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FINANCIAL INSTITUTIONS ADVISORY & FINANCIAL REGULATORY GROUP NEWSLETTER

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Financial Regulatory Developments Focus

In this 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.

Click here if you wish to access our Financial Regulatory Developments website.

In this Issue (please click on any title to go directly to the corresponding discussion):

Bank Prudential Regulation & Regulatory Capital

US Federal Deposit Insurance Corporation Vice Chairman Hoenig Objects to Proposed Revisions to the Basel III Leverage Ratio Framework

On May 23, 2016, as part of his remarks at a global economic symposium in Paris, US Federal Deposit Insurance Corporation Vice Chairman Thomas Hoenig stated his objections to the Basel Committee on Banking Supervision's recently proposed revisions to the Basel III leverage ratio framework. In his speech, Hoenig noted that the banking industry has begun to lobby for special treatment or exemptions from capital requirements for a host of assets included in the leverage ratio calculation. Hoenig argued that if accepted, the effect of such proposed revisions would be to again lower acceptable industry capital standards.

Specifically, Hoenig pointed to the April 6, 2016, Basel Committee's proposal to change the Standardized Approach to Counterparty Credit Risk (SA-CCR) by applying measurement methodologies previously used for the risk-based capital ratio to the leverage ratio. Hoenig described that under the proposal, the Basel Committee could exempt from inclusion in the denominator of the leverage ratio certain types of assets that are deemed lower risk, permit more types of collateral to offset certain exposures and, thus, remove assets from the balance sheet for purposes of judging the adequacy of capital. According to Hoenig, the proposal could go so far as to reduce capital requirements against derivatives, which are intrinsically levered instruments and were at the forefront of the last financial crisis.

Hoenig argued that these and other potential changes in the computation and measurement of capital adequacy, if adopted, would convert the leverage ratio—the purpose of which is to provide a pure measure of equity capital to total assets—into a risk-based measure. Such proposed changes would "confound the purpose and obscure the conclusions of the leverage ratio." Hoenig concluded that, "[a]ssuming the leverage ratio, like the risk-based ratio, decreases reported bank assets, capital levels would trend down and would again, over time, compromise the strength of the industry, expose the public to loss, and undermine the stability of the economy."

Vice Chairman Hoenig's remarks are available at: https://www.fdic.gov/news/news/speeches/spmay2316a.pdf.

US Federal Deposit Insurance Corporation Extends Comment Period on Deposit Account Recordkeeping Proposal

On May 20, 2016, the FDIC extended the comment period for proposed recordkeeping requirements for FDIC-insured institutions with at least 2 million deposit accounts. The purpose of the proposed recordkeeping requirements is to facilitate rapid payment of insured deposits to customers if large institutions were to fail. The proposed requirements would not apply to smaller institutions, including community banks.

The proposal was published in the Federal Register on February 26, 2016, with a 90-day comment period. All comments must now be received on or before June 25, 2016. This 30-day extension will allow interested parties additional time to consider the proposal and the issues and questions posed for comment, particularly those related to the estimated cost of compliance. The FDIC has published a report prepared for the agency on the estimated cost of compliance to assist commenters.

The FDIC's extension notice is available at: https://www.fdic.gov/news/news/press/2016/pr16041a.pdf.

Federal Reserve Bank of New York Report Assesses Impact of Supervisory Guidance on Leveraged Lending

On May 16, 2016, the Federal Reserve Bank of New York published a post on its Liberty Street Economics blog assessing the impact of interagency guidance intended to curtail leveraged lending issued by the Office of the Comptroller of the Currency, Federal Reserve Board and the FDIC in March of 2013. The post shows that banks, in particular the largest institutions, cut leveraged lending while nonbanks increased such lending after the guidance. During the same period of time, nonbanks increased their borrowing from banks, possibly to finance their growing leveraged lending activity. The post notes that this evidence highlights an important challenge of macroprudential policies. Since those policies reach beyond individual banks and target risk in the entire banking system, they are more likely to trigger significant responses that may have unintended consequences.

The New York Fed post is available at: http://libertystreeteconomics.newyorkfed.org/2016/05/did-the-supervisory-guidance-on-leveraged-lending-work.html.

European Banking Authority Decision on Unsolicited Credit Assessments

On May 17, 2016, the European Banking Authority published a Decision permitting the use of unsolicited credit assessments of certain External Credit Assessment Institutions for calculating firm capital requirements. The Decision aims to harmonize regulation related to the use of solicited and unsolicited credit assessments across the European Union. Under the Capital Requirements Regulation, unsolicited credit assessments of an ECAI can be used to determine the risk weights to be assigned to assets and off-balance sheet items subject to confirmation from the EBA that the unsolicited assessment does not differ in quality from the solicited assessment of that same ECAI. The EBA is required to refuse or revoke this confirmation if the ECAI has used an unsolicited assessment to put pressure on the rated entity to place an order for credit assessment or other services. The Decision confirms that the quality of the unsolicited credit assessments of the ECAIs set out in the annex to the Decision does not differ from the quality of the solicited credit assessments of those ECAIs.

The EBA published a report providing quantitative and qualitative analysis of both solicited and unsolicited credit assessments of ECAIs. The evidence contained in the report formed the basis of the Decision. The analysis did not identify any difference in the quality of unsolicited and solicited credits ratings for a given ECAI. Also, no evidence in the analysis suggested any use of unsolicited ratings by ECAIs had put pressure on rated entities to place an order for a credit assessment or other services. The Decision will enter into force 20 days from publication in the Official Journal of the European Union.

The EBA decision is available at: http://www.eba.europa.eu/documents/10180/1466166/EBA-DC-2016-151+Decision+on+the+Use+of+Unsolicited+Credit+Assessments.pdf and the EBA Report is available at: http://www.eba.europa.eu/documents/10180/1466166/EBA+Report+on+Unsolicited+Credit+Assessments+%28Article+138+CRR%29.pdf.

European Banking Authority Sets Timeline for Provision of Advice to the European Commission on Review of EU Capital Requirements

On May 11, 2016, the EBA published a letter from it to the European Commission relating to the Calls for Advice on various aspects of the revised international regulatory capital requirements. The Commission has requested advice from the EBA on the revision of the own funds requirements for market risk, counterparty credit risk, exposures to CCPs, large exposures and the net stable funding requirement.

The EBA has begun work on the advice requested. However, the EBA does not think that the deadlines for the advice are feasible. The EBA sets out the dates by which it will be able to provide certain aspects of the advice requested. The EBA considers that it will be able to provide some analysis and information by June 1, 2016 and other points by November 1, 2016. However, the EBA is experiencing difficulties accessing the market risk data of the Basel Committee and the analysis on firms' exposures to CCPs will be impossible to provide by June 1, 2016, because the EU data does not include sufficiently granular information and the Basel data is no longer considered representative.

The EBA has also been asked to provide an overview of possible errors and inconsistencies in the CRR using the Single Rulebook Q&A tool. The EBA states that it will concentrate its efforts on those areas of CRR that would be subject to review by the end of 2016.

The EBA's letter to the Commission is available at: http://www.eba.europa.eu/documents/10180/1466081/%28EBA+2016+D+697%29%20Letter+to+O.+Guersent%2C%20DG+FISMA+re+Calls+for+Advice+to+assist+Commission+revision+-+signed.pdf/014cd6d6-afc2-4409-b704-a9237f07ff3a.

The Commission's request for advice on the NSFR is available at: http://www.eba.europa.eu/documents/10180/1162591/Call+for+advice.pdf, the Commission's request for advice on counterparty credit risk is available at: http://www.eba.europa.eu/documents/10180/1466081/%28EBA-2016-E-668%29%20Guersent%2CDG+FISMA+re+CfA+Com+implement.+counterparty+credit+risk%2CAres%282016%291900009.pdf/f26b23a2-2ddb-46f9-9cfc-1f2eba416bd3, the Commission's request for advice on exposures to CCPs is available at: http://www.eba.europa.eu/documents/10180/1466081/%28EBA-2016-E-667%29%20Guersent%2CDG+FISMA+re+CfA+COM+review+of+OF+req+for+exp+to+CCPs+%28Ares1899567%29.pdf/be14a685-e650-49b2-87f0-0a9d32167ba0 and the Commission's request for an overview of errors and inconsistences is available at: http://www.eba.europa.eu/documents/10180/1466081/ %28EBA-2016-E-677%29%20Letter+from+Mario+Nava%2C%20FISMA+to+I.+Vaillant+re+QA+tool+for+CRR+and+CRD%2C%20Ares%2816%291421682.pdf/ac8bfacc-e0c0-4dfc-b7e1-551d0ea773f9.

Competition

UK Competition and Markets Authority Consults on Proposals to Reform Retail Banking

On May 17, 2016, the Competition and Markets Authority published a provisional decision on how they propose to remedy competition issues they have identified in the supply of personal current accounts and retail banking services for small and medium-sized enterprises. The decision is part of the CMA's retail banking investigation which commenced on June 19, 2013. The CMA considers that competitive pressures in retail banking are weak and that break up or other structural changes to the banking sector are not the most effective and proportionate way to increase competition. Instead, the CMA is proposing a package of remedies, focused on innovation and the provision of information to customers, coupled with technological development.

The package of remedies includes: (i) cross-cutting foundation measures with the objective of increasing customer engagement via customer prompts, to improve transparency and make better quality information available to customers; (ii) implementation of measures to make current account switching more efficient, building on and improving the existing Current Account Switch Service; (iii) the introduction of a set of interventions aimed at overdraft users, in particular, those who have suffered from competition failures in the personal current account market; and (iv) targeted measures aimed at specific problems faced by SMEs in comparing different providers of loans and accounts.

The CMA is also exploring the nature of "free-if-in-credit" current accounts, commenting that whilst the account may suit some customers, it may not be appropriate for many customers who have overdraft accounts. The CMA also noted that unarranged overdrafts generate large revenue streams for banks whilst consumers may be unaware of the costs that they are incurring. To address this, the CMA has proposed that banks set a monthly maximum charge for unarranged overdrafts on personal accounts. Responses to the CMA's proposals are due by June 7, 2016.

The provisional decision on remedies is available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/523755/retail_banking_market_pdr.pdf.

Consumer Protection

US Financial Regulators Issue Guidance on How Banks Handle Consumer Deposit Account Discrepancies

On May 18, 2016, the US Board of Governors of the Federal Reserve System, the FDIC, the National Credit Union Administration, the OCC and the Consumer Financial Protection Bureau issued interagency guidance regarding supervisory expectations on how financial institutions should handle consumer deposit discrepancies. In some instances, when a consumer makes a deposit, the sum the bank credits to the account may be different from the total amount deposited. These deposit discrepancies can occur if the amount written on a deposit slip does not match the cash transferred into the bank or as a result of encoding errors or a poor image capture by the bank when it scans or reads a deposit slip.

The interagency guidance calls on banks to avoid or reconcile, or resolve deposit discrepancies and to adopt policies that treat consumers fairly when they make deposits and do not violate laws and regulations that apply to deposit discrepancy practices. If a financial institution fails to comply with applicable laws and regulations, including prohibitions against unfair, deceptive and abusive practices, it could open itself up to liability and possible action by an agency.

The interagency guidance is available at: http://www.consumerfinance.gov/f/documents/201605_cfpb_interagency-guidance-regarding-deposit-reconciliation-practices.pdf.

US Consumer Financial Protection Bureau Issues Rulemaking Agenda; Delays Issuance of Prepaid Card Rule

On May 18, 2016, the CFPB issued a semiannual update of its rulemaking agenda which provides an overview of the agency's major current initiatives. Among other initiatives, the CFPB notes that it expects to issue a final rule this summer to create a comprehensive set of consumer protections for prepaid financial products, such as general purpose reloadable cards and other similar products.

The CFPB issued a proposed rule in November 2014 to bring prepaid products expressly within the realm of the Electronic Fund Transfer Act and its implementing Regulation E as prepaid accounts and to create new provisions specific to such accounts. The agency also proposed to amend Regulation E and Regulation Z (which implements the Truth in Lending Act) to regulate prepaid accounts with overdraft services or credit features. The CFPB had previously announced Spring 2016 for the release of the final prepaid account rule, but the current rulemaking agenda now lists July 2016.

The CFPB's Spring 2016 rulemaking agenda is available at: http://www.consumerfinance.gov/about-us/blog/spring-2016-rulemaking-agenda/.

The proposed rule is available at: https://www.gpo.gov/fdsys/pkg/FR-2014-12-23/pdf/2014-27286.pdf.

Derivatives

US Commodity Futures Trading Commission Issues Final Cross-Border Margin Rule

On May 24, 2016, the US Commodity Futures Trading Commission issued a rule implementing a cross-border approach to the CFTC's margin requirements for uncleared swaps. The CFTC's margin rule applies to CFTC-registered swap dealers and major swap participants for which there is no prudential regulator (collectively, Covered Swap Entities or CSEs) but these rules are closely aligned with the cross-border margin requirements already adopted by the prudential regulators.

The final rule generally requires CSEs to comply with the CFTC's margin requirements for all uncleared swaps in cross-border transactions, with a limited exclusion for certain non-US CSEs. In certain circumstances, the final rule would allow CSEs to comply with comparable margin requirements in a foreign jurisdiction as an alternative means of complying with the CFTC's margin rule for uncleared swaps (Substituted Compliance) to the extent that the CFTC determines that the foreign jurisdiction's requirements are comparable to the CFTC's (Comparability Determination).

The final rule also includes special provisions to accommodate swap activities in jurisdictions that do not have a legal framework to support custodial arrangements or that do not have netting arrangements that comply with the CFTC's margin rule. Finally, the rule establishes a process for requesting Comparability Determinations, including eligibility and submission requirements, as well as the standard of review the CFTC would apply in assessing the comparability of a foreign jurisdiction's margin requirements.

The CFTC's press release is available at: http://www.cftc.gov/PressRoom/PressReleases/pr7370-16, the CFTC's final rule is available at: http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/federalregister052416.pdf and a fact sheet on the final rule is available at: http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/crossborder_factsheet052416.pdf.

Financial Crime

US Financial Crimes Enforcement Network Deputy Director El-Hindi Addresses New Customer Due Diligence Rule and Beneficial Ownership Proposal

On May 16, 2016, as part of his remarks at the Institute of International Bankers Annual Anti-Money Laundering Seminar, US Financial Crimes Enforcement Network Deputy Director Jamal El-Hindi discussed certain US Department of Treasury efforts that have been rolled out in the last several months, including: (i) the final customer due diligence (CDD) rule; (ii) draft legislation requiring legal entities to provide beneficial ownership information at the company formation stage; and (iii) the use of FinCEN's geographic targeting orders.

The CDD final rule amends existing Bank Secrecy Act regulations to clarify and strengthen obligations of covered financial institutions, specifically banks, brokers or dealers in securities, mutual funds, futures commission merchants and introducing brokers in commodities. The final rule also adds a new requirement that these financial institutions know and verify the identities of the natural persons who own, control and profit from the legal entities the financial institutions service. Finally, the rule harmonizes BSA program rules and makes explicit several components of customer due diligence that have long been expected under existing regulations. El-Hindi noted how FinCEN relied on significant engagement with industry in finalizing this rule.

El-Hindi also highlighted the draft beneficial ownership legislation that FinCEN sent to Congress on May 5, 2016, requiring companies to know and report adequate and accurate beneficial ownership information at the time of a company's formation. The legislation would authorize the Treasury Department to require that legal entities formed or qualified to do business within the US file beneficial ownership information with FinCEN, or else face penalties for failure to comply. El-Hindi noted that a remaining challenge for FinCEN is to find support for the draft legislation in Congress, among the states and within industry.

Deputy Director El-Hindi's speech is available at: https://www.fincen.gov/news_room/speech/pdf/20160518.pdf.

EU Technical Standards on Market Soundings under the Market Abuse Regulation

On May 17, 2016, the European Commission adopted Regulatory Technical Standards on the arrangements, systems and procedures for market participants disclosing inside information while conducting market soundings. The Market Abuse Regulation, which will apply across the EU from July 3, 2016, provides that when a disclosing market participant discloses inside information during a market sounding, that disclosure will be deemed to be made in the normal course of the exercise of the person's employment, profession or duty, provided that certain conditions are met. Such disclosure would not therefore constitute market abuse. The adopted RTS require disclosing market participants to establish procedures which describe the way in which market soundings are conducted, to provide certain information to the person receiving the market sounding, including, where possible, an estimate as to when the information will cease to be inside information, and to keep records of the persons who have received market soundings.

In addition, a disclosing market participant must, once he assesses that the information has ceased to be inside information, provide the receiving individual with the following information: (i) the identity of the disclosing market participant; (ii) the date and time of the market sounding; (iii) the identification of the transaction subject to the market sounding; (iv) that the disclosed information has ceased to be inside information; and (v) the date on which the information ceased to be inside information. However, there is no precise time set for such cleansing to take place. The requirements are in line with the approach adopted by the European Securities and Markets Authority following its consultation on the proposed RTS. ESMA took the view that it would not be possible to establish procedures for a situation where a transaction failed or was abandoned because the information might remain inside information. The adopted RTS is subject to scrutiny by the European Parliament and the Council of the European Union.

The adopted RTS are available at: https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2859-EN-F1-1.PDF.

Financial Services

US Office of the Comptroller of the Currency Issues Bulletin Regarding Compliance with Compliance with Securities and Exchange Commission Money Market Fund Rules

On May 19, 2016, the OCC issued a bulletin to highlight actions that national banks and federal savings associations should take and factors that banks should consider based on the US Securities and Exchange Commission's revised money market fund rules. Although these rules directly apply only to MMFs, the rules indirectly affect: (i) banks that make MMFs available to their customers through their fiduciary and custody activities; (ii) bank programs that automatically sweep funds between deposit accounts and MMFs; and (iii) banks that invest in MMFs. The MMF rules were revised in 2010 and again in 2014, and the 2014 rules are currently being phased in with a final compliance date of October 14, 2016.

The bulletin describes how the SEC's MMF rules are likely to affect banks and addresses the product and process changes that affected banks should consider. The bulletin also highlights how banks that are involved in any of these activities will likely be affected by compliance, liquidity, operational and strategic risks related to the SEC's revised rules.

The OCC bulletin is available at: http://www.occ.gov/news-issuances/bulletins/2016/bulletin-2016-17.html?_sm_au_=iVVjfvPT4jnSjDWr.

Funds

UK Regulator Consults on UCITS, SFTR and consequential Changes to the Handbook

On May 20, 2016, the Financial Conduct Authority published a consultation paper outlining proposed changes to the rules and guidance in the Client Assets sourcebook and the Collective Investment Schemes sourcebook (COLL), following the adoption of the UCITS V (the Undertakings for Collective Investment in Transferable Securities V Level 2 Regulation). The consultation paper also proposes minor changes to the Senior Management Arrangements Systems and Controls sourcebook (SYSC) and consequential amendments in COLL and the Investment Funds sourcebook (FUND) to reflect certain measures in the Securities Financing Transactions Regulation. The UCITS V Level 2 Regulation sets out additional, detailed requirements for UCITS management companies and depositaries and will apply to UCITS management firms from October 13, 2016. Requirements include, for example, minimum terms in the contract between a management company and depositary, detailed oversight, cash monitoring and safe-keeping requirements for depositories and requirements for independence between management companies and the depositaries.

The FCA has proposed consequential amendments to CASS, including disapplying certain CASS rules and guidance to ensure consistency with requirements under the UCITS V Level 2 Regulation. The FCA has also proposed guidance to signpost the conditions for meeting the independence requirements under the UCITS V Level 2 Regulation. Minor amendments to SYSC will set out circumstances where a UCITS management company must appoint a remuneration committee. Lastly, the FCA is consulting on transplanting SFTR provisions into COLL which require managers of UCITS and Alternative Investment Funds to disclose details of their use of Securities Financing Transactions and total return swaps in funds' pre-contractual documents and periodical reports to investors. Responses to the consultation are due by July 19, 2016. The FCA intends to publish a policy statement between July and September 2016.

The consultation paper is available at: http://www.fca.org.uk/static/documents/consultation-papers/cp16-14.pdf.

MiFID II

EU Legislation Amends Technical Standards for Ratio of Unexecuted Orders to Transactions

On May 18, 2016, a Commission Delegated Regulation, outlining the RTS on ratios of unexecuted orders to transactions, was adopted by the European Commission. The adopted RTS will supplement the requirements set out in the Markets in Financial Instruments Directive on algorithmic trading for both investments firms and trading venues.

The adopted RTS will impose an obligation on trading venues to calculate the ratio of unexecuted orders to transactions by each of their members and participants for every financial instrument traded under an electronic continuous auction order book or a quote-driven or hybrid trading system. The adopted RTS specify the methodology to be used by trading venues to calculate an order-to-order ratio for each member or participant and for each financial instrument traded. Trading venues must calculate the ratio of unexecuted orders for each of their members or participants at least at the end of every trading session. Such data will be expressed in terms of both volume and number, where volume is expressed as the total volume of orders in relation to the total volume of transactions and number is expressed in terms of the total number of orders in relation to the total volume of transactions. The RTS also provides a list of order types and the

relevant methodology to be used when calculating ratios. Where an order type is not listed, the RTS provides that the methodology used should be that which applies to the most similar listed order type. The RTS must still be considered by the European Parliament and the Council of the European Union before they are finalized.

The adopted RTS are available at: https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2775-EN-F1-1.PDF.

Payment Services

UK Payment Systems Regulator Consults on Application of Interchange Fee Regulation in the UK

On May 19, 2016, the UK Payment Systems Regulator published a consultation paper on the application of provisions in the Interchange Fee Regulation, which take effect in the UK from June 9, 2016. The IFR sets a limit on interchange fees on debit and credit card transactions where both the issuer and acquirer are located in the European Economic Area and outlines a number of business rule provisions that require affected parties to amend their business practices. The consultation paper is Phase II of the PSR's consultation on the IFR; the previous Phase I paper outlined the PSR's powers and procedures as the designated competent authority for monitoring and compliance of the IFR provisions. The IFR came into effect on December 9, 2015. This consultation concerns the PSR's approach to the remaining IFR provisions which will come into effect on June 9, 2016, focusing on three areas: (i) business rules; (ii) monitoring and enforcement of the IFR business rules; and (iii) amendments to the Phase I Guidance. Responses to the consultation are due by July 8, 2016.

The consultation paper is available at: https://www.psr.org.uk/sites/default/files/media/PDF/CP163-IFR-Phase-2-draft-guidance-document.pdf and further information on Phase I Guidance is available at: http://finreg.shearman.com/uk-payment-systems-regulator-final-guidance-on-ap.

UK Payment Systems Regulator Policy Statement and Guidance on Alternative Arrangements for Switching Accounts

On May 17, 2016, the UK PSR published a Policy Statement and final Guidance on the application of the Payment Accounts Regulations 2015 in respect of alternative arrangements for switching accounts. The final guidance sets out the approach under the PSR to designating alternative switching schemes and is relevant to operators of alternative switching schemes, payment service providers, consumers and regulators. The Payment Accounts Directive outlines the common regulatory standards across EU Member States to improve transparency and comparability of current account fees; facilitate current account switching; and ensure access to bank accounts with basic features. The PAR transposed the Directive into UK law and requires payment services providers to offer a switching service for payment accounts. Under the PAR the PSR has been nominated as the regulator for designating alternative switching schemes and monitoring and enforcing schemes.

The designation criteria have been amended in response to numerous comments. The PSR has altered the information requirements for applications, reporting on complaints and compensation to customers. The PSR has also made changes where applications cannot be processed in time for the September 18, 2016 deadline; where these circumstances arise, the PSR will now inform the relevant operators as soon as practicable that a decision will not be made by September 18, 2016. The PSR made no changes on its approach to monitoring compliance of designated schemes. Operators that wish to be designated under the PAR by the appropriate deadline should submit their application by June 10, 2016.

The Policy Statement is available at: https://www.psr.org.uk/sites/default/files/media/PDF/PS162-the-application-of-the-PARs.pdf and the Final Guidance is available at: https://www.psr.org.uk/sites/default/files/media/PDF/PARs-final-guidance.pdf.

Recovery & Resolution

EU Technical Standards on the Valuation of Derivatives for Bail-in Adopted by the European Commission

On May 23, 2016, the European Commission adopted RTS on the valuation of derivatives for the purpose of bailing-in derivative liabilities. The Bank Recovery and Resolution Directive provides that 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 the value of those derivative liabilities at the moment of exercise of the resolution power. The adopted RTS provide a methodology 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, principles for determining the point in time at which the value of a derivative should be established and measures for establishing the value of classes of derivatives. The Commission has adopted the final draft RTS submitted by the EBA without any substantive amendments. The adopted RTS will now be considered by the European Parliament and Council of the European Union.

The adopted RTS are available at: http://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2967-EN-F1-1.PDF.

EU Technical Standards on Minimum Requirement for Own Funds and Eligible Liabilities Adopted by the European Commission

On May 23, 2016, the European Commission adopted RTS on criteria relating to the methodology for setting the Minimum Requirement for Own Funds and Eligible Liabilities (MREL). MREL is the European equivalent of US TLAC. There are some differences between the adopted RTS and the final draft RTS submitted by the European Banking Authority with its Opinion published in February 2016 which expressed disagreement with certain of the European Commission's proposed amendments to the final draft RTS submitted in July 2015.

In its Opinion, the EBA had agreed that the RTS should not set a minimum contribution to loss absorption and recapitalization of 8% of total liabilities and own funds for systemic institutions but proposed that the RTS should require resolution authorities to assess whether the burden-sharing requirements set out in the Bank Recovery and Resolution Directive would be met. The EBA had also disagreed with the change to the transitional compliance period to "as short as possible" on the basis that it would create legal uncertainty for firms. The adopted RTS do not take into account the EBA's concerns on the Commission's amendments.

The adopted RTS must still be approved by the European Parliament and the Council of the European Union and be published in the Official Journal before they can enter into force.

The RTS are available at: http://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2976-EN-F1-1.PDF.

The Opinion is available at: http://www.eba.europa.eu/documents/10180/1359456/EBA-Op-2016-02+Opinion+on+RTS+on+MREL.pdf.

EU Guidelines on Business Reorganization Plans Following a Bail-In

On May 20, 2016, the EBA published translations of its Guidelines on business reorganization plans following a bail-in. The BRRD requires a firm that has been recapitalized through a bail-in to produce a reorganization plan that sets out how the firm will be restored to long-term viability and to submit progress reports twice annually throughout the reorganization period.

The EBA's Guidelines provide the minimum criteria that the business reorganization plan must fulfill for approval by a resolution authority and set out how national regulators and resolution authorities should assess whether the business reorganization plan is credible, realistic and consistent with other business plans prepared by the firm in parallel. The Guidelines will apply to resolution authorities and national regulators from August 20, 2016.

The Guidelines are available at: http://www.eba.europa.eu/documents/10180/1312845/EBA-GL-2015-21+GLs+on+Business+Reorganisation+Plans.pdf/76c11392-79dc-4db4-bbe5-772133d2f715.

EU Regulation Supplementing Bank Recovery and Resolution Directive Published

On May 20, 2016, Commission Delegated Regulation on deferral of extraordinary ex post contributions to a resolution financing arrangement and the criteria for determining critical functions was published in the Official Journal of the European Union. The Regulation sets out the assessment that a resolution authority should undertake of a firm's application for deferral from the obligation to contribute to extraordinary ex post contributions to a resolution financing arrangement, including an assessment of the impact on the firm's financial position. The Regulation also provides the criteria for determining whether a function is a critical function. The BRRD requires firms to identify all of the critical functions within the firm or its group in the firm's recovery plan to aid the assessment of how a critical function could be continued when the firm is under financial stress. The Regulation applies from June 9, 2016.

The Delegated Regulation is available at: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016R0778&from=EN

Financial Conduct Authority Consults on Wind-Down Planning

On May 23, 2016, the FCA launched a consultation on the proposed Guidance on wind-down planning. The proposed Guidance is intended to assist firms regulated only by the FCA (i.e. it would not apply to any firm authorized by the Prudential Regulation Authority) to develop an approach to wind-down planning. The FCA is not prescribing an approach to winding down and is not requiring firms to create wind-down plans. The FCA's proposed Guidance covers the concept and process of wind-down planning, including the time horizon of the wind down period, the people involved in the planning process, potential wind-down scenarios, resource assessment, operational analysis including communication plans and a quick reference guide for smaller firms. Responses to the FCA's consultation are requested by July 22, 2016.

The proposed Guidance is available at: http://www.fca.org.uk/static/fca/documents/guidance-consultations/gc1605.pdf.

UK Regulator Provides Feedback on Recovery Plans

On May 19, 2016, the FCA published initial feedback on the recovery plans submitted by investment firms regulated by it. Recovery plans are required to be submitted by banks and certain investment firms to national regulators under the EU Bank Recovery and Resolution Directive. The FCA regulates those investment firms in the UK that are not designated by the Prudential Regulation Authority. The FCA identifies key areas for improvement in recovery plans, including identifying and analyzing internal and external interconnectedness, identifying and calibrating recovery plan indicators, demonstrating that recovery plan options are comprehensive and credible, capturing the minimum range of scenarios or properly explaining why certain scenarios are not applicable, correctly defining core business lines and critical functions and designing appropriate communication strategies for crisis management. The FCA expects firms to implement appropriate remedial actions without delay where gaps and deficiencies have been identified.

The FCA's feedback is available at: http://www.fca.org.uk/news/recovery-plans-initial-observations.

Upcoming Consultation Deadlines

June 2, 2016: UK Government Consultation on proposed amendments to anti-money laundering and counter-terrorist finance legislation

June 2, 2016: HM Treasury Consultation on UK Government's proposed secondary annuities market due to be introduced in April 2017

June 3, 2016: Federal Reserve Board Notice of Proposed Rulemaking on Single-Counterparty Credit Limits for Domestic and Foreign Bank Holding Companies

June 3, 2016: Federal Reserve Board Notice for Proposed Agency Information Collection Activities regarding New Data Items for Regulatory Reporting by Foreign Banking Organizations

June 3, 2016: Basel Committee Consultation on Standard Measurement Approach for Operational Risk

June 3, 2016: PRA Consultation on Risk-Based Levies for the Financial Services Compensation Scheme Deposit Class

June 7, 2016: UK CMA Provisional Decision on Remedies to Reform Retail Banking

June 10, 2016: Basel Committee Proposal for a Revised Pillar 3 Disclosure Framework

June 14, 2016: European Commission Consultation on Harmonizing EU Insolvency Regimes under its Capital Markets Union Action Plan

June 21, 2016: FCA Consultation on Proposed Rules and Guidance for the Secondary Annuity Market due to start in April 2017

June 22, 2016: EBA Consultation on Changes to Calculation of Interest Rate Risk on Capital Requirements

June 25, 2016: FDIC Notice of Proposed Rulemaking on Recordkeeping for Timely Deposit Insurance Determination

June 29, 2016: PRA Consultation on Underwriting Standards for Buy-to-Let Mortgage Contracts

July 6, 2016: Basel Committee Consultation paper on proposed revisions to the Basel III leverage ratio framework

July 6, 2016: EBA Consultation on amendments to the RTS for determining proxy spread and the specification of a limited number of smaller portfolios for credit valuation adjustment risk under the CRR

July 8, 2016: UK PSR Consultation on the application of provisions in the Interchange Fee Regulation

July 13, 2016: FCA Report on Investment and Corporate Banking Strategy

July 14, 2016: FCA and PRA Consultation on Proposed Implementation of the Enforcement Review and the Green Report

July 15, 2016: Basel Committee Consultation on Guidelines for Prudential Treatment of Problem Assets

July 19, 2016: FCA Consultation on UCITS, SFTR and consequential Changes to the Handbook

July 22, 2016: FCA Consultation on Proposed Guidelines for Wind-Down Planning

July 22, 2016: US Federal Reserve Board, OCC, FDIC, NCUA, FHFA and SEC Notice of Proposed Rulemaking on Incentive-Based Compensation Restrictions

July 29, 2016: PRA Consultation on future reporting of balance sheet, statement of profit and loss and forecast capital data

August 4, 2016: EBA Consultation on risks and benefits associated with the innovative uses of consumer data by Financial Institutions

August 5, 2016: US Federal Reserve Board, OCC and FDIC Notice of Proposed Rulemaking to Establish the Net Stable Funding Ratio

August 5, 2016: US Federal Reserve Board Notice of Proposed Rulemaking on Restrictions on Qualified Financial Contracts of Systemically Important US Banking Organizations and the US Operations of Systemically Important Foreign Banking Organizations; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions

August 11, 2016: EBA Consultation on LCR Disclosure and Disclosure of Liquidity Risk Management

August 12, 2016: PRA Consultation on Pillar 2 Liquidity Risk Requirements

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:

Contacts

BARNEY REYNOLDS
T: +44.20.7655.5528
barney.reynolds@shearman.com
London

REENA AGRAWAL SAHNI
T: +1.212.848.7324
reena.sahni@shearman.com
New York

RUSSELL D. SACKS
T: +1.212.848.7585
rsacks@shearman.com
New York

THOMAS DONEGAN
T: +44.20.7655.5566
thomas.donegan@shearman.com
London

DONNA M. PARISI
T: +1.212.848.7367
dparisi@shearman.com
New York

NATHAN J. GREENE
T: +1.212.848.4668
ngreene@shearman.com
New York

GEOFFREY B. GOLDMAN
T: +1.212.848.4867
geoffrey.goldman@shearman.com
New York

JOHN ADAMS
T: +44.20.7655.5740
john.adams@shearman.com
London

CHRISTINA BROCH
T: +1.202.508.8028
christina.broch@shearman.com
Washington, DC

TIMOTHY J. BYRNE
T: +1.212.848.7476
tim.byrne@shearman.com
New York

JAMES CAMPBELL
T: +44.20.7655.5570
james.campbell@shearman.com
London

AYSURIA CHANG
T: +44.20.7655.5792
aysuria.chang@shearman.com
London

UXSHELY CHOTAI
T: +44.20.7655.5569
uxshely.chotai@shearman.com
London

TOBIA CROFF
T: +39.02.0064.1509
tobia.croff@shearman.com
Milan

ANNA DOYLE
T: +44.20.7655.5978
anna.doyle@shearman.com
London

SYLVIA FAVRETTO
T: +1.202.508.8176
sylvia.favretto@shearman.com
Washington, DC

MAK JUDGE
T: +65.6230.8901
mak.judge@shearman.com
Singapore

HERVÉ LETRÉGUILLY
T: +33.1.53.89.71.30
hletreguilly@shearman.com
Paris

OLIVER LINCH
T: +44.20.7655.5715
oliver.linch@shearman.com
London

BEN MCMURDO
T: +44.20.7655.5906
ben.mcmurdo@shearman.com
London

JENNIFER D. MORTON
T: +1.212.848.5187
jennifer.morton@shearman.com
New York

BILL MURDIE
T: +44.20.7655.5149
bill.murdie@shearman.com
London

BRADLEY K. SABEL
T: +1.212.848.8410
bsabel@shearman.com
New York

JENNIFER SCOTT
T: +1.212.848.4573
jennifer.scott@shearman.com
New York

KOLJA STEHL
T: +49.69.9711.1623
T: +44.20.7655.5864
kolja.stehl@shearman.com
Frankfurt / London

ELLERINA TEO
T: +44.20.7655.5070
ellerina.teo@shearman.com
London