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BROKER-DEALER

FINRA Issues Guidance on FOCUS Reporting for Operating Leases

On March 19, the Financial Industry Regulatory Authority, Inc. (FINRA) released Regulatory Notice 19-08 to provide guidance to members for reporting lease assets and liabilities on their FOCUS reports. FINRA's notice follows an October 2018 No-Action Letter (the No-Action Letter) in which the staff of the Securities and Exchange Commission's Division of Trading and Markets (the Staff) addressed the treatment of operating leases under Securities Exchange Act Rule 15c3-1 in connection with the Financial Accounting Standards Board's Accounting Standards Update for Leases.

Rule 15c3-1(c)(2)(iv) generally requires broker-dealers calculating net capital to deduct fixed assets and assets that cannot be readily converted into cash from their net worth. Consequently, absent relief, a broker-dealer lessee would be required to deduct its operating lease from its net worth when computing net capital. In its No-Action Letter, the Staff explained that, subject to certain conditions, it would not recommend enforcement action to the SEC if a broker-dealer:

1. computes net capital by adding back an operating lease asset to the extent of the associated operating lease liability; and
2. does not include in its aggregate indebtedness an operating lease liability to the extent of the associated operating lease asset for purposes of calculating its minimum net capital using the aggregate indebtedness standard.

Building on the No-Action Letter, FINRA's notice provides guidance regarding the reporting of an operating lease asset and an operating lease liability on FOCUS Report Part II, Part IIA and Part II CSE. Members should follow such guidance in their FOCUS reports going forward but are not required to refile previously submitted FOCUS reports to comply with the guidance.

Regulatory Notice 19-08 is available here.

FINRA Reminds Firms of Obligations Under Rule 15c2-11(a)(4)

On March 20, the Financial Industry Regulatory Authority, Inc. (FINRA) released Regulatory Notice 19-09, which reminds members of their obligations under Securities Exchange Act Rule 15c2-11 and FINRA Rule 6432 (Compliance with the Information Requirements of Rule 15c2-11). Rule 15c2-11 prohibits a broker-dealer from publishing (or submitting for publication) a quotation in an unlisted security on a quotation medium unless the broker-dealer has reviewed current information regarding the issuer of the security. With respect to quotes in the security of a foreign private issuer, Rule 15c2-11(a)(4) requires a broker-dealer to review and make reasonably available upon request certain information published by the issuer since the beginning of its last fiscal year. In Regulatory Notice 19-09, FINRA informed members that linking to an issuer's website that requires the investor to attest that he or she is a resident of a non-US jurisdiction or that prohibits US persons from accessing the website will not satisfy the Rule 15c2-11(a)(4) requirements (or the related FINRA Rule 6432 requirements) as such information is not considered to be "reasonably available" to US persons.

More information is available in Regulatory Notice 19-09.

DERIVATIVES

See also "CFTC Announces Global Markets Advisory Committee Meeting" and "CFTC Announces Energy and Environmental Markets Advisory Committee Meeting" in the CFTC section and "ESMA Extends Its Register of Derivatives to be Traded On-Venue Under MiFIR" in the Brexit/EU Developments section.

Banking Regulators Adopt Swap Margin Safe Harbor

On March 15, the five US regulators (the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Farm Credit Administration, the Federal Housing Finance Agency and the Federal Deposit Insurance Corporation) that are responsible for the margin rules for uncleared swaps that apply to prudentially regulated swap dealers adopted an interim final rule designed to ensure that qualifying swaps may be transferred from a UK entity to an affiliate in the European Union or the United States without triggering new margin requirements.

The interim final rule was needed because of the position taken by the regulators that the swap margin rules will apply to a swap executed before the margin rule compliance date (a "legacy swap") if it is amended in a material way after the compliance date. Recognizing that Brexit might force some UK swap dealers to amend legacy swaps on a large scale to transfer or novate them to affiliates in other jurisdictions, the regulators took affirmative action to define circumstances in which such transfers or novations would not trigger an adverse margin result.

The interim final rule went into effect on March 19, but the regulators are accepting comments on the interim rule until April 18 (presumably concerning ways in which the rule can be made more effective).

The interim final rule is available here.

CFTC

CFTC Announces Global Markets Advisory Committee Meeting

The Commodity Futures Trading Commission has announced that its Global Markets Advisory Committee (GMAC) will hold a meeting on April 15. The GMAC will hear presentations on how regulators are fulfilling the 2009 G20 directive regarding the OTC derivatives market. Specifically, the GMAC will examine the status of the four key pillars of the original G20 directive:

- trading on exchanges or electronic trading platforms;
- clearing through central counterparties;
- margin requirements for non-centrally cleared derivatives; and
- data reporting to trade repositories.

The meeting is open to the public and will take place at the CFTC headquarters. A live webcast also will be offered. More information is available here.

CFTC Announces Energy and Environmental Markets Advisory Committee Meeting

The Commodity Futures Trading Commission has announced that its Energy and Environmental Markets Advisory Committee (EEMAC) will hold a meeting on April 17. The meeting will focus on the following three topics:

- derivatives markets' responses to physical markets' developments;
- exchange-traded energy derivatives markets; and
- the availability of clearing and other services in the energy derivatives markets.

The meeting is open to the public and will take place at the CFTC headquarters. A live webcast will also be offered. More information is available here.

UK DEVELOPMENTS

House of Lords Bribery Act 2010 Committee Publishes Post-Legislative Scrutiny

On March 14, the House of Lords Select Committee (Select Committee) on the Bribery Act 2010 (Bribery Act) published its report, "Bribery Act 2010: post-legislative scrutiny," to establish whether the Bribery Act is achieving its intended purposes.

In its report, the Select Committee concludes that the Bribery Act is an excellent piece of legislation, creating offenses that are "*clear and all-embracing*." In particular, the offense of corporate failure to prevent bribery is regarded as effective and enables those in positions of influence in a company to ensure that the company operates ethically.

However, the report states that guidance from the UK Ministry of Justice (MoJ) is less helpful in providing small and medium enterprises with the information and advice needed for developing formal anti-bribery policies. For example, for companies considering exporting services, the Select Committee notes that the MoJ's guidance should give more guidance on the point at which hospitality exceeds what a reasonable member of the public might think was acceptable and begins to influence the recipient's course of action.

The Select Committee's report reminds firms in the financial services sector that they must (where relevant) abide by legislation which goes beyond the Bribery Act, such as the revised Markets in Financial Instruments Directive (MiFID II). It also notes that the UK Financial Conduct Authority (FCA) "*takes a stern line on hospitality*" and considers sporting or social events as not meeting the requirement that hospitality should be "*conducive to business discussions*." The FCA also considers activities provided after training events or conferences, such as evening dinners or attendance at rugby games, are often not appropriate—therefore firms regulated by the FCA have no choice but to observe the FCA's guidelines. The Major Event Organisers Association considers this as an "*overreaction*" from firms' compliance officers in implementing legislation, resulting in event organizers being unintentionally negatively impacted by the Bribery Act and MiFID II.

In the absence of judicial interpretation of the Bribery Act's provisions on bribing another person or a foreign public official from a hospitality point of view, the Select Committee has suggested that it may help businesses to look at the situation from the point of view of the recipient of hospitality. For example:

1. would the guests expect to be treated in such a way, regardless of the decision they might reach on the business in question;
2. would the guests believe that the level of hospitality offered was an attempt to influence them improperly into making a decision which they might not otherwise have made; or
3. what would a reasonable member of the public, who is properly informed, think of the hospitality a business is proposing to offer.

The Select Committee has encouraged professional organizations and trade associations to provide sector-specific guidance on where their members should draw the line on hospitality.

The Select Committee's report is available here.

BREXIT/EU DEVELOPMENTS

ECB Announces Euro Short-Term Rate Start Date and Recommendations on Transition From EONIA

On March 14, the European Central Bank (ECB) working group on euro risk-free rates published recommendations on transitioning from the euro overnight index average (EONIA) to the euro short-term rate (€STR). The ECB's recommendations include the following:

1. market participants should gradually replace EONIA with €STR for all products and contracts, making €STR their standard reference rate once the period of transitioning to the €STR ends at the end of 2021;

2. EONIA's administrator, the European Money Markets Institute, should modify the current EONIA methodology to become €STR (plus a spread) for a limited period of time, allowing market participants sufficient time to transition to €STR; and
3. market participants should make all reasonable efforts to replace EONIA with €STR as a basis for collateral interest for both legacy and new trades with each participant's counterparties (clean discounting).

The ECB also published a press release announcing that it will start publishing the €STR from October 2, reflecting the trading activity of October 1.

The ECB's recommendations are available here.

The ECB's press release are available here.

ESMA Extends Its Register of Derivatives to be Traded On-Venue Under MiFIR

On March 21, the European Securities and Markets Authority (ESMA) updated its public register of derivative contracts that are subject to the trading obligation under the Markets in Financial Instruments Regulation (MiFIR).

ESMA's update follows the authorization, on the same date, of additional trading venues where the classes of derivatives subject to the trading obligation are available for trading. The recently authorized trading venues are located in France and the Netherlands.

ESMA's public register is available here.

ESMA Publishes Statement on the Impact on the MiFIR Trading Obligation for Shares; the FCA Responds

On March 19, the European Securities and Markets Authority (ESMA) published a statement on the impact on the Markets in Financial Instruments Regulation (MiFIR) trading obligation for shares (TO) if the United Kingdom left the European Union on March 29 (Brexit) without a withdrawal agreement (no-deal Brexit) and without an equivalence decision for the United Kingdom made by the European Commission.

ESMA recognizes that its approach may lead to an overlap of trading obligations for a number of shares and potentially a greater level of fragmentation of trading if the United Kingdom applies an identical approach. However, in the absence of any clarification by ESMA, this would, by default, lead to the application of the MiFIR TO to shares traded in the remaining 27 Member States of the European Union. ESMA's approach aims to limit potential market disruption while also ensuring that the MiFIR TO for investment firms is adequately and consistently applied across the European Union.

ESMA's statement reflects these aspects and contains guidance on the application of the MiFIR TO for shares in a no-deal Brexit scenario. To inform market participants effectively, ESMA has published a public statement on the impact of Brexit on the trading obligations for shares together with a list of instruments that would be subject to the TO for shares. ESMA also highlighted that the guidance provided in the public statement should only apply in the case of a no-deal Brexit occurring on March 29.

On the same date, the UK Financial Conduct Authority (FCA) published its response to ESMA's statement. In its statement, the FCA stated that it believes that only a "*comprehensive and coordinated approach can provide the necessary certainty to market actors,*" without which it will not be possible to address the issues of conflicting obligations applying to the same instruments. The FCA also has urged further dialogue with ESMA and other EU authorities on the issue of the on-shoring of EU legislation and the overlap between UK and EU obligations, to minimise the risks of disruption in the interests of orderly markets.

ESMA's statement is available here and the list of instruments subject to the MiFIR TO for shares is available here.

The FCA's statement is available here.

ESMA Announces Results of MiFID II Annual Calculations of LIS and SSTI Thresholds for Bonds

On March 19, the European Securities and Markets Authority (ESMA) published a press release announcing the results of the annual transparency calculations of the large in scale (LIS) and size specific to the instruments (SSTI) thresholds for bonds. ESMA's publication had originally been planned for March 1, but was postponed as its IT systems required more time than anticipated to complete the calculations, as reported in the *Corporate & Financial Weekly Digest* edition of March 8, 2019.

Under Commission Delegated Regulation (EU) 2017/583, national competent authorities (NCAs) must publish information on LIS sizes compared to the standard market size, and the SSTI above which pre-trade transparency requirements can be waived and the publication of post-trade transparency information can be deferred. ESMA has conducted these calculations on behalf of the NCAs who have delegated this task to ESMA and the results have been published on a register based on bond type.

ESMA will publish results on a per-International Securities Identification Number (ISIN) basis through the financial instruments transparency system (FITRS) and through a web interface from April 30. It also will publish records with calculations for each ISIN until May 31.

The transparency requirements based on the results of the annual calculations of the LIS and SSTI thresholds for bonds will apply from June 1, 2019 to May 1, 2020. ESMA will publish the results of the next annual calculations of the LIS and SSTI thresholds for bonds by April 30, 2020, which will apply from June 1, 2020.

ESMA's press release is available here.

The register is available to here.

For additional coverage on financial and regulatory news, visit *Bridging the Week*, authored by Katten's Gary DeWaal.

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