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9 October 2019

Financial Regulation Monthly Breakfast Seminar

Overview



An update on Brexit

An update on benchmarks, including preparations for LIBOR transition

The FCA's recent multi-firm review on research unbundling and corporate access

An update on the European Commission's review of the Market Abuse Regulation



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An update on Brexit
Anne Mainwaring

No-deal readiness

- HM Government – No-Deal Readiness Report
- UK Parliament written questions and answers
 - Financial Services: Written question – 290966
- Market Watch 61

Andrew Bailey speech – preparing for Brexit in financial services; the state of play

- Clear policy:
 - FCA intends to preserve open markets and not limit access
 - FCA will not compromise protection for consumers wherever they are domiciled
 - FCA will take a pragmatic approach to issues as they arise and will use forbearance generously but appropriately

Day 1 approach

UK FIRMS	TEMPORARY PERMISSION FIRMS	EU FIRMS WITHOUT TEMPORARY PERMISSION
<ul style="list-style-type: none">• UK onshored legislation• Temporary Transitional Relief (“TTR”) until end of next year• TTR is subject to exceptions	<ul style="list-style-type: none">• All UK rules that currently apply plus those currently reserved to home state• Substituted compliance will be permitted in relation to the latter where compliance with home state rules is sufficient	<ul style="list-style-type: none">• Contractual Continuity Regime - automatic for EEA firms that passport into the UK and fail to notify to enter the TPR but still have regulated business in the UK to run off

Temporary Transitional Relief – UK firms

- Gives the FCA the ability to delay or phase in changes to regulatory requirements made under the EU Withdrawal Act
- Intention is to provide a transitional relief period up to the end of next year
- This means that firms generally do not need to prepare now to meet the changes to their UK regulatory obligations resulting from onshoring

Temporary Transitional Relief – UK firms

- However TTR will not apply in all areas
- In these areas compliance is required from Day 1
- How to determine whether TTR applies
- Primary Markets Bulletin No. 24

Outstanding issues

- Share trading obligation EU and UK
 - Overlapping share trading obligations
 - For those shares where the trading obligations overlap, “market liquidity would be damaged to no good end”
 - Could be solved by an equivalence agreement between the UK and the EU
 - “The UK authorities would do this, and take the issue away. The EU have said to date they will not do that”

Outstanding issues

- Share trading obligation (continued)
 - Read across from Swiss experience with trading equivalence
 - Shows equivalence can be lost
 - Otherwise read across is limited as this issue related to trading of Swiss shares, whereas in this context the issue relates to the trading of non-UK shares

Outstanding issues

- Share trading obligation (continued)
 - “We could however use our transitional powers to mitigate disruption caused by the overlap. The extent to which we choose to use these powers to minimise the overlap is a genuine choice, but we cannot fully mitigate the damage done by the STOs. For example, due to the EU’s STO, EU investors will not be able to access liquidity on EU shares listed in London. You do not need to guess that our preference would be to emphasise open markets, free trade, and the principle of best execution being achieved by markets not by regulators, where we can. We would like to think that the EU would follow the same approach but we need to find a way through this together that does not create barriers and distortions on either side. We stand ready to enter into dialogue with our European counterparts before we finalise our approach”

Outstanding issues

- Derivatives Trading Obligation
 - Unless the UK and EU find each other's regulatory regimes as equivalent, EU firms will not be able to meet the EU's DTO by using UK trading venues to trade in-scope derivatives, and vice versa
 - Currently all OTC derivatives subject to the EU DTO have their main pool of liquidity on a UK venue. Without action, EU firms may lose access to UK liquidity pools and liquidity would be fragmented, harming both EU and UK markets
 - The FCA considers an equivalence agreement between the UK and EU is the best solution
 - "In the absence of equivalence, we will work with EU regulators to try and avoid firms being caught by both the EU and UK DTOs. We believe the right outcome would be for regulators to ensure that where there is a conflict of law, we are clear which rule firms should follow. But this would only work if EU regulators were able to do the same"

Outstanding issues

- Clearing
 - Temporary recognition of UK CCPs expires in March 2020
 - If no further clarity is given on the regulatory status of UK CCPs after this date, the contracts that EU members clear with UK CCPs will need to be closed out or transferred by March 2020. This process would need to begin by the end of this year resulting in significant costs for EU firms as well as potentially straining market capacity
 - FCA suggested solution: EU permanent recognition of UK CCPs

Outstanding issues

- Uncleared derivatives
 - EU has not reciprocated in putting in place measures to allow firms to service existing uncleared derivatives between UK and EU counterparties
 - FCA notes certainty is required to minimise disruption

Outstanding issues

- Data exchange
 - Firms
 - Regulators
- Contract repapering

The EU perspective

- ESMA's Data Operational Plan
- Impact of no-deal on application of MiFID
- Use of UK data in ESMA databases



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An update on benchmarks, including preparations for
LIBOR transition
Becky Critchley

Overview

- Brexit and BMR
 - Helpful transitionals in the onshored BMR
- BMR update
 - 1 January 2020 – all EU administrators of significant and non-significant benchmarks must have applied for authorisation / registration
- LIBOR transition
 - Transfer to risk-free rates



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The FCA's recent multi-firm review on research
unbundling and corporate access
Nicola Higgs

Key points

- Overall, the FCA found that the rules have produced “positive changes” and have had the intended effect of improving scrutiny of research costs and lowering costs for investors
- However, the FCA acknowledges that valuation and pricing models are still evolving, and says it plans to carry out further work in this area in 2020 or 2021

What's in the detail?

- Research being paid for out of managers' own funds: use of research payment accounts is rare
- Research budgets have fallen by between 20% - 30% on average
- “Clear gap” between the best and worst practices
- Must show rationale and consistent judgement on how to value research
- No evidence of inflated trade commissions
- Managers say they get what they need - UK SMEs not getting enough coverage

What's in the detail?

- Low “entry level” pricing for research accompanied by higher fees for more exclusive interactions could be a reasonable pricing strategy overall
- Grey areas: what benefits other than research can be accepted from third parties in compliance with the inducements rules, in particular in terms of what can constitute a minor non-monetary benefit. (Note: trade association events; research trial periods and issuer-sponsored research; brokers’ contributions to consensus forecasts)
- Wide variation in prices for corporate access



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An update on the European Commission's
review of MAR
Rob Moulton

Background

- MAR always envisaged a review on some specific technical points
 - Always likely to be added to
- 20 March 2019 EC letter to ESMA
 - Published 14 May 2019
- 3 October 2019 ESMA consultation
 - Industry already in action e.g. AFME Working Group

ESMA – spot FX

- Asked to consider whether spot FX should be in scope of MAR
- For
 - “only the national legislative framework for one Member State enables the relevant NCA to act [on] ancillary activities carried out in connection with regulated activities”
 - Interlinkages between spot FX and FX derivatives
- Against
 - FX Global Code of Conduct “has already achieved progress in promoting higher standards”
 - Practical difficulties without being in scope of MiFID e.g. who is the issuer?

ESMA – benchmarks

- Definitions in MAR and BMR “broadly the same”
 - Although BMR definition includes financial contracts and investment funds
- BMR subject to a review by the EC due 1 January 2020
- Lack of sanctions in MAR against administrators and submitters
 - May be a systems and controls rule breach by administrators
 - Could add a MAR reference to submitters

ESMA – buy-backs

- Issuers should only report to NCA of most liquid market
- Only a subset (10) of data fields (41) currently reported are needed
- Data should be published on an aggregated daily basis
 - Aggregated daily volume
 - VWAP

ESMA – inside information definition

- Q13 – “Have market participants experienced any difficulties with identifying what information is inside information?”
- Pre-hedging issues
 - “request for quote often meets the definition of inside information”
 - “pre-hedging, then declining to provide a quote”
 - “broker could fill a client order from existing inventory but trades aggressively”
 - “trading in a way which disadvantages another broker who executes the order for that client”
 - Must provide “sufficient transparency and disclosure” of pre-hedging

ESMA – market soundings

- “ESMA is of the view...DMPs are under the obligation to follow the requirements set out in Article 11”
- ESMA is assessing whether some types of transactions should be excluded
- ESMA considering whether “prior to the announcement of the transaction” wording should be revised
- ESMA considering whether DMPs should always be required to use a recorded line
 - No consent

ESMA – insider lists

- Should only include persons who accessed information, not those who could have accessed it but didn't
- Permanent insiders
 - Not a substitute for event based lists
 - Only very senior employees, e.g. CEO, CFO, their Executive Assistants, Chairman, Head of Legal, Chief Compliance Officer, Chief Technical Officers

ESMA - PDMRs

- ESMA thinks the regime broadly working well
- The €5,000 and €20,000 limits are understood
- The 20% fund holding limit “functioning well”
- May expand the closed period requirements to “persons closely associated with PDMRs”

Publications

- [Research Unbundling - FCA Finds Rules Working Well](#)
- [Key Emerging Regulatory Issues and Focus Areas for Institutional Asset Managers](#)
- [US Secondary Sanctions are a 'Mandatory Provision' of English Law](#)

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Questions?