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Printable version of the e-mail alert
sent on 30 March 2016

Banks and investment firms
Regulatory update

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AML

1. BCBS issued general guide to account opening

On 4 February 2016, the Basel Committee on Banking Supervision published a general guide to account opening.

This guide is an annex to the guidelines on the Sound management of risks related to money laundering and financing of terrorism, which was first published in January 2014.

It is intended to assist banks in defining their approach to account opening and takes into account the significant enhancements to the Financial Action Task Force (FATF) Recommendations and related guidance.

Read more

CRR

2. Regulatory technical standards for prudent valuation under Article 105(14)

On 28 January 2016, the Commission Delegated Regulation (EU) 2016/101 with regard to regulatory technical standards (RTS) for prudent valuation under Article 105(14) of Regulation (EU) No 575/2013 was published in the Official Journal of the European Union.

Institutions shall calculate the total valuation adjustments (AVAs) necessary to quarterly adjust the fair values to the prudent value and shall calculate those AVAs.

The combination of Article 34 and Article 105 of Regulation (EU) No 575/2013 implies that the prudent valuation requirements in these RTS apply to all fair-valued positions regardless of whether they are held in the trading book or banking book.

Positions refers solely to financial instruments and commodities.

The delegated act specifies two approaches for calculating additional valuation adjustments for the purpose of determining the prudent value of fair-valued positions:

- the Simplified approach;
- the Core approach.

Institutions shall apply the Core approach, unless they meet the conditions required for applying the Simplified approach.

Entry into force

This Regulation entered into force on 17 February 2016.

Simplified approach

Institutions can apply the simplified approach provided the sum of the absolute value of on-and off-balance sheet fair valued assets and liabilities is less than EUR 15 billion and provided they are not part of a group that exceeds this threshold.

The calculation of the required AVA under the simplified approach is based on a percentage of the aggregate absolute value of fair-valued positions held by the institution which amounts to 0,1%.

Core approach

The Core approach is obligatory for institutions that are above the threshold of the simplified approach, but may also be implemented by institutions that are below this threshold.

The Core approach can be split in the following key features:

- Every AVA must be calculated as the excess of valuation adjustment required to achieve the identified prudent value over any adjustments applied in the institution's fair value adjustment that can be identified as addressing the same source of valuation uncertainty as the AVA;
- Where possible, the prudent value of a position is linked to a range of plausible values and a specified target level of certainty (90%)
- For all other cases, an expert based approach is specified, together with the key factors that are required to be included in that approach, (90%) target level certainty should also be set.

CRD IV

3. BCBS d355 - Standardised Measurement Approach for Operational Risk

On 4 March 2016 the Basel Committee on Banking Supervision issued its consultation paper on Standardised Measurement Approach for operational risk. The consultation is open until 3 June 2016. We are currently analysing the paper and highlighting the key impacts and will provide you with an overview in the coming days.

Read more

EMIR

4. Sanctions for non-respect of EMIR

On 23 February 2016, the Luxembourg Parliament voted the Draft Law 6846 on OTC derivatives, central counterparties and trade repositories (Draft Law). A request to waive the second vote was introduced.

One particular objective of the Draft Law is to ensure the effective implementation of Regulation (EU) N° 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (EMIR).

In this context, the Commission de Surveillance du Secteur Financier (CSSF) is responsible to ensure the correct application of EMIR.

Powers conferred to the CSSF

The CSSF is vested with all the supervision, intervention, inspection and investigation powers necessary for the exercise of its functions within the limits defined by EMIR (Article 2).

The CSSF is empowered to sanction financial counterparties and non-financial counterparties subject to its supervision for the non-respect of EMIR (Article 3).

Sanction powers

The CSSF can use its power of sanction in case of non-respect of the requirements of

- Article 4 - clearing obligation
- Article 5 - clearing obligation procedure
- Article 9 - reporting obligation
- Article 10 - non-financial counterparties
- Article 11 - risk-mitigation techniques for OTC derivatives contracts not cleared by a central counterparty

Furthermore, in the application of the provisions of the Regulation (EU) N° 648/2012, the before mentioned counterparties can be sanctioned if they:

- Publish inaccurate, false or incomplete information
- Refuse to provide the requested documents
- Provide inaccurate, false or incomplete documents or information when requested
- Interfere with the exercise of the supervision, intervention and inspection powers of the CSSF
- Do not comply with the CSSF injunctions

The following sanctions may be pronounced by the CSSF, depending on the severity of the breach:

- A warning
- A blame
- An administrative fine (from 125 EUR to 1.500.000 EUR)
- A withdrawal of the authorisation to exercise one or more operations and/or activities

The sanctions will be published by the CSSF.

5. EMIR Gears up

New collateral requirements for OTC derivative contract not cleared by a CCP

Following the publication of the Consultation Paper in June 2015, the European Supervisory Authorities (EBA, EIOPA, ESMA - ESAs) published the 8th of March, 2016 their final draft Regulatory Technical Standards (RTS) on margin requirements for non-centrally cleared OTC derivatives under the European Market Infrastructure Regulation (EMIR).

Three main pillars:

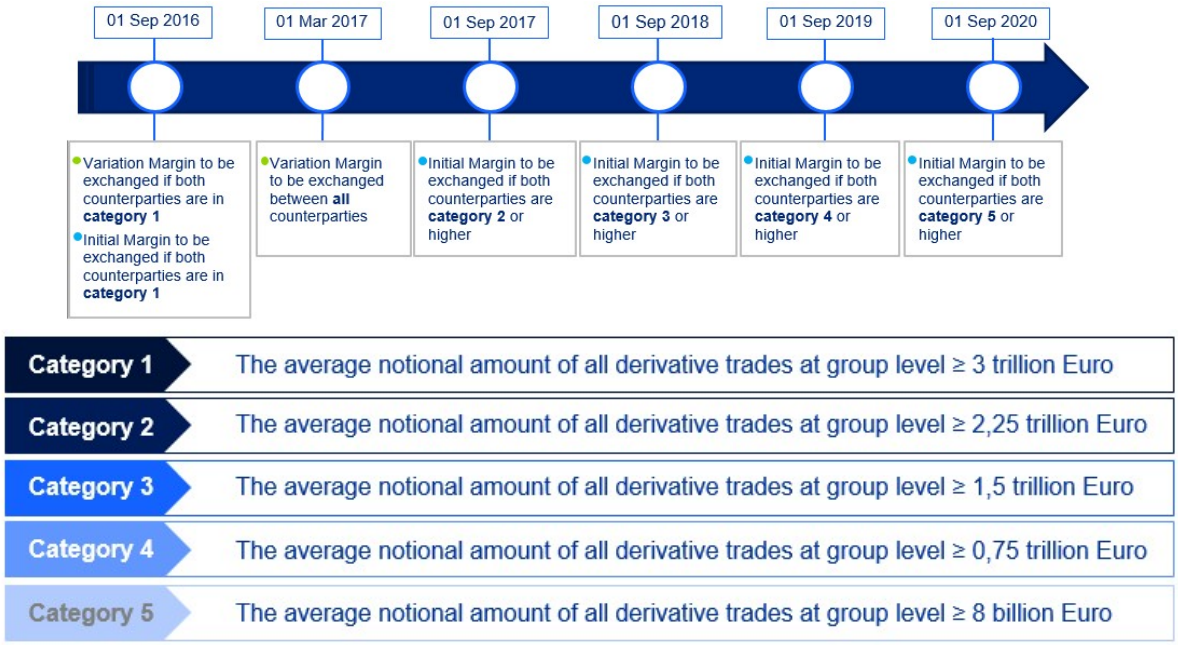
This final draft RTS covers three main parts:

1. An outline of the collateral eligible for the exchange of margins, the criteria to ensure that the collateral is sufficiently diversified and not subject to wrong-way risk, and the methods for determining appropriate collateral haircuts.
2. The operational procedures related to documentation, legal assessments of the enforceability of the agreements and the timing of the collateral exchange
3. The procedures for counterparties and competent authorities related to the treatment of intragroup derivative contracts

From September 2016, EMIR will require some financial and non-financial counterparties transacting in (non-centrally cleared derivatives) to exchange variation and initial margin:

- Daily exchange of Variation Margin (VM) will be phased in between 1st September 2016 and 1st September 2020
- Exchange two-way Initial Margin (IM) to cover future exposure from a counterparty default will be phased in between 1st September 2016 and 1st March 2017

The next milestones:



Key notes:

Main amendments to the second consultation paper published on June 2015

- **Scope of instruments:** The introduction of the margin requirements for single stock options and index options was postponed to avoid any regulatory arbitrage.
- **Segregation:** Cash initial margin cannot be re-used or re-hypothecated. Initial margin in the form of cash should be segregated through a third party or via other legally binding arrangements.
- **Concentration limits were relaxed** – in particular, for the treatment of government bonds.
- **Intragroup transactions:** Initial margin for intragroup transactions to be exchanged from 1 March 2017. This is to tackle the issue of the absence of equivalence with the US in the meantime.

Additional impacts for clients:

Even if margin is already being collected, possibly by a third party custodian, there will still be an impact

- The new rules regarding initial margin will apply to financial counterparties, non-financial counterparties and their third country equivalents, which belong to a group whose aggregate three month-end average notional amount of non-centrally cleared derivatives exceeds EUR 8 billion.
- Thresholds should always be calculated at group level. Investment funds should be treated as a special case and captured as a single group. Where the funds are distinct pools of assets they should be treated as separate entities when calculating the thresholds.
- The new rules regarding variation margin will apply to financial counterparties, non-financial counterparties exceeding the clearing thresholds and their third-country equivalents.
- Firms will need to assess their systems and procedures, as well as the models they will utilise to calculate margin, and factor in the increased trading cost arising from the rules and prepare for the resultant repapering. Firms should also consider whether directing non-cleared transactions to central counterparties will be a more cost-efficient solution for their business.
- The type of collateral which may be posted and received will be limited to specific classes of liquid instruments, with requirements on diversification. The haircut for each category of assets must not be lower than an amount determined by the regulator.
- For firms looking to utilise the intragroup transactions exemption, they should prepare their application for their regulator's approval.

MiFID

6. EU rejects three Mifid II technical standards)

On 17 March 2016, the European Commission rejected three of ESMA's MiFID II technical standards, which will delay their adoption while ESMA makes amendments. The RTS in question were on 'ancillary services', position limits for commodity derivatives, and transparency requirements. ESMA has six weeks to make amendments.

7. Commission extends by one year the application date for the MiFID II package

In its meeting of February 10th 2016, the College of Commissioners officially announced its final position concerning the delayed coming into force of the revised Markets in Financial Instruments Directive ("MiFID II / MiFIR"). The key points of this announcement are as follows:

MiFID II

- The legislative proposal postpones by a year the application date (January 2018), the repeal of MiFID I as well as all the review clauses contained in the legislation
- Article 93(1) MiFID II, requiring Member States to transpose MiFID II in national legislation by 3 July 2016 does not seem to have been modified, contrary to the wish of Member States as expressed during the Financial Services Committee of 21 January 2016

MiFIR

- The legislative proposal postpones by a year the application date (January 2018), as well as all the review clauses contained in the regulation
- In addition, the proposal postpones all deadlines for reports and the expected technical standards on the double volume cap mechanism which are to be produced by ESMA and the Commission by a year

For more information, view the official European Commission release here.

In light of this delay, we foresee several available options for the MiFID II / MIFIR Compliance Program within your organisation:

1. **Continue as planned**
    - This option would maximize your chance of being compliant on time, by ensuring knowledge and momentum preservation
    - In this scenario, your program must ensure that it integrates the latest market practices on an ongoing basis, and the latest interpretations in a way that they do not interfere with your implementation process
    - Due to the extended timeline, and considering the potential delay in publishing the final technical standards, a strict budget monitoring will be key to avoid an increase in the overall project management effort
2. **Finalize gap assessment & strategic decisions**
    - This option would allow momentum and knowledge retention, while adapting the use of business and IT resources in a more flexible way
    - The definition of the implementation phase will have to quickly follow the endorsement by the Commission of the technical standards, in order to maximise your chances of being compliant on time
3. **Phase the implementation**
    - This option would allow phasing developments, while taking complexity of implementation and business criticality into account. In terms of deadline feasibility, it would have the same impact as finalizing gap assessment & strategic decisions
    - The implementation plan must also take into account regulatory certainty in order to delay topics on which market practice and regulatory interpretations are still needed

SFTR

8. Draft RTS and ITS

On 11 March 2016, the Discussion paper draft RTS and ITS under SFTR has been published as part of ESMA's consultations on Level 2 measures under the Securities Financing Transactions Regulation. ESMA will consider the feedback it received to this document in Q2 2016 and expects to publish a consultation paper early in Q3 2016.

The final report and the draft technical standards will be submitted to the European Commission for endorsement by 13 January 2017.

Read more

9. Securities Financing Transaction Regulation - SFTR January 2016

On 23 December 2015, the Securities Financing Transaction Regulation (SFTR) was published in the EU Official Journal.

Key attention points

The Regulation affects investment firms, credit institutions, UCITS/UCITS managers and AIFs/AIFMs.

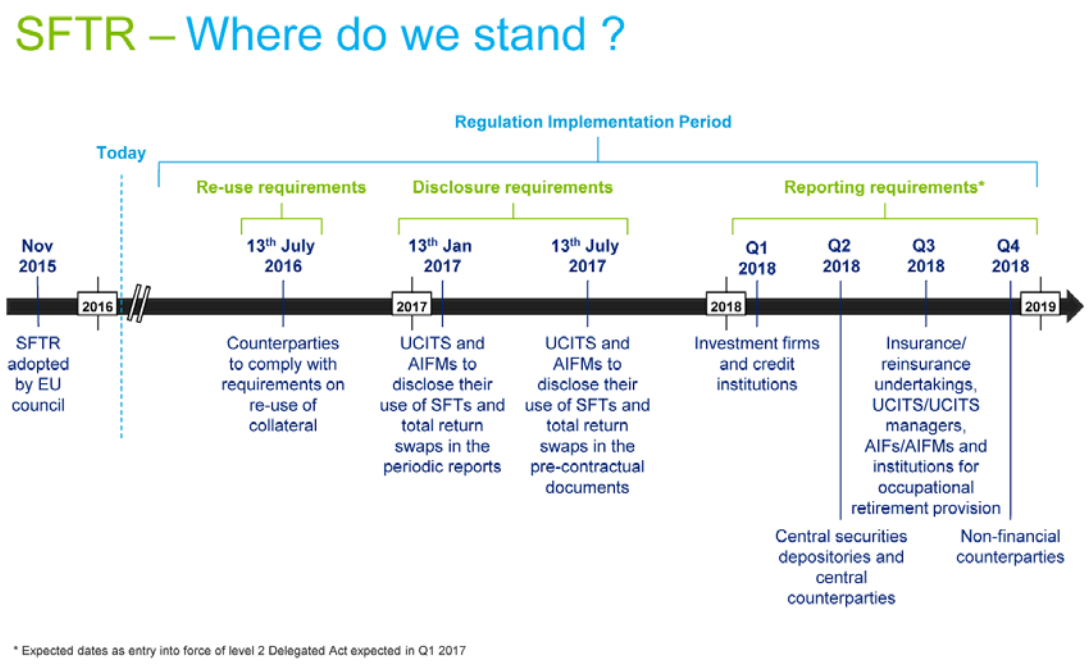
The main requirements of SFTR are:

- transaction reporting to a trade repository and record keeping requirements for the counterparties of securities financing transactions (SFTs); broadly securities and commodities lending, repo and margin lending transactions;
- disclosure requirements for the managers of undertakings for collective investment in transferable securities (UCITS) and alternative investment fund managers (AIFMs); and
- specific requirements for the re-use (re-hypothecation) of collateral.

For trade repositories currently authorized under EMIR by ESMA, a simplified application procedure will apply.

Timeline

The Regulation will enter into force on 12 January 2016 with implementation estimated to be phased-in until the end of 2018.



Key impacts for you

- The Regulation affects investment firms, credit institutions, UCITS/UCITS managers and AIFs/AIFMs.
- The transaction reporting rules for SFTs are similar to those for derivatives under EMIR meaning firms should be able to use some existing internal infrastructure. When undertaking MiFID II transaction reporting implementation or EMIR remediation, firms should be building in flexibility to comply with the final transaction reporting rules for SFTs.
- Firms will also need to undertake a re-papering exercise to comply with the new requirements on re-use of collateral.

Next steps

- ESMA is expected to publish draft technical standards by the end of 2016 specifying the details of the requirements. Following the publication of ESMA's RTS, the European Commission will have three months to endorse it.
- The date of publication of the Commission's Delegated Act is important as it will trigger the start of the phase-in period for the implementation of the reporting requirements.
- By 13 October 2017, the European Commission should submit a report on the progress of the FSB recommendations for haircuts on non-centrally cleared SFTs and propose whether these recommendations are suitable for the EU markets, which leaves open the possibility of the introduction of haircut floors into EU law through the SFTR at a later date.

UCITS V

10. UCITS V: CSSF Press Release 16/10

In its press release 16/10 the CSSF clarified its position on practical issues in relation to the implementation of the UCITS V regime and depositary aspects in relation to Part II UCIs.

UCITS V applicable provisions

The substantive rules of the UCITS V regime on remuneration and depositary bank aspects will enter into force in phases. The UCITS V regime will be put in place through the following instruments:

- The Luxembourg UCITS V transposition law (the "Transposition Law"), which is expected to be adopted and to enter into force on or close to 18 March 2016;
- The UCITS V Delegated Act (the "Delegated Act") with the Level II measures regarding depositary bank aspects; this Delegated Act is expected to be published in the Official Journal of the European Union by the end of March 2016. It will enter into force 20 days after such publication and is expected to be applicable 6 months after its entry into force, i.e. towards the end of September/beginning of October 2016;
- The ESMA Guidelines on Sound Remuneration Policies under the UCITS Directive, which are expected to be published by the end of March 2016, and which will enter into force as of 1 January 2017;
- The ESMA Questions and Answers on the application of the UCITS Directive.

Timing with respect to changes to UCITS KIID and Prospectuses

The CSSF confirmed that it will generally apply the timeline outlined in the ESMA Q&A that was published on 1 February 2016. Please also refer to our previous News Alert on this issue from 3 February 2016.

As a consequence, generally speaking, KIIDs and Prospectuses of Luxembourg domiciled UCITS will need to be updated with relevant UCITS V language concerning remuneration policy at the next available update opportunity after 18 March 2016, but no later than 18 March 2017. The CSSF will put in place a fast-track procedure for the approval of changes to UCITS prospectuses which are limited to amendments relating to the remuneration policy under UCITS V.

UCITS depositary bank aspects as per Circular CSSF 14/587

The CSSF confirmed that the Circular CSSF 14/587 as clarified by the Circular CSSF 15/608 will entry into force as of 18 March 2016. In case of conflict between the provisions of the circular and the Transposition Law, **the provision of the Transposition Law shall prevail.**

The CSSF will adapt and amend the Circular CSSF 14/587 when the Delegated Act will be applicable (i.e. end of September/beginning of October 2016).

The CSSF clarified that "the Reviseur's (auditor) report on the adequacy of the depositary's organisation (on an annual basis)" as required in Circular CSSF 14/587, will be required for a full year that start after the 18 March 2016.

UCI established under Part II of the Law of 17 December 2010 relating to undertakings for collective investments

The CSSF confirmed in the press release that under the Transposition Law, the depositary regime applicable to UCI part II of the Law of 17 December 2010 shall be aligned to the depositary regime applicable to UCITS as of the date of the entry into force of the Transposition Law. Clarifications of the provisions applicable to Part II UCI will be made when the Circular CSSF 14/587 will be amended (i.e. end of September, beginning of October 2016).

Read the CSSF's Press Release 16/10.

11. UCITS V: Level 2 issued

On 24 March 2016, the European Commission Delegated Regulation EU 2016/438 supplementing the Directive 2009/65/CE (UCITS V Directive) with regard to obligations of depositaries has been published in the Official Journal of the European Union. It will apply as from 13 October 2016.

We will provide you with an overview of the level 2 measures in the coming days.

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