Financial Markets Law Committee ("FMLC")

Banking Scoping Forum

Date: Tuesday 11 December
Time: 2.00pm to 3.30pm
Location: Bank of England, Threadneedle Street, London, EC2R 8AH.

In Attendance:

Clare Dawson (Chair) Loan Market Association
Alex Biles Ashurst LLP
Thomas Donegan Shearman & Sterling (London) LLP
Charles Gray (dial in) Sullivan & Cromwell LLP
Ian Jameson Sumitomo Mitsui Banking Corporation Europe Limited
Jons Lehmann Fried, Frank, Harris, Shriver & Jacobson (London) LLP
Dorothy Livingston Herbert Smith Freehills LLP
John McGrath Sidley Austin LLP
Monica Sah Clifford Chance LLP
Jeremy Stokeld Linklaters LLP

Venessa Parekh FMLC
Thomas Willett FMLC

Guest Speaker

Timothy Cleary Clifford Chance LLP

Regrets:

James Bresslaw Simmons & Simmons LLP
Mark Kalderon Freshfields Bruckhaus Deringer LLP
Amy Kennedy Gibson, Dunn & Crutcher UK LLP
Suhaib Khawaja Wilmington Trust
Knox McIlwain Cleary Gottlieb Steen & Hamilton
Oliver Moullin The Association for Financial Markets in Europe ("AFME")
Jan Putnis Slaughter and May
Mitja Siraj FIA
Julia Smithers Excell White & Case LLP
Stuart Willey White & Case LLP
Minutes:

1. **Introductions**

1.1. Clare Dawson opened the meeting.

2. **Administration: Scoping Exercise – Lifecycle of a Project and confirmation of the 2019 Forward Schedule (Venessa Parekh)**

2.1. Venessa Parekh described to the members how new issues of legal uncertainty on which the FMLC can undertake work are raised. She elaborated on the Committee’s process of adopting new projects, how working groups operate, the publication drafting process and the profile of past FMLC publications.

2.2. Attendees did not raise any issues in relation to the draft Forward Schedule of meetings for 2019. These meetings dates were therefore confirmed.

3. **Update on the phasing out of LIBOR (Clare Dawson)**

3.1. Clare Dawson led a discussion on the phasing out of the London Inter-bank Offered Rate (“LIBOR”). She began by mentioning recent developments with regards to consultations including: (i) the preliminary results of a consultation by the International Swaps and Derivatives Association on certain aspects of fallbacks for derivatives referencing GBP LIBOR, CHF LIBOR, JPY LIBOR, TIBOR, Euroyen TIBOR and BBSW; and (ii) Alternative Reference Rates Committee Consultations on Fallback Contract Language for Bilateral Business Loans and Securitizations for Public Feedback.

3.2. Ms Dawson then explained that the derivatives market is relatively comfortable with moving to an overnight rate; the cash market, on the other hand, is finding the transition more difficult. She highlighted that some issues include practical concerns with the bank loans systems and bonds systems, as well as what methodology to use for calculating an overnight rate instead of a forward looking term rates in term structures. Members agreed that there needs to be a reasonable degree of market consensus regarding the methodology.

3.3. With regards to cash products, Ms Dawson explained that there is no protocol mechanism for those contacts that reference LIBOR to provide a fallback reference rate. She mentioned that it will be difficult to amend large numbers of deals without having to amend each contract.

---

1 Please see Appendix I below.
3.4. One member raised an uncertainty regarding the adjustment spread and the worry that it might not prevent a transfer of economics when LIBOR is to be phased out. Ms Dawson agreed that this was one of the most challenging areas to be considered; she did stress, however, that with increasing derivative activity of risk free rates the more the industry will become comfortable with using them.

3.5. Another member mentioned currency divergence, with some such as sterling moving quicker than others to replace LIBOR. Members agreed that this creates problems with regards to transitioning away from referencing LIBOR.

4. **CRR Amending Regulation – ECON draft report (Timothy Cleary)**

4.1. Timothy Cleary delivered a presentation on the draft European Parliament legislative resolution amending Regulation (EU) No 575/2013 as regards exposures in the form of covered bonds (the “legislative proposal”). He explained the regulation being amended establishes a common standard for a covered bond and sets out basic requirements.

4.2. Mr Cleary explained that the legislative proposal aims to:

   i. reinforce and complement the requirements for the preferential capital treatment of covered bonds through proposed amendments to Article 129 of Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms (the “Capital Requirements Regulation” or the “CRR”); 

   ii. provide a definition of covered bonds that is intended to replace the definition in Article 52(4) of Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (“UCITS”); and 

   iii. establish a common set of characteristics and structural features that a debt instrument must satisfy in order to be recognised as a covered bond under E.U. law.

4.3. Mr Cleary also emphasised the proposed additional requirements for covered bonds which will enable banks to benefit from preferential capital treatment by reference to the definition, governance and transparency provisions in the new Covered Bonds Directive. In particular, the legislative proposal suggests that a new requirement on a minimum level of over-collateralisation would be introduced.
5. **Plenary discussion on recent development and legal uncertainties concerning banking** (Clare Dawson)

5.1. A discussion was held of the U.S. sanctions against Iran with emphasis on the conflict of laws between the blocking regulations. Ms Parekh mentioned the FMLC has established a working group to analyses legal uncertainties concerning the U.S. sanctions and asked members to get in contact should they like further information.

5.2. The proposed Directive on credit servicers, credit purchasers and the recovery of collateral was also raised by a member. Ms Dawson mentioned that the Loan Market Association have continued to hold discussions with regards to the proposed Directive. Forum members agreed to keep a watching brief for any developments.

6. **Any other business**

6.1. No other business was raised.
Lifecycle of a Project
How an issue of legal uncertainty is raised

• New issues of legal uncertainty on which the FMLC can undertake work are raised in Scoping Forum meetings, bilateral radar meetings with Joanna Perkins (FMLC CEO) and during monthly Patron relationship calls with members of the Secretariat.

• Once an issue is raised, the Secretariat usually asks for a briefing note to be prepared by the person(s) making the recommendation. This is then put before the Committee for their consideration. (The FMLC Secretariat will normally offer formatting and other assistance in preparing the brief.)
The brief

FINANCIAL MARKETS LAW COMMITTEE ("FMLC")

Briefing Note: Issues of Legal Uncertainty on Brexit and Judicial Interpretation

1. Introduction

1.1. Following the referendum in June 2016, in which the UK voted to withdraw from the European Union, the FMLC established a High Level Advisory Group ("HLAG") of experts to give direction to the Committee’s work relating to Brexit. At a meeting of the HLAG in December 2017, members of the HLAG recommended that the FMLC establish a Working Group to identify potential legal uncertainties arising from the interpretations by U.K. courts of autonomous E.U. legal concepts which appear in received E.U. legislation as it is incorporated into U.K. law.

1.2. An overview of HM Government’s proposal to incorporate E.U. law into the U.K. and the various legal complexities relating to the interpretation of autonomous E.U. terms are set out below.

2. The European Union (Withdrawal) Bill—and domestic preparations for Brexit so far

2.1. In the run-up to the referendum, those who campaigned for withdrawal from the E.U. argued for an end to the supremacy of E.U. law and judgments of the European Court of Justice ("ECJ"). The European Union (Withdrawal) Bill (the "Withdrawal Bill") introduced into the House of Commons on 13 July, aims to fulfil this purpose by: (i) repealing the European Communities Act 1972 on the day the U.K. leaves the E.U. and (ii) incorporating E.U. law as it stands into domestic law. The Withdrawal Bill also provides guidance for a new relationship between domestic law and U.K. law.

2.2. Clause 5 of the Withdrawal Bill states that the principle of the supremacy of E.U. law will not apply to any enactment or law passed or made on or after Exit Day (i.e., the term defined in the Withdrawal Bill as the day the U.K. leaves the E.U., except so far as relevant to the interpretation, disapplication or nullifying any enactment or law passed or made before Exit Day). Clause 6, quoted below, provides guidance on the relationship between courts in the U.K. and the ECJ.

Interpretation of retained EU law

(1) A court or tribunal—
(a) is not bound by any principles laid down, or any decisions made, on or after exit day by the European Court, and
(b) cannot refer any matter to the European Court on or after exit day.

(2) A court or tribunal need not have regard to anything done on or after exit day by the European Court, another EU entity or the EU but may do so if it considers it appropriate so to do (emphasis added).

3. Relevant Issues of Legal Uncertainty

3.1. As a consequence, where the meaning of an autonomous E.U. term or concept is defined before Exit Day, the U.K. will follow that interpretation. Where the meaning of terms, which may appear in the incorporated aspects of E.U. law, is not fixed by Exit Day—or their interpretation is discussed and incorporated aspects by the ECJ post-Brexit—there remains ambiguity as to how U.K. courts should proceed. Following the publication of the Withdrawal Bill, the former President of the Supreme Court, Lord Neuberger, remarked in the media that judges would require guidance from HM Government on how U.K. courts should interpret European concepts and judgments post-Brexit.

3.2. Referring to this, members of the HLAG also highlighted the importance of interpretational equivalence between the U.K. E.U. in preventing legal uncertainty in the context of negotiations for a future trade agreement, or in the event the U.K. applies for “equivalence” under the E.U.’s Third Country regimes, where regulatory coordination might be deemed important.

3.3. The questions before HM Government and U.K. judges (and for this Working Group to study and attempt to address) begins with a consideration of whether, and in what circumstances, U.K. courts might follow the ECJ’s judgments as so far as they settle, after Brexit, the meaning of terms in E.U. legislation previously received into U.K. law.

3.4. In the event that the U.K. courts choose not to abide by the ECJ’s interpretative questions of legal complexity arise in relation to other aids to interpretation on which judges in the U.K. might rely. Our next aide might be found, it has been suggested, in the Model conventions and laws proposed and signed under the auspices of the United Nations. The Model Conventions are not, however, signed by a majority of E.U. Member States, which elicits further questions as to their authority and comprehensiveness.

3.5. A final area of legal uncertainty which requires consideration is the basis for judicial interpretation in the event it is agreed that international conventions and existing aids do not provide sufficient guidance. In such a scenario, Lord Neuberger’s call on Parliament for direction becomes more relevant. The Working Group might well reflect upon the overarching principles which might facilitate Parliament’s determination of its guidance to judges on the interpretations of E.U. law and ECJ judgments post-Brexit.

4. Working Group—Brief

4.1. The Working Group is invited to examine in general the legal issues surrounding the judicial interpretation of autonomous legal terms post-Brexit and to document the results of these inquiries into a paper. As a guide, the paper should address the subject according to the following outline: (i) summary and introduction; (ii) legislative background; (iii) legal issues analysis; (iv) market impact or potential impact of the issues; (v) proposed solutions and mitigants; and (vi) conclusion.

4.2. More detail about drafting a paper for the FMLC can be found in the FMLC Contributors’ Guidelines.

* The FMLC has previously considered, for instance, the effects of the UNIDRR Model Law on Cross-Border Insolvency (1995) in the context of cross-border continuing proceedings post-Brexit. This Working Group’s research brief required such work.
The Committee considers the issue

- The issue is adopted
- Only a limited number of uncertainties are identified, or it is a reiteration of comments the FMLC has made previously
- The Committee delegates to the Secretariat responsibility for undertaking research and drafting of the publication
- The issues of uncertainty are complex and numerous
- The Committee resolves to establish a working group to conduct an in-depth analysis which will lead to a publication

The issue does not fall within the remit of the FMLC e.g. too political in nature, not an issue of legal uncertainty etc. and is benched
Working Group membership, conduct of business

- Members of the relevant Scoping Fora as well as academics, experts and other FMLC stakeholders are invited to join working groups.

- Working groups are convened under Terms of Reference, including conduct of business guidelines. These include the following:

  1. participation is limited to one member per organisation;
  2. alternates are not permitted to attend meetings; and
  3. working group meetings are to be attended in person, where possible. Dial-in details are only provided to members who are permanently based abroad.
Working Group meetings

• Working groups typically meet between two and five times to identify relevant issues of legal uncertainty, make decisions as to any work product (i.e., a paper or a letter), and review draft contributions. Working group members volunteer to draft sections of the paper.

• The Secretariat will support the Chair and the working group during meetings and manage Group-related communications. The Secretariat will help draft and circulate meeting agenda and related documents and take minutes.

• On completion of a publication, the Working Group is likely to shut down.
Review process and publication

- For publications drafted by the Secretariat, draft copies will be circulated to the individual(s) who raised the issue for comment and then to the Committee for their review before being finalised. In these cases, the Scoping Forum, as the Committee's pool of experts on the general area of financial services law, will be asked if they have any feedback.

- For working groups, members who committed to writing sections of a paper will send their drafts to the Secretariat, who will align it to FMLC house-style as defined in the contributors’ guidelines and collate the sections into one document. Working group members will have the opportunity to comment on the draft publication before it is sent to the Committee.

- Once approved by the Committee, the publications will be uploaded to the FMLC website and circulated to relevant stakeholders and authorities.
Examples of recent projects suggested by Scoping Fora

<table>
<thead>
<tr>
<th>Category</th>
<th>Project Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banking</td>
<td>• <a href="#">Report</a>: Analysis of the Proposal to Amend Moratorium Powers: April 2018</td>
</tr>
<tr>
<td>Finance and Technology</td>
<td>• <a href="#">Report</a>: Distributed Ledger Technology and Governing Law: March 2018</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>• <a href="#">Report</a>: EMIR: the European Commission's Legislative Proposal to Amend Procedures for recognition of Third Country Central Counterparties: July 2018</td>
</tr>
<tr>
<td>Insurance</td>
<td>• <a href="#">Report</a>: Establishment of an E.U. Insurer in AnotherMember State: July 2018</td>
</tr>
<tr>
<td>Sovereign Debt</td>
<td>• <a href="#">Report</a>: <a href="#">Pari Passu</a> Clauses in Sovereign Debt Obligations: April 2015</td>
</tr>
</tbody>
</table>
Achievements and impact

Professor Hugh Beale (University of Warwick) and Simon Firth (Linklaters LLP) gave evidence to the House of Lords E.U. Financial Affairs Sub-Committee on the topic of post-Brexit contractual continuity as an extension of work conducted by the FMLC Working Group on Brexit—Robustness of Financial Contracts.

In response to the FMLC paper exploring uncertainties as to the financial instruments that fall within the scope of MAR, the FMLC received a letter from the FCA stating that the paper was circulated to the FCA policy team who worked with ESMA to develop the MAR guidance materials. Subsequent ESMA Q&A’s on MAR were updated to include questions on market soundings.

In response to the FMLC paper on issues of uncertainty arising from the European Commission’s proposed directive and regulation on data protection, the FMLC was asked by the Commission to conduct further work. Subsequently, draft texts of the regulation were closely aligned with changes proposed by the FMLC.