

January 15, 2019

## Legal News - November-December 2018

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### Our recent seminars...

- 05/11/2018 – **Legal crypto Mondays** – H. de Vauplane, G. Kolifraith
- 07/11/2018 – **Kramer Levin Derivatives Breakfast - Brexit: Will derivatives go off on a tangent?** – G. Kolifraith, J. Blanchet, L. Sharkey
- 15/11/2018 – **Fintech Breakfast - The treatment of cryptocurrencies in the PACTE Law and the 2019 Finance Bill** -H. de Vauplane
- 17/11/2018 – **European Reformists Summit: 2019 the democratic challenge in Europe** – N. Lenoir
- 27-28/11/2018 – **Blockchain Paris 2018** – H. de Vauplane
- 27-29/11/2018 – **Trustech** – P. Storrer
- 03/12/2018 – **Legal crypto Mondays** – H. de Vauplane, G. Kolifraith
- 11/12/2018 – **Banking and Financial Law Mornings - Professional secrecy: where to go for information (banker, authorities)?** – Th. Bonneau, G. Kolifraith, D. Penin
- 11/12/2018 - **Launch meeting of the working group on "The attractiveness of the Paris legal centre"** - N. Bodega
- 12/12/2018 - **Blockchain Conference at the Faculty of Law** - H. de Vauplane
- 12/12/2018 - **2018 Anacofi Great Debate - Regulation of our businesses: the situation after the entry into force of the main texts (MiFID, PRIIPS, DDA, RGPD, etc.)** – G. Kolifraith
- 07/01/2019 – **Legal Crypto Monday After work** – H. de Vauplane, G. Kolifraith

### ... and coming soon

- 17/01/2019 - **AFG Conference - Specialised financing bodies: new investment and financing funds offering multiple opportunities** - G. Saint Marc
- 19/02/2019 - **EIFR Conference - Clearing derivatives between EMIR and Brexit** - G. Kolifraith
- 19/02/2019 - **Banking and Financial Law Mornings - Banker's liability** - H. Bouchetemblem, M-C. Fournier-Gille, Th. Bonneau, G. Kolifraith
- 31/01/2019 – **Legal crypto Mondays - Paris Finance Week Special** – H. de Vauplane, G. Kolifraith

## Capital markets

### ESMA publishes its guidelines for non-significant benchmark indices

On December 20, 2018, ESMA published its guidelines for non-significant benchmark indices and proposes less stringent requirements for both their directors and supervised contributors in the following four areas:

- procedures, characteristics and positioning of the supervisory function;
- relevance and verifiability of the underlying data;
- transparency of the methodology; and
- governance and control requirements for supervised contributors.

The first three points apply to the administrators of these indices, while the fourth applies to supervised contributors.

### ESMA publishes updates to the Q&A on benchmark indices

On December 18, 2018, ESMA updated the Q&As for benchmark indices on a specific issue related to the methodology and underlying data.

The question is whether the methodology of a benchmark index can include factors that are not underlying data.

ESMA responds in the affirmative by specifying that the factors should not measure the underlying market or an economic reality that the benchmark index intends to measure but are elements that improve the reliability and representativeness of the index. This would be the essential distinction between the factors inherent in the methodology and the underlying data.

For example, the methodology of an equity benchmark index may include, in conjunction with the values of the underlying shares, a number of other elements, such as the float rate, dividends, volatility of the underlying shares, *etc.* These factors are included in the methodology to adjust the formula to obtain a more accurate quantification of the equity market than the benchmark index intends to measure, but they do not represent the share price of the benchmark index.

## **ESMA publishes updates to the Q&A on the market abuse regulation**

On November 12, 2018, ESMA updated the Q&As on market abuse by answering the following question:

"Does the prohibition in Article 19 (11) of the MAR Regulation include the issuer's transactions in its own financial instruments, in the case where it is *PD MRs (Person discharging managerial responsibilities)* who make the decision or put a previous decision into practice?"

ESMA replied in the negative. Indeed, Article 19 (11) of the MAR prohibits an issuer's PD MRs, and not the issuer itself, from entering into any "*transactions on its own account or for the account of a third party, directly or indirectly, relating to the shares or debt instruments of the issuer or to derivatives or other financial instruments linked to them during a closed period of 30 calendar days*" before the announcement of a financial report.

Since the actions of the PD MR (officer or employee of the issuer) are not undertaken on behalf of a third party, but on behalf of the issuer itself, the prohibition in Article 19(11) does not apply.

However, it should be noted that any transaction carried out by the issuer during a closing transaction must be treated with caution, as the issuer is still subject to the prohibition (of insider trading) referred to in Article 14 of MAR.

Consequently, when the issuer is in possession of inside information relating to its own financial instruments, the issuer will not be able to trade them unless it has established and implemented the necessary procedures referred to in Article 9 (1) of MAR.

## **The AMF adjusts the timetable for updating Base Prospectuses**

After consulting the AFTE at the end of November, the AMF organised the timetable for updating the Base Prospectuses of EMTN Programmes (and structured securities) with a view to the Prospectus Regulation taking full effect on July 21, 2019 (AMF Press Release of December 20, 2018). This will allow an orderly process (1) of the updates normally scheduled before that date, but above all (2) of the early updates (taking into account the publication of the latest Annual Report / Reference Document), in order to benefit from the "grandfather clause" of Article 46.3 of the new Prospectus Regulation.

The text allows, for Base Prospectuses approved before July 21, to benefit for 1 year from the old regime applicable until that date, not only as regards issues made under the Programme,

but also as regards the structure and content of updates. For issuers with an EMTN Programme or a Structured Securities Programme, this is equivalent to a one-year postponement of the application of the new Prospectus Regulation (from the date of update of the Base Prospectus), provided that they do not offer to the public or quote "stand alone" bonds or issue equity securities after July 21, 2019. This would require managing the distortion of information and risk factors which would necessarily be done under the new regime.

### **Trend analysis of Initial Coin Offerings**

On November 14, 2018, the AMF published, following its UNICORN programme, a two-part study on ICOs: an analysis from the perspective of the French market and a questionnaire study of the global market.

Concerning the French market, the ICOs concern:

- small companies whose activity is mainly related to blockchain or finance;
- increasingly diversified projects that already use traditional financing methods; and
- only 6% of *tokens* qualified as financial instruments.

Concerning the global market:

- this method of financing remains marginal (around €20 billion since 2014);
- the majority of ICOs were conducted in the United States; and
- projects now cover a wide range of fields such as health, energy and retail trade.

The AMF's analysis also looks at the success factors of an ICO, which it considers can be summarised in the following two points:

- strong anti-money laundering procedures; and
- transparency of information provided to investors.

In this context, the AMF recalls that it has opted for an optional visa for ICOs under the PACTE bill and that international cooperation is essential to identify fraud and establish a coherent regulatory framework.

## **ESMA publishes updates to the Q&A on the prohibition of marketing, distribution or sale of binary options and the restriction of marketing, distribution or sale of contracts for difference for retail customers**

On November 9, 2018, ESMA specified in its Q&As the nature of the payments considered to have been made for the purpose of entering into a contract for difference ("CFD"). ESMA now specifies that these payments must be made in cash.

ESMA further clarifies that cash paid by companies to a customer's account when it provides cash collateral for retail customer assets is not considered to be a payment for the purposes of this definition, regardless of whether the assets are segregated or form part of a trading account dedicated to contracts for difference.

ESMA also clarified the extent to which a company can ensure the visibility of the warning provided for in Annex II of ESMA Decision 2018/796 on the temporary restriction of contracts for difference in the Union ("CFD Decision").

As a reminder, Article 2(e) of said CFD Decision stipulates that companies must inform retail customers of the risks related to the conclusion of CFDs as soon as they promote them. This rule applies to all communications of information, whether paper or electronic. In the case of a website, all pages of the website must include this warning. In addition, companies must do so as soon as they inform the customer of a possible benefit that may be derived from an investment service or financial instrument.

Section A of Annex II of the CFD Decision specifies that this warning must be of prominent visibility (highlighted), of a font size equal to the predominant font and in the same language as the rest of the document.

ESMA clarified that, when determining the visibility of the warning, companies should take into account the nature of its target audience, the characteristics of CFDs and the likely information needs of the customer to whom the information is addressed.

## Banking

### 15th edition of the Report on corporate governance and executive compensation: thematic approach of the AMF

On November 26, 2018, the AMF published its 15th report on corporate governance and executive compensation, this time focusing on a new approach based on two topical themes: executive movements and the vote on compensation.

In addition to regulatory changes in governance and compensation, including:

- Articles 61 (social issues) and 66 (information transmission) of the PACTE bill;
- the June 2018 revised version of the AFEP-MEDEF code; and
- the integration of the proposals of its working group on "*Shareholders' rights and voting at general meetings*";

The AMF focused on the two themes mentioned above.

With regard to the movements of executives, the AMF reports several statistics regarding in particular the companies and representatives concerned (notably CAC 40), the functions of executives, the procedures for implementing the succession plan and information on the departure of executives.

With regard to the "say on pay" vote on compensation, the AMF analysed the information published on the occasion of the *ex ante* and *ex post* votes on executive compensation for the same sample. Based on the study carried out, it notes that the resolutions on executive compensation are fairly widely approved by the general meetings. On the other hand, the compensation policies implemented do not always offer a dynamic vision (due to the gap between the time when decisions are taken and the time when compensation is awarded).

## Collective management

### Publication by the AMF of various Guides relating to UCIs

At the beginning of 2019, the AMF published the 2019 versions of the following different positions-recommendations/guides as applicable on January 3, 2019, namely the guide:

- for the drafting of commercial documents and the marketing of collective investments;
- relating to expenses;
- the monitoring of UCIs;

- the regulatory documents of UCIs; and
- relating to employee savings funds.

The main points of clarification include:

- the use of preference shares or any instrument with an asymmetrical risk/return profile;
- "Buy & Hold" type management;
- portfolio insurance management;
- the liquidation of ETFs; and
- funds with an outperformance fee.

These various Guides are now up to date with the various amendments (in particular the new provisions relating to the entry into force of MiFID 2 texts and the separation of the legal regimes of investment firms and portfolio management companies). Emphasis was also placed on certain specific points identified during the examination of approval and/or monitoring files.

### **Publication by the AMF of a summary of its thematic audits of the equity capital of portfolio management companies**

On November 22, 2018, the AMF conducted five so-called "SPOT" audits (Supervision of Operational and Thematic Practices) on the monitoring and investment of the equity capital of portfolio management companies. Following these audits, based on its past experience and as part of its supervisory strategy for 2022, the AMF announced its intention to introduce more short thematic audits. The AMF is now presenting the results of these observations made during these various SPOT audits on equity, in particular on:

- the organisation and procedures implemented by the management companies;
- the procedures for determining the minimum capital requirement and regulatory capital;
- the investment of equity capital; and
- their associated control system.

These controls show that the procedures for regulatory valuation, investment and control of equity are insufficiently detailed and operational, but nonetheless to a very limited extent.

In this respect, the AMF recalls certain good practices to prevent the risk of non-compliance (e.g. simulation on the basis of uncertified interim accounts).

Following these audits, the AMF wishes to hold a market discussion to modify the 2012-19 position-recommendation on the Guide to the Preparation of the Programme of Activities for



Portfolio Management Companies and Self-Managed Collective Investments by placing it in a more European context.

### **Publication in November 2018 by AFG and AFTI of the Guide to outperformance fees for UCITS and General Purpose Investment Funds (FIVG)**

Some of the funds in the market operate with pricing structures that include outperformance fees designed to align the interests of investors and management companies.

For the purpose of analysing these commissions, AFG and AFTI have collected a set of best market practices in order to promote them as market standards with the aim of better aligning the interests of investors and management companies.

The Guide is divided into two parts:

- a first part which concerns the methodological principles for calculating outperformance fees; and
- a second which focuses more on the technical aspects of the application of outperformance fees.

The Guide is didactic, very detailed and gives an exhaustive overview of the applicable methodologies, as well as many examples from market practice.

## **Insurance**

### **Consultation of ESAs on the proposed amendments to the key information document on PRIIPs**

On November 8, 2018, the ESAs were consulted on the proposed amendments to the PRIIPs KID.

On October 1, 2018, the ESAs announced in a letter to the European Commission their intention to make proposals to support the legislative amendments in order to avoid the possibility of duplicating the information requirements for investment funds from January 1, 2020 and to resolve the key issues that had arisen since the implementation of the KID.

This consultation of November 8, 2018 deals in particular with changes to the information relating to performance scenarios for investment products.

These proposals fall within the framework of the ongoing discussions between European legislators on the application of KID by certain investment funds and the broader and more comprehensive review of PRIIPs. The results of this consultation are without prejudice to the results of the wider review to be carried out at the beginning of the European Parliament's next term of office.

In addition, in deciding on the nature of their final recommendations following the full consultation of PRIIPs, the ESAs will take into account the responses to this consultation.

### **EIOPA consultation on the integration of risks and sustainability factors**

Following the request of the European Commission of August 1, 2018, on November 26, 2018, EIOPA published for consultation its draft technical opinion on possible amendments to the delegated acts adopted in accordance with the Solvency II Directive and the Insurance Distribution Directive in order to take into account risks and sustainability factors.

The proposed amendments to the Solvency II Delegated Regulation aim to ensure that risks related to sustainable development in investment activities are identified and assessed. Insurance companies must take into account the potential long-term impact of investment decisions on sustainability factors (management principle) and, where applicable, the environmental, social and governance ("ESG") preferences of subscribers.

These proposed amendments include progress in the following two areas:

- conflicts of interest: when identifying the types of conflicts of interest that may affect a customer's interests, insurance companies and insurance intermediaries should include those that may potentially arise in terms of sustainability. Insurance undertakings and insurance intermediaries must put in place appropriate provisions to ensure that ESG considerations are included in the advisory process and do not lead to misleading practices; and
- product supervision and governance: ESG preferences of customers in a target market must be taken into account at different stages of the product life cycle when the insurance product is offered to customers seeking ESG insurance products.

## **EIOPA publishes its opinion on long-term cross-border non-life insurance activities and their supervision**

On December 21, 2018, EIOPA published its opinion on long-term cross-border non-life insurance activities and their supervision. The opinion is addressed to the competent national authorities and describes EIOPA's expectations regarding the calculation of technical provisions and their governance.

The purpose of this opinion is to ensure the consistent and correct application of the practical legal requirements in this area. Such an activity requires both knowledge of the specificities of the market and actuarial skills to calculate technical and management provisions for this activity.

Unfortunately, experience has shown that these activities attract actors who do not have the required knowledge and skills.

This opinion underlines the need for all parties concerned to be aware of local specificities and describes EIOPA's expectations of companies and the recommendations addressed to the competent national authorities, namely:

- expectations for actuarial provisions with an emphasis on the calculation of the best estimate;
- governance expectations, regarding in particular key functions and management or supervisory bodies; and
- recommendations on the prudential supervision process and collaboration between national competent host authorities.

In addition, the opinion contains annexes providing concrete examples and quantitative analyses of information on the technical provisions of French insurance against construction defects and Italian insurance against medical malpractice.

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