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SEC/CORPORATE

NYSE and NASDAQ Propose Compensation Committee and Compensation Adviser Independence Rules

Earlier this week, the New York Stock Exchange and NASDAQ Stock Market each filed proposed rules regarding the independence of compensation committees and compensation advisers of listed companies, as required by Rule 10C-1 adopted by the Securities and Exchange Commission on June 20. Click here for a *Katten Client Advisory* from earlier this year addressing these final rules.

Subject to certain exemptions noted below, the proposed NYSE and NASDAQ rules each set forth the following requirements for listed companies:

- Listed companies must establish and maintain a formal compensation committee (NASDAQ currently allows compensation decisions to be made by a majority of the board's independent directors in the absence of a compensation committee). Each member of a listed company's compensation committee must be a member of the board of directors and must be independent (although companies listed on NASDAQ may continue to rely on an existing exception that allows certain non-independent directors to serve on a compensation committee under "exceptional and limited circumstances"). For determinations of independence, the board of directors must consider relevant factors, including the source of compensation of a director and whether a director has an affiliated relationship with the company. The proposed NASDAQ rules would prohibit a compensation committee member from accepting, directly or indirectly, any consulting, advisory or other compensation fee other than for board service, but there is no "lookback" period, while the proposed NYSE rules allow for board discretion. Both NYSE and NASDAQ provide for "bright line" independence tests, including that a director who received more than $120,000 in fees not related to board service in any 12-month period within the previous three years may not be deemed independent. The proposed NYSE and NASDAQ rules would allow the board of directors to conclude that a director with a large equity ownership in the company is independent for these purposes.

- A compensation committee must be appropriately funded by the listed company and must have a written charter.

- A compensation committee <u>may</u>, in its sole discretion, obtain the advice of a compensation adviser and the compensation committee is directly responsible for the appointment, compensation and oversight of compensation advisers.

- A compensation committee may select a compensation adviser only after considering the following independence factors: (i) whether the person that employs the compensation adviser is providing any other services to the company, (ii) the amount of fees paid to the person that employs the adviser as a percentage of that person's total revenues, (iii) the policies and procedures of the person that employs the adviser that are designed to prevent conflicts of interest, (iv) whether the adviser has any business or personal relationship with a member of the compensation committee, (v) whether the adviser owns any stock of the company, and (vi) whether the adviser or the person employing the adviser has any business or personal relationship with an executive officer of the company.

"Smaller reporting companies" are exempt from the proposed NYSE rules. Under the NASDAQ proposed rules, smaller reporting companies must have compensation committees, but they are not required to adhere to certain compensation committee eligibility requirements or the requirements relating to compensation advisers. Further, the following issuers are exempt from the proposed NYSE and NASDAQ rules: (i) limited partnerships, (ii) companies in bankruptcy proceedings, (iii) open-end management investment companies registered under the Investment Company Act of 1940, (iv) any foreign private issuer that discloses in its annual report the reasons that it does not have an independent compensation committee, and (v) controlled companies. In addition, other types of existing issuers that are exempt from compensation-related requirements under existing NYSE and NASDAQ rules will be exempt from the proposed rules.

The proposed NYSE rule changes will not become operative until July 1, 2013, and listed companies would have until the earlier of their first annual meeting after January 15, 2014, or October 31, 2014, to comply with the new compensation committees independence standards. Certain of the proposed NASDAQ rules relating to the compensation committee's responsibilities and authority (including the consideration of the independence of compensation advisers) would be effective immediately upon the SEC's approval of the proposed rules. Listed companies would be required to comply with the remaining NASDAQ proposed rules (including the compensation committee independence requirement) by the earlier of the second annual meeting held after the date of approval by the SEC or December 31, 2014.

Click here to view the NYSE proposed rule change. Click here to view the NASDAQ proposed rule change.

BROKER DEALER

SEC Report Regarding Handling of Material Non-public Information by Broker-Dealers

The Securities and Exchange Commission issued a report by its Office of Compliance Inspections and Examinations intended to help broker-dealers safeguard material non-public information from insider trading and other misuse. The report is a result of the examinations by the SEC of six of the largest broker-dealers and the examinations by the Financial Industry Regulatory Authority and the New York Stock Exchange of an additional thirteen broker-dealers. The report discusses the examination staff's observations of the policies and procedures, referred to as "information barriers," that exist at such broker-dealers to ensure that material non-public information is not being misused.

In the course of the examinations the staff noted the following areas of concern:

- Informal and undocumented interaction between groups that have material non-public information and internal and external groups with sales and trading responsibilities that might profit from the misuse of such information;
- Senior executives overseeing a business unit having access to material non-public information from a different business unit that could potentially profit from misuse of that information, with no or limited restrictions or monitoring to prevent such misuse;
- Broker-dealers without risk controls to address the need for information against the restrictions required with respect to discussions between two internal business groups in which material non-public information is provided to one unit for business purposes (e.g., sales, trading or research personnel); and
- Broker-dealers that have gaps in oversight with respect to reviewing the trading in the accounts of institutional customers, retail customers and asset management affiliates or review of firm personnel who receive information through business activities outside of investment banking.

The report provides that the foregoing concerns, by themselves, may not necessarily suggest violations of Section 15(g) of the Exchange Act of 1934, but broker-dealers may find it helpful to consider them in reviewing their policies and procedures. The report also highlights effective practices that the staff observed during the examinations, such as:

- Adopting processes that differentiate between types of material non-public information based on the nature of the information or where it originated;
- Expanding reviews for potential misuse of material non-public information to include reviewing the trading of credit default swaps, equity or total return swaps, loans, components of pooled securities such as unit investment trusts and exchange traded funds, warrants and bond options;
- Using and monitoring electronic sources of confidential information to identify which employees had accessed such information; and
- Monitoring access rights for key cards and computer networks to confirm that only authorized personnel had access to sensitive areas.

Click here to read the Staff Summary Report on Examinations of Information Barriers: Broker-Dealer Practices Under Section 15(g) of the Securities Exchange Act of 1934.

Read more.

CFTC

CFTC Issues Guidance on Trade Acceptance Requirements

The Commodity Futures Trading Commission's Division of Clearing and Risk (Division) has advised clearing member futures commission merchants (FCMs) and derivatives clearing organizations (DCOs) of the Division's position regarding their obligations under Rules 1.74 and 39.12(b)(7)(B), respectively. CFTC Rule 1.74 requires clearing member FCMs to "accept or reject each trade submitted by or for it or its customers as quickly as would be technologically practicable if fully automated systems were used." Similarly, CFTC Rule 39.12(b)(7)(B) provides that DCOs must "accept or reject each trade submitted to the derivatives clearing organization for clearing by or for the clearing member or a customer of the clearing member as quickly as would be technologically practicable if fully automated systems were used." The effective date for compliance with both rules is October 1, 2012.

The Division advised clearing member FCMs and DCOs that:

1. With respect to Rule 1.74, clearing member FCMs must accept or reject a trade for clearing and submit it to the relevant DCO for clearing within 120 seconds after the trade has been submitted to it by or for a customer.

2. With respect to Rule 39.12(b)(7)(B), DCOs must accept or reject trades no later than 60 seconds after submission.

The Division further indicated that, when the clearing requirement determinations for credit default swaps and interest rate swaps are finalized and in effect, a clearing member FCM must accept or reject a trade for clearing within 60 seconds after the trade has been submitted to it for clearing.

CFTC Issues Extension of Time for Compliance with Certain Pre-Trade Screening Requirements

In a letter to the Futures Industry Association, the Commodity Futures Trading Commission's Division of Clearing and Risk has extended the time for clearing member FCMs to comply with certain provisions of CFTC Rule 1.73. Among other requirements, the rule provides that clearing member FCMs must (i) establish risk-based limits for all customer and proprietary accounts and (ii) screen orders subject to automated execution on a designated contract market (DCM) for compliance with the FCM's risk-based limits prior to execution. The effective date of the rule is October 1, 2012.

The Division's letter extends the compliance deadline to June 1, 2013, for give-ups and bunched orders for both futures and swaps and confirms that FCM-set risk controls at some of the exchanges, such as the CME's Globex and ICE's WebICE platforms, will be acceptable for compliance with the automated screening of orders requirement in Rule 1.73. Where exchanges do not offer these types of FCM-set controls, the CFTC letter grants clearing member FCMs utilizing these exchanges relief from complying with those provisions, if necessary, until the earlier of the date on which the DCM implements such system, or June 1, 2013. The letter reiterates CFTC's position that risk controls that are reasonably designed to ensure compliance are sufficient for non-automated open outcry and voice execution.

The CFTC letter is available here.

CFTC Provides Clarification on Customer Initial Margin Requirements

The Commodity Futures Trading Commission's staff has issued interpretive guidance regarding the intended implementation of CFTC Rule 39.13(g)(8)(ii), which provides that each derivatives clearing organization (DCO) must require its clearing members to collect initial margin from their customers for non-hedge positions at a level that is greater than 100 percent of the DCO's initial margin requirements. First, the staff made clear that the rule is not intended to change existing practice in which exchange members and certain other customer accounts are designated as "member" or "hedge" accounts that are subject to a lower initial margin requirement. The staff further indicated that it generally would not object to the application of clearing or maintenance margin requirements to customer omnibus accounts or to the imposition of higher initial margin requirements for positions within a clearing member's house account

More information is available here.

LITIGATION

Derivative Action Alleging Board's Refusal to Prevent Regulatory Action by the FDA Failed to Overcome Requirement of Demand on Board

Last week the US District Court for the Northern District of Illinois dismissed a derivative action brought in a consolidated suit by various shareholders of healthcare company Baxter International based on the shareholders' failure to establish demand futility. The shareholders claimed that members of the Baxter board (1) failed to comply with a Federal Drug Administration (FDA) consent decree regarding one of the company's faulty products, (2) failed to adequately monitor the manufacture of a drug marketed by Baxter, (3) made misrepresentations regarding the company's profits and revenues and (4) engaged in insider trading. The shareholders argued that demanding the board pursue this litigation would have been futile because the board was not impartial.

A key issue was the standard applicable to the shareholders' claims of a failure to comply with the consent decree. The parties disagreed with whether *Aronson* – the more lenient test for futility where an affirmative decision of the board of directors is being challenged – or *Rales* – a more demanding test where a shareholder alleges an unconsidered failure of the board to act or manage – should apply. The District Court, applying the Seventh Circuit decision *Abbott Labs*, found the shareholders adequately pled that the board had made a "knowing choice" not to comply with the FDA consent decree. As a result, the *Aronson* test applied, requiring the shareholders to show either reasonable doubt that the board members were independent or disinterested, or had acted in bad faith.

On all claims, the shareholders failed to meet the high standard of acting in bad faith. In particular, with regard to Baxter's alleged failure to comply with the FDA consent degree, the District Court found that, even accepting the shareholders' allegations, the board had acted with good faith in its efforts. Although the FDA ultimately demanded a product recall, the board members could not be liable for business judgments even if their efforts were "deeply flawed" or "fail[ed] spectacularly." Despite the benefit of the more lenient *Aronson* test, the shareholders' inability to plead a defect in the board's decision process, rather than the outcome, was fatal. Because the shareholders "had ample opportunity to put [their] best foot forward," having had access to Baxter's books and records, submitted witness affidavits, and previously amended their complaint, the claims were dismissed with prejudice. *North Miami Beach General Employees Retirement Fund v. Parkinson*, No. 1:10-cv-06514 (N.D. Ill. Sept. 19, 2012).

SEC Targets CEO’s Lockout of Duly Elected Board Members

A recent Securities and Exchange Commission enforcement action filed in the US District Court for the Middle District of Florida aims to hold a director liable for a host of false statements made while he strong-armed the remainder of the board and improperly claimed the company as his own. According to the SEC’s complaint, defendant Michael Borish worked to exclude duly elected board members, including the chairman of the board and president, from the company. Borish was the CEO of Freedom Environmental Services, Inc. when, as part of a reverse merger, it acquired B&P Environmental Services, LLC. When the controllers of the former B&P were elected to the board, and one was elected chairman and president, Borish – now CEO and vice president of the new Freedom entity – refused to release control of the company or recognize the new board members. Borish refused to provide directors with Freedom’s books and records, and operated Freedom as though he was the sole officer and director. After two attempts in Florida state court to have Borish comply with the purchase agreement and election results, the board members filed for voluntary Chapter 11 bankruptcy protection.

The civil litigation proved unsuccessful to resolve the dispute over corporate control and the SEC stepped in, bringing claims against Borish and Freedom, which he was exclusively controlling, under Section 17(a) of the Securities Act of 1933, Sections 10(b), 13(a)-(b), and 14(c) of the Securities Exchange Act of 1934, and SEC Rules 13a-14 and 14c-6. Specifically, the SEC alleged that Borish caused Freedom to file with the SEC numerous reports containing the false statements that Freedom’s board of directors and management did not change after the merger with B&P, and that Borish was the president and sole director of Freedom. Borish and Freedom were also charged with issuing a false press release, claiming that Freedom had acquired a company when in fact the parties to that acquisition had only entered into a letter of intent, and the deal was never closed. The SEC also brought claims against Borish and Freedom’s COO, Michael Ciarlone, for misappropriation of Freedom’s funds into their own personal accounts. *SEC v. Freedom Environmental*, No. 6:12-cv-01415-JA-DAB (M.D. Fl. Filed Sept. 17, 2012).

BANKING

Federal Banking Regulators Issue Basel III Calculator

On September 24, the federal banking regulators, the Federal Deposit Insurance Corporation (FDIC), the Board of Governors of the Federal Reserve System, and the Office of the Comptroller of the Currency (OCC) (the regulators) released a Basel III “calculator” intended to help estimate the impact of the proposed new capital rules on banks and bank holding companies. The regulators have stated the tool is intended to help institutions estimate the potential effect the proposals could have on capital ratios, “but should not be relied on as an indicator of a bank’s actual regulatory capital ratios.” In June 2012, the Federal Reserve Board, the FDIC and the OCC approved joint proposals for comment that would revise their current regulatory capital standards. The public comment period for these proposals ends on October 22. The Basel III notice of proposed rulemaking (NPR) focuses primarily on strengthening the level of regulatory capital requirements and improving the quality of capital by revising risk-based and leverage capital requirements consistent with agreements reached by the Basel Committee on Banking Supervision. The Standardized Approach NPR proposes a number of enhancements to the risk-sensitivity of the agencies’ capital standards, including revising rules for calculating risk-weighted assets to enhance risk sensitivity and address weaknesses identified over recent years, incorporating aspects of the Basel II standardized framework, and alternatives to credit ratings, consistent with Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act. These revisions will impact methods for determining risk-weighted assets for residential mortgages, securitization exposures and counterparty credit risk. The NPR also would introduce disclosure requirements that would apply to US banking organizations with $50 billion or more in total assets.

According to the American Bankers Association,

> the calculator is useful as a starting point for bankers to consider the effect of the proposed rules on their banks and customers, but ABA cautions against overreliance on its results. The tool offers only a point-in-time and high-level overview of the capital requirements, does not consider the increased volatility resulting from the proposals, and has gaps in its securitization treatment. The proposals’ actual impact is heavily dependent on technical new definitions, individual loan underwriting data, and changing market conditions.

The regulators themselves further cautioned that

> the estimation tool is designed primarily for use by smaller, non-complex banking organizations that are not subject to the agencies' market risk capital rule or the advanced approaches capital rule. It provides a general estimate of a banking organization's leverage and risk-based capital ratios under the NPRs. Because the estimation tool was designed as a standardized mechanism for banking organizations to broadly understand the potential impact of the NPRs, it has certain inherent limitations and contains some simplifying assumptions to facilitate its widespread use. For example, the tool uses publicly available regulatory reporting data to limit the amount of additional information that banking organizations would need to prepare in order to develop an estimate. The tool also uses a 10-year period for phasing out non-qualifying capital instruments such as trust preferred securities. As a result of these and other assumptions that are described within the tool itself, a particular banking organization's leverage and risk-based capital ratios under the NPRs may vary from the estimates produced using this tool.

Read more.

Agencies Reopen Comment Period on Swap Margin and Capital Proposed Rulemaking

On September 26, five federal agencies, including the Federal Deposit Insurance Corporation, The Office of the Comptroller of the Currency and the Board of Governors of the Federal Reserve System, the Farm Credit Administration and the Federal Housing Finance Agency, reopened the comment period on a proposed rule to establish margin and capital requirements for swap dealers, major swap participants, security-based swap dealers, and major security-based swap participants for which one of the agencies is the prudential regulator, pursuant to sections 731 and 764 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The comment period—which originally ended July 11, 2011—was reopened until November 26, 2012, "to allow interested persons more time to analyze the issues and prepare their comments in light of the consultative document on margin requirements for noncentrally-cleared derivatives recently published for comment by the Basel Committee on Banking Supervision and the International Organization of Securities Commissions."

Read more.

OCC Issues Bulletin on Investor-Owned Residential Real Estate

On September 17, the Office of the Comptroller of the Currency (OCC), which regulates national banks and federal savings associations (collectively, banks), issued guidance on appropriate credit risk management practices for investor-owned, one- to four-family residential real estate (IORR) lending where the primary repayment source for the loan is rental income. According to the OCC, "this type of lending has increased because of a variety of economic factors. This bulletin is intended to promote consistent risk management practices for IORR lending and to summarize the applicable requirements for regulatory capital and call reports for IORR lending." In issuing the guidance, the OCC noted that "some banks manage IORR loans in a similar manner to owner-occupied one- to four-family residential loans. The credit risk presented by IORR lending, however, is similar to that associated with loans for income-producing commercial real estate (CRE). Because of this similarity, the Office of the Comptroller of the Currency expects banks to use the same types of credit risk management practices for IORR lending that are used for CRE lending."

The guidance sets out the OCC's expectations in several key areas including credit risk management, loan underwriting standards, IORR identification and portfolio monitoring, loan losses, risk assessment and rating systems, and regulatory reporting and risk-based capital treatment.

Read more.

Bi-partisan Group of US Senators Urge Banking Regulators to Protect Community Banks

Criticizing implicitly notices of proposed rulemakings with respect to new capital requirements, on September 27, 53 US Senators from both parties urged federal banking regulators to consider the "unintended consequences and their effect on the viability of community banks across the country." The letter, addressed to Federal Reserve Board Chairman Ben Bernanke, Acting FDIC Chairman Marty Gruenberg and Comptroller of the Currency Tom Curry, admonished the regulators that community banks "are different from many larger institutions in size and scope, and we do not see the value in requiring them to adhere to regimes designed to manage larger and more complex risks. The proposed [Basel III] rules could make it even harder to raise needed capital. Community banks may change their business plans as a result of the rules, thereby reducing lending and economic growth in the communities in which they serve."

Read more.

EXECUTIVE COMPENSATION AND ERISA

State Levy on Paid Health Care Claims Survives ERISA Preemption Challenge

Under the Michigan Health Insurance Claims Assessment Act (HICA Act) (P.A. 142 of 2011), third-party administrators, carriers and self-insured entities are required to pay assessments on the amount of health care claims paid by them. This assessment will be used by the State in funding its Medicaid program. Presumably, the payers will seek to pass these assessments on to their clients, which include health care benefit plans under the Employee Retirement Income Security Act (ERISA).

An organization representing entities involved with self-insured health care benefit plans filed a complaint against various Michigan authorities, seeking a declaration that the HICA Act was preempted by ERISA and, in addition, violates the supremacy clause of the United States Constitution. In arguing for preemption, the complaint asserted that the HICA Act imposes administrative burdens and fees that conflict with ERISA and undermine ERISA's interest in uniform nationwide administration of ERISA plans. The complaint also referenced the fact that the HICA Act expressly referred to ERISA plans in its text.

The US District Court for the Eastern District of Michigan held that the HICA Act is not preempted by ERISA. The court determined that the HICA Act, which assesses the tax only after a coverage decision has been made and a claim has been paid, does not impermissibly "relate to" ERISA plans, as it has neither a prohibited "reference to" nor "connection with" ERISA plans. It is well-established in the case law that a state law must have one of those two relationships to ERISA plans to trigger preemption.

With respect to the "reference to" test, the court found that the HICA Act "does not act exclusively on ERISA plans or single them out for different treatment." Instead, ERISA plans are one of numerous claims-paying entities that are subject to the HICA Act, so that ERISA plans are not singled out, and the impermissible "reference to" was not present.

Turning to the "connection with" test, the court stated that the HICA Act "does not mandate any particular benefit structure or bind administrators to certain benefit choices," and thus does not have an impermissible "connection with" ERISA plans. In reaching its decision, the court relied on US Supreme Court and lower court decisions noting that laws that do not mandate particular structures for or decisions about the processing of claims and disbursement of benefits are not preempted, even if they may impose burdens on the administration of ERISA plans or increase the cost of providing benefits to covered employees. In this analysis, the court referenced a US Supreme Court decision holding that a state's general tax on hospitals—including hospitals owned by ERISA plans—was not preempted.

Based on these "reference to" and "connection with" analyses, the court concluded that the HICA Act was not preempted by ERISA. Having completed its ERISA analysis, the court, in a footnote, rejected the plaintiff's supremacy clause argument "for the same reasons."

If the District Court's holding is upheld on appeal, other states may seek to impose similar levies, which could be expected to be passed on to plans.

Self-Insurance Institute of America, Inc. v. Snyder, 2:11-cv-15602-JAC-DRG (E.D. Mich. Aug. 31, 2012).

UK DEVELOPMENTS

FSA Warns Firms About Financial Promotions

On September 21, the UK Financial Services Authority (FSA) released a speech entitled "Financial Promotions: Keeping Connected and Compliant" delivered by Clive Gordon, FSA's Head of Conduct Risk. The speech highlighted common poor practices identified by the FSA during its routine monitoring of digital media promotions.

Mr. Gordon drew particular attention to what he termed "a couple of common regulatory myths about using digital media"

- First, there is no "one click rule". Website banner adverts or sponsored search engine results need to be compliant in their own right. Being one click away from the information does not necessarily make it compliant.
- Roll-over risk warnings are not sufficient on website banner adverts. In most cases he does not think a roll-over risk warning is appropriate, as many people may still read the advert without hovering over it.

He emphasized the need for risk information to be prominent and clearly displayed and for digital promotions to meet the FSA's requirements for stand-alone compliance regardless of where or how a promotion appears.

It is proposed under the Financial Services Bill currently before Parliament that the FSA's successor regulator the Financial Conduct Authority (FCA) will have the power to ban misleading financial promotions. Mr. Gordon stated that the FCA "will be ready to take faster and more effective action from the first day we get these powers" and will act to remove misleading promotions from the market immediately. When it uses this power, the FCA will publish the promotion and the reasons for banning it to act as a deterrent to other regulated firms.

Read more.

FSA Notification Procedure for Short Selling Regulation Exemptions

Article 17 of the EU Short Selling Regulation (EU236/2012) (the Short Selling Regulation) provides for certain exemptions for market-making activities and primary market operations from the requirements to make notifications and public disclosures of net short positions and the restrictions on entering into uncovered short sales under the Short Selling Regulation. This exemption can be used by a person who has made a "legitimate notification" to the relevant competent authority at least 30 days before the exemption is intended to be employed and where the competent authority has not objected to its use. (On September 17, the European Securities and Markets Authority (ESMA) published a consultation paper on guidance on the exemptions under Article 17; see the September 21, 2012, edition of *Corporate and Financial Weekly Digest*.)

On September 24, the UK Financial Services Authority (FSA) published guidelines for the making of notifications to the FSA in order to obtain market maker and primary dealer exemptions under Article 17. The exemptions apply only to transactions carried out in performance of market-making activities or as authorized primary dealers; they do not apply to other activities carried out by the entity making the notification. Since notification must be made to the relevant regulator 30 days before it is relied on, for an entity to be able to rely on an exemption from November 1 (the date the Short Selling Regulation comes into effect), the FSA must receive any relevant notification no later than October 2.

Read more.

On September 26, the FSA published the relevant notification forms. They require detailed information (including name of issuer, type of financial instrument and ISIN code (International Security Identification Number)) for each instrument with respect to which a market maker or primary dealer exemption is notified.

Read more.

Treasury Announces Recommendations for LIBOR Reform

On September 28, the UK Treasury released the Final Report of the Wheatley Review of LIBOR setting out recommendations for LIBOR reform. (The Wheatley Review, headed by Martin Wheatley, the CEO-designate of the Financial Conduct Authority, was launched in mid-August (see the August 17, 2012, edition of *Corporate and Financial Weekly Digest*).

The Review recommends that:

- Administering LIBOR and submitting rates should become regulated activities under the UK's financial services regime.
- Persons performing key roles in the submission of rates and the administration of LIBOR should be registered with the UK Financial Services Authority (FSA).
- Manipulation of LIBOR should be made a specific criminal offense under the investigation and prosecution power of the FSA.
- The British Bankers Association should transfer responsibility for LIBOR to a new administrator.
- The new administrator should introduce a code of conduct for submitters, including systems and controls, transaction recordkeeping responsibilities and providing for external audit of submissions.
- LIBOR submissions be explicitly and transparently supported by transaction data.
- LIBOR for currencies and tenors with insufficient trade data to corroborate submissions be phased out.
- Publication of individual submissions change from current daily publication alongside the LIBOR rate to publication after a delay of at least three months.
- Measures be taken to increase the number of banks participating in the rate submission process.
- UK regulators work closely with their European and international counterparts to establish and promote clear principles for effective global benchmarks.

The Treasury minister, Greg Clark, said that the Wheatley Review had made a series of "comprehensive and practical recommendations" designed to restore LIBOR's credibility. Any necessary legislative changes will be considered for inclusion in the Financial Services Bill which is currently before Parliament or the Banking Reform Bill which will be introduced shortly.

Read more.

EU DEVELOPMENTS

ESMA Releases EMIR Technical Standards

On September 27, the European Securities and Markets Authority (ESMA) published its final report containing draft technical standards for the EU Regulation on Over-the-Counter Derivatives, Central Counterparties and Trade Repositories (EU648/2012) (Regulation). The Regulation, which is generally known as the "European Market Infrastructure Regulation" or EMIR, was adopted by the European Parliament on March 29 (see the March 30, edition of *Corporate and Financial Weekly Digest*). EMIR is intended to improve the functioning of over-the-counter (OTC) derivatives markets in the European Union by reducing risks (by the use of central clearing and other risk mitigation techniques), increasing transparency (by the use of trade repositories) and mandating the use of central counterparties (CCPs) meeting approval and supervision criteria designed to ensure that CCPs are sound and resilient. The report sets out details of how ESMA considers certain of EMIR's detailed requirements should be implemented.

The ESMA final report is the result of ESMA's June 25 consultation paper on proposed technical standards (see the June 29 edition of *Corporate and Financial Weekly Digest*). It will be submitted to the European Commission (Commission) for its approval by September 30. The Commission has three months to decide whether to endorse ESMA's draft technical standards.

The matters that ESMA consulted on included:

- Defining the framework for the application of the mandatory clearing obligation;
- Specifying the risk mitigation techniques for non-cleared OTC derivatives;
- Requirements for the application of exemptions to the mandatory clearing obligation for non-financial counterparties and intragroup transactions.
- Details of derivatives transactions required to be reported to trade repositories;
- Details of data from trade repositories to be provided to relevant regulatory authorities;
- Organizational, conduct of business and prudential requirements for the authorization of CCPs; and
- Information to be provided by trade repositories in connection with their authorization and ongoing supervision.

Among the many detailed changes made to the draft standards which were the subject of ESMA's June consultation are the following:

- Substantial revisions to the requirements for indirect clearing arrangements;
- Changes to the criteria for the assessment of whether particular contracts should be subject to mandatory clearing;
- Changes to margin criteria including greater flexibility for portfolio margining models;
- Amended risk mitigation criteria for OTC derivatives not cleared by a CCP;
- Detailed changes to the CCP recognition criteria;
- Amendments to the content and format of reports to trade repositories; and
- Changes in the information required to be provided by trade repositories seeking authorization.

Read more.

In addition, on September 26, the European Banking Authority adopted its draft technical standards under EMIR on capital requirements for CCPs which will also be sent to the European Commission for approval.

Read more.

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