



Financial Regulatory Developments Focus

In this week’s newsletter, we provide a snapshot of the principal US, European and global financial regulatory developments of interest to banks, investment firms, broker dealers, market infrastructure providers, asset managers and corporates.

Our European Governance & Securities Law Focus Newsletter is available [here](#).

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Compensation

Application of EU Requirements for Remuneration Policies for Small and Non-Complex Firms Confirmed

On May 14, 2015, the European Banking Authority published letters between itself and the European Commission which address the issue of application of the proportionality principle to the requirements under the EU Capital Requirements Directive and Capital Requirements Regulation. The proportionality principle states that firms should implement the remuneration provisions in a manner and to the extent that is appropriate to the firm's size, internal organization and the nature, scope and complexity of its activities. The EBA wrote to the Commission on January 8, 2015, requesting views on the approach that the EBA should adopt to interpreting the proportionality principle in its guidelines on sound remuneration policies. The EBA's letter pointed out that on a legal interpretation of CRD IV and CRR the remuneration principles must be applied proportionately, but that there was no room for any waiver for small or non-complex firms. However, the EBA noted that a waiver might be justified on policy grounds for small and non-complex firms because variable remuneration paid is low and the incentives for employees to take risks is low. The cost of implementing the requirements would however, be significant for such firms. The response from the European Commission confirmed that the EBA should follow its legal interpretation and that to do otherwise would be to take a policy decision, which is outside of its powers. The EBA launched its consultation on draft guidelines on sound remuneration policies on March 4, 2015 in which it adopts the approach suggested by the Commission. Responses to EBA's consultation are due on June 4, 2015. A review of the remuneration requirements under CRD IV is required to be undertaken by the EBA and the Commission and a report should be submitted to the European Parliament and Council, together with a legislative proposal if appropriate, by June 30, 2016. Any amendments to the current requirements may result in firms having to amend their remuneration policies, potentially adding to the costs for small and non-complex firms.

The EBA letter is available at:

<http://www.eba.europa.eu/documents/10180/1073529/2015+01+08+%28Letter+to+Ms+Michou+DG+Justice+on+Proportionality%29.pdf/838642d8-6a1f-442f-8cb6-23eaf4ba9649> and the Commission's response is available at:

<http://www.eba.europa.eu/documents/10180/1073529/2015+02+23+%28Response+EU+COM+re+proportionality%29.pdf/14888706-e787-4efb-bf41-460cd0dd0f0e>.

Derivatives

US Regulators Issue the Final Interpretation on Forward Contracts with Embedded Volumetric Optionality

On May 12, 2015, the US Commodity Futures Trading Commission and the US Securities and Exchange Commission, after consultation with the US Board of Governors of the Federal Reserve System, jointly issued an interpretation concerning forward contracts with embedded volumetric optionality. The interpretation clarifies certain aspects of the original CFTC proposal made in November 2014 and identifies when an agreement, contract or transaction would fall within the forward contract exclusions from the "swap" and "future delivery" definitions in the Commodity Exchange Act, allowing for forward contracts that provide for variations in delivery amount (i.e., contains "embedded volumetric optionality").

Although the interpretation was issued jointly, it is solely an interpretation of the CFTC and does not apply to the exclusion from the swap and security-based swap definitions for security forwards or to the distinction between security forwards and security futures products.

The CFTC's Final Interpretation is available at: <http://www.cftc.gov/ucm/groups/public/@lfederalregister/documents/file/2015-11946a.pdf> and the 'Fact Sheet' providing a summary of the interpretation is available at:

http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/volumetric_factsheet051215.pdf.

European Securities and Markets Authority Consults on Expanding the Scope of the Clearing Obligation for Interest Rate Swaps

On May 11, 2015, the European Securities and Markets Authority launched a consultation on proposed regulatory technical standards on the clearing obligation for additional classes of OTC interest rate derivatives not already included in the first RTS on the clearing obligation for interest rate swaps. The additional classes of OTC interest rate derivatives are those denominated in certain non-G4 European currencies. The additions are: (i) fixed-to-float interest rate swaps denominated in Czech Koruna,

Danish Krone, Hungarian Forint, Norwegian Krone, Swedish Krona and Polish Zloty; and (ii) forward rate agreements denominated in Norwegian Krone, Swedish Krona and Polish Zloty. The consultation also includes a summary of the clearing obligation procedure, the structure of the classes of OTC interest rate derivatives and the determination of the classes subject to mandatory clearing. Comments on the proposed RTS should be provided to ESMA by July 15, 2015.

The consultation paper is available at: <http://www.esma.europa.eu/content/Consultation-Paper-No-4-Clearing-Obligation-under-EMIR>.

Financial Services

US Office of the Comptroller of the Currency Issues Final Rule Integrating National Bank and Federal Savings Association Licensing Activities

On May 18, 2015, the US Office of the Comptroller of the Currency released a final rule integrating policies and procedures for certain corporate activities and transactions by national banks and federal savings associations. The OCC aims to make the regulatory regime for both national banks and federal savings associations more efficient and streamlined, where possible, to promote fair supervision and to promote the safe and sound operation of the institutions it supervises. The final rule makes technical and conforming changes that will allow certain provisions to apply to national banks and federal savings associations and provides clarity on OCC licensing offices' responsibilities. The rule also updates the description of the OCC supervision structure and contact information.

The published Federal Register notice, which provides a detailed summary of changes made to the proposed rule in response to comments received by the OCC, is available at: <https://www.federalregister.gov/articles/2015/05/18/2015-11229/integration-of-national-bank-and-federal-savings-association-regulations-licensing-rules> and the OCC press release is available at: <http://www.occ.gov/news-issuances/news-releases/2015/nr-occ-2015-70.html>.

European Supervisory Authorities Publish Recommendations for Improving the EU Securitization Framework

On May 12, 2015, the European Supervisory Authorities published a report setting out the outcome of their review of EU legislative disclosure and due diligence requirements for securitizations and making recommendations for removing inconsistencies across the EU framework. The recommendations constitute the ESA's response to the European Commission's consultation on securitization published in February 2015 as part of the Capital Markets Union initiative. The EU framework for structured finance instruments, covering investor due diligence, originator, issuer and sponsor retention and disclosure requirements, is established under a number of EU legislative measures including the Prospectus Directive, the Capital Requirements legislation, the Alternative Investment Fund Managers Directive, the Credit Rating Agency Regulation and Solvency II. The ESAs are recommending: (i) harmonization of due diligence requirements across investor types; (ii) that investor due diligence needs and requirements are met by the disclosure requirements; (iii) a standardized investor report which is available in a centralized public space; (iv) that loan by loan data should be provided to investors; (v) that data providers should be able to fulfill disclosure requirements provided the data owner retains responsibility for the quality of the information; (vi) that all investors should be able to conduct stress tests on all types of structured finance instruments; (vii) a review of the definitions and key terms in the legislation with a comprehensive glossary to support the framework; and (viii) mandatory disclosure requirements for all structured finance instruments admitted to trading on an EU regulated market or offered to the public.

The ESA's report is available at: <http://www.esa.europa.eu/documents/10180/950548/JC+2015+022+-+Final+JC+Report+on+securitisation.pdf>.

European Regulators Announce Delay for Delivery of Draft Technical Standards under the Market Abuse Regulation and the Markets in Financial Instruments Regulation and Directive

On May 13, 2015, ESMA published letters between itself and the European Commission which set out their agreement for the deadline for delivery by ESMA of technical standards due under the Market Abuse Regulation and the Markets in Financial Instruments Directive II to be postponed to the end of September 2015. The extension is a result of the European Commission conducting an early legal review of draft technical standards. The early legal review will assess the legality and legislative consistency of technical standards under UCITS V, the Transparency Directive, the Central Securities Depository Regulation, MAR and MiFID II.

ESMA's letter is available at: http://ec.europa.eu/finance/general-policy/docs/level-2-measures/2015-05-11-letter-maijoor-faull_en.pdf and the European Commission's letter is available at: http://ec.europa.eu/finance/general-policy/docs/level-2-measures/2015-05-11-letter-faull-maijoor_en.pdf.

Recovery & Resolution

Chairman of US Federal Deposit Insurance Corporation Delivers Speech on the Resolution of Systemically Important Financial Institutions

On May 12, 2015, Martin J. Gruenberg, Chairman of the US Federal Deposit Insurance Corporation, delivered a speech regarding the progress the FDIC has made in developing a framework for the orderly resolution of large, complex, systemically important financial institutions (SIFIs) in the event that a SIFI experiences failure or other financial distress. Among other topics, the speech addressed the FDIC's effort to strengthen the bankruptcy process and define the purpose of Orderly Liquidation Authority, a public-sector bankruptcy process prescribed by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd Frank Act) for institutions whose resolution under the US Bankruptcy Code Bankruptcy Code would pose systemic concerns.

The full text of the speech is available at: <https://www.fdic.gov/news/news/speeches/spmay1215.html>

European Banking Authority Consults on Valuation of Derivatives under the Banking Recovery and Resolution Directive

On May 13, 2015, the EBA published its proposed draft RTS on the valuation of derivatives under the Banking Recovery and Resolution Directive. Under the BRRD, a resolution authority may bail-in relevant derivative liabilities provided that the authority complies with certain conditions including exercising the bail-in power only upon or after closing out the derivatives and ensuring that derivatives subject to a netting agreement are bailed-in on a net basis following the terms of the netting agreement. Before exercising the bail-in power, a resolution authority is required to ensure that an independent valuation of the assets and liabilities of a firm is carried out. For derivative liabilities, the valuation will determine a value of those derivative liabilities at the moment of exercise of the resolution power. The EBA's proposed draft RTS (i) provides a methodology for resolution authorities to follow with the close-out amount being based on the principle of replacement cost; and (ii) sets out the approach for resolution authorities to follow when comparing the destruction in value that would arise from the close-out with the losses that those derivatives would incur in a bail-in which should be done on a case-by-case basis. The consultation closes on August 13, 2015. The EBA is required to submit the final draft RTS to the European Commission by January 3, 2016. Member states are required to implement the bail-in tool by January 1, 2016.

The EBA's consultation paper is available at: <http://www.eba.europa.eu/documents/10180/1073039/EBA-CP-201-10+CP+on+RTS+on+derivatives+valuation.pdf>.

Upcoming Events

May 29, 2015: European Commission public hearing on the revision of EMIR.

June 2, 2015: CFTC Market Risk Advisory Committee public meeting.

June 3, 2015: EBA workshop on application of proportionality principle in the EU banking supervisory framework.

June 3, 2015: Joint Committee of European Supervisory Authorities Third Consumer Protection Day 2015.

June 8, 2015: European Commission public hearing on next steps to build a Capital Markets Union.

June 11, 2015: EBA public hearing on draft ITS on the mapping of External Credit Assessment Institutions' for securitization positions.

June 17 and 18, 2015: International Organization of Securities Commissions Annual Conference.

July 2, 2015: EBA public hearing on methodologies for the valuation of derivative liabilities.

July 6, 2015: EBA public hearing on assigning risk weights to specialized lending exposures.

July 16 and 29, 2015: SEC outreach programs to aid firms in compliance with Regulation Systems Compliance and Integrity.

This newsletter is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired. If you wish to receive more information on the topics covered in this publication, you may contact your usual Shearman & Sterling representative or any of the following:

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