Recent Policy Developments in Financial Services

ACROSS THE POND

GLOBAL REGULATORY UPDATE – 26 OCTOBER, 2012

ASIA

Australia

- The Parliament's Joint Committee on Corporations and Financial Services tabled a **report** on 11 October outlining proposed amendments designed to implement commitments for OTC derivatives reform. If passed, the legislation would establish a framework for increased regulation of OTC derivatives through further legislation and regulatory rules, rather than explicitly introducing new requirements for OTC transactions.
- In early October the Australian Prudential Regulation Authority published final rules to implement a number of aspects of Basel III. According to the APRA, "the rules cover a new definition of regulatory capital which puts greater emphasis on common equity, an increase in the level of capital required, a capital conservation buffer, and a countercyclical capital buffer. Further aspects of Basel III will be implemented through rules to be released in November." The rules are to come into effect on 1 January 2013.

Hong Kong

- Hong Kong issued its revised capital requirements for locally incorporated authorised institutions in an effort to implement the first phase of Basel III requirements. Under the revised framework, "a bank will need to maintain three capital ratios calculated as a percentage of its risk-weighted assets. These are: a Common Equity Tier 1 capital ratio of at least 4.5 per cent and a Tier 1 capital ratio of at least 6 per cent (both to be phased in from 1 January, 2013, to 1 January, 2015), as well as a total capital ratio of at least 8 per cent from 1 January, 2013."

Japan

- Japan's Minister of State for Financial Services, Ikko Nakatsuka, recently sent a joint letter to CFTC Chairman Gensler in an effort to persuade the Commission to reconsider the scope of its swaps regime. The letter, cosigned by the UK's Chancellor of the Exchequer, George Osborne, EU Internal Market Commissioner, Michel Barnier, and Pierre Moscovici, French Minister of Finance, urged the CFTC to delay finalizing any new rules before taking the time to "ensure that US rulemaking works not just domestically but also globally."

Singapore

- Singapore recently moved two Bills to the Parliament for first reading, including **amendments** designed to strengthen regulation of the OTC derivatives market. The amendments introduce a new regulatory regime for trade repositories, extend the existing regime for clearing facilities to OTC derivatives, and introduce mandatory reporting and clearing requirements for certain OTC derivatives transactions.

EUROPE

Council of the EU

- The Council continues to discuss MiFID II/R and is aiming to reach a political agreement by November 2012 and conclude negotiations by mid-2013. The current priorities are definitions of High-Frequency Trading (HFT) and algorithmic trading, OTF's, pre and post-trade transparency, commodity derivatives trading and provisions around data consolidation for equities. The Cypriot Presidency scheduled four October meetings to accelerate decision making, but it is likely that the Irish Presidency, taking office on 1 January, will finalise the dossier.

European Parliament

- The European Parliament ECON Committee voted on 26 September and reached a broad compromise on the MiFID II report prepared by Markus Ferber MEP. The Plenary is expected to vote on 26 October (amendments only), but not on a legislative resolution text, meaning that the text itself will not be voted until the end of the trialogues. The biggest changes compared to the original Commission proposals are on OTFs, which are now restricted to non-equity products and on CCP access, where the Parliament text has decoupled access and interoperability for bonds and derivative products, albeit with the protection of access for cash products – effectively mirroring the EMIR provisions in MiFD/R II.
- The ECON Committee held a public hearing on global action post LIBOR/EURIBOR, inviting CFTC's Gensler as well as EU Commissioners Barnier and Almunia. The Brussels consensus is that LIBOR should be replaced. The ECON Committee voted in favor of the revised Market Abuse legislative package as amended after the Libor scandal, introducing criminal offences for index manipulation and insider dealing.

European Commission / European Securities Market Authority (ESMA)

- The ESMA regulatory standards paper is being discussed by different units of the European Commission and is expected to be approved by the Parliament/Council in late 2012/early 2013. The standards suggest a phase-in of derivatives reporting by asset class (following the US regulators example with credit and interest rate scheduled for 1 July, 2013, and the remaining three asset classes six months later). Uniquely, ESMA has suggested reporting of collateral to follow six months after implementation of the final asset repositories (mid 2014). On clearing, ESMA and EBA standards were published and sent to the Commission for review/approval.

- The Commission launched a consultation paper on recovery and resolution for market infrastructure (CCPs and CSDs) as well as other systemically important institutions (insurance companies in particular). The consultation aims to ascertain how and when the failure of a non-bank financial institution could jeopardise financial stability as well as the arrangements needed to prevent the failure of such entities' from compromising financial stability. The consultation sets 28th December as a deadline for industry responses and the Commission is likely to come forward with a legislative proposal in Q2 2013.

What is Brussels Talking about?

The European Banks restructuring plans: The Liikanen Group presented its report on structural reforms for the EU banking sector, suggesting that banks should ring-fence their trading activities away from their deposit operations. Rather than picking one of two approaches proposed by Volcker in the US and Vickers in the UK, Liikanen proposed a hybrid version that combines elements of both: systemically important banks will be forced to separate trading from retail activities meaning that proprietary trading activity can only be carried out within a separate legal entity. The universal banking model would remain, and trading for clients would remain part of the retail part of the group. Consequently, the Commission launched a consultation on the report (deadline for comments is 13 November) and, if willing to release a legislative proposal on the matter, will have to find a way to clearly define when a bank is trading for its clients or for its own account.

Is EU banking union closing in? The legislative proposals for a Single Supervisory Mechanism (SSM) continue to be the EU's highest priority with European leaders agreeing that the mechanisn should be agreed upon by January 2013 and be in place in mid-2013. The complexity of the legislative dossier, coupled with the political divide between Germany and the UK on one hand, and France, Italy and Spain on the other, suggest that Member States will have to make extra efforts to respect the deadline. The Commission will likely explore other alternatives, such as creating a new Supervisory Board which would make recommendations directly to the ECB's Governing Council. The ECB is expected to complete a review of how much supervisory powers it could be granted in mid-November.

Towards a watered down FTT: Following intensive lobbying by the French and German governments, a tax across several EU Member-States is a real possibility as 11 states have pledged their support. The scope and level of the tax remains unclear, but it is expected to be similar to the Commission's original 2011 proposal, which stated that the countries would collect a tax of 0.1% for trades in shares and bonds and a 0.01% tax on derivatives trades. The aim is to implement the tax in the Member States on a voluntary basis by the end of 2012.

AMERICAS

Canadian Parliament

- Canadian Finance Minister, Jim Flaherty, has introduced legislation providing a legal framework for centralized clearing of standardized OTC derivatives under the Payment Clearing and Settlement Act.

United States – Commodity Futures Trading Commission (CFTC)

- The Commission recently approved a new **proposal** to introduce a series of measures – including additional capital and higher liquidity standards – to enhance the safeguarding of customer funds. The proposal will have a 60 day comment period.
- Also this month, the CFTC approved by a vote of 3-2 its final Interpretive Guidance regarding the Confidentiality and Indemnification Provisions of the DFA. Commissioners O'Malia and Sommers voted against the measure, citing concerns that it does not actually solve the problem and will continue to constrain certain foreign and domestic regulators from accessing data stored in SDRs without indemnification agreement.
- On October 11-12, the Commission released a series of documents in an effort to provide greater clarity to market participants. The documents, which can be found on the CFTC's **website**, address a wide range of topics, including issues related to which swaps to include in swap dealer and MSP *threshold* calculations, cross-border scope, securitizations, FX forwards and swaps, among others.

U.S. Securities and Exchange Commission

- The SEC recently adopted a rule that establishes standards for how registered clearing agencies should manage their risk and run their operations. According to the release, "the new rule would require registered clearing agencies that provide CCP services to maintain certain standards with respect to risk management and operations. Among other things, the rules would set standards with respect to measurement and management of credit exposures, margin requirements, financial resources and margin model validation. The new rule will become effective 60 days after publication in the Federal Register.
- The Commission also recently approved proposals related to capital, margin, and segregation requirements for security-based swap dealers and major security-based swap participants. A fact sheet on the new requirements can be found on the SEC's **website**.

U.S. Congressional Oversight

- Federal lawmakers are among an increasing broad collection of stakeholders – including associations such as SIFMA, ISDA, the American Bankers Association and the Financial Services Roundtable, among others – to voice their concerns about the U.S. Basel III capital requirement proposal. In late September, a group of 53 bipartisan Senators sent a joint letter to the heads of the U.S. regulatory agencies responsible for Basel III implementation asking for it to be reconsidered in order to avoid negatively impacting community banks. More recently, a group of Senators urged regulatory heads to avoid imposing the requirements on the insurance industry.

What is Washington Talking About?

2012 Elections – With less than two weeks until the 2012 General Election, President Obama and Mitt Romney are locked in a virtual dead heat and the outcome is far from certain. In a series of contentious debates, the candidates sparred on a range of issues, most notably the economy, the federal deficit, and job creation. And while a controversial issue amongst financial stakeholders, Dodd-Frank has been a relatively minor issue in the broader scheme of the political battle.

The "fiscal cliff" – Reaching a political resolution on the so-called fiscal cliff issue – a series of automatic taxes hikes and spending cuts set to kick in at midnight on December 31 – is increasingly a top priority amongst policymakers and is viewed as critical to the country's economic recovery. Recently, more than a dozen CEOs of America's top banks and insurance companies sent a letter to the White House and Congress urging political action. The issue presents a difficult test for Congress during the upcoming "lame duck" Congressional session.

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