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Corporate & Financial
Weekly Digest

June 22, 2018 Volume XIII, Issue 25

CFTC

NFA Proposes Amendments to Compliance Rule 2-9(c) and Interpretive Notice: Compliance Rule 2-9: FCM and IB Anti-Money Laundering Program

On June 15, the National Futures Association (NFA) submitted to the Commodity Futures Trading Commission proposed amendments to NFA Compliance Rule 2-9(c) and the NFA Interpretive Notice entitled Compliance Rule 2-9: FCM and IB Anti-Money Laundering (AML) Program (collectively, the Amendments). Rule 2-9(c) requires futures commission merchants (FCMs) and introducing brokers (IBs) to develop and implement anti-money laundering programs designed to achieve compliance with the requirements of the Bank Secrecy Act.

NFA proposed the Amendments in response to the Financial Crimes Enforcement Network's (FinCEN) new regulations that (1) require financial institutions to identify and verify the identity of beneficial owners of legal entity customers and (2) amend the AML program requirements to require appropriate risk-based procedures to conduct ongoing customer due diligence. FCMs and IBs were required to comply with FinCEN's new regulations prior to May 11.

The Amendments add a new clause 5 to Rule 2-9(c) requiring FCMs and IBs to establish appropriate risk-based procedures for conducting ongoing customer due diligence. Further, the Amendments amend the Interpretive Notice to:

- add a section on identifying and verifying beneficial owners pursuant to FinCEN's requirements;
- add requirements that FCMs and IBs develop risk-based ongoing customer due diligence procedures in accordance with FinCEN's requirements; and
- clarify that FCMs and IBs should use the beneficial ownership information to help ensure that they are in compliance with the Office of Foreign Assets Control regulations.

NFA invoked the "ten-day" provision of Section 17(j) of the Commodity Exchange Act and, subject to possible CFTC review for approval, plans to make the Amendments effective 10 days after the CFTC's receipt of the proposed amendments.

NFA proposed amendments are available here.

BANKING

Federal Reserve Adopts Final Rule for Single Counterparty Credit Limit

On June 19, the Federal Reserve adopted a final rule that sets overall single counterparty credit limits for global systemically important banking entities (GSIBs) and US bank holding companies with at least $250 billion in total consolidated assets.

The new rule implements section 165(e) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which requires the Federal Reserve to impose limits on the amount of credit exposure that such a bank holding company or foreign banking organization can have to an unaffiliated company in order to reduce the risks arising from the company's failure.

Under the final rule, a US GSIB is prohibited from having aggregate net credit exposure to another GSIB in excess of 15 percent of its tier 1 capital. For exposure of a GSIB to a non-GSIB counterparty or any single counterparty exposure of a bank holding company with total consolidated assets of $250 billion or more that is not a GSIB, that limit increases to 25 percent. The rule also applies to foreign banking organizations operating in the US with at least $250 billion in total global consolidated assets (as well as their intermediate holding companies with $50 billion or more in total US consolidated assets).

GSIBs will be required to comply with the new rule by January 1, 2020. All other firms are required to comply by July 1, 2020.

The rule, which takes the form of a new Subpart H for Regulation YY, is available here.

EXECUTIVE COMPENSATION AND ERISA

Update: 5th Circuit Confirms Decision To Vacate DOL Fiduciary Rule

After much anticipation, the US Court of Appeals for the Fifth Circuit on Thursday confirmed its earlier decision to vacate the Department of Labor's "fiduciary advice rule."

The controversial rule became effective June 2017 and significantly expanded the universe of broker-dealers and other financial advisers subject to ERISA's fiduciary standards. In March of this year, however, in *Chamber of Commerce of the USA vs. US Dep't of Labor* the Fifth Circuit determined that the DOL exceeded its authority in implementing the rule and ordered its vacatur. Following the unsuccessful attempt by various parties to intervene in the litigation and expiration of the parties' right to appeal the decision to the US Supreme Court, the Fifth Circuit gave effect to its earlier decision by issuing its mandate — officially vacating the rule.

It remains unclear how financial advisers and institutions will react to the fiduciary rule's vacatur, including those institutions that made significant changes to their business practices following its issuance. In addition, this past April the SEC issued its own "best interest" regulations, and various states have undertaken similar initiatives to regulate the investment advice provided to retirement investors. While the fiduciary rule's vacatur is no doubt welcomed by many in the financial industry, it appears that, in the near term, regulation in this area will remain uncertain.

We will continue to monitor these developments and provide additional information as it becomes available. More information on this topic is available in prior advisories: "Closer Look at the 5th Circuit Decision Vacating the Fiduciary Rule," and "5th Circuit Vacates DOL Fiduciary Rule."

UK DEVELOPMENTS

PRA Publishes Policy and Supervisory Statements on Algorithmic Trading

On June 15, the UK Prudential Regulation Authority (PRA) published a policy statement and a supervisory statement on algorithmic trading.

While the PRA's policy only directly applies to PRA-regulated and dual-regulated firms, such as banks, UK Financial Conduct Authority-regulated firms (e.g., most proprietary trading firms) may wish to take into account the PRA's expectations regarding governance and risk management in relation to their algorithmic trading activity.

The policy and supervisory statements follow the Bank of England and PRA's consultation paper, which was published in February 2018. Five responses were received to the consultation paper; the PRA stated that these were generally supportive of the proposals for the risk management and governance of algorithmic trading. The respondents also supported further clarification and alternative wording in certain areas.

The policy statement includes the PRA's feedback to the responses, along with final decisions and the rationale for related amendments to the supervisory statement, including the following changes in light of respondents' comments:

- Algorithm approval process—Each function that has a role in the approval of algorithms (including, front office, risk management, and other systems and controls functions) is expected to sign off on the risks which are relevant to them, rather than *all* the risks applicable to a specific algorithm.
- Testing and deployment—When testing algorithms, firms are only expected to document *material* differences between the test environment and production environment, rather than all differences.
- Inventories and documentation—The expectation is that inventories and documentation will be available rather than "immediately available'" to all personnel who have responsibility for the oversight of algorithmic trading.

The expectations in the supervisory statement will take effect from June 30. Any remediation work required by firms after that date will be carried out as part of the PRA's ordinary supervisory role.

The PRA policy statement and supervisory statement are available here and here respectively.

FCA Publishes List of Overseas Cooperation Agreements for Outsourcing Portfolio Management

On June 14, the UK Financial Conduct Authority (FCA) published a list of cooperation agreements it has in place in relation to the outsourcing of portfolio management. The list contains the supervisory authorities in three countries with which the FCA has cooperation agreements that meet the requirements of the Commission Delegated Regulation (EU) 2017/565 on organizational requirements and operating conditions for investment firms (MiFID Org Regulation).

The list, which includes the United States, Switzerland and Japan, can be used by firms to assess their compliance with the MiFID Org Regulation. Firms should also examine the outsourcing requirements set out separately in the MiFID Org Regulation, as well as those in the *FCA Handbook*.

The FCA's list of cooperation agreements is available here.

EU DEVELOPMENTS

Fifth Money Laundering Directive Published in Official Journal of the EU

On June 19, the text for the Fifth Money Laundering Directive (MLD5) was published in the *Official Journal of the European Union*. MLD5 will enter into force on July 9, and EU member states must transpose MLD5 into their national laws by January 10, 2020.

The introduction of MLD5 forms part of the European Commission's action plan to counter terrorist financing and money laundering, published in February 2016 (further details are available in the February 12, 2016 edition of the *Corporate & Financial Weekly Digest*).

Previous coverage of MLD5 is available in the May 18 edition of the *Corporate & Financial Weekly Digest*.

MLD5 is available here.

ESMA Confirms No Extension to LEI Introduction Period

In a press release of June 20, the European Securities and Markets Authority (ESMA) confirmed that the temporary introduction period for the use of legal entity identifiers (LEIs) will not be extended beyond July.

The six-month period was designed to allow for a smooth introduction of the revised Markets in Financial Instruments Directive (MiFID II), despite not all firms succeeding in obtaining LEIs mandated by MiFID II from its effective date of January 3. ESMA announced the introduction period in December 2017 (further details can be found in the January 5 edition of the *Corporate & Financial Weekly Digest*).

ESMA's press release of June 20 is available here.

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

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