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Ad Hoc Capital Markets and OTC Derivatives Seminar

Capital Markets Union: clearing, insolvency and listing package

- an initial in-depth analysis of the proposal of the European Commission

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Overview

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- On 7 December 2022, European Commission proposed measures to facilitate further development of EU capital markets in following areas:

  - **Listing Act**:
    - amends **Prospectus Regulation** (making it easier and cheaper for companies to get listed);
    - amends **Market Abuse Regulation** (MAR) (providing greater legal clarity about what information needs to be disclosed by companies and reinforcing supervisory cooperation between market authorities);
    - amends **Markets in Financial Instruments Regulation** (MiFIR);
    - amends **MiFID II** and repeals **Listing Directive**;
    - introduces new directive on **multiple-vote share structures** (allowing companies to use multiple-vote share structures when first listing on SME Growth Markets)

Overview (cont'd)

- On 7 December 2022, European Commission proposed measures to facilitate further development of EU capital markets in following areas:
  - **Clearing**
    - Regulation amends European Market Infrastructure Regulation (EMIR), Capital Requirements Regulation (CRR) and Money Market Funds (MMF) Regulation;
    - Directive amends Capital Requirements Directive (CRD), Investment Firm Directive (IFD), and Directive on Undertakings for Collective Investment in Transferable Securities (UCITS)
  - **Corporate Insolvency**
    - New Insolvency Directive harmonising legal provisions related to insolvency proceedings

Aims and Objectives

- Background
  - EU capital markets remain fragmented and underdeveloped in size;
  - Many EU companies find it too burdensome to get listed on stock exchanges
- Aims and Objectives
  - make public markets more attractive for EU companies and **facilitate access to capital for SMEs**;
  - introduce technical adjustments to EU rulebook that **reduce issuers' regulatory and compliance costs**;
  - streamline **listing process** and enhance **legal clarity**, while ensuring appropriate level of investor protection and market integrity;
  - enhance production and distribution of **investment research on midcaps and SMEs**; and
  - address **pre-IPO regulatory barriers and unequal opportunities** for companies when choosing governance structures

Aims and Objectives

- Benefits
  - For **companies**
    - Significant **cost reductions** and **boost to IPOs** in EU
      - Estimated € 67 million savings per year from simpler prospectus rules;
      - Estimated € 100 million per year from lower compliance costs for listed companies;
      - Multiple-vote right shares could potentially **increase** number of **IPOs** in EU **by 20%**;
      - For SMEs enhanced visibility and more proportionate sanctioning regime for minor infringements (*e.g.* MAR infringements)
  - For **investors and supervisors**
    - Easier navigation of corporate information;
    - More efficient supervision due to simpler and clearer listing rules

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Section 2:

Amendments to Prospectus Regulation

New exemptions for secondary issuances of securities fungible with securities already admitted to trading

- Existing exemption from prospectus requirement if new securities represent, over 12-month period, less than 20% of securities already admitted to trading **expanded** to apply to **both public offer of securities** and their **admission to trading** and companies that have had securities traded on **SME growth market;** applicable threshold increased from 20% to **40%**;
- **New exemption** for companies issuing securities fungible with securities already admitted to trading on regulated market or SME growth market continuously for at least 18 months. Instead of prospectus, these companies must prepare and file **short summary document** (including statement of compliance with ongoing and periodic reporting, transparency obligations etc.);
- Exemption does **not** apply to
  - secondary issuances of securities **not fungible** with securities already admitted to trading; and
  - secondary issuances by companies that are in **financial distress** or that are going through **significant transformation** (*e.g.* change of control resulting from takeover, merger or division)
- who must prepare **EU Follow-on Prospectus**.

Exemptions based on offer size

- New unique harmonized (single) threshold of EUR 12 million;
  - Below this threshold, public offers of securities are exempted from obligation to publish prospectus, provided that those offers do not require passporting.
  - Threshold is based on total consideration of aggregated offers made by same issuer in EU over 12-month period.
- Member States allowed to require national disclosure documents for smaller offers, unless these documents constitute disproportionate or unnecessary burden;
- Temporarily adopted threshold of EUR 150 million for offers of non-equity securities by credit institutions made permanent

More standardised and streamlined prospectus requirements for primary issuances

- New **standardised format and sequence of disclosure** for
  - prospectus (specifics to be set out in delegated acts); and
  - summary (prescribed order of information, increase of maximum length by three pages where there are multiple guarantors and use of charts, graphs or tables);
- **300-page** limit for **IPO prospectuses** (not applicable for non-equity *etc.*);
- **Mandatory incorporation by reference;**
- **Supplements** to reflect new **financial information** which is incorporated by reference **no longer required;**
- **Streamlined risk factors;**
- Investors can **no** longer request **paper copies** of the prospectus;
- Prospectuses can be prepared in **English only**, except for summary;
- IPO: Minimum **period** between publication of prospectus and end of **offer three** days

Streamlined risk factors

- Risk factors to be limited to those that are **specific to issuer** and to **securities**, and **material** for making informed investment decision, as corroborated by prospectus content;
- **No generic risk factors**, those that only serve as disclaimers or do not give sufficiently clear picture of specific risk factors of which investors are to be aware;
- **Ranking** requirement **removed**: risk factors that have been assessed as most material no longer need to be mentioned first;

Changes to supplement requirements

- Supplement to base prospectus must not be used to introduce **new type of security** for which necessary information has not been included in base prospectus;
- **ESMA to develop guidelines** specifying circumstances in which supplement is to be considered to introduce new type of security, *e.g.* whether only brand new financial product or mere tweaks within existing financial product would count;
- Proposal makes permanent previously temporary change that extended from two to **three working days** period within which investors may **withdraw their subscriptions** for securities after issuers publish supplement;
- Clarification of which investors financial intermediaries must contact when supplement is published and extension of deadline to **contact** those **investors** from publication day of supplement to end of following working day;
- Proposal clarifies that, if supplement is published, financial intermediary is required to inform only those investors who are its clients and agreed to be **contacted by electronic means**.

Simplification of universal registration document regime

- Frequent issuer status after **one year** of approval instead of two
- Can be prepared in English only

Mandatory incorporation by reference

Article 19 para (1), as revised:

Article 19

Incorporation by reference

1. Information ~~may~~ that is to be ~~incorporated~~ included ~~by reference~~ in a prospectus ~~where it has been previously or simultaneously published electronically, drawn up in a language fulfilling the requirements of Article 27 and where it is contained in one of the following documents:~~pursuant to this Regulation and the delegated acts adopted on the basis of it, shall be incorporated by reference in that prospectus where it has been previously or simultaneously published electronically, drawn up in a language fulfilling the requirements of Article 27 and where it is contained in one of the following documents:

(a) documents which have been approved by a competent authority, or filed with it, in accordance with this Regulation or Directive 2003/71/EC;

(b) the documents referred to ~~in points (f) to (i) of Article 1(4) and points (e) to (h) and point (j)(v) of the first subparagraph of Article 1(5);~~in Article 1 (4), first subparagraph, points (db) and (f) to (i), and in Article 1(5), first subparagraph, points (ba) and (e) to (h);

(c) regulated information;

(d) annual and interim financial information;

(e) audit reports and financial statements;

(f) management reports as referred to in Chapter 5 and 6 of Directive 2013/34/EU ~~of the European Parliament and of the Council (12);~~including, where applicable, the substainability reporting;

(g) corporate governance statements as referred to in Article 20 of Directive 2013/34/EU;

(h) reports on the determination of the value of an asset or a company;

(i) remuneration reports as referred to in Article 9b of Directive 2007/36/EC of the European Parliament and of the Council (13);

(j) annual reports or any disclosure of information required under Articles 22 and 23 of Directive 2011/61/EU of the European Parliament and of the Council (14);

(k) memorandum and articles of association.

Article 19, new para. 1a:

1a. Information that is not to be included in a prospectus may still be incorporated by reference in that prospectus on a voluntary basis, where it has been previously or simultaneously published electronically, drawn up in a language fulfilling the requirements of Article 27 and where it is contained in one of the documents referred to in paragraph 1, first subparagraph.

Supplements to reflect new financial information which is incorporated by reference no longer required

Article 19, new para. 1b:

1b. An issuer, an offeror or a person asking for admission to trading on a regulated market shall not be required to publish a supplement pursuant to Article 23(1) for updating the annual or interim financial information incorporated by reference in a base prospectus that is still valid under Article 12(1).

Preamble:

(37) To remove unnecessary costs and burdens and to increase the efficiency and effectiveness of the incorporation into the prospectus of information by reference, companies should not be required to publish a supplement for updating the annual or interim financial information incorporated by reference in a base prospectus which is still valid.

Integration of ESG related disclosure into prospectus

The powers for the EC in Art. 13 Article for the adoption of delegated acts have been extended to consider in the relevant issuer and product disclosure annex the following ESG related aspects:

'(f) whether the issuer is required to provide sustainability reporting, together with the related assurance opinion, in accordance with Directive 2004/109/EC and Directive 2013/34/EU of the European Parliament and of the Council[52];

(g) whether non-equity securities offered to the public or admitted to trading on a regulated market are advertised as taking into account environmental, social or governance (ESG) factors or pursuing ESG objectives.

Detailed explanation:

The empowerment to the Commission to adopt delegated acts to set out the format and content of the prospectus is amended accordingly (Article 13(1) and Annexes I to III of the Prospectus Regulation). It is furthermore clarified that those delegated acts should also consider (i) for issuers of equity securities, whether the issuers is subject to the sustainability reporting under the upcoming Corporate Sustainability Reporting Directive[34], and (ii) for issuers of non-equity securities, whether those non-equity securities are marketed as taking into account ESG factors or pursuing ESG objectives.

Recitals:

Regulation (EU) 2019/980[53].

(23) Due to the growing importance of sustainability considerations in investment decisions, investors are increasingly considering information on environmental, social and governance (ESG) matters when taking informed investment decisions. It is therefore necessary to prevent greenwashing, by establishing ESG-related information to be provided, where relevant, in the prospectus for equity or non-equity securities offered to the public or admitted to trading on a regulated market. That requirement should, however, not overlap with the requirement laid down in other Union law to provide that information. Companies that offer equity securities to the public or seek the admission to trading of equity securities on a regulated market should therefore incorporate by reference in the prospectus, for the periods covered by the historical financial information, the management and consolidated management reports, which include the sustainability reporting, as required by Directive 2013/34/EU of the

[53] Commission Delegated Regulation (EU) 2019/980 of 14 March 2019 supplementing Regulation (EU) 2017/1129 of the European Parliament and of the Council as regards the format, content, scrutiny and approval of the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Commission Regulation (EC) No 809/2004 (OJ L 166, 21.6.2019, p. 26).

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European Parliament and of the Council[54]. Moreover, the Commission should be empowered to set out a schedule specifying the ESG-related information to be included in prospectuses for non-equity securities that are advertised as taking into account ESG factors or pursuing ESG objectives.

New EU Follow-on Prospectus

- Replaces simplified disclosure regime for secondary issuances and EU Recovery Prospectus;
- New prospectus format on permanent basis **for secondary issuances** for **equity and non-equity securities**;
- Applies to **secondary issuances that do not fall under an exemption** (*e.g.* where fungibility criterion is not fulfilled);
- **Voluntary prospectus is possible** for issuances that fall under exemption;
- **Standardised format and sequence** containing the information set out in Annex IV or V;
- Specific **short-form summary** (e.g. maximum length of 5 pages)
- **Reduced scrutiny period** of 5 days for competent authorities
- **50-page limit** for prospectuses related to share or equivalent securities; and
- Can be prepared in language customary in international finance (except for summary)

New EU Growth Issuance Document

- New **EU Growth issuance document** replaces the EU Growth Prospectus
- For SMEs, issuers the securities of which are listed or to be listed on an SME growth market and offers from small unlisted companies up to EUR 50 Mio.
- Standardised format and sequence containing the information set out in Annex VII or VIII;
- Specific **short-form summary** (e.g. maximum length of 5 pages)
- 75-page limit for shares or equivalent securities;
- Can be prepared in language customary in international finance (except for summary) ;
- For whom required (mandatory) and when?
  - SMEs and issuers whose securities are admitted or to be admitted to trading on SME growth market;
  - If they do not already have securities admitted to trading on regulated market (in that case EU Follow-on prospectus is possible);
  - offers from small unlisted companies up to EUR 50 Mio. Over a period of 12 months; and
  - If no exemption from obligation to publish prospectus for public offers of securities otherwise applies

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Section 3:

Amendments to Market Abuse Regulation

Narrowed scope of duty to disclose inside information

- Applies to protracted processes (*i.e.* multi-staged events, such as mergers);
- Disclosure obligation does not cover intermediate steps but only completion events;
- Prohibition of insider dealing continues to apply for intermediate steps as notion of inside information is not amended;
- Obligation to ensure confidentiality of inside information until moment of disclosure;
- Immediate disclosure required in case of leakage

Clarification of what information needs to be disclosed when

- Delegated act to be adopted with non-exhaustive list of:
  - relevant information categories; and
  - disclosure timing guidance for each category, *i.e.* indication of moment when disclosure is expected to occur

Clarification of conditions for issuers to delay disclosure

- General condition that delay should not mislead public replaced by specific conditions that inside information must:
  - not be materially different from issuer's previous public announcements on matter;
  - not regard fact that issuer's previously announced financial objectives are not likely to be met; and
  - not be in contrast with market's expectations based on signals issuer had sent.
- Competent authority to be notified immediately after issuer **makes decision to delay**, rather than immediately after disclosure.

Sanctions

- Administrative sanctions for infringements of disclosure requirements to be proportionate to issuer size
- Pecuniary sanctions by default calculated as percentage of issuer's total annual turnover

Simplification of insider lists

- For (all) issuers, less burdensome list of "permanent insiders" => list to include all persons having regular access to inside information relating to that issuer due to their function and position within insider (such as members of administrative, management and supervisory bodies, executives who make managerial decisions affecting future developments and information) ;
- Alleviation does **not** apply to those acting on issuer's behalf (*e.g.* accountants, lawyers and rating agencies) ;
- Member States can opt out and require preparation of "full insider list"
  - by issuers whose securities have been admitted to trading on regulated market for at least five years
  - if justified by market integrity concerns

Changes to management transaction notices

- Threshold for reporting raised from EUR 5,000 to EUR 20,000;
- Dispensation to local competent authorities to raise from EUR 20,000 to EUR 50,000 at national level;
- Newly exempted management transactions during closed period:
  - Employees' schemes not involving shares
  - Transactions where no investment decision is taken by management

12. Without prejudice to Articles 14 and 15, an issuer may allow a person discharging managerial responsibilities within it to trade or to make transactions on its own account or for the account of a third party during a closed period as referred to in paragraph 11 ~~either~~:

(a) on a case-by-case basis due to the existence of exceptional circumstances, such as severe financial difficulty, which require the immediate sale of shares; or

(b) due to the characteristics of the trading involved for transactions made under, or related to, an employee share or saving scheme and employees' schemes concerning financial instruments other than shares, qualification or entitlement of shares and qualifications or entitlement of financial instruments other than shares, or transactions where the beneficial interest in the relevant security does not change; or~~.~~

(c) where those transactions or trade activities do not imply active investment decisions by the person discharging managerial responsibilities, or result from external factors or third parties, or are the exercise of derivatives based on predetermined terms.

Clarification of safe-harbour nature of market sounding procedure

- Requirements are only "safe-harbour" for disclosing market participants ("**DMPs**") but no presumption of unlawful disclosure if DMPs opt to carry out market soundings without complying with requirements;
- DMPs must consider whether process involves inside information and make written record of conclusions and underlying reasons and provide it to competent authorities upon request;
- Definition of market sounding expanded to include cases where deal is eventually not announced

Clarifications to exceptions for buy-back programmes and stabilisation

- Simplification of reporting mechanism that issuer must follow for its buy-back programme to benefit from MAR exceptions;
- Issuers must report information only to competent authority of most relevant market in terms of liquidity for their shares and publicly disclose only aggregated information

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Section 4:

New Directive on Multiple-Vote Share Structures

General provisions

- Only applies to adoption of multiple-vote share structures by companies seeking first-time listing on SME growth market in one or more Member States;
- Minimum harmonisation Directive: Member States may adopt or retain national provisions allowing companies to adopt multiple-vote share structures in other situations;
- Member States must ensure that companies may adopt multiple-vote share structures when seeking first-time admission to trading of shares on SME growth market;
- Member States to leave flexibility to companies to adopt multiple-vote share structures before seeking admission of shares to trading. In those cases, Member States may set out that enhanced voting rights associated with multiple vote shares can only be used after admission to trading has occurred

Minimum safeguards

- Member States must ensure fair and equal treatment of shareholders and provide for adequate protection of interests of company and shareholders that do not hold multiple-vote shares by introducing appropriate safeguards;
- Minimum level of harmonisation for safeguards:
  - Ensuring that company's decision to adopt multiple-vote share structure and any subsequent decision to modify multiple-vote share structure that affects voting rights are taken by general shareholders' meeting and approved by qualified majority as specified in national law;
  - Limiting voting weight of multiple-vote shares on exercise of other shareholders' rights, in particular during general meetings, by introducing either:
    - maximum weighted voting ratio and requirement on maximum percentage of outstanding share capital that total amount of multiple-vote shares can represent;
    - restriction on exercise of enhanced voting rights attached to multiple-vote shares for voting on matters to be decided at general meeting of shareholders and that require approval by qualified majority.

Additional safeguards

- Additional safeguards that Member States may consider adopting:
  - provisions to avoid enhanced voting rights attached to multiple-vote shares
    - being transferred to third parties or continuing to exist upon death, incapacitation or retirement of original holder of multiple-vote shares (transfer-based sunset clause);
    - continuing to exist after designated period of time (time-based sunset clause);
    - continuing to exist upon occurrence of specified event (event-based sunset clause); and
  - requirement to ensure enhanced voting rights cannot be used to block adoption of decisions by general shareholders' meeting aimed at preventing, reducing or eliminating adverse impacts on human rights and environment related to company's operations

Disclosure requirements

- Disclosure requirements for companies that adopted multiple-vote share structures apply both at point of admission to trading of company's shares and recurrently on annual basis;
- Required disclosure categories:
  - structure of share capital;
  - restrictions on transfer of securities;
  - restrictions on voting rights;
  - characteristics of multiple-vote shares; and
  - presence of other control-enhancing mechanisms

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Section 5:

Changes to EMIR

Proposal for a Regulation amending

- the European Markets Infrastructure Regulation (EMIR),
- the Capital Requirements Regulation (CRR) and
- the Money Market Funds Regulation (MMFR)

Overview

Role of derivatives

- Derivatives play an important role in the economy, but they also bring certain risks. These risks were highlighted during the 2008 financial crisis, when significant weaknesses in the OTC derivatives markets became evident.
- In 2012 the EU adopted the European market infrastructure regulation (EMIR). The aims were to
  - increase transparency in the OTC derivatives markets
  - mitigate credit risk
  - reduce operational risk

Enhancing transparency

- EMIR introduces reporting requirements to make derivatives markets more transparent.
- Under the regulation detailed information on each derivative contract needs to be reported to trade repositories and made available to supervisory authorities
- trade repositories have to publish aggregate positions by class of derivatives, for both OTC and listed derivatives

Mitigating credit risk

- EMIR introduced rules to reduce the counterparty credit risk of derivatives contracts
- In particular, all standardised OTC derivatives contracts must be centrally cleared through CCPs

Proposal for a Regulation amending EMIR, the Capital Requirements Regulation (CRR) and the Money Market Funds Regulation (MMFR)

Key Points:

The proposed measures will, in view of the Commission:

- make the European Union's clearing landscape more attractive
- enable central counterparties (CCPs) to expand their products/introduce new products quicker and easier
- further incentivise EU market participants to clear and build liquidity at EU CCPs instead of third-country CCPs
- help build a safe and resilient clearing system, by strengthening the EU supervisory framework for CCPs
  - for example, by increasing the transparency of margin calls, so that market participants (including energy firms) are in a better position to predict them
- reduce excessive exposures of EU market participants to CCPs in third countries, particularly for derivatives identified as substantially systemic by the European Securities and Markets Authority
- require all relevant market participants to hold active accounts at EU CCPs for clearing at least a portion of certain systemic derivative contracts
- improve the management of financial stability risks in the EU

Why is the Proposal needed?

- The proposed package aims to improve the central clearing system in the EU, making EU CCPs more efficient and attractive.
- It addresses the vulnerabilities that stem from the current excessive reliance on certain third-country CCPs deemed to be substantially systemic for the EU, ensuring that the EU has a competitive and efficient clearing system that is safe and resilient.
- The Commission, as well as the European Securities Markets Authority (ESMA), have previously expressed concerns about the possible financial stability risks associated with the excessive reliance of EU financial markets on a few CCPs based in the UK.
- In addition, the energy crisis has affected the real economy in the EU and had ramifications on certain areas of financial markets, including clearing.
- EU CCPs will benefit from being able to quickly bring new products to the market and consequently meeting the demands for new clearing offers by clearing members and clients. In addition, they will be able to adapt the models they use to measure the risks they face more quickly, allowing a timely management of such risks.
- Clearing members (mainly banks) will benefit from extended, faster clearing offers by CCPs, thereby providing more choices on where to clear.

What will happen to Firms that are under the Clearing Obligation?

- Firms subject to the clearing obligation will be required to clear at least a portion of certain systemic derivatives through active accounts at EU CCPs.
- The specific derivatives are the following:
  - Interest rate derivatives denominated in euro and Polish zloty
  - Credit default swaps
  - Short-term interest rate derivatives denominated in euro
- The requirement to clear such specific derivatives in an EU CCP can be met via accounts opened directly at an EU CCP or indirectly through a clearing member (further specified through regulatory technical standards)
- It is expected that firms subject to this requirement will have to bear some costs, due to the loss of some netting benefits, reduced collateral optimisation and some (limited) additional operational costs due to maintaining several accounts in the EU and in third-country CCPs.
- At the same time, several EU market participants already have accounts at CCPs in the EU, so the additional costs for them would be negligible.

Changes to certain Provisions concerning Equivalence

The proposal entails two different aspects related to the equivalence framework under EMIR

1. **Intragroup transactions**: Simplification of the framework for intragroup transactions:
   - provides more legal certainty to market participants and international partners by deleting the condition of an equivalence decision to benefit from intragroup exemption
   - in order to benefit from the intragroup exemption, entities located in third countries should be in a country that is not identified as having deficiencies in terrorist financing and anti-money laundering regulations, or considered as a non-cooperative jurisdiction for tax purposes
2. **Recognition of third-country CCPs**: Introduction of the possibility for the Commission to take a more proportionate approach when adopting an equivalence decision for a third country by waiving the requirement to have an effective equivalent system for recognising third-country CCPs.
   - this will be possible only when it is deemed to be in the interests of the Union and particularly when the risks involved in clearing in that third country are low

33 EMIR Changes in Detail (1)

1. Intragroup transactions

EMIR provides for a framework exempting intragroup transactions (domestically and cross-border) from the clearing obligation under Article 4 and the margin requirements under Article 11 of that Regulation. In order to provide more legal certainty and predictability concerning the framework for intragroup decisions, the need for an equivalence decision is replaced by a list of jurisdictions for which an exemption cannot be granted. Article 3 should therefore be amended to replace the need for an equivalence decision with a list of third countries for which an exemption should not be granted and Article 13 should be deleted. These third countries should be those that are listed as a high-risk third country that has strategic deficiencies in its regime on anti-money laundering and counter terrorist financing.

2. Clearing obligation

Article 4 is amended to introduce an exemption from the clearing obligation where an EU financial counterparty or a non-financial counterparty, subject to the clearing obligation under EMIR, enters into a transaction with a pension scheme arrangement established in a third country which is exempted from the clearing obligation under its national law.

33 EMIR Changes in Detail (2)

3. Clearing obligation for financial counterparties

Article 4a is amended and as a result, when calculating the position towards the thresholds under Articles 4a of EMIR, only those derivative contracts that are not cleared at a CCP authorised under Article 14 or recognised under Article 25 of that Regulation should be included in that calculation.

4. Active account

A new Article 7a is introduced in order to address the risks associated with excessive exposures of EU clearing members and clients to third-country CCPs that provide clearing services identified as of substantial systemic importance by ESMA, and thereby ensure the integrity and stability of the EU financial system. This article requires financial counterparties and non-financial counterparties that are subject to the clearing obligation, to hold active accounts, directly or indirectly, at CCPs established in the EU, to clear at least a certain proportion of the services identified as of substantial systemic importance at EU CCPs, and to report on that. This requirement should lead to a reduction of excessive exposures in substantially systemic clearing services offered by the relevant Tier 2 CCPs, to the extent necessary to safeguard financial stability. ESMA, in cooperation with EBA, EIOPA and the ESRB and after consulting the ESCB, shall establish the details of the calibration of the activity to be maintained in these active accounts and the reporting requirements of transactions cleared at such active accounts. The Commission is empowered, where ESMA undertakes an assessment pursuant to Article 25(2c), to adopt a delegated act to amend the list of categories of derivative contracts which are subject to the active account requirement by adding or removing categories from that list.

33 EMIR Changes in Detail (3)

5. Information on clearing services

A new Article 7b is introduced to require clearing members and clients that provide clearing services, to inform their clients about the possibility to clear a relevant contract at an EU CCP.

Article 7b also introduces an obligation for EU clearing members and EU clients to report to their competent authority the scope of clearing undertaken at non-EU CCPs. To ensure that the information to be submitted is specified and provided in a harmonised manner, ESMA is required to develop draft regulatory and implementing technical standards specifying the required information.

6. Reporting obligation

Article 9 is amended to remove the exemption from reporting requirements for transactions between counterparties within a group, where at least one of the counterparties is a non-financial counterparty, in order to ensure visibility on intra-group transactions.

33 EMIR Changes in Detail (4)

7. Clearing obligation for non-financial counterparties

Article 10 is amended to require ESMA to review and clarify, where appropriate, the regulatory technical standards relating to the criteria for establishing which OTC derivative contracts are objectively measurable as reducing risks, the so-called hedging exemption, and the designation of thresholds in order to properly and accurately reflect the risks and characteristics in derivatives, and to consider whether the classes of OTC derivatives, namely interest rate, foreign exchange, credit and equity derivatives, are still the relevant classes. ESMA is encouraged to consider and provide, amongst others, more granularity for commodity derivatives.

Article 10 is also amended to require, when calculating the positions towards the thresholds, that only those derivative contracts that are not cleared at a CCP authorised under Article 14 or recognised under Article 25 should be included in that calculation.

8. Risk-mitigation techniques for OTC derivative contracts not cleared by a CCP

Article 11 is amended to provide non-financial counterparties that become subject for the first time to the obligation to exchange collateral for OTC derivative contracts not cleared by a CCP, with an implementation period of 4 months in order to negotiate and test the arrangements to exchange collateral.

EBA may issue guidelines or recommendations to ensure a uniform application of the risk-management procedures in cooperation with the other ESAs.

33 EMIR Changes in Detail (6)

9. Authorisation of a CCP and extension of activities and services

Articles 14 and 15 are amended to clarify that authorised CCPs should also be able to be authorised to provide clearing services and activities in non-financial instruments, in addition to their authorisation to provide clearing services and activities in financial instruments.

10. Authorisation of a CCP, extension of activities and services and procedure for granting and refusing authorisation

Articles 14, 15 and 17 are amended in order to ensure the relevant procedures for CCPs to expand their product offer are shorter, less complex and more certain in their outcome for EU CCPs. The competent authorities are required to swiftly acknowledge receipt of the application assessing whether the documents required for the authorisation or extension have been provided by the CCP. To ensure that EU CCPs submit all required documents with their applications, ESMA is required to develop draft regulatory and implementing technical standards specifying such documents, their format and content. In addition, the CCP should submit all documents to a central database where they should be shared instantaneously with the CCP's competent authority, ESMA and the college. Furthermore, the CCP's competent authority, ESMA and the college, during a predefined assessment period, should interact with each other and ask the CCP questions to ensure a flexible and cooperative process.

33 EMIR Changes in Detail (7)

11. Non-objection and ex-post procedures for granting a request fo extension of activities or services

A new Article 17a is introduced to provide CCPs with the possibility to undergo a non-objection procedure, instead of a regular procedure, for the authorisation of additional services or activities a CCP intends to offer which do not increase the risks for the CCP. Article 17a states which additional services and activities are considered non-material and are therefore to be approved through such a non-objection procedure by that CCP's competent authority and for which the CCP may start to offer before the decision is received by the CCP's competent authority. Apart from these cases, a CCP may also ask its competent authority for the non-objection procedure to apply where it considers that the proposed additional service or activity would not increase its risks.

12. Procedure for seeking the opinion from ESMA and the college

A new Article 17b is introduced in order to clarify the scope and process to be followed where a competent authority seeks the opinion of ESMA and the college before adopting a supervisory decision for which the CCP does not submit an application, e.g. regarding a CCP's compliance with requirements on record-keeping or conflicts of interests.

13. College and opinion of the college

Articles 18 and 19 are amended to further foster a cooperative supervision of CCPs on an ongoing basis. The college is therefore requested to also issue an opinion where a competent authority considers withdrawing a CCP's authorisation as well as when a competent authority conducts the annual review and evaluation of that CCP. ESMA should manage and chair the college for each EU CCP and be granted the right to vote.

33 EMIR Changes in Detail (8)

14. Withdrawal of authorisation

Article 20 is amended to require the competent authority to consult ESMA and the members of the college before the CCP's competent authority takes a decision to withdraw, or restrict the scope of, a particular service or activity , except where a decision is required urgently.

15. Annual review

Article 21 is amended to indicate that the annual review should consider the services or activities the CCP provides or the model changes the CCP uses based on a non-objection procedure. Also, the frequency of the report resulting from the review is further specified (the report should be delivered, at least, on a yearly basis on a given date). Moreover, it is specified that the report is subject to the opinion by ESMA and the college.

33 EMIR Changes in Detail (9)

17. Joint Supervisory Teams, non-objection procedures for granting a request of extension of activities or services and review and evaluation

A new Article 23b is introduced in order to increase the cooperation of the authorities involved in the supervision of authorised EU CCPs by establishing joint supervisory teams. The tasks of joint supervisory teams include: (i) to provide input to the CCP's competent authority within the context of the non-objection procedure for extending a CCP's existing authorisation, (ii) to assist in establishing the frequency and depth of a CCP's review and evaluation and (iii) to participate to on-site inspections.

18. Joint Monitoring Mechanism

A new Article 23c is introduced in order to establish a cross-sectoral monitoring mechanism bringing together Union bodies involved in the supervision of EU CCPs, clearing members and clients. ESMA, in cooperation with the other bodies participating to the Joint Monitoring Mechanism, is to submit an annual report to the European Parliament, the Council and the Commission on the results of the monitoring activity in order to inform future policy decisions. ESMA may also issue guidelines or recommendations if it considers that competent authorities fail to ensure clearing members'and clients'compliance with the active account requirement or it identifies a risk to the EU financial stability.

33 EMIR Changes in Detail (10)

19. Emergency situation

Article 24 is amended to further enhance the role of ESMA in an emergency situation by enabling ESMA to convene meetings of the CCP Supervisory Committee, either on its own initiative or upon request, potentially with an enlarged composition, to coordinate effectively competent authorities'responses. ESMA is also empowered to ask, by simple request, information from market participants in order to perform its coordination function in these cases. ESMA may also issue recommendations directed to the CCP's competent authorities.

20. CCP Supervisory Committee

Article 24a is amended in order for ESMA to map and identify the supervisory priorities, to consider cross-border risks including interconnections, interlinkages and concentration risks. In addition, Article 24a is amended to allow central banks of issue to attend all meetings of the CCP Supervisory Committee for EU CCPs and for the relevant authorities for clients and EU bodies to be invited, where appropriate.

33 EMIR Changes in Detail (11)

21. Recognition of a third-country CCP

Article 25 is amended to clarify that where ESMA undertakes a review of a third-country CCP's recognition, that CCP should not be obliged to submit a new application but should provide ESMA with all information necessary for such review.

Article 25 is amended to introduce the possibility for the Commission, where in the interests of the Union, to take a proportionate approach and waive the requirement for a third country to have an effective equivalent system for the recognition of third-country CCPs when adopting an equivalence decision for that third-country.

To ensure that cooperation arrangements are proportionate, ESMA should tailor them to different jurisdictions based on the CCP(s) established in the respective jurisdiction. For Tier 2 CCPs the cooperation arrangements should cover a broader range of information to be exchanged between ESMA and the relevant third-country authorities and with an increased frequency.

Article 25 is further amended in order for cooperation arrangements to include the right for ESMA to also be informed where a Tier 2 CCP is required to enhance its preparedness in financial distress, by, for example, establishing a recovery plan or where an authority in such a third country establishes resolution plans. ESMA is also to be informed of the aspects relevant for the financial stability of the EU in relation to emerging crisis.

33 EMIR Changes in Detail (12)

22. Ongoing compliance with the conditions for recognition

Article 25b is amended to clarify that Tier 2 CCPs are to provide ESMA with information on a regular basis.

23. Withdrawing of recognition and public notice

Article 25p and 25r are amended to clarify that ESMA can withdraw the recognition where a non-EU CCP infringes any of the requirements under EMIR and can issue a public notice where fees are not paid or where a CCP has not taken a remedial action requested by ESMA.

24. Information to competent authorities

Article 31 on the notification on changes to the management of a CCP is amended to clarify the procedure in relation to the sharing of information and issuing ESMA and college opinions.

33 EMIR Changes in Detail (13)

25. ESMA and college opinions

Articles 32, 35, 41 and 54 are amended to clarify the requests for ESMA and college opinions.

26. Participation requirements and general provisions regarding organisational requirements

Articles 26 and 37 are amended to clarify that CCPs should not be allowed to be clearing members of other CCPs nor accept to have other CCPs or clearinghouses as clearing members or indirect clearing members.

27. Participation requirements

Article 37 is amended to set out that where a CCP has on-boarded or intends to on-board non-financial counterparties as clearing members, that CCP should ensure that certain additional requirements on margin requirements and default funds are met. Non-financial counterparties should not be permitted to offer client clearing services and only be allowed to keep accounts at the CCP for assets and positions held for their own account. The competent authority for the CCP should report to ESMA and the college on a regular basis on the appropriateness of accepting non-financial counterparties as clearing members. ESMA is mandated to prepare a draft RTS on the elements to be considered when determining the access criteria and might issue an opinion on the appropriateness of such arrangements following an ad-hoc peer review.

33 EMIR Changes in Detail (14)

28. Transparency

Article 38 is amended in order to ensure that clients and indirect clients have better visibility and predictability of margin calls. Clearing members and clients providing clearing services should ensure transparency towards their clients.

29. Margin requirements

Article 41 is amended to ensure that CCPs continuously revise the level of their margins while taking into account any potentially procyclical effects of such revisions, reflecting current market conditions and considering the potential impact of their intraday margin collections and payments on the liquidity position of their participants.

30. Liquidity risk controls

Article 44 is amended to better reflect the entities whose default could materially affect a CCP's liquidity position by requiring a CCP to take into account the liquidity risk generated by the default of at least two entities, including clearing members and liquidity service providers.

33 EMIR Changes in Detail (15)

31. Collateral requirements

Article 46 is amended to allow bank guarantees and public guarantees to be considered eligible as highly liquid collateral provided that they are unconditionally available upon request within the liquidation period and making sure a CCP takes them into account when calculating its overall exposure to the bank. Furthermore, a CCP should take into account any potential procyclical effects when revising the level of the haircuts it applies to the assets it accepts as collateral.

32. Review of models, stress testing and back testing

Article 49 is amended in order to ensure the relevant procedures for CCPs to apply model changes are shorter, less complex and more certain in their outcome. The competent authorities are required to swiftly acknowledge receipt of the application for the model change by assessing whether the documents required have been provided by the CCP. To ensure that EU CCPs submit all required documents with their applications, ESMA is required to develop draft regulatory and implementing technical standards specifying such documents, their format and content. In addition, the CCP should submit all documents to a central database where they should be shared instantaneously with the CCP's competent authority, ESMA and the college. Article 49 also introduces the possibility to undergo a non-objection procedure, instead of a regular procedure, for the validation of model changes considered not significant and specifies which changes are considered significant. Where a CCP considers the change as non-significant it may start to use the model change before the decision is received by the CCP's competent authority.

35 EMIR Changes in Detail (16)

33. Amendments to the Reports and Review

Article 85 is amended to require the Commission to submit by [5 years after the entry into force of this Regulation] a report assessing the application of this Regulation. The Commission is required to submit that report to the European Parliament and to the Council, together with any appropriate proposals. In addition, the current requirement to deliver a report by 2 January 2023 is removed. ESMA is also required to submit a report by [3 years after the entry into force of this Regulation] on its staffing and resources.

34. Amendments to the Capital Requirements Regulation (CRR)

Article 382(4) of the CRR is amended in order to align relevant provisions in the CRR with the changes suggested in this proposal. The amendment adjusts the scope of the own funds requirement for credit valuation adjustment risk, notably by clarifying which intragroup transactions can be excluded from that requirement.

35. Amendments to the Money Market Funds Regulation (MMFR)

Article 17 of the MMFR23is amended regarding the provisions on investment policy regarding counterparty risk limits. It excludes centrally cleared derivative transactions from the counterparty risk limits set out in Article 17(4) and 17(6)(c) of the MMFR. Furthermore, a definition of a CCP is added in Article 2, specifically as a new point (24).

Changes to CRR, MMFR, UCITS, CRD and IFD (1)

- **CRR** (Capital Requirements Regulation): CCR amendment adjusts scope of own funds requirement for credit valuation adjustment risk, notably by clarifying which intragroup transactions can be excluded from requirement.
- **MMFR** (Money Market Funds Regulation): Amendment to MMFR provisions on investment policy regarding counterparty risk limits excludes centrally cleared derivative transactions from counterparty risk limits.

Proposal is complemented by a proposal for a Directive introducing a limited number of changes to

- the CRD (Capital Requirements Directive)
- the IFD (Investment Firms Directive) and
- the UCITS Directive (Undertakings for Collective Investment in Transferable Securities Directive)

as regards the treatment of concentration risk towards CCPs and the counterparty risk on centrally cleared derivative transactions. These amendments are necessary to ensure that the objectives of this EMIR review are achieved as well as to assure coherence. The two proposals should therefore be read in conjunction.

Changes to CRR, MMFR, UCITS, CRD and IFD (2)

In detail:

- **UCITS:** UCITS are allowed to invest in both OTC and exchange traded derivatives, but UCITS Directive imposed regulatory limits on counterparty risk only to OTC derivative transactions, regardless of whether derivatives were centrally cleared.

  → Change: To ensure alignment with applicable regulations, establish level playing-field between exchange traded and OTC derivatives and better reflect risk reducing nature of CCPs in derivative transactions, new Directive amends UCITS Directive to eliminate counterparty risk limits for all derivative transactions that are centrally cleared by authorised or recognized CCP.

- **CRD** (Capital Requirements Directive) **and IFD** (Investment Firms Directive): Proposes amendments to Capital Requirements Directive (CRD) and Investment Firms Directive (IFD) to encourage institutions, investment firms, and their competent authorities to address excessive concentration risk that may arise from their exposures towards CCPs and reflect broader policy objective of safer, more robust, efficient and competitive market for EU central clearing services.
- New Directive amends CRD to require institutions to include concentration risk arising from exposures towards CCPs, in particular those offering services of substantial systemic importance for EU or one or more Member States, in institutions' strategies and processes for evaluating internal capital needs and adequate internal governance. Request for management body to develop concrete.
- New Directive amends CRD mandating EBA to issue guidelines on uniform inclusion of concentration risk arising from exposures towards central counterparties in supervisory stress testing.
- New Directive amends CRD to facilitate possibility for competent authorities to address specifically concentration risk arising from institutions' exposures towards CCPs, by adding concrete supervisory power to address such risk.
- Parallel amendments to IFD proposed for investment firms.

Further updates on EMIR

- Commission Delegated Regulation (EU) 2022/2310:
  - Regulation increasing the commodity clearing threshold from €3 billion to €4 billion, enabling energy companies to enter into more over-the-counter transactions without being subject to margin requirements. This is for the benefit of non-financial counterparties only, and another review of the clearing thresholds may be forthcoming.

- Commission Delegated Regulation (EU) 2022/2311
  - Regulation widening, on a temporary 12-month basis and subject to conditions, the list of eligible assets that can be used as collateral to meet margin calls to include public guarantees and uncollateralised bank guarantees. This may be extended further depending on how the energy derivative markets function over the coming months.

→ Both measures came **into force** on **29 November 2022.**

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Section 6:

Other Amendments

MiFID II amendments

- conditions for admission of shares to trading on regulated market: **EUR 1 million** minimum **market capitalisation** and **10%** minimum **free float**
- EC may adopt delegated acts to change thresholds when they hamper liquidity on public markets, taking into account financial developments
- research provided by third parties must be fair, clear and not misleading
- research labelled as "issuer-sponsored research" must comply with code of conduct, which is subject to requirements for content, publication and review, and clear indication of preparation in line with code of conduct on front page of research
- research paid by issuer but not produced in compliance with code of conduct must be labelled as marketing communication
- issuers may submit sponsored research to collection body under proposal for EU single access point
- "SME growth markets" definition broadened to include MTF segments
- increased threshold of companies' market capitalisation to EUR 10 billion, below which unbundling rules do not apply

Changes to insolvency regime

- Harmonises conditions for “transaction avoidance”, protecting insolvency estate by clawing back assets that were wrongfully disposed of prior to opening insolvency proceedings (*e.g.* if debtor makes donation to friend just before insolvency proceedings);
- Facilitates tracing assets across borders by easing insolvency practitioners' access to registers;
- Allows for preparation and negotiation of sale of debtor's business before opening of insolvency proceedings (‘pre-pack’), helping prevent quick deterioration of company’s value (‘melting ice cube effect');
- Requires directors to file for insolvency without undue delay to avoid potential asset value losses for creditors (‘zombie firms');
- Provides simplified procedures for insolvent microenterprises, reducing costs and guaranteeing orderly liquidation;
- Improves representation of creditors' interests through creditors' committees;
- Makes key features of national regimes, including insolvency triggers and ranking of claims, more transparent for creditors to reduce information-gathering costs for cross-border investors

MiFIR

- For introduction of cross market order book surveillance mechanism, MiFIR is amended to enable:
  - competent authorities to request order book data from trading venues; and
  - ESMA to harmonise format of template that is used to store such data.

Listing Directive repealed

- Subsumed by proposed Listing Act provisions

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Section 6:

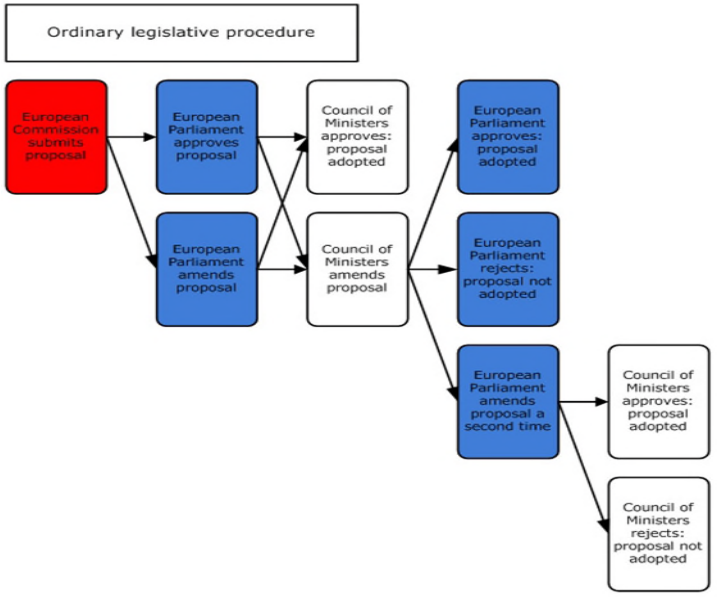
Summary and Next Steps

Summary

- Clearing Package
  - Communication;
  - Regulating amending European Market Infrastructure Regulation (EMIR), Capital Requirements Regulation (CRR), Money Market Funds Regulation (MMF);
  - Directive amending Capital Requirements Directive (CRD), Investment Firm Directive, and Directive on Undertakings for Collective Investment in Transferable Securities (UCITS)
- Listing Package
  - Regulation amending Prospectus Regulation, Market Abuse Regulation (MAR) and Markets in Financial Instruments Regulation (MiFIR);
  - Directive amending Markets in Financial Instruments Directive and repealing Listing Directive; and
  - Directive on multiple-vote shares
- Corporate Insolvency Package
  - Directive on corporate insolvency

Next Steps

- Legislative proposals will now be submitted to European Parliament and Council for adoption.



Additional Resources

LinkedIn Group. Stay up to date on structured and market-linked products news by joining our LinkedIn group.

Suggestions? *REVERSEinquiries* is committed to meeting the needs of the structured and market-linked products community, so you ask and we answer. Send us questions that we will answer on our LinkedIn anonymously or topics for future issues.

To request to join the LinkedIn group or send us suggestions/comments, please scan the QR code, which will notify us via email at REVERSEinquiries@mayerbrown.com.

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