Kramer Levin

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Our recent seminars…

- 17/01/2019 - **AFG Conference - Specialised financing bodies: new investment and financing funds offering multiple opportunities** - G. Saint Marc
- 31/01/2019 – **Legal crypto Mondays - Paris Finance Week Special** – H. de Vauplane, G. Kolifrath, V. Charpiat
- 13/02/2019 - **Cercle Gödel meeting - What must be done to conclude OTC derivative transactions on April 2 due to Brexit?** – G. Kolifrath
- 14/02/2019 - **Blockchain Breakfast: Blockchain ready to transform the academic world** - H. de Vauplane
- 19/02/2019 - **Banking and Financial Law Mornings - Banker's liability** - H. Bouchetemble, M-C. Fournier-Gille, Th. Bonneau, G. Kolifrath
- 19/02/2019 - **EIFR Conference - Between EMIR and BREXIT, what compensation for derivatives?** – G. Kolifrath

... and coming soon

- 14/03/2019 – **National symposium - Blockchains and skills: developing talent, protecting professionals** - H. de Vauplane
- 21/03/2019 - **GDPR Thursdays - GDPR where you don't always expect it: M&A operations, insurance brokerage** - N. Lenoir, A. Paszkiewicz, G.Kolifrath and E. David
- 19-20/03/2019 – **Africa Sukuk Conference** – H. de Vauplane, G. Saint Marc

Capital markets

ESMA Recommendation on ICOs and Cryptoassets

On January 9, 2019, ESMA published its recommendations on ICOs and cryptoassets to EU institutions. The recommendations clarify the EU rules applicable to *security tokens* and give ESMA's position on the shortcomings of the current regulatory framework.

As such, ESMA has identified two categories and two findings:

- for *security tokens* within the meaning of MiFID 2, certain areas require a reinterpretation or reassessment of certain specific requirements in order to allow effective application of the regulations in force; and
- for cryptoassets other than *security tokens*, the absence of applicable rules exposes investors to significant risks.

ESMA believes that at a minimum, anti-money laundering (AML) requirements should apply to all activities related to cryptoassets and that appropriate risk information should also be put in place prior to the purchase of such assets.

These recommendations are not new and are in line with the work and studies carried out in the EU during 2018, which mainly distinguish *tokens* according to whether they are *security tokens* or other types of *tokens*.

ESMA report on accepted market practices

On December 18, 2018, ESMA published its annual report on *accepted market practices (*AMP), in accordance with the *Market Abuse Directive/Regulation* (MAD/MAR).

As a reminder, the objective of MAD/MAR is to guarantee the integrity of European financial markets and promote investor confidence by generally combating insider trading, illegal disclosure of inside information and market manipulation.

However, MAD/MAR do allow certain exceptions, practices considered admissible by the legislator when they are supervised and controlled by the competent national authorities (NCAs). A list of non-exhaustive criteria should be taken into consideration by NCAs when assessing whether these practices can be accepted.

Thus, the report presents ESMA's views on the implementation of AMPs, as well as recommendations to NCAs.

The report thus covers several European AMPs (per NCA). Among those targeted are the AMPs of the *Portuguese Securities Market Commission* (Portugal), *the Netherlands Authority for the Financial Markets* (Netherlands), *the Comisión Nacional del Mercado de Valores* (Spain), *the Commissione nazionale per le società e la Borsa* (CONSOB) (Italy) and the AMF.

ESMA notes that the only MAR AMPs (as opposed to MAD) are AMPs relating to the management of issuers' liquidity through the provision of liquidity contracts. ESMA considers in its analysis that alternatives to liquidity contracts should be developed by the players.

On the basis of its overall analysis, ESMA considers that the legal framework designed by MAR is stricter than that of MAD. Therefore, ESMA that fears normative contradictions arise allowing MAD-based AMPs where MAR would have prohibited them.
For example, with regard to CONSOB, it was noted that the two of the three MPAs established do not seem to be compatible with MAR. Consequently, ESMA recommends that CONSOB withdraw these MAD-based AMPs.

Recommendation and Joint ESA Report on KID amendments (PRIIPs)

On February 8, 2019, the ESAs published a joint final report on the changes to the KID documentation (PRIIPs). This report contains their final recommendations following a targeted consultation on the amendments to the delegated regulations governing KID rules.

Indeed, the ESAs had noted in particular that while these certain practices in the drafting of the KID may have been intended to protect retail investors, some of them nevertheless raised other concerns (in particular effective control) insofar as they could be perceived as contradictory and not complementary to other information provided in the KID.

Therefore, in the consultative document, the ESAs had declared their intention to communicate their views on these practices in order to promote appropriate and consistent approaches before a full review of PRIIPs.
After taking into account the reactions received and considering in particular the implications of a possible decision by the European co-legislators to postpone the application of the KID for certain types of investment funds beyond 2020, the ESAs decided:

- not to propose any targeted changes at this stage; and
- to initiate a more comprehensive review of the delegated PRIIPS regulations during 2019, including the publication of a consultation on the draft NTR.

In addition, on the same day, the ESAs issued a *Supervisory statement* on performance scenarios to promote consistent approaches and improve the protection of retail investors before the end of the review. The ESAs consider that there is a risk that retail investors may have inappropriate expectations regarding returns and performance. Therefore, the ESAs recommend that producers of products (PRIIPs) include a warning in the KID to ensure that retail investors are fully aware of the limitations of the figures provided in the performance scenarios.

Update of ESMA Q&As on EMIR reporting

Update on February 4, 2019, of ESMA's EMIR Q&As for EMIR reporting for trade repositories.

These changes concern:

- question-answer 34 on contracts with no maturity date, and now confirm that counterparties can report "P" for a derivative in the *Action Type* field if the derivative is included in a position on the same day it is reported;
- question-answer 38, and further clarify when reports must be submitted to the *Action Type* "N" and "P" field for derivatives that expired before the reporting date; and finally
- a new question-answer 50, and specify the approach that counterparties must take to report the *Confirmation Means* field. Following the modification of the EMIR report validation rules on August 9, 2018, scenarios may be reported in which a derivative is traded on a platform and then confirmed on a different or finally unconfirmed platform.

Update of ESMA Q&As on MiFIR reporting

Update on February 4, 2019, of ESMA's MiFIR Q&As for MiFIR reporting for NCAs.

Two new Q&As provide additional clarification regarding:

- reporting of issuers' LEIs to the *Financial Instrument Reference Data System* (FIRDS) in cases where the issuer of the instrument has one or more branches that have an LEI; and
- notification of maturity, expiry and termination dates to the FIRDS.

A change is also made to the question-answer regarding the reporting of complex transactions, namely the use of the *Trading Venue Transaction Identification Code* (TVTIC).

While these obligations are not new, we have seen an increase in questions relating to transaction reporting regimes in recent months. On this occasion, it will be necessary to specify the outlines of the reporting obligations arising from the EMIR (for OTC) and MiFIR (for the list) regulations, obligations that may be separate or sometimes complementary due to the sometimes complex nature of the financial instruments declared.

Compliance

Guidelines for identification, identity verification and customer knowledge

On February 18, 2019, the ACPR published a detailed analysis of due diligence obligations related to identification, identity verification and customer knowledge. This publication aims to contribute to the establishment of an effective AML/CFT preventive system and a system for the detection of persons subject to asset freezing measures.

In this document, the ACPR recalls the distinctions that must be made between the occasional client and the business relationship. For example, the ACPR points out that, in accordance with Article R. 561-38 of the Monetary and Financial Code, financial institutions must set up a monitoring and surveillance system to enable them to identify their business relationships (the use of an automated system that may be necessary based on several criteria such as the size of the structure, the nature of the activities, distribution channels, *etc*.).

This document also details the due diligence measures to be taken with regard to customers in business relationships, in particular:

- the identification and verification of the client's identity;
- the identification of beneficial owners;
- the identification of the beneficiaries of life insurance or capitalisation policies and, where applicable, of its beneficial owners;
- the new identification and verification of identity during the course of a business relationship; and
- the knowledge of the business relationship.

The document also recalls the absence of generic controls for occasional clients (except in cases of suspicion or the case of the conditions listed in II of Article R. 561-10 of the Monetary and Financial Code).

The document outlines the use of a third party for the implementation of due diligence measures, the refusal to enter into a business relationship or execute a transaction, the termination of the business relationship and finally describes the regime for document retention.

This document comes after several national and international convictions of financial institutions and is an opportunity to recall the fundamentals of compliance.

Collective management

AMF study of the characteristics of AIFs managed by French management companies: exposure, liquidity risk and use of leverage

On January 23, 2019, the AMF published a study based on French AIFM declarations giving a view of the AIF market representing nearly €690 billion in net assets and €915 billion in exposure.

In the light of these studies, the AMF notes that:

- the most speculative funds *(hedge funds*) are few in number (about 0.6% of total net assets);
- the funds have sufficient liquidity to meet the timing of investor redemptions under normal market conditions (with the exception of certain real estate and private equity funds, AIFs can generally liquidate a majority of their assets in less than one day);
- leverage levels are generally in line with the investment strategies implemented; and
- exposures are consistent with AIF strategies: 71% of real estate funds are exposed to physical assets, 85% of private equity funds to securities, 58% of funds of funds to collective investment schemes, and 60% of "other" strategy funds to securities.

The study also shows the limitations of this reporting from the Directive:

- lack of relevance in the strategy categories of the funds present in the reporting; and
- a difficulty in processing the information due in particular to the substantial nature of the information provided (most of which is optional).

As such, future emphasis will be placed on including more risk indicators or monitoring tools, better data coverage or possible revisions.

Brexit

Publication of Order 2019-75 of February 6, 2019 on measures to prepare for the withdrawal of the UK and the EU in the field of financial services and the report to the President of the Republic

The Order rules on insurance, collective management and derivatives matters.

For derivatives, the Order amends: the scope of transactions eligible for clearing-settlement, which does not currently cover FX spot transactions, the sale, purchase, delivery of precious metals or CO2 quota transactions, and the possibility for two parties to a derivatives contract to invoice capitalised late payment arrears in the event of non-payment.

Article 3 provides for the creation of an automatic master agreement corresponding to a "replication" contract according to certain modalities. Care should be taken to verify to what extent the replication conditions do not require specific renegotiations with the new entity. In addition, British entities also have several ways to continue their business with French entities.

Several discussions have been launched concerning the applicability of this Order, in particular by certain French financial market associations. It is certain that the practice will make it possible to define the specific outlines very quickly.

Insurance

EIOPA recommendations regarding the withdrawal of the United Kingdom from the EU

On February 19, 2019, EIOPA issued recommendations in the run-up to the United Kingdom's withdrawal from the EU, which will take place unless an agreement is reached on March 30, 2019, unless the two-year period is extended.

As from the withdrawal, the United Kingdom becomes a third country and insurance companies and British intermediaries lose their right to operate in the Member States under the freedom of establishment and the freedom to provide services.

EIOPA has made nine recommendations that can be summarised as follows:

- **Recommendation 1**: the competent authorities should endeavour to minimise the damage caused to policyholders and beneficiaries,

- **Recommendation 2 on the "run-off"**:

  - the competent authorities should put in place measures to facilitate the run-off of activities which will therefore be considered as unauthorised;

  - they must also prevent the conclusion or renewal of insurance policies with British insurers, as long as the latter are not authorised to carry on insurance business in France; and

  - they will have to supervise the companies concerned in order to ensure compliance with prudential insurance rules.

- **Recommendation 3 on the authorisation of third-country branches:**

  - in accordance with Article 162 of the Solvency II Directive, British insurance companies may be authorised to carry on cross-border activities through a branch in an EU Member State;

  - for such authorisation to be granted, the competent authorities will have to apply the principle of proportionality and take into account that the insurance undertaking was subject to Solvency II requirements before its withdrawal; and

- they may, in order to speed up the authorisation procedure, limit the authorisation to the run-off only.

- **Recommendation 4 on the withdrawal of authorisation**: if the legislation of a Member State contains provisions on the withdrawal of authorisation (Article 144(1)(a) of the Solvency II Directive), they should be applied.

- **Recommendation 5 on portfolio transfer**: the competent authorities should authorise the finalisation of portfolio transfers from British insurance companies to insurance companies in EU Member States, provided that it has been initiated before the withdrawal date.

- **Recommendation 6 on the change of the subscriber's habitual residence or establishment**: where a policyholder with his habitual residence or, in the case of a legal person, its place of establishment in the United Kingdom has concluded a life or non-life insurance contract, excluding home and motor insurance, with a United Kingdom insurer and has subsequently transferred his habitual residence or its place of establishment to an EU Member State, the competent authorities must take into account, when carrying out prudential supervision, that the contract was concluded in the United Kingdom and that undertaking does not provide cross-border services to the EU for that contract.

- **Recommendation 7 on cooperation between competent authorities**: where a UK insurance undertaking carries on cross-border activities in more than one Member State, the competent authorities of those Member States will be required to cooperate with each other.

- **Recommendation 8 on information due to subscribers and policyholders**: British insurers should inform their policyholders and subscribers of the consequences of Brexit on the policies taken out with them.

- **Recommendation 9 on the distribution activity**: the competent authorities should ensure that UK intermediaries and entities intending to continue or distribute insurance products in the EU after withdrawal from the United Kingdom are established and registered in accordance with existing regulations. In particular, the competent authorities should ensure that these intermediaries do not have the characteristics of a "shell".

Decree relating to the information due to insured persons by companies no longer in one of the situations provided for in I of Article L. 310-2 of the Insurance Code

We draw your attention to an order, issued pursuant to Article 2 of Ordinance No. 2019-75 of February 6, 2019, relating to the information due to insured persons by foreign companies no longer in one of the situations provided for in I of Article L. 310-2 of the Insurance Code, which should be published shortly.

It will amend Article L.310-1 1° by adding that the companies concerned must, in particular, inform their policyholders and subscribers within fifteen days of the change in situation, that the contract will not be renewed, that no new premiums will be issued and that no payments, other than those already due, will be accepted.

The insurer concerned must also provide information on the expiry of the contract, two months before its arrival, and recommend to its policyholders that they take out a new guarantee with an insurer authorised to carry out insurance operations in France. However, this obligation does not apply to commitments maturing less than three months after the information due under 1°.

The bill for the growth and transformation of companies known as the "Pacte Act"

We draw your attention to several provisions of the bill for the growth and transformation of companies known as the "PACTE Act" that could have an impact on the insurance market:

- the Senators have attempted to reintroduce into the bill by way of an amendment the possibility for life insurance policyholders to change insurers without losing the acquired tax benefits, provided that the contract has been in effect for at least eight years. This possibility was rejected by the *Assemblée Nationale*'s special committee examining the project. However, MEPs have not completely closed the door to the portability of life insurance policies. Indeed, such transfers would be permitted in respect of all or part of the acquired tax benefits under an existing policy, which would be credited to a subsequently subscribed contract within the same insurance company. A transfer of a life insurance contract within the same company would therefore be possible,

- on February 7, the Senators also adopted at first reading an amendment to the Pacte Act aimed at defining the framework for the future self-regulation of brokerage, the principle of which had already been validated by the General Treasury Department last September. Brokerage will be regulated through the creation of professional associations, which are mandatory and accredited by the ACPR. They may accompany and exercise

disciplinary power over their members, including dismissal, in the event of breaches or inactivity,

- the Senators also adopted in public session an amendment proposing to tighten the conditions of practice of foreign insurers outside the European Economic Area (EEA) by making their construction insurance activities subject to the control of the ACPR. In other words, to carry out structural damage or ten-year guarantee activities, the insurers concerned will have to obtain an administrative agreement. One of the objectives of this measure is to avoid the risk of default by foreign insurers that construction insurance has recently experienced.

Implementation of continuous training in accordance with the Insurance Distribution Directive (ICD)

Since February 23, 2019, insurance intermediaries and employees of insurance companies have been required to regularly update their professional skills.

Thus, in addition to the initial training already required for professional competence, Ordinance No. 2018-361 of May 16, 2018 on the distribution of insurance now imposes a training or continuous professional development obligation of at least 15 hours per year.

The list of persons subject to this obligation is quite broad since it includes insurance and reinsurance intermediaries, their staff and employees of insurance and reinsurance undertakings whose activities consist in providing recommendations on insurance or reinsurance contracts, in presenting, proposing or assisting in the conclusion of insurance contracts or in carrying out other preparatory work for their conclusion. The managers of insurance intermediaries are also required to provide training.

However, insurance intermediaries on an ancillary basis, as well as the staff of intermediaries and insurance companies engaged solely in the management of insurance contracts, are excluded.

In addition, persons subject to this obligation must ensure that training measures are adapted to the person concerned according to the nature of the products distributed, the methods of distribution used and the functions performed.

The ACPR pointed out that this new training requirement is in line with the objectives set out in the DDA, which stipulates that every insurance distributor must act honestly, impartially and

professionally in the best interests of its customers. Consequently, the training obligation would ultimately contribute to improving the quality of the advice given to customers.

The ACPR indicated in its February 2019 review that, during its audits in 2019, it will pay attention to the steps taken by professionals to comply with these new obligations. Professionals must therefore be able to submit, as of now, the list of persons or categories of persons subject to the obligation of continuous training.

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