

A blue-toned background image featuring a financial line chart with multiple data series and a grid. The chart shows various trends, including a sharp decline followed by a recovery and another decline.

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6 December 2017

Financial Regulation Monthly Breakfast Seminar

Overview

- FCA's first competition enforcement case
- FCA's Policy Statement on reordering the IPO process
- MiFID II – Mandatory Trading Obligation
- EU Benchmarks Regulation – latest Q&A
- Market Abuse: Walter Fine



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FCA's first competition enforcement case

David Berman

FCA: Competition Enforcement

- First FCA competition enforcement case – brought under Competition Act 2008
- FCA has issued statement of objections to 4 asset managers in respect of alleged pricing collusion ahead of an IPO/placing
- Allegations that the asset managers disclosed and/or accepted information on what they intended to pay for shares or were willing to pay for shares
- Provisional finding at this stage – the four firms now have the opportunity to make formal representations before final determination is made (as to whether the law has been breached)

Practicalities

- Analysis/visibility of risks and hot-spots
- Incorporation of competition law risks/considerations into firm's risk assessment/management and control framework
- Monitoring/assurance
- Knowledge across firm of how competition law may apply to businesses, including regular training
- Appropriate systems, process and procedures to ensure continuous ability to fulfil notification obligations
- Incident review and response protocol – where necessary, effective paper trail of review of, and response to, incidents
- Adapting internal processes and language to reflect competition law considerations



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FCA's Policy Statement on reordering the IPO process

Rob Moulton

Background

- PS17/23 is a follow up to the March CP
- Aims
 - Make the prospectus great again
 - Create conditions for unconnected research to flourish
 - Focus on standards of conduct and management of conflicts in connection with connected research
- Background of MiFID II assault on the research industry
- FCA has decided not to apply the rules to AIM, but recommends them as best practice, in particular in larger AIM IPOs

Timing and Sequencing of the IPO Process

- Approved prospectus to be published before any connected research
- Underwriter must select a range of unconnected analysts that have a reasonable prospect of enabling investors to make better-informed decisions
 - No restriction on access to the issuer by unconnected analysts to discourage the production of unconnected research
 - Firm must not disseminate connected research until after publication of prospectus (if unconnected analysts are briefed at the same time as connected analysts) or seven days after publication of the prospectus
- Firm must keep written records to demonstrate unconnected analysts had access to identical information
 - How can this be done if they are not in the same room?

Conflicts of Interest

- FCA's view is that analysts can come under pressure to produce favourable research to help their bank secure a mandate
- Analyst interactions therefore banned before the bank has accepted a mandate and its position in the syndicate is confirmed in writing
- Restriction does not apply if the analyst is unaware of pitches, and does not believe a pitch has taken place
- FCA notes that MiFID II explicitly obliges firms to physically separate analysts producing Investment Research
- Above rules do not apply to non-independent research (although FCA warns of conflict management points)

Market Abuse Considerations

- Recommendation of an ongoing assessment of price/value relationships between existing instruments and potential IPO instruments
- Proposed IPO is not necessarily inside information, but nor is it the only potential inside information that may need to be considered, in particular in analysts' presentations
- FCA reiterates its statements about wall-crossing analysts not necessarily being in the course of the issuer's employment, profession or duties (one week for unconnected analysts is seen as long enough)

The background of the slide is a blue-toned financial chart. It features a grid of horizontal and vertical dashed lines. A thick, glowing blue line represents a data series, showing a downward trend on the left, a small peak, a dip, and then a sharp decline. On the right side, the line becomes more jagged and fluctuates. At the bottom of the chart, there are some faint, partially visible labels like '12h' and ':30'.

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MiFID II – Mandatory Trading Obligation

Stuart Davis

Mandatory Trading Obligation for Shares

- Article 23 MiFIR: Firms must ensure all trades (including trading on own account and trading for clients) it **undertakes** in shares admitted to trading on a regulated market or traded on a trading venue take place on a regulated market, MTF or SI, **or an equivalent third country trading venue**, unless the trading falls within the following exclusions:
 - non-systematic, ad-hoc, irregular and infrequent; or
 - carried out between eligible and/or professional counterparties and do not contribute to the price discovery process (e.g. give up trades)
- Investment firms operating BCNs/internal matching engines for shares, depositary receipts, ETFs, certificates and other similar financial instruments on a multilateral basis must ensure they are authorised as MTFs

Extraterritoriality Issues: AFME / IA / AIMA Letter

September 2016

- No equivalence determinations yet been made under MiFID II / MiFIR
- A large number of shares that are traded on an EEA venue have their primary listing (and often most liquidity) in a third country, e.g. Börse Berlin enables trading “in over 10,000 shares from 120 countries. Are these shares within the scope of the MTO?”
- Equivalence decisions may not be made in relation to less developed markets causing uncertainty in relation to shares with a primary listing in those markets
- Possible negative impact on investment from EEA, resulting in a likely movement of funds and capital out of the EEA over the longer term

ESMA Statement Alongside Q&A

- Primary market transactions out of scope but ABBs and share buybacks in scope (as secondary market transactions)
- Where there is a chain of transmission of orders concerning shares falling within the scope of the MTO, all EU investment firms that are part of the chain (either initiating the orders or acting as brokers) should ensure that the ultimate execution of the orders complies with the MTO
- Therefore, where an **EU investment firm** transmits an order for a share admitted to trading on a regulated market or traded on a trading venue to an EU investment firm that subsequently passes it on to a **non-EEA firm**, the **EU investment firm** should ensure the trade is undertaken in accordance with the requirements set out in Article 23 of MiFIR, i.e. on a regulated market, MTF, SI or equivalent third country venue

ESMA Statement alongside Q&A

- *“ESMA is aware that the scope of the MTO, and the absence of the relevant equivalence decisions, might cause issues for investment firms that wish to undertake trades in non-EEA shares in the primary listing venues of such shares. ESMA and the European Commission are working closely together to resolve those issues. While the Commission is preparing equivalence decisions for the non-EU jurisdictions whose shares are traded systematically and frequently in the EU, the absence of an equivalence decision taken with respect to a particular third country's trading venues indicates that the Commission has currently no evidence that the EU trading in shares admitted to trading in that third country's regulated markets can be considered as systematic, regular and frequent”*
- “Verena Ross, Executive Director of ESMA, ASIFMA Speech on 30 Nov 2017: ESMA currently assessing 200+ trading venues for MiFID II equivalence. “I hope that our recently issued guidance together with the European Commission provided you with some comfort that, in the absence of an equivalence decision, transactions in shares would not be considered to be of a systematic, regular and frequent nature and therefore not subject to the trading obligation for shares”

ESMA Statement Alongside Q&A

- Ongoing issues:
 - How binding is the ESMA statement?
 - Does this put equivalent jurisdictions in a worse position than non-equivalent jurisdictions
- Recent FCA dialogue with trade associations

Update on Mandatory Trading Obligation for Derivatives

- Applies to FCs and NFC+ but not intra-group transactions under Article 3 of EMIR
- Transactions in OTC Derivatives which are subject to the mandatory clearing obligation under EMIR, and which have been declared as subject to the MTO for derivatives by ESMA and the European Commission, must be traded on:
 - A regulated market;
 - An MTF;
 - An OTF; or
 - A third-country trading venue in a jurisdiction that has been deemed equivalent in relation to its legal and regulatory framework for trading venues
- Commission has adopted RTS on (i) fixed to float in EUR, USD, GBP and (2) iTraxx Main and Crossover, which should be finalised by 3 January
- Commission has adopted equivalence decisions for certain US derivatives trading venues

A blue-toned background featuring a financial line chart with multiple data series and a grid. The chart shows various peaks and troughs, with some lines appearing more prominent than others. The overall aesthetic is professional and data-oriented.

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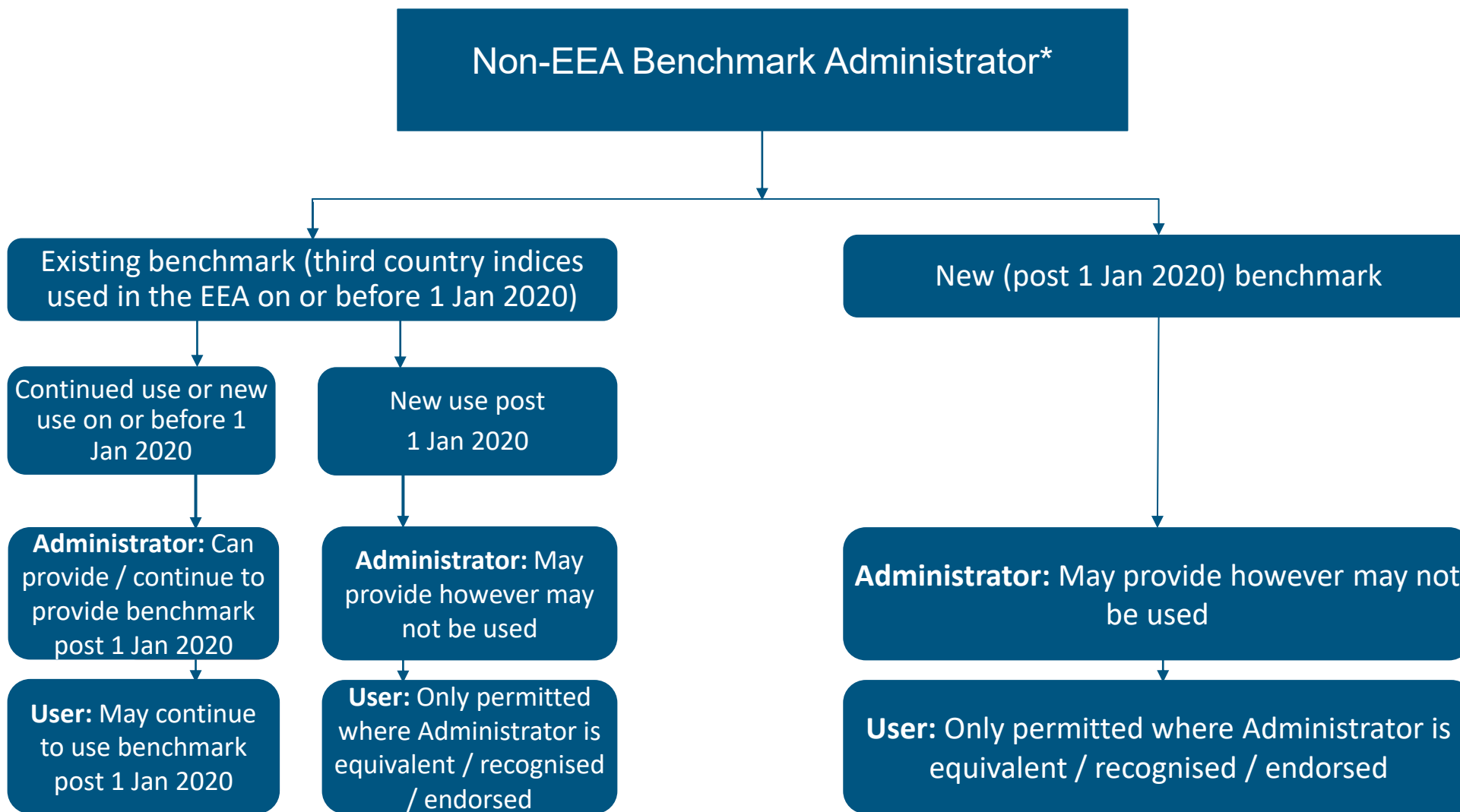
EU Benchmarks Regulation – latest Q&A

Becky Critchley

EU Benchmarks Regulation - latest ESMA Q&A

- ESMA updated Q&A published 8 November 2017
- Application outside the EEA:
 - BMR does not apply to:
 - Benchmarks used exclusively outside the EEA (local law applies)
 - Contributions to benchmarks used exclusively outside the EEA
- Third country benchmarks:
 - Existing non-EEA indices (third country indices already in use in the EEA on or before 1 Jan 2020) can continue to be provided into the EEA until 2020 without action. This covers:
 - Existing financial contracts linked to existing non-EEA indices; and
 - Financial contracts linking to existing non-EEA indices for the first time before 1 Jan 2020. (Note, this is subject to EEA users being happy to continue to link to non-BMR compliant indices post 1 Jan 2018)
 - Action is required if any new non-EEA indices are intended to be sold into the EEA post 1 Jan 2020

EU Benchmarks Regulation – guide to implementation dates



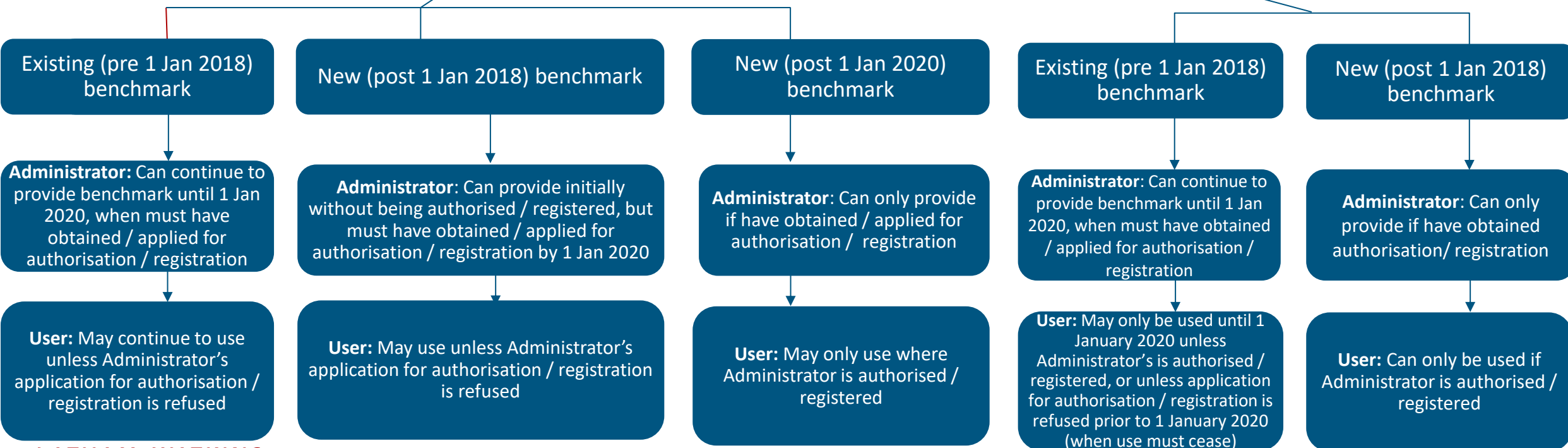
***Note:**

- Non-EEA Benchmark Administrators are not caught by the BMR, the use of their indices in the EEA is. Therefore they may provide indices into the EEA but they may not be used by regulated users
- Irrelevant whether a non-EEA administrator provided

EU Benchmarks Regulation – guide to implementation dates

EEA Benchmark Administrator -
began providing benchmarks:

| | |
|---------------------------|-------------------------|
| On or before 30 June 2016 | On or after 1 July 2016 |
|---------------------------|-------------------------|



EU Benchmarks Regulation – Brexit impact

BMR timetable

30 June 16
BMR in force
(applies to
critical
benchmarks)

1 Jan 18
BMR applies to
all other
benchmarks

1 Jan 20
End of
transitional
period for third
country
benchmarks

29 March 17
Article 50
triggered

29 March 19
UK leaves the
EU and
becomes a third
country;
discussions on
equivalence can
begin

Post 1 Jan 20
Likely to still be
waiting for
positive
equivalence
decision
regarding the
UK

Brexit timetable

EU Benchmarks Regulation Updates

- Updates from FCA engagement
- Industry group responses



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Market Abuse: Walter Fine Nicola Higgs

Market Abuse: Walter Fine

- **Breach:**

- Walter (a Market Maker) entered Best Bid / Best Offer quotes onto BrokerTec in relation to six Dutch State Loans that: (i) were designed to induce; and (ii) had the effect of inducing, other market participants who were tracking quotes to raise or lower their quotes, in order to benefit from price movement
- Legitimate trading:
 - posting bid with either high bid or low offer price and waiting for another market participant to aggress the low bid / high offer; or
 - aggress the bid / offer of another market participant
- Abusive trading:
 - entering quotes at levels that are unlikely to be aggressed by other market participants
 - waiting for other market participants to (auto) adjust their quotes and then entering new quotes (to be automatically tracked by market participants)
 - once quotes hit the desired level – execute transaction
 - cancel own quote to avoid being aggressed

Market Abuse: Walter Fine

- **Key points:**

- Fine: £60,900
- Took advantage of auto tracking algos following Best Bid / Best Offer
- Ignorance no excuse: breach committed 'negligently rather than deliberately'
- 12 instances of abuse over a six week period (20 year career)
- Profit of €22K on Walter's book (no personal profit made / loss avoided)
- Behaviour did not cease when put on notice of concerns about his behaviour (raised by BrokerTec in a phone call)
- Walter did not respond honestly to BAML's internal investigation / FCA investigation

Market Abuse: Walter Fine

- **Key take aways:**

- Actions did not: change the overall liquidity for investors, move market price or create a false or misleading impression as to the **overall supply** and demand in the market place
- Market manipulation includes: creating a false or misleading impression as to **your own intentions** as a buyer / seller
- Does not matter if the misleading impression is '**momentary**'

MAR 1.6.2E(4) (manipulating transactions – false or misleading impressions); **MAR 1.6.4E(3)** (manipulating transactions – price positioning), **MAR 1.6.5E** (not legitimate reasons); **MAR 1.6.9E (5) & (6)** (false / misleading impression); **MAR 1.6.10E** (abnormal or artificial price levels)



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Questions?