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Banks and investment firms
Regulatory update

Topics covered in this issue

BRRD

1. *Calculation of 2016 ex-ante contributions*

BRRD/DGSD

2. *Luxembourg Law published*

CRD/CRR

3. *Countercyclical Capital Buffer*
4. *Remuneration policies*
5. *Sound prudential regime for investment firms*
6. *Limits on exposures to shadow banking*

Dormant Accounts

7. *Circular CSSF 15/631*

EDIS

8. *Proposal for an EU Regulation*

EMIR

9. *Starting in June 2016*

MiFID II/MiFIR

10. *Go-live postponed*
11. *Guidelines on complex instruments*
12. *Final report on ITS*
13. *Guidelines on assessment of knowledge and competence*

Single European Market

14. *Retail Financial Services*

BRRD

1. Calculation of 2016 ex-ante contributions

CSSF Circular 15/626 on Single Resolution Fund – Information request by the Single Resolution Board for the calculation of the 2016 contribution according to Articles 4 and 14 of the Commission Delegated Regulation (EU) 2015/63 Processes for notifying that a banking institution is failing

On 1 December 2015, the Commission de Surveillance du Secteur Financier published its CSSF Circular 15/626 on Single Resolution Fund – Information request by the Single Resolution Board for the calculation of the 2016 contribution according to Articles 4 and 14 of the Commission Delegated Regulation (EU) 2015/63. The purpose of this circular is to collect data for the calculation of 2016 *ex-ante* contributions to the Single Resolution Fund.

According to Article 100 of Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms (BRRD)", EU Member State are required to establish one or more national resolution financing arrangements in order to ensure the effective application by the resolution authority of the resolution tools and powers.

According to Article 103(1) of the BRRD, ex-ante contributions shall be raised at least annually from all institutions incorporated under Luxembourg law.
Branches established in Luxembourg by institutions having their head office outside the Union will be covered by the Luxembourg Resolution Fund and not by the present circular.

For EU Member States participating in the Single Supervisory Mechanism (SSM), a Single Resolution Fund (SRF) is established under the responsibility of the Single Resolution Board (SRB) from 01/01/2016 onwards.

The methodology for the calculation of the ex-ante contributions to the Single Resolution Fund and the obligation of the credit institutions as regards the necessary information to be provided in a Single Resolution Mechanism context are specified in the Commission Delegated Regulation (EU) 2015/63 with regard to ex-ante contributions to resolution financing arrangements (DR) and in the Council Implementing Regulation (EU) 2015/81 specifying uniform conditions of application of Regulation (EU) No 806/2014 of the European Parliament and of the Council with regard to ex-ante contributions to the Single Resolution Fund (CR).

The duly filled in template (Annex 2) necessary for calculation of 2016 ex-ante contributions must be submitted by the institutions no later than 1 February 2016 24:00 Brussels time.

Where an institution does not submit the data by the aforementioned deadline, the SRB will use estimates or its own assumptions in order to calculate the annual contributions of the institution concerned.

In addition, each credit institution must make the relevant file (Annex 2) available to the resolution department of the CSSF, which will ensure transmission to the SRB, a document certifying that the submitted template complies with the general instructions.

For this purpose Annex 3 (to this Circular) has to be completed, to be signed by at least one of the members of the banks' authorised management and to be sent to the CSSF also at the latest by 1 February 2016.

BRRD/DGSD

2. Luxembourg Law published

Summary

The Law of 18 December 2015 on resolution, recovery and liquidation measures of credit institutions and some investment firms, on deposit guarantee schemes and indemnification of investors ("the Law" hereafter), has been published on 24 December 2015 on Luxembourg official journal.

This Law implements two European directives in Luxembourg Law:

- Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms (BRRD)
- Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes (DGSD)

The Law already entered into force and is structured as follow:

- Part I – Resolution
- Part II - Reorganisation and winding up
- Part III - Protection of depositors and investors
- Part IV - Amending, transitional and final provisions, introducing notably the recovery provisions

Part I – Resolution

The resolution procedure would be enforced in Luxembourg by the Resolution Committee. It aims to restructure credit institutions encountering serious financial difficulties in order to allow the continuity of their core activities and avoid any systemic impact.

Scope

These provisions are notably applicable to:

- Luxembourg credit institutions
- Luxembourg investment firms
- Financial institutions which are subsidiary of a credit institution or an investment firm supervised on a consolidated basis
- Some financial holding companies
- Branches of credit institutions or investment firms from third countries.

Resolution tools

The Law foresees the following resolution tools:

- Disposal of activities (part or all)
- Set-up of a bridge bank (identification of good assets or essential functions and segregation to create a new bank. Doubtful assets or non-core functions are liquidated)
- Segregation of assets (transfer to a management structure ("bad bank") of doubtful assets).
- Bail-in (recapitalize by cancelling or diluting shares and reducing debts by converting into shares)

Minimum requirement for own funds and eligible liabilities (MREL)

Institutions are required to comply at any times with a minimum eligible own funds and liabilities requirement. MREL provisions are applicable on consolidated basis.

Fonds de Résolution Luxembourg (FRL)

The Luxembourg Resolution Fund FRL is set-up to finance the implementation of resolution tools. The FRL target level is at least 1 percent of guaranteed deposits, and shall be reached no later than 31 December 2024.

The contribution of each credit institutions is proportional to the ratio of:

- Amount of liabilities of each institution (excluding equity), less guaranteed deposits; and
- Cumulated liabilities (excluding own funds) of all authorised institutions contributing to the FRL, less cumulated guaranteed deposits.

The annual ex-ante contributions is adjusted in proportion to the risk profile of credit institutions.

The CSSF Circular 15/628 specifies that aggregate amount of up to 10% of the target level should be raised in 2015. Based on the sum of covered deposits as reported further to circular CSSF 15/619, the aggregate amount to be raised from the Luxembourg credit institutions in 2015 is EUR 28.550.229.

The CSSF requires that contributions to FRL for 2015 has to be paid directly in cash (no commitment), according to individual notices sent in December.

Part II - Reorganisation and winding up

This part of the Law aims to abrogate part IV of the Law of 5 April 1993 on the financial sector and to comply with the provisions of BRRD. It is applicable notably to credit institutions, investment firms and other FSPs managing third parties funds. The covered topics are:

- Payments reprieve
- Voluntary liquidation
- Bankruptcy
- Information to creditors
- Withdrawal of authorisation
- Effects on contracts
- Compensation

Part III - Protection of depositors and investors

Part III of the Law implements notably the provisions of DGSD in Luxembourg Law, with the objective to improve the protection and shorten the delay for compensation of depositors.

Fonds de Garantie des Dépôts Luxembourg (FGDL)

Luxembourg credit institutions and Luxembourg branches of credit institutions having their head office in a third country are required to adhere to the new Luxembourg deposit guarantee scheme, *Fonds de Garantie des Dépôts Luxembourg* (FGDL).

- Covered deposits

The FGDL covers all eligible deposits for each depositor up to a total amount of EUR 100,000. Deposits are covered per depositor per bank, the limit of EUR 100 000 applies to all aggregated accounts at the same bank. A higher protection is foreseen in certain situations.

The Law specifies the exclusions of some deposits, such as interbank deposits, UCI's deposits, insurances deposits, etc.

- Target levels of the FGDL and financing

A first target level of 0.8% of covered deposits is set-up by the Law which shall be reached no later than 31 December 2018.

When the first target level is reached, the institutions will contribute to an additional buffer of 0.8% of covered deposits within 8 years.

The FGDL is financed by ex-ante contributions. These contributions are calculated based on the amount of covered deposits and the risk profile of the institution.

The ESMA opinion on accounting for cash contributions to the Deposit Guarantee Schemes under IFRS specifies that as soon as the obligating event of a non-refundable cash contribution to a DGS is identified, the contribution must be recognised as an expense in full.

- Repayment deadlines

On 1st June 2016, the repayment deadlines will be reduced from 20 working days to 7 working days.

Système d'indemnisation des investisseurs Luxembourg (SIIL)

The set-up of a new compensation scheme for investors, *Système d'indemnisation des investisseurs Luxembourg* (SIIL) is also foreseen by the Law. The SIIL protects investors (natural or legal entities) in Luxembourg credit institutions and investment firms, Luxembourg branches of credit institutions and investment firms having their head office in a third country. The SIIL will be financed by ex-post contributions.

- Covered investments

The SIIL covers all investment transactions for each investor up to a total amount of EUR 20.000. The Law specifies a list of assets excluded from the protection.

- Repayment deadlines

The repayment shall be done no later than 3 months after the agreement on the eligibility and the amount of the debt.

Part IV - Amending, transitional and final provisions

Part IV of the Law amends notably the Law of 5 April 1993 on financial sector in order to introduce the BRRD provisions on recovery. These provisions are applicable to credit institutions, some investment firms and some financial holding companies. The Law foresees exemptions and simplified obligations in some cases.

Each institution in scope, which is not a subsidiary of a group subject to supervision on a consolidated basis, establishes a recovery plan for the measures it would take to restore its financial position after significant turmoil. Contents of the plan is are detailed in Article 206 8° *"Art. 59-18. Plans de redressement"*. The recovery plan shall be updated annually (except under simplified obligations).

These provisions should not be seen as new for credit institutions as all covered institutions had to prepare their recovery plan for the first time in 2014 or 2015.

CRD IV/CRR

3. Guidance on the countercyclical capital buffer

Countercyclical capital buffer (limiting procyclicality)

More Capital to Counter System-Wide Risk

In the aftermath of the financial crisis, the Basel Committee on Banking Supervision (BCBS) published a new set of capital and liquidity standards aiming to strengthen the banking sector's resistance and resilience to economic and financial shocks. As part of these new standards, the Basel III regulatory capital framework introduced the Countercyclical Capital Buffer (CCyB).

Binding as from 2016, the CCyB will aim to achieve the broader macro prudential goal of protecting the banking sector during periods of excessive credit growth by maintaining a sufficient capital base to absorb losses in stressed periods.

The *Commission de Surveillance du Secteur Financier* (CSSF) is responsible to assess the Luxembourgish domestic buffer rate by relying on the monitoring of indicators that may signal a build-up of system-wide risk, such as credit-to-GDP. A CCyB ranging from 0.0% to 2.5% of risk-weighted assets - or higher under specific conditions - will be implemented from 2016 onwards.

The CCyB regime will be fully applicable in Luxembourg as from 1st January 2016 onwards through the CSSF Regulation 15-01. However, **the rate applicable to relevant credit exposures located in Luxembourg is set to 0.0% by the CSSF Regulation 15-04**. The CCyB is applicable to all Luxembourg CRR institutions, Luxembourg branches of third country institutions and CRR investment firms not considered as SME. CSSF Regulation 15-05 indeed exempts the application of the CCyB to investment firms qualifying as SME, i.e. investment firms with a total of employees of less than 250, and with a total annual turnover not exceeding EUR 50 million and/or with a total annual balance sheet not exceeding EUR 43 million.

Regulatory Requirements

The CCyB should reflect the location of residence of the ultimate obligor of the institution's portfolio of relevant credit exposures, which include credit risk exposures, exposures held in the trading book and securitisation excluding governments and institutions obligors. As a result, CRR institutions which have exposures to counterparties in more than one jurisdiction compute their institution-specific CCyB by applying the CCyB applicable in the country of location of these exposures.

For exposures located in non-EEA (outside the 28 states within the European Economic Area) and non-BCBS countries, the CCyB rate is set to zero in the absence of any CSSF specific decision.

Internationally active CRR institutions will need to analyse the geographical location of their relevant credit exposures and then calculate their specific CCyB requirement as a weighted average of the CCyB requirement which is applied in each jurisdiction of location of relevant credit exposures. The weighting applied to the buffer in place in each jurisdiction will be calculated as the institution's total credit risk charge that relates to relevant credit exposures in that jurisdiction divided by the total credit risk charge arising from relevant credit exposures across all jurisdictions.

Specific calculation rules*	
Investment in CIU units or securitisation	The geographical location of relevant exposures shall be recognised either at the level of underlying assets or at the level of the most representative location in underlying assets. If this identification cannot be performed without disproportionate efforts, allocation to the home Member State.
Facility granted to CIU (fund)	Recognised as a relevant exposure (i.e. corporate exposure class under the standardised approach), the geographical location is the country of establishment of the CIU.
Collateralised or guaranteed loans	The ultimate obligor is the collateral issuer or guarantee provider for the recognition of the geographical location of the exposure.
Specialised lending exposure	The geographical location to be recognised is the country of location of the asset generating the income that is the primary source of repayment of the exposure.
Other items	Exposures in the 'other items' exposure class under the standardised approach whose obligors cannot be identified are allocated to the home Member State.
Banking book foreign exposures	These exposures may be allocated to the home Member State if they account for 2% or less of the aggregate value of relevant exposures.
Trading book foreign exposures	These exposures may be allocated to the home Member State if they account for 2% or less of the aggregate value of relevant exposures.
* Technical instructions on the identification of the geographical location of relevant exposures may be found in Regulation (EU) N° 1152/2014.	

CRR institutions will be required to calculate and publically disclose - in the so-called "Pillar III report" -the key elements of the calculation of the CCyB, in particular the geographical distribution of their relevant credit exposures, the respective CCyB rates applicable to the relevant credit exposures, their institution-specific CCyB rate and the final amount of CCyB.

In practice, the CCyB rate applies 12 months after the publication by the CSSF of the CCyB rate for Luxembourg, and by the relevant authorities for other countries, or less than 12 months after the publication if justified on the basis of exceptional circumstances. By derogation, any CCyB rate reduction by the CSSF and other relevant authorities applies immediately.

Further details, relevant information and binding CCyB rates can be found at: http://www.bis.org/bcbs/ccyb/index.htm.

4. Remuneration policies

On 21 December 2015, the European Banking Authority (EBA) published final draft Guidelines on sound remuneration policies. These guidelines will apply from 1 January 2017.

The EBA also issued an opinion on the application of the proportionality principle to the remuneration provisions in Directive 2013/36/EU.

Read more.

5. Sound prudential regime for investment firms

On 14 December 2015, the European Banking Authority (EBA) published a report setting out its recommendations for a "more proportionate and risk-based" **prudential regime for investment firms**. It identified a number of issues in the current application of the CRD/CRR regime for investment firms, including "inadequate" risk sensitivity and complexity of the framework stemming from the current categorisation of investment firms based on MiFID investment activities and services.

The EBA suggests **a new categorisation of investment firms** which would distinguish between systemic and "bank-like" investment firms to which full CRD/CRR requirements should apply, and other investment firms, namely those that are considered "not systemic" or "not interconnected". For the latter, specific requirements should be defined to capture investment business risks, such as credit, market, operational and liquidity risks taking particular account of the holding of client money and securities. The report did not set out any specific thresholds or other criteria for the proposed categorisation.

The EBA also recommended extending the **waiver for commodity trading firms** (that are currently exempt from the large exposures and capital adequacy provisions) until 31 December 2020.

Implications for investment firms

At this stage, the EBA has provided **no specific thresholds or criteria** for categorisation of firms and no calibrations for a new prudential framework; it is too early to say what implications this review will have for each category of investment firms. However, it raises a possibility that a simpler regime will be introduced for some firms.

As part of the review, the EBA is going to conduct a **data collection exercise**; firms should be ready to input into that.

Next steps

Following the EBA's report, the European Commission is now expected to report to the European Parliament and to the Council. The CRR specifies that the EBA's report could be followed by a legislative proposal.

The EBA has already said that it would prepare **a second**, **more detailed report** with specific thresholds for categorisation and calibrations of a new prudential regime. To inform this follow-up report, the EBA is going to conduct the data collection exercise at a firm level.

6. Limits on exposures to shadow banking

The European Banking Authority (EBA) has published its final Guidelines regarding limits on institutions' exposures to 'shadow banking entities' that carry out bank-like activities outside a regulated framework. In particular, these Guidelines introduce an approach that will allow EU institutions to set internal limits for their exposures to 'shadow banking entities', hence addressing in a proportionate way the risks that these exposures pose to the EU banking sector. The Guidelines were informed by a Report on the exposures of a sample of EU institutions to 'shadow banking entities' and the impact of setting limits.

The EBA Guidelines will apply as of 1 January 2017 and, together with the Report, will inform the European Commission's work in relation to its upcoming report on the appropriateness and impact of imposing limits on exposures to shadow banking entities.

Read more.

Dormant Accounts

7. Circular CSSF 15/631

CSSF Circular 15/631 of 28 December 2015 on dormant or inactive accounts refers to the business relationship between the professional subject to the prudential supervision of the CSSF and the bank account holders, regardless of the accounts' nature: cash accounts, securities accounts, e-money accounts, safes…

Obligations of the professional to avoid accounts becoming dormant

Pursuant to MiFID/MiFIR and AML/CFT requirements, each professional should maintain regular contact, preferably at least annually, with its clients and monitor client relationships with vigilance.

The professional must set clear rules to determine when a relationship is considered to become inactive or an account to become dormant. At a minimum, the professional should consider the relationship with a client as inactive and therefore the client's account as dormant

(i) when there has been no communication from the client or his authorised representative during the last six years; and if

(ii) the client or his/her authorised representative has not initiated any transaction (transfer instruction, cash withdrawal or deposit, sale or purchase orders, etc.) on any of the accounts held by the professional during the last three years.

Obligations of the professional when an account becomes dormant

Monitor dormant accounts	In particular, when an account identified as dormant becomes active as a result of initiation of a transaction, this event should trigger an alert for the professional to verify that this renewed activity on the account is not of suspicious nature.
Seek to establish contact with the client or his/her heirs	The professional attempts to restore contact with the client by all appropriate means of communication, without prejudice to any specific provisions in the contract terms. Any initiative to recontact the client and search for possible heirs that generates costs must be undertaken according to the principle of proportionality.
Administer the assets deposited on dormant accounts	Continue to administer the client's assets in compliance with the contractual obligations. Charge justifiable and transparent administrative expenses as long as they remain higher than the value of the deposit, failing which they may proceed with the closure of the account.

Non-prescriptibility of the restitution requirement

Professionals are not authorised to appropriate the assets in their custody, whatever their amount, or to use them for purposes other than their restitution to the entitled beneficiaries.

EDIS

8. Proposal for a European Deposit Insurance Scheme (EDIS)

On 24 November 2015, the European Commission published its Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 806/2014 in order to establish a European Insurance Scheme. This legislative proposal envisages the establishment of a European Deposit Insurance Scheme (EDIS) as the third pillar of Banking Union in three successive stages:

- a reinsurance scheme for participating national Deposit Guarantee Schemes (DGSs) in a first period of three years;
- a co-insurance scheme for participating national DGSs in a second period of four years;
- full insurance for participating national DGSs in the steady state.

A national DGS can only benefit from EDIS if its funds are being built up in line with a precise funding path and it otherwise complies with essential requirements under Union law.

The Single Resolution Board, which would be expanded to administer EDIS, would monitor national DGSs and release funds only where clearly defined conditions are met. The introduction of EDIS would be accompanied by ambitious measures in parallel to reduce risks in the banking sectors of Member States.

EDIS would progressively evolve from a reinsurance scheme into a fully mutualised co-insurance scheme over a number of years.

In the context of efforts to deepen the Economic and Monetary Union (EMU), together with the work on the establishment of bridge-financing arrangements for the Single Resolution Fund (SRF) and on developing a common fiscal backstop, this step is necessary to reduce the bank/sovereign links in individual Member States by means of steps towards risk sharing among all the Member States in the Banking Union, and thereby to reinforce the Banking Union in achieving its key objective.

EDIS addresses the misalignment between the Union supervision and resolution of banks in the participating Member States, on the one hand, and the effectiveness and credibility of national DGSs in case of failure of those same banks on the other.

EDIS would contribute to reducing the link between the perceived fiscal position of individual Member States and the funding costs of banks operating in those Member States and thereby help breaking the link between sovereigns and banks.

This would increase the resilience of the banking sector against future crises and contribute to the overall objective of financial stability which underpins the economic and monetary policy of the Union.

EDIS applies to all DGSs that are officially recognised in a participating Member State and to all credit institutions affiliated to such schemes. The participating Member States are those whose currency is the euro and those other Member States that have established a close cooperation with the European Central Bank to participate in the SSM.

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

EMIR

9. EMIR clearing obligations to start in June 2016

The clearing obligation in the EU will enter into force following the publication of a Regulation (EU) 2015/2205 (the “Regulation”) supplementing the European Markets Infrastructure Regulation (“EMIR”)

Background and scope

ESMA has determined the classes of interest rates OTC derivatives that should be subject to the clearing obligation as set out in EMIR (648/2012 Article 4 & 5).

The clearing obligation covers the following class of OTC interest rate derivatives denominated in the following currencies:

- Fixed-to-float interest rate swaps (also known as plain vanilla) for EUR, GBP, JPY, USD
- Float-to-float swaps (also known as basis swaps) for EUR, GBP, JPY, USD
- Forward rate agreements for EUR, GBP, JPY, USD
- Overnight index swaps for EUR, GBP, USD

The clearing obligation will be phased in based on the categorisation of both counterparties in the derivative trade.

The clearing obligation will take effect as form June 21st, 2016 and depending on the remaining maturity of the derivative contracts on that date, backloading will be required.

The phase-in is planned as per the below time-table:

Category of counterparty	1	2	3	4
1	21 June 2016	21 December 2016	21 June 2017	21 December 2018
2	21 December 2016	21 December 2016	21 June 2017	21 December 2018
3	21 June 2017	21 June 2017	21 June 2017	21 December 2018
4	21 December 2018	21 December 2018	21 December 2018	21 December 2018

Counterparties are classified as per the below table:

Category 1	Counterparties which are currently clearing members clearing one of the above four derivatives on the 21st December 2015
Category 2	FCs, NFC+s and Alternative Investment Funds (AIFs), whose average outstanding gross notional of non-centrally cleared derivatives for January, February and March 2016 is above EUR 8 billion.
Category 3	FCs or AIFs that are NFC+s not in category 1 or 2
Category 4	NFC+s not in categories 1, 2 or 3

It is to be noted that certain alternative investment funds not captured by the definition of financial counterparties under Regulation 648/2012 (EMIR) for purpose of the technical standards will be considered as financial counterparties when dealing in OTC derivatives above the clearing threshold.

The deadlines for counterparties in the second and third categories aim to take into account the timing required to get access to CCP (as client of a clearing member or indirect client of clearing member) which may vary from 12 to 18 months depending of the level of preparation.

Next steps

It has already been announced that the next clearing obligations will cover index credit default swaps as well as interest rate swaps denominated in NOK, PLN and SEK. The European Securities and Market Authority (ESMA) has submitted draft regulatory technical standards to the Commission regarding these classes of OTC derivative instruments in October and November 2015 respectively.

In addition, as per the joint consultation paper of EU regulators from June 10th, 2015, as from 01 September 2016, the phase in of mandatory collateral exchange and margin requirements for non-centrally cleared derivatives is expected to start.

Both implementation measures will over time increase collateral requirements, organizational and operational burden as well as system requirements for counterparties and their service providers.

MiFID II/MiFIR

10. Potential implementation delay of MiFID II / MiFIR

On 17 November 2015, the European Securities and Markets Authority (ESMA) released a note suggesting a potential delay in the implementation of certain provisions of MiFID II / MiFIR. The note follows a recent study conducted by ESMA on the feasibility to have certain systems required under MiFID II / MiFIR ready by the implementation deadline in January 2017.

Timing of IT systems implementation vs. legislative calendar

Provisions under MiFID II / MiFIR not only require updates of existing systems but also the development of a new set of systems in order to retrieve, consolidate and report data. This, in practice, is a lengthy process, which often exceeds a year and which also needs to account for requirements lay down in both Level 1 texts (i.e. Regulation and Directive) and Level 2 texts (i.e. RTS/ITS). However, even when considering the shortest delay in the legislative cycle (e.g. objection period from the EU Parliament and Council), final Level 2 texts are not expected to be published in the Official Journal before March 2016. Given a nine months timeframe at best, it has become evident that ESMA, National Competent Authorities (NCAs) as well as market players will face challenges to deploy all new requirements for 3 January 2017.

Transaction reporting and data availability

When looking at the reporting of data on financial instruments, reference data play a key role as it is the baseline which many IT systems point or refer to. Under MiFID II the scope of financial instruments to be reported has been enlarged beyond Regulated Markets (e.g. ETFs, derivatives). Current data references only exist for shares and bonds, and NCAs as well as Trading Venues are already expecting delay in the publication of new reference data, affecting therefore the availability of data in early 2017.

Transparency and position reporting

Transparency and position reporting are both data-heavy obligations that are narrowly linked to the implementation of reference data systems and the availability of all required data by early 2017. Alongside traditional regulated markets and Multilateral Trading Facilities (MTFs), transparency will also be organised around a third type of multilateral system, known as Organised Trading Facility (OTF).

Maintain the momentum

While the European Commission has acknowledged that a delay may be needed to ensure a smooth and effective implementation, others including some representatives of the EU Parliament believe that any delay will put at risk the overall legislation. At this stage, no official decision has been taken, but one can reasonably anticipate the postponement of some Level 2 provisions, namely with respect to market trading for non-equity instruments and financial transactions reporting. The continuous discussions between the industry, the ESMA and the European Commission reflect the inherent complexity and regulatory issues at stake.

Despite the need to monitor the potential delays in the entry into force, we believe it is appropriate to maintain the momentum on the currently on-going design, analysis, development and implementation of your MiFID 2 solutions.

For your reference, you may read the ESMA note available in English.

11. Guidelines on complex instruments

On 30 November 2015, the ESMA published its Final Report on Guidelines on complex debt instruments and structured deposits.

Purpose

The purpose of these guidelines is to specify the criteria for the assessment of

1. debt instruments incorporating a structure which makes it difficult for the client to understand the risk involved and;

2.structured deposits incorporating a structure which makes it difficult for the client to understand the risk of return or the cost of exiting the product before term.

These guidelines also clarify the concept of “embedded derivatives”.

ESMA expects to promote greater convergence in the classification of “complex” or “non-complex” financial instruments or structured deposits for the purposes of the appropriateness test/execution-only business in accordance with Article 25(3) and 25(4) of MiFID II.

Deadline

These guidelines apply from 3 January 2017.

Instruments embedding a derivative

An embedded derivative should be interpreted as meaning a component of a debt instrument that causes some or all of the cash flows that otherwise would result from the instrument to be modified according to one or more defined variables.

In comparison to the list of examples that ESMA considered as embedding a derivative in its consultation paper, only inflation-indexed bonds have been removed. Such bonds are mainly used by retail investors as a hedge against inflation. Convertible and exchangeable bonds, indexed bonds and “turbo” certificates, contigent convertible bonds, callable or puttable bonds, credit-linked notes and warrants remain within the non-exhaustive list of debt instruments embedding a derivative.

Instruments incorporating a structure making it difficult for the client to understand the risk

Any of the following (non-exhaustive):

a) Debt instruments, the return of which is dependent on the performance of a defined asset pool;

b) Debt instruments, the return of which is subordinated to the reimbursement of debt held by others;

c) Debt instruments where the issuer enjoys discretion to modify the cash flows of the instrument;

d) Debt instruments lacking a specified redemption or maturity date;

e) Debt instruments having an unusual or unfamiliar underlying;

f) Debt instruments with complex mechanisms to determine or calculate the return (new*);

g) Debt instruments structured in a way that may not provide for a full repayment of the principal amount;

h) Debt instruments issued by a special purpose vehicle;

i) Debt instruments with complex guarantee mechanisms;

j) Debt instruments with leverage features.

Structured deposits incorporating a structure making it difficult for the client to understand the risk of return

It concerns structured deposits where (non-exhaustive):

a) More than one variable affects the return received;

b) The relationship between the return and relevant variable or the mechanism to determine or calculate the return is complex;

c) The variable involved in the calculation of the return is unusual or unfamiliar to the average retail investor;

d) The contract gives the credit institution the unilateral right to terminate the agreement before maturity (new*).

Structured deposits incorporating a structure making it difficult for the client to understand the cost of exiting before term

It concerns structured deposits where the exit cost is (non-exhausitive):

a) Neither a fixed sum;

b) Nor a fixed sum for each month (or part thereof) remaining until the end of the agreed term;

c) Nor a fixed percentage of the amount deposited.

* *Was not included in the consultation paper.*

12. Final Report - Draft implementing technical standards under MiFID II

On 11 December 2015, the European Securities and Markets Authority (ESMA) has published Implementing Technical Standards (ITS) regarding the implementation of the Market in Financial Instruments Directive (MiFID II). ESMA's ITS translate how the legislation will apply in practice to market participants, market infrastructures and national supervisors. With this report ESMA publishes its final proposals for a total of eight draft technical standards.

This final report deals with eight technical standards in the following areas:

ITS 1 : standard forms, templates and procedures for cooperation arrangements in respect of a trading venue whose operations are of substantial importance in a host Member State;

ITS 2 : format and timing of the communications and the publication regarding the suspension and removal of financial instruments from trading on a Regulated Market (RM), a Multilateral Trading Facility (MTF) or an Organised Trading Facility (OTF);

ITS 3 : standard forms, templates and procedures for the authorisation of data reporting services providers;

ITS 4 : position reporting (Article 58(5));

ITS 5 : format and timing of weekly position reports (Article 58(7));

ITS 6 : standard forms, templates and procedures for competent authorities to cooperate in supervisory activities, on-site verifications, and investigations and for the exchange of information;

ITS 7 : standard forms, templates and procedures for the consultation of other competent authorities prior to granting an authorisation (IPISC - Investor Protection & Intermediaries SC);

ITS 8 : procedures and forms for submitting information on sanctions and measures.

This final report also describes the feedback received in the public consultations and the rationale behind ESMA's final proposals.

Next Steps

The final report has been submitted to the European Commission on 11 December 2015. The Commission has three months (this period can be extended by one additional month) to decide whether to endorse the technical standards.

13. Guidelines on assessment of knowledge and competence

The European Securities and Markets Authority (ESMA) has published the Final Report on guidelines for the assessment of knowledge and competence.

These guidelines are intended to enhance investor protection by increasing the knowledge and competence of natural persons giving investment advice or providing information about financial instruments, investment services or ancillary services to clients on behalf of investment firms.

As required under Article 25(9) of MiFID II, these guidelines specify the criteria for the assessment of the necessary knowledge and competence requirements of investment firms' staff. These guidelines have been developed to enable firms to fulfil their obligations under Articles 24 and 25 of MiFID II, such as meeting general conduct of business principles, information and reporting to clients, and suitability and appropriateness requirements, through the attainment of appropriate qualifications and appropriate experience by their staff.

The guidelines will come into effect on 3 January 2017.

Single European Market

14. Guidelines on assessment of knowledge and competence

On 10 December, the EU Commission published a Green Paper on retail financial services: better products, more choice and greater opportunities for consumers and businesses.

Key points

The paper is very high-level and wide-ranging. It does not put forward policy proposals, but consults on a number of questions aimed at improving products, choice and opportunities for firms and consumers across insurance, loans, payments and savings accounts and other retail investments. It seeks to make it easier for companies to sell into other Member States, consumers to buy products from other Member States, and for consumers to take all their products with them if they move to another Member State ("portability").

The paper finds that in the EU there are fragmented markets and insufficient competition; limited cross-border activity; differences in price and choice across Member States; and minimal consumer switching.

The report highlights the role that new players and new techniques in the digital market might have in improving competition and choice. It also discusses how, in the area of payments in particular, new opportunities are emerging with the development of mobile, internet and instant payments.

The Green Paper is intended to complement other EU Commission initiatives, such as the Capital Markets Union, the Digital Single Market, and the Single Market Strategy. It demonstrates how the Commission has entered a new phase of activity, where the focus is on improving growth and the single market. There is a clear trend now in the EU of policymakers and regulators seeking to remove barriers to digital innovation.

Areas consulted on in the Green Paper

- Raising the awareness of consumers about products on offer in different Member States and helping consumers to switch products. The Commission suggests that one way this could be done is through consumer access to channels e.g. financial intermediaries, independent comparison websites, or independent financial advice services. Consumer engagement could also be promoted through targeted disclosure at key moments when a consumer may benefit from changing products e.g. when a bonus period is due to end.
- Whether action is needed to address "excessive fees" (e.g. transaction charges and currency exchange fees) that consumers can face when transferring money involving different currencies in the EU, or to help consumers understand the currency conversion rate that is applied to cash withdrawals or purchases with payment cards in Member States with a different currency.
- How to increase consumer access to products from other Member States to limit unjustified discrimination on the grounds of residence. The Commission also states that it will publish legislative proposals in mid-2016 to end unjustified "geo-blocking" (where consumers' access to websites is blocked because of their location).
- Taking action to facilitate portability of retail financial products e.g. life assurance and private health insurance, and promoting the recognition of personal indemnity insurance cross-border.
- Improving the transparency and comparability of products e.g. through disclosure, consumer organisations posting reviews, or digital solutions.
- Strengthening the redress architecture e.g. increasing consumer awareness of the Financial Dispute Resolution Network (FIN-NET), which was set up in 2001 to facilitate the resolution of cross-border disputes in financial services.
- Whether action is needed to protect the victims of car accidents in other Member States, in cases where the insurance company becomes insolvent, and whether further measures could be taken to enhance transparency about ancillary insurance products e.g. add-on products in the car rental market.
- Supporting firms in creating and providing innovative digital services across the EU, with appropriate levels of security and consumer protection.

- Improving the ability of firms to identify customers at a distance for Anti-Money Laundering (AML) purposes and whether further action is needed to promote the uptake and use of e-IDs and e-signatures.
- Improving access to and usability of financial data e.g. so that a lender can access credit information of a consumer who lives in another Member State.
- Whether further action is required to support firms in providing post-contractual services (e.g. claims handling) in another Member State without a subsidiary or branch.
- Encouraging lenders to provide mortgages or loans cross-border.
- Making it easier for firms to navigate the various legal and regulatory requirements in host member states e.g. by Governments or regulators setting up 'one-stop-shops' to help facilitate cross-border sales, harmonising EU regimes, or establishing an opt in regime for a pan-European life insurance product.

Implications

Making it easier for firms to sell into other Member States will increase opportunities for financial services firms. However, we are only at the start of this process. There are a number of practical difficulties that may make this goal difficult to achieve, for example, language barriers and differing risk profiles in each Member State. The greatest opportunities may be where barriers can be reduced between countries with the same language or with respect to consumers who live near a border with another Member State. Firms should also consider use of digital distribution on a cross-border basis.

Increasing transparency in pricing and access by consumers to products in other Member States might also, in the long term, have an impact on pricing and competitiveness. Currency conversion rates, transaction charges and currency exchange fees involving different currencies in the EU may also face regulatory pressure.

Next steps

Responses to the Green Paper are due by 18 March 2016.

The Commission will organise a conference in early 2016 to discuss the results of the consultation and plans to publish an Action Plan on Retail Financial Services in Summer 2016.

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