EU Financial Regulatory Reform: The End of Trading As We Know It?

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New EU Legislation Financial Markets

- The EU has recently introduced and is on the verge of introducing new rules and regulations pertaining to the financial services industry.
- These rules and regulations cover virtually all types of financial markets, all types of financial services and products and all types of market participants.
- They deal with public offerings, trading (OTC and on regulated venues), market access, financial instruments, conduct and prudential requirements, funding, clearing, recovery and resolution and payment services.
Aim of New EU Financial Legislation

• The aim of this new EU legislation is to offer greater protection to customers, more in particular to retail investors and consumers, and making markets safer, more transparent and more efficient

• The new legislation also seeks to improve competition by opening up markets or market segments to new entrants thus fostering greater efficiency and cost reduction
Possible Impact New EU Financial Legislation

- The key question is whether these new rules and regulations will indeed contribute to financial stability, better products and lower costs or whether they will result in impediments for trading.

- Another question is what the cross-border effects of these rules will be. Will they contribute to the creation of more integrated financial markets or will they effectively block market participants from other jurisdictions from competing and offering their services on a cross-border basis?
EU Financial Regulatory Developments

- Benchmark Regulation
- PRIIPs Regulation
- MiFID II/MiFIR
- PSD2
- EU Banking Reforms
- Capital Markets Union:
  - Securitisation Regulation
  - Framework Covered Bonds
- EMIR
- Recovery and Resolution CCPs and Insurers
Benchmark Regulation

- Benchmark Regulation deals with the use of benchmarks and aims to safeguard the accuracy and integrity thereof.
- It introduces requirements for benchmark administrators and contributors but also for benchmark users, such as banks, investment firms and investment funds.
- Requirements include a prohibition to make use of unregistered benchmarks and the obligation to prepare robust written plans for the scenario that a benchmark would change or become unavailable.
- Benchmark Regulation applicable in EU Member States as from 1 January 2018.
PRIIPs Regulation

- Packaged Retail and Insurance-based Investment Products Regulation (PRIIPs Regulation) obliges market participants that offer financial products containing an investment component to retail investors to provide a standardised short form of disclosure document, the PRIIPs Key Information Document (KID).
- PRIIPs Regulation applies to investment products under MiFID II, investment funds under AIFMD and UCITS and insurance products with an investment component.
- PRIIPs Regulation applicable in EU Member States as from 1 January 2018.
MiFID II/MiFIR

- MiFID II/MiFIR is the updated and recast version of the Markets in Financial Instruments Directive
- MiFID II/MiFIR applicable in EU Member States as from 3 January 2018
- MiFID II/MiFIR provides new rules on, amongst others:
  - trading venues (OTF, for non-equities)
  - cost transparency: splitting payments for research and trading commission (unbundling)
  - pre- and post-trade transparency: detailed reporting and record keeping requirements
  - independent investment advice
MiFID II/MiFIR (2)

• Other new rules pertain to:
  - trading obligation: moving trades in certain derivatives from over-the-counter (OTC) to regulated venues
  - inducements/remuneration
  - product development: higher standards for investment products
  - best execution
  - knowledge and expertise of employees
  - asset segregation
  - (title transfer) financial collateral arrangements
  - client classification
PSD2

• Revised Payment Services Directive, applicable in EU Member States as from 13 January 2018
• PSD2 widens the scope of the PSD by covering new services provided by third party providers (TPPs), such as account information services providers (AISPs) and payment initiation services providers (PISPs)
• PSD2 allows TPPs to access client accounts held at other payment services providers solely on the basis of client consent
• RTS to PSD2 introduces strict requirements for customer authentication and exchange of information between payment account providers and AISPs and PISPs
EU Banking Reforms

• Package of proposals – dated 23 November 2016 – for new legislation enhancing the rules of the Banking Union
• Not constituting a complete overhaul of the current legislative framework, but with huge consequences
• Proposals consist of amendments to:
  - CRD IV/ CRR: “CRD V/CRR II” - Minimum Leverage Ratio (3%) and NSFR
  - SRM and BRRD - MREL and TLAC
  - introduction of Basel III and IV:
    * re-assessment of IRB-approach
    * backstops for risk weighted capital requirements
Capital Markets Union

• Action Plan EC – dated September 2015 – containing a package of 33 proposals for new legislation aimed at enhancing the possibilities for companies, in particular SME enterprises, to get access to capital markets and obtain alternative funding and for investors to provide such funding
• Action Plan provides, for instance, for an amendment of the Prospectus Directive and legal frameworks for securitisation and covered bonds respectively

• CMU to be implemented in the summer of 2019
Securitisation/Covered Bonds

- Securitisation Regulation and related CRR Amending Regulation
- Aim to facilitate actual risk transfers by harmonising and reforming existing rules on due diligence, risk retention and disclosure and creating a new framework for simple, transparent and standardised securitisations and implementing the revised Basel rules on securitisation
- Approved by European Parliament on 8 November 2017 and Council on 20 November 2017, applicable in EU Member States as from 1 January 2019
- Legal Framework Covered Bonds: proposal EC to be expected in Q1 2018
EMIR (1)

- RTS Risk Mitigation Uncleared Derivatives in force on 4 January 2017
- RTS obliges FCPs and NFCPs\(^+\) to post sufficient collateral (margin) in bilateral derivative transactions and contains rules on VM, IM and Eligible Collateral
- RTS further provides for risk management requirements (electronic confirmations, portfolio valuation, daily marking to market) and additional capital requirements for broker-dealers subject to CRD IV/CRR
- VM and IM requirements to become applicable over time from 4 February 2017 until 1 September 2020
EMIR (2)

• EC proposal for a revision of EMIR dated 4 May 2017
  • Proposal includes:
    - extension temporary clearing exemption for pension schemes for another 3 years
    - relief reporting requirements for NFCPs
    - removal backloading requirement
    - further rules on segregation
  • EC proposal for a revision of EMIR dated 13 June 2017
  • Proposal includes:
    - stringent requirements for systematically relevant CCPs
    - two tier system for qualified third country CCPs
Recovery and Resolution

- EC proposal for regulation recovery and resolution CCPs
- Set up along the lines of BRRD and SRM for banks and large investment firms
- Proposal to be expected in the course of 2018

- EC proposal for directive recovery and resolution insurers
- Set up along the lines of BRRD and SRM for banks and large investment services
- Proposal to be expected in the course of 2018
Impact Benchmark and PRIIPs Regulation

• Benchmark Regulation may have an impact on trading, due to:
  - the prohibition to make use of unregistered benchmarks
• Benchmark Regulation may also have effects outside the EU, due to:
  - the fact that non-EU index providers must be qualified under the applicable third country regime
• PRIIPs Regulation may have an impact on trading, due to:
  - the detailed KID transparency requirements
• PRIIPs Regulation may also have effects outside the EU, due to:
  - its worldwide scope
Impact MiFID II/MiFIR

- MiFID II/MiFIR will have a huge impact on trading, due to:
  - stringent conduct requirements for investment firms
  - detailed reporting requirements (65 fields!) and record keeping requirements (5 years)
  - complexity and unclarity of some of the rules

- MiFID II/MiFIR will also have effects outside the EU, due to:
  - its international scope and the lack of equivalence and recognition agreements with third countries
Impact PSD2

- PSD2 will have a huge impact on payment services, due to:
  - AISPs and PISPs being allowed to access payment accounts of clients held at other payment services providers solely on the basis of the accountholder’s consent and without the consent of the account provider being required.
Impact proposed EU legislation

- The proposed EU Banking Reforms, the proposals for a Capital Markets Union, the proposals for EMIR and the envisaged recovery and resolution regimes for CCPs and insurers will certainly have an impact on trading and will also have cross-border effects.
- Consider in this connection the envisaged higher risk weighting of and capital requirements for mortgage loans, standardisation of securitisation transactions, possible relocation of CCPs that pose a significant systemic risk to the EU, contractual bail-in, resolution stay.
Role P.R.I.M.E. Finance

• Possible role of P.R.I.M.E. Finance and its experts in support of legislative efforts to contribute to legal transparency and financial stability:
  - educating legislators, market and prudential regulators, judges and market participants in understanding and interpreting complex financial products
  - come up with proposals if existing or proposed rules could be made simpler and less burdensome without reducing safety and soundness
  - support legal research and engage with academia on research projects