Kramer Levin

Banking, Finance and Insurance Letter

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Legal News: May-June 2019

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- 09-10/07/2019 – **Paris Europlace International Financial Forum** – H. de Vauplane
- 11/07/2019 – **GDPR Thursdays Breakfast - "HR management in the GDPR environment: how to adopt a practical approach"** – N. Lenoir, C. de Guillebon and H. Bérion
- 16/07/2019 – **Real estate tax conference "Restructuring of real estate companies: the FRA ruling of the Conseil d'Etat (April 24, 2019), a review of the Quemener case law"** – P. Appremont

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BANKING & FINANCE

PACTE Law on the grown and transformation of companies (JORF no. 0119 of May 23, 2019)

The PACTE Law includes many provisions... You will find the main themes below.

1. **Simplify the applicable thresholds**: Threshold obligations will be significantly eased and simplified to create a new legal environment that is more conducive to the growth of SMEs.
2. **Remove the social contribution on incentive and profit-sharing schemes**: Incentive agreements will be made easier for companies with less than 250 employees with the abolition of the social contribution.
3. **Rethinking the place of the company in society**: The Civil Code and the Commercial Code will be amended to strengthen the consideration of social and environmental issues in the strategy and activity of companies.
4. **Create your business fully online at a lower cost**: The lives of entrepreneurs will be simplified through the creation of a single online platform for business formalities.
5. **Facilitate the rebound of entrepreneurs**: The time and costs of judicial liquidation proceedings will be reduced and their predictability improved.
6. **Bringing public research closer to the company**: The journey of researchers wishing to create or participate in the life of a company will be simplified in order to boost the links between public research and the private sector.
7. **Facilitate business transfers**: The Dutreil pact will be renewed for free transfers. Business transfers to employees and the financing of the takeover of small businesses will be facilitated.
8. **Simplify and ensure the portability of retirement savings products**: Everyone will be able to keep and pay into their savings product throughout their professional career and the capital outflow will be facilitated.
9. **Supporting export SMEs**: The export support model will be transformed by the creation of a one-stop shop in the region so that international business is a natural outlet for SMEs.
10. **Protecting strategic companies**: The prior authorisation procedure for foreign investment in France (IEF) will be strengthened and extended in order to better protect strategic sectors.

European Union: Prudential regime for investment firms

The Decree of April 24, 2019 (JORF no. 0104 of May 4, 2019) aims to align the prudential regime for investment firms and that of credit institutions by making the delegated regulations, implementing regulations and implementing decisions adopted by the European Commission for credit institutions applicable to investment firms, pursuant to Regulation (EU) No. 575/2013 of the European Parliament and of the Council of June 26, 2013 and Directive 2013/36/EU of the European Parliament and of the Council of June 26, 2013.

Cross-border mergers: The obstacles to overcome

In its current form, the Banking Union makes cross-border mergers unattractive, the main obstacle being the fragmentation of capital and liquidity faced by transnational institutions. A high-level working group set up by Ecofin on December 4, 2018 is discussing the subject and should soon take stock of its progress" - Dossier published in the June 2019 Revue Banque.

COMPLIANCE

France: Adoption of the new decree implementing the Data Protection Act

On May 29, 2019, the government adopted the new decree implementing the Data Protection Act. The adoption of this implementing decree finalises the adaptation of the French legal framework for the protection of personal data to the General Data Protection Regulation (GDPR).

The adoption of this decree follows the amendment of the Data Protection Act by the Law of June 20, 2018, followed by its rewriting by the Order of December 12, 2018.

The decree therefore improves the legibility of the French data protection regulatory framework. It also makes some substantive amendments and repeals Decree No. 2005-1309 implementing the Data Protection Act. The decree clarifies and details the regime applicable to professional secrecy and the role of the CNIL as relevant lead authority or supervisory authority. It also provides for the possibility for data subjects to exercise their rights by means of a mandate and details the system for the liquidation of penalty payments in the event of non-compliance with a compliance order.

CAPITAL MARKET

First ESMA Q&As relating to the Prospectus Regulation

On March 27, 2019, the European Securities and Markets Authority (ESMA) published its first Q&A document on the Prospectus Regulation (EU) 2017/1129 of the European Parliament and of the Council of June 14, 2017.

They specify the scope of the grandfathering clause of documents approved on the basis of the Prospectus Directive, which governs the content, approval, updating and passport of the "old" rules of the Prospectus Directive; however, the rules of the Prospectus Regulation on advertising are applicable in this case.

It is specified that the existing Q&As on the Prospectus Directive are applicable to prospectuses drawn up pursuant to the Prospectus Regulation, insofar as they are compatible with it.

In addition, ESMA is working on the complete update of its Q&As. It will probably not be published until July 21, 2019.

ESMA Guidelines on risk factors in the Prospectus

On March 29, 2019, ESMA published its final report on the guidelines for risk factors in the prospectus.

The following principles are addressed directly at the competent national authorities for application when approving a prospectus:

1. the risk factors are limited to those risks that are specific to the issuer and/or the securities and that are important for making an informed investment decision;
2. each risk factor must explain how it affects the issuer or the securities, in concise, simple, non-technical language that can be understood by any investor;
3. the materiality and specificity of the risk factors are corroborated by the content of the prospectus (universal registration document, base prospectus, note on securities) with a consistent and coherent presentation;
4. risk factors are presented in categories (normally limited to a total of 10) according to their nature, both for the company and the securities. In some cases, such as in structured securities programs, the number of categories may be increased;
5. the significance of risk factors should be assessed in terms of the probability of their occurrence and the estimated magnitude of their negative impact. The most important risk factors are mentioned first. A qualitative scale can be used, indicating whether the risk is low, medium or high; and
6. in the Summary, where required, the exercise will consist in giving, in a concise and non-misleading manner, an image of the key information on the risks relating to the company and the securities, consistent with the "Risk Factors" Section of the prospectus.

AMF public consultation on the adaptation of its General Regulations to take into account the Prospectus Regulation

On May 14, 2019, the AMF launched a public consultation (closed on June 14) on the amendment of around 100 articles of its General Regulations designed to ensure that domestic law is consistent with the Prospectus Regulation, without disrupting current practices in France.

These are:

- the consideration of the consequences of the adoption, under French law, of the European definition of the public offering of securities;
- the "negative transposition" of the Prospectus Regulation (deletion of certain national provisions and direct reference to the provisions of the Regulation); and
- the deletion or modification of articles identified as "over-transposing" European texts.

The changes concern in particular the following subjects:

1. the Prospectus Regulation extends the definition of the public offering and includes offers which, until now, were not considered as public offers under French law (e.g. "private placements" or offers relating to crowdfunding). French law would now refer directly to the definition in the Prospectus Regulation, not with regard to the prospectus publication requirement, but with regard to the determination of issuers authorised to offer securities to the public;
2. the necessity, exception and form of the offer document will depend on the offer: either (i) the Prospectus Regulation will apply directly or (ii) national law (for public offers of less than €8 million on unlisted securities, equity financing, public offers on company shares and mutual certificates);
3. the scope of the issuers concerned would be extended: companies would no longer simply be concerned but "persons and entities", i.e. associations, EIGs, natural persons, etc.;
4. the securities concerned would include financial securities, company shares and securities within the meaning of MiFID;
5. the definition of qualified investor would be the definition in the Prospectus Regulation; the reference to an offer which is addressed exclusively to "persons providing the investment service of portfolio management on behalf of third parties" would therefore be deleted as redundant;
6. certain provisions or exceptions that applied to "private placements" should therefore be included: for example, the provision exempting offers of less than €8 million or whose

entry ticket exceeds €100,000 from appointing representatives of the group in the issue contract;

7. with regard to the language regime, it is proposed to clarify that not only the prospectus but also the offer document equivalent to a prospectus exemption may, in certain cases, be drawn up in "another language customary in financial matters";
8. the principles relating to the responsibility for drawing up the prospectus, which until now appeared, in part, in the AMF General Regulation, would be transferred in full to the Monetary and Financial Code;
9. the new text proposes to modulate the obligation to disseminate information by means of the written press;
10. The obligation to file an information document in the event of a merger, demerger or partial contribution of assets on which the Prospectus Regulation is silent would be maintained; only significant transactions would be subject to a prior filing obligation (admission of at least 20% more securities than those already admitted); and
11. in order to ensure consistency with the sanctions provided for in the event of breaches of other European financial texts, it is proposed that the maximum amount of administrative sanctions applicable in the event of an irregular public offer in violation of the provisions resulting from the Prospectus Regulation may be increased to 15% of the total turnover of the person sanctioned.

Update of ESMA Q&As on the Benchmarks Regulation

On May 23, 2019, ESMA published an update of its Q&As document on the Benchmarks Regulation ((EU) 2016/1011). Three clarifications are provided:

1. the date of determination of the reference Member State, on the occasion of an application for recognition of an administrator located in a third country, shall be the date of the application;
2. in order to be able to use a benchmark provided by an administrator located in a third country, the administrator must first be recognised by the competent authority of his reference Member State. For this purpose and to assess compliance with the International Organization of Securities Commission (IOSCO) on benchmark indices, the competent authority of the reference Member State "may rely" on an assessment by an independent external expert. The Q&As state that it is not simply a matter of relying on such an assessment. The text gives some examples of elements of the audit report that can be considered by the competent authority; and
3. the register of administrators must not only indicate the contact details of an administrator but also include the administrator's website and the link to the web page where the administrator publishes the benchmark.

Official translations of the ESMA Guidelines on Insignificant Benchmarks

On June 19, 2019, ESMA published the official translations of its guidelines for insignificant benchmarks. The final report was published on December 20, 2018.
The competent authorities of the Member States must inform ESMA of their compliance or intention to comply with these guidelines within two months of the publication of the translations.
ESMA also provided clarifications in its Q&As document updated on March 29, 2019.

ICO

Recognition of tokens within the framework of an ICO

In France, the Accounting Standards Authority (ANC) has specified the accounting treatment of tokens issued and held. The question of IFRS treatment is raised...

MIFID 2

Europe in the face of regulation and its negative impacts on the economy

Just over a year after its implementation, the European MiFID 2 Directive has already revolutionized the world of financial analysis. By reforming the research funding model, these new rules highlight the limits of a regulation that focuses exclusively on the cancellation of externalities and the absence of a European Union financial strategy, which are detrimental to the real economy.

INSURANCE

EIOPA reminder on the importance of big data analysis in the insurance context

Like banks, insurance is largely affected by the evolution of new technologies. Having an efficient digital strategy then becomes a sine qua non condition for maintaining the activity.

EIOPA notes that the development of big data is an opportunity for professionals to improve the analysis of customer needs and behaviour, and hence the insurance offer.

As EIOPA points out, data processing has always been at the heart of insurance companies' activities. Data collection is the first step towards the development of new insurance products and services.
The use of data makes it possible to understand and anticipate customer behaviour, to assess risks as accurately as possible and, finally, to improve production processes.
In this context, EIOPA launched a thematic review on the use of big data by insurance companies in the summer of 2018, focusing on two sectors: motor insurance and health insurance.

- **Who participated?**

More than 222 insurance companies and intermediaries participated in this extensive study. The data collected represents 60% of the total gross premiums written in the motor and health insurance lines of the 28 states covered by this consultation.
The study focused both on traditional insurers, who have been in business for a long time, and on *start-ups*, which are not very representative in terms of the number of policyholders but are the first users of innovative digital solutions, including big data.
EIOPA also received comments from the competent national authorities and two consumer associations.

- **What are the results?**

First, EIOPA notes an increase in the number of data collected through big data. In addition to traditional demographic and exposure data, new sources have been added, such as online and telematic data. As a result, information is improved and products and services are increasingly personalised.
Second, the study focuses on a new practice: the use of external data from third-party data providers. Based on state-of-the-art algorithms, they refine the calculations of credit, driving, claims and other scores.

- **What are the main analytical tools used by insurance companies?**

More than 30% of companies are already actively using machine learning and more than 24% are in the proof-of-concept stage. For the most part, they are used to establish the underwriting policy, in particular the pricing policy, and for claims management.
The EIOPA report shows that the consequence of using big data is the development of many analytical tools that allow accurate assessments with limited human intervention, and therefore, a significant reduction in operating costs.
Finally, the study noted the new importance of data storage in the clouds (more than 60% of companies already use or will use the cloud to store the data collected by 2021). IT and data protection security then become essential issues for insurance companies.

- **The insurance value chain and big data**

Big data is increasingly used throughout the value chain. Models based on these tools are mainly used for pricing, underwriting, claims management and commercial distribution.
Insurance companies have developed a sophisticated customer relationship through customized platforms and chatbots, allowing minimal permanent interaction with the customer while saving time.
Big data is also already widely used to detect fraud during the claims process and in the context of payment automation.
Big data also makes it possible to develop data analysis tools to improve risk assessment, particularly through new risk scores.
Finally, all the so-called "connected" elements (connected cars, 5G mobile technology, etc.) will significantly increase the range of services offered to customers.

➢ What is the conclusion?

EIOPA concludes that big data represents a real opportunity for both the insurance industry and its customers.
However, it notes that with big data, if not new risks, there are increased risks of compromising the protection, transparency, monitoring and verifiability of data collected and used by insurance companies.

Reminder of the recommendations resulting from the 2018 EIOPA stress test on insurance

In accordance with Article 21 §2 b) and 32 of Regulation 1094/2010, EIOPA launched a Europe-wide stress test in 2018. The results of this insurance stress testing exercise resulted in a series of recommendations.

This stress test consisted of three exercises: the first two were based on scenarios combining specific market and insurance risks (either a sudden reversal of risk premiums in global markets leading to tighter financial conditions or a prolonged period of extremely low interest rates) and the third followed a natural disaster scenario.
The 42 insurance companies participating in this stress test calculated the impact on their own funds and solvency capital requirement of the three scenarios considered.
The objective of this simulation exercise was to assess the resilience of the European insurance sector to adverse scenarios that could have negative repercussions on the stability of financial markets and the real economy.
The results of this major simulation exercise demonstrated that the European insurance sector is sufficiently capitalized to absorb the combination of shocks proposed by the various scenarios without, however, denying a significant sensitivity of the insurance sector to market shocks.
Low returns, longevity risks, a sudden and sharp reversal of risk premiums combined with a instantaneous shock to lapse rates and claims inflation are all risks that insurers should better anticipate.
The exercise also highlighted the different transmission channels and catalysts of insurance crises. The vulnerabilities of the sector as a whole have thus been identified, and have given rise to the EIOPA recommendations set out below.

- **Recommendation 1: The need to strengthen surveillance**

NCAs should strengthen the supervision of the Groups identified as facing greater exposure to Yield Curve Up and/or Yield Curve Down scenarios.

- **Recommendation 2: Review capital and risk management strategies**

Regulators are encouraged to challenge the capital and risk management strategies of affected groups.
EIOPA emphasizes three points. They must require groups:

- To clarify the impact of the stress test in terms of capital and risk management,
- For the affected groups, stress test scenarios similar to those performed as part of the 2018 stress test will have to be taken into account in risk management policies,
- Examine the "risk appetite" of the different groups affected.

- **Recommendation 3: Assessment of potential management measures to mitigate identified risks**

EIOPA recommends that regulatory authorities:

- require groups to indicate the range of actions to be taken based on the results of stress testing,
- assess whether the actions identified are realistic,
- take into account any potential second-round effects.

Only then can they consider corrective measures to be taken by the groups concerned, such as, for example, increasing the current capital surplus to absorb losses in the most serious scenarios or imposing greater diversification of the product portfolio, seeking measures to reduce portfolio risk, reduce the cost of guarantees to a sustainable level on the basis of current asset returns or reduce the dependence of the SCR calculation on loss absorption mechanisms.

- **Recommendation 4: Improve the stress assessment process in light of future exercises**

EIOPA is committed to improving the relevance of stress tests. To do this, regulators will need to verify the adequacy of supporting systems and technologies and the flexibility of risk modelling used by groups to conduct national stress tests and prepare for large-scale European exercises.

They should also ensure that national experts make resources available for future exercises.

- **Recommendation 5: General recommendation for cross-sectoral coordination**

EIOPA is mandated by its regulations to act in the field of financial conglomerates' activities. Indeed, the results of the stress test showed that some of the insurers most affected were part of financial conglomerates. These groups are then particularly vulnerable either to low returns and longevity risk, or to a sudden and abrupt reversal of risk premiums combined with an instantaneous shock to lapse rates and claim inflation.

Thus, EIOPA recommends that supervisory authorities strengthen the dialogue with competent authorities, such as those that manage prudential supervision at the level of the group of financial conglomerates and banking groups with large insurance subsidiaries.

Finally, EIOPA recommends that regulatory authorities keep it informed of related cross-sectoral discussions.

Update of the joint guidelines of the Directorate General of the Treasury and the ACPR and resolution on the implementation of asset freezing measures

On June 17, 2019, the ACPR published an updated version of its joint guidelines with the Directorate General of the Treasury (DGTRESOR).

This version updates the guidelines published in June 2016 in order to take into account, in particular, the reform of the assets freezing mechanism resulting from Order No. 2016-1575 of November 24, 2016 and Decree No. 2018-264 of April 9, 2018.

Although no major changes are made, some modifications are nevertheless worth noting:

- the concept of nuclear proliferation is replaced by that of weapons of mass destruction;
- the guidelines now highlight the fact that freezing measures, like other financial penalty regimes, cannot in themselves constitute discriminatory treatment of categories of clients on the basis, for example, of residence or nationality alone;
- as regards the definition of assets, the guidelines specify that the definitions of the terms "freezing of funds", "freezing of economic resources", "funds" and "economic resources" are to be found in each European regulation and in Article L562-1 in a virtually identical manner;
- the ACPR and DGTRESOR expressly point out that non-life insurance is also defined as an economic resource insofar as it provides access to funds;
- the two authorities have expressly pointed out that the freezing of the assets of a legal person owned or controlled by a natural or legal person subject to an asset freezing measure is not systematic, unless an order or regulation expressly designates that legal person. The organisation which detects a situation of control or ownership of a legal person by a natural person subject to an asset freezing measure shall inform DGTRESOR.
- the guidelines specify the points to be audited, namely:
  - the adaptation of the system's configuration to national, European (or local in groups) requirements for freezing assets,
  - the appropriateness of the scope of the system and the quality of customer databases and operational messages,
  - the time required to integrate updates of freeze lists into the filtering system,
  - the time required for the tool to generate alerts,
  - the time required and quality of the analyses of the alerts generated by the tool,
  - compliance with the obligations to declare the implementation of freezing measures to DGTRESOR and, where applicable, to local authorities,
  - monitoring the practical application of the freezing or prohibition of the provision of funds or economic resources,
  - the training, qualification of the personnel concerned or their timely access to all necessary information.

- in accordance with Article R. 562-1 of the amended Monetary and Financial Code, the guidelines now specify that insurance brokers or brokers in banking and payment services must set up an internal control system for freezing measures adapted to their size and activity. This obligation is without prejudice to the permanent and periodic internal control exercised by the delegating organisation. They also add that the group parent company ensures, as part of the internal control system it sets up at group level, that the group's entities concerned properly implement national and European measures. Failing this, the organisations must inform DGTRESOR without delay.
- there is also an obligation to screen candidates for recruitment: in accordance with the provisions of Article L. 561-32 and Article R. 561-38-1, financial institutions ensure that persons involved in the implementation of asset freezing obligations and the fight against money laundering and terrorist financing are not subject to national or European asset freezing measures.
- as regards the implementation of freezing measures and the prohibition on the provision of funds by institutions in the banking, payment and investment services sector, the guidelines now address new situations, namely: leasing, documentary credits, prepaid cards and jackpots; and
- finally, with respect to the treatment of business relationships with the person, the guidelines specify that organisations must implement appropriate due diligence measures with respect to business relationships with the spouse, parents, siblings and any other family members of their client subject to a measure.

ACPR report on insurers subject to Solvency II at the end of 2018

In its report, the ACPR points out that the French insurance market grew in 2018 both in terms of turnover and technical results.

From its market analysis, the ACPR deduced several major trends, namely:

- 2018 was characterised by a reversal in the collection of funds on Euro-denominated instruments. Thus, the regulator points out that the trend towards net outflows on Euro-denominated instruments that was observed at the end of 2016 was reversed in 2018. It explains that this trend is due to a sharp slowdown in redemptions (decrease of 10 billion between 2017 and 2018);
- the non-life insurance claims ratio remained at high levels: the ACPR noted that the claims ratio (up 2.4% in fire and other property damage and 4.7% for other motor vehicle insurance) in 2018 was, for the most part, borne by insurers. The claims ratio of reinsurers has therefore declined;
- the solvency of insurers remains satisfactory: the ACPR report shows that the coverage rate of the solvency capital requirement increased by 6 points over the period and has

therefore risen to 240%. The solvency level of non-life organisations remains higher even though the ACPR notes that the increase is less than that of life organisations. As for the coverage ratio, the minimum capital requirement has increased by 13 points to 585%;

- the impact of the poor performance of the financial markets on insurers' investments: the ACPR notes that the value of French insurers' investments remained at €2,493 billion in market value at the end of 2018, down slightly by 0.3% year-on-year; and
- insurers were preparing for Brexit: the ACPR noted that the United Kingdom's share of activity carried out in France by foreign bodies via the European passport (LPS-LE) decreased by 11 percentage points between 2016 and 2017.

Pacte Law: Impact on life insurance

Law No. 2019-486 of May 22, 2019 on the growth and transformation of companies (the Pacte Law) was published in the Official Gazette on May 23, 2019. Article 72 of the Pacte Law amends certain provisions relating to the French regime applicable to life insurance contracts.

Thus, the list of eligible investment vehicles that may be offered in unit-linked life insurance policies is extended to new investment vehicles such as units in alternative investment funds open to professional investors, subject to certain conditions, linked in particular to the financial situation, knowledge or financial experience of the subscriber.

In addition, at least one type of unit of accounts in funds labelled SRI (Socially Responsible Investment), green finance, or financing solidarity businesses should be proposed.

Article 72 also includes certain provisions relating to the delivery of securities or shares when the insurance contract ends and creates new disclosure requirements.

Thus, quarterly information will be due on the amount of the surrender value and the value of the units of account, and annual information, relating to the commissions received by the insurer for asset management, and more generally, on the fees charged by the insurance company.

A new pre-contractual information obligation has also been created for insurance companies and/or intermediaries distributing unit-linked life insurance policies.

The various provisions of the Pacte Law enter into force the day after the publication of the law, subject to specific provisions.

European Union: Solvency II - Technical information

The European Commission's Implementing Regulation 2019/699 under the Solvency II Directive was published in the Official Journal of the European Union on May 7, 2019.

It thus defines the technical information to be used by insurance and reinsurance undertakings for calculating actuarial liabilities and core capital for declarations with a reference date between March 31, 2019 and June 29, 2019.

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