both counterparties where the transaction is between FCs and/or NFCs. In addition, the ESAs continue to consider a requirement to exchange, post or collect initial margin collateral. With respect to the capital requirements, the ESAs are of the opinion that the capital requirements specified in prudential legislation for prudentially regulated financial counterparties (PRFC) provide a sufficient regime for any remaining risks not covered by the exchange of collateral. Capital requirements should not be developed for non-prudentially regulated financial counterparties (PRFC). The risk arising should therefore be fully covered through the adequate exchange of collateral. In addition to the aforementioned, the Discussion Paper contains three proposals for the provision of initial margin collateral between counterparties: 1) the posting of initial margin collateral by all counterparties, 2) the collection of initial margin by PRFCs only or 3) PRFCs would not be required to collect initial margin collateral if the exposure is to certain counterparties and below a certain threshold. The paper also sets out proposed requirements for the method of pricing/calculation, segregation and re-hypothecation of initial margin collateral. It is the ESAs view that there should be at least a standardized approach available in order to ensure that all counterparties subject to the requirements will be in a position to calculate their margin requirements. However, the ESAs also consider the option to allow for the use of appropriate internal models for the calculation of initial margins, subject to further specified minimum requirements. The ESAs are of the opinion that for initial margin collateral to be effective, it should be held on a segregated basis and should not be reused. With respect to the variation margin collateral, ESAs are considering whether there should be a requirement of a daily exchange of collateral given that the valuation of the outstanding contracts is required on a daily basis. As the ESAs are required to define the level of collateral which should be specified depending on the type of collateral exchanged to satisfy initial margin or variation margin requirements, the Discussion Paper also sets proposals for eligible collateral, namely 1) linking collateral requirements to ESMAs criteria-based collateral requirements set out in

➲ESMAs Discussion Paper on Draft Technical Standards for

the Regulation on OTC Derivatives, CCPs and Trade Repositories or 2) a prescribed list of eligible collateral could be provided, e.g. by referring to the list of financial collateral eligible under the Capital Requirements Regulation. Finally, the Paper sets out the ESAs views on the risk management procedures, operational process for the exchange of collateral and minimum transfer amount. Pursuant to the Regulation, the ESAs will develop, draft technical standard specifying the risk management procedures for the exchange of collateral and in particular the operational process relating to the exchange of collateral. As the exchange of collateral is a key risk mitigation technique for non-centrally cleared OTC derivative, the operational process for the exchange of collateral should be robust. The ESAs are of the opinion that counterparties should have appropriate documentation and processes including systems and controls in place. Also, the ESAs are considering setting a cap to the minimum transfer amount below which no collateral needs to be transferred.

Prospectus Directive

On 1 March, ESMA published ➲its second part of its final advice on possible delegated acts for the Prospectus Directive (the ➲first part of the advice was published on 5 October 2011). In its advice, ESMA proposes how to use a prospectus in a retail cascade and provides input on how to review the provisions of the Prospectus Regulation concerning tax information, indices, auditor's report on profit forecasts and estimates and audited historical financial information. Regarding the use of prospectus in a retail cascade, the advice concludes with a view to transparency, legal certainty, investor protection and the regulatory needs of competent authorities as regards market supervision, that the consent to use a prospectus needs to be public and shall be included in the prospectus or base prospectus/final terms. However in order to take into account the current market practices where the issuer's ability to identify all financial intermediaries in the prospectus or final terms might be limited, ESMA proposes a two type consent approach consisting of 1) an individual consent approach when financial intermediaries are known to the issuer or 2) a general consent approach when the financial intermediaries are unknown to the issuer. In situations where the issuer knows the identity of only some of the financial intermediaries at the time of approval of the prospectus these are to be included regardless of the use of a general consent approach. The Technical Advice sets out the principles which need to be respected by issuers or persons responsible for the drawing up the prospectus and financial intermediaries, as well as specifying the minimum content of the general consent and any conditions attached thereto. On the subject of the review if the provisions of the Prospectus Regulation concerning tax information, indices, auditor's report on profit forecasts and estimates and audited historical financial information, the technical advice proposes the following:

- Tax information: ESMA proposes to keep the current requirement of the Prospectus Regulation but revise its ➲FAQ no. 45 to reflect that such information shall

be included in the prospectus.

- Indices: ESMA is of the view that, among all indices, there is a clear conflict of interest in the case of proprietary indices. Although disclosure on conflicts of interest is already required, a description of the index in the prospectus would provide additional transparency on the issue, ensure that the respective competent authorities have the possibility to scrutinize the description and ensure comprehensibility of the prospectus. The description is required if the index is composed by the issuer and/or any entity belonging to the same group as the issuer. In addition, with regard to an index composed by an entity acting in association with, or on behalf of, the issuer, there is a presumption of a conflict of interest. If the issuer is able to controvert this presumption by including in the prospectus certain statements the description would not be required.
- Auditor's report on profit forecasts and estimates: The Technical Advice proposes to keep the current requirement of an auditor's report on profit forecasts and estimates as it believes that reports prepared by independent accountants or auditors provide investors with confidence in and ensures a certain quality of the profit forecasts or estimates being prepared on the basis of the underlying assumptions. With regard to market announcements concerning figures to be published in the next annual audited financial statements in relation to the financial year that has expired, ESMA considers that a report is not required if certain criteria are met to ensure the figures are non-misleading and the investor is aware of the nature of the included figures.
- Audited historical financial information: ESMA proposes to keep the current regime of including three years of audited historical financial information.

Federation of European Securities Exchanges (FESE)

Market abuse

On 15 March, the FESE published ➲its comments on the European Commission's proposals for a ➲Regulation on insider dealing and market manipulation, and for a ➲Directive on criminal sanctions for insider dealing and market manipulation.

Short selling and credit defaults swaps

On 8 March, the FESE published ➲its response to ➲ESMA's consultation on the draft technical advice on possible Delegated Acts concerning the regulation short selling and certain aspects of credit default swaps.

International Capital Market Association (ICMA)

ETFs and Structured UCITS

On 30 March, the ICMA published its ➲response to the ➲ESMA consultation paper on guidelines for UCITS Exchange-Traded Funds and Structured UCITS.

Short selling and credit default swaps

On 10 March, the ICMA published the ➲joint comments of the Association for Financial Markets in Europe ("AFME"), the International Capital Markets Association ("ICMA"), the International Securities Lending Association ("ISLA") and the International Swaps and Derivatives Association ("ISDA") on ➲ESMA's consultation on the draft technical advice on possible Delegated Acts concerning the regulation short selling and certain aspects of credit default swaps.

International Organization of Securities Commissions (IOSCO)

Systemic Risk Data Requirements for Hedge Funds

On 22 March, the IOSCO published ➲an updated list of categories of data for the global collection of hedge fund information which it believes will assist in assessing possible systemic risks arising from the sector. The revised list reflects the minimum information that the IOSCO will collect for the its next hedge fund survey. The survey will assist IOSCO in assessing possible systemic risks arising from the sector.

Regulation of Exchange Traded Funds

On 14 March, the IOSCO published a ➲consultation paper entitled, Principles for the Regulation of Exchange Traded Funds (ETFs). The paper examines the key regulatory issues regarding ETFs and proposes 15 principles against which both the industry and regulators can assess the quality of regulation and industry practices relating to ETFs regarding investor protection, sound functioning of markets and financial stability. The Consultation Paper also considers the potential broader risks to financial stability arising from ETFs and other ETPs. It suggests that regulators should bear in mind that recommendations made for the ETF industry may be applied elsewhere to other areas of financial services. These potential broader risks include the following:

- Risks arising on secondary markets (the risk of shock transmission)
- ETFs and market integrity (risk of misconduct)
- Risks to financial stability

Comments on the Consultation Paper can be submitted until 27 June.

Insurance, reinsurance and pensions

Consultative or informative documents

European Fund and Asset Management Association (EFAMA)

IORP Directive

On 1 March, the EFAMA published a ➲Background Note regarding the review of Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision ("IORP Directive"). The publication of the note was accompanied by a ➲press release.

Insurance Europe

Anti-Discrimination Directive proposal

On 14 March, Insurance Europe published ➲its comments on the revised Anti-Discrimination Directive proposal.

Insurance mediation

On 12 March, Insurance Europe published ➲a position paper reiterating its proposals for the revision of the Insurance Mediation Directive.

Regulatory and market access issues

On 12 March, Insurance Europe published a ➲briefing note on regulatory and market access issues. The note provides a high level summary of the key issues faced by the European insurance industry when trading with the US, Brazil, Argentina, Japan, India, Russia and China.

Tax

Consultative or informative documents

Belgian Council of Ministers

Budget 2012

On 29 March 2012, the Belgian Council of Ministers approved the third wave of tax measures (➲in Dutch and ➲in French). The approved proposal contains several tax measures, among which (i) the abolition of "carry-forward" notional interest deduction and (ii) the abolition of the

taxation of the capital gains arising from the redemptions of own accumulating shares by a SICAV with EU passport investing more than 40% in receivables/debts securities:

- NID carried forward: The possibility to carry-forward excess NID for 7 taxable periods will be abolished as of tax year 2013. However, the current "stock" of NID carry-forwards will remain available but its use will be restricted. The NID stock deduction will become the last operation in the corporate tax return to determine the taxable base. The maximum NID stock deduction that a company can use per tax year will be limited to 60% of the taxable base. This limitation will however not apply to the first €1 million of the taxable base remaining before the deduction of the NID stock. The NID stock which remains unused further to this limitation can be carried forward until full utilization of the amount which would have been deductible if the 60% restriction had not existed (regardless of the expiration of the 7-year carry-forward period). This comes down, in principle, to allowing deduction of NID stock which would have been deductible under the current 7 year carry-forward rule, but spread over a longer period.
- capital gains arising from the redemptions of own accumulating shares by a SICAV : The tax treatment of capital gains arising from the redemptions of own accumulating shares by a SICAV will be abolished. The exemption granted to the EU Member States should be extended to the EEA Member States. The threshold of investment in receivables/debt securities has also been adapted in order to be in line with the EU Savings Directive. This threshold is set at 25% (previously, at 40%).

Belgian Tax Authorities (FPS Finance)

(Withholding) tax implications of the conversion of a life insurance contract into a unit – linked life insurance contract

In March, the tax authorities issued the Circular n° Ci.RH.231/610.219 on the conversion of a life insurance contract into a unit-linked life insurance contract by the same insurer and on the same insured person (➲in Dutch and ➲in French). The Circular indicates that the conversion should in principle be considered as triggering the exigibility of the withholding tax (provided article 364*quater* BITC or article 21,9° BITC are not applicable).

Council of the European Union

Financial transaction tax

On 13 March 2012, the Council published a ➲briefing detailing the preparatory work carried out with respect to the proposed financial transaction tax Directive, and on its plans for moving the proposal forward.

European Banking Federation (EBF)

Financial Transaction Tax

On 9 March, the EBF published ➲its report on the proposed ➲Financial Transactions Tax (FTT) Directive.

European Commission

Financial transaction tax

In a ➲press release of 23 March, the European Commission announced that if the financial transaction tax (the FTT) is adopted as a new own resource of the EU budget, it will significantly reduce the contributions of member states to the EU budget. According to estimates presented yesterday by the EU Commission, Member States' contributions would be slashed by 54 billion EUR in 2020.

Savings Directive

On 2 March 2012 the European Commission published a ➲report on the results of the European Savings Taxation Directive. The report covers the period 2005-2010. In a nutshell, the report shows that the common EU rules on automatic exchange of information has improved the quality and usability of data transmitted within the Member States. The report also provides for practical suggestions to make the current system even more transparent in the future. Finally, the report also identifies a number of loopholes in the current Savings Tax Directive.

We are always interested in your feedback. Please let us know what you think of this newsletter and send your comments to Regulatory Radar.

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