## Financial Markets Law Committee ("FMLC")

## Sovereign Debt Scoping Forum

Date: Tuesday 3 September 2019

Time: 8.30am to 10.00am

Location: Linklaters LLP, One Silk Street, London EC2Y 8HQ

### In Attendance:

| | |
|---|---|
| Richard O'Callaghan (Chair) | Linklaters LLP |
| Leland Goss | International Capital Market Association |
| Jim Ho | Cleary Gottlieb Steen & Hamilton LLP |
| Yannis Manuelides | Allen & Overy LLP |
| Rodrigo Olivares-Caminal | Queen Mary University of London |
| Tolek Petch | Slaughter and May |
| Harriet Territt | Jones Day |
| Deborah Zandstra | Clifford Chance LLP |
| | |
| Venessa Parekh | FMLC Secretariat |
| Katja Trela-Larsen | FMLC Secretariat |

### Regrets:

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|---|---|
| Carter Brod | Morgan, Lewis & Bockius UK LLP |
| Ian Clark | White & Case LLP |
| Jason Crelinsten | Greylock Capital Management LLC |
| Emma Dickinson | Deutsche Bank AG |
| Francis Fitzherbert-Brockholes | White & Case LLP |
| Duncan Kellaway | Freshfields Bruckhaus Deringer LLP |
| Rosa Lastra | Queen Mary University of London |
| John McGrath | Sidley Austin LLP |

## Minutes:

### 1. Introductions

1.1. Mr O'Callaghan opened the meeting. Attendees introduced themselves.

### 2. The FMLC's Public Education Function: Speeches (Venessa Parekh)

2.1. Ms Parekh delivered a short presentation on the FMLC's Public Education Function, a key aspect of the FMLC's mission as a charity.[1] She encouraged Forum members to get in touch with the Secretariat should they wish to arrange a talk by a member of the Secretariat at their offices.

### 3. U.S. sanctions and sovereign debt renegotiations—Venezuela (Harriet Territt)

3.1. Ms Territt introduced her presentation on U.S. sanctions on Venezuela with the illustration of an unstoppable force meeting an immovable object. She emphasised that sanctions cannot be considered as existing or operating in the same way as normal legislation. In particular, the rules of statutory interpretation do not easily apply to sanctions. Ms Territt briefly described the different types of sanctions. Primary sanctions apply to U.S. "persons" whereas "secondary sanctions" are stated to apply to non U.S. persons. The scope of that definition has been widened gradually to include transactions with a sufficient nexus in the U.S.

3.2. Ms Territt then turned to the U.S. Department of the Treasury's Office of Foreign Assets Control ("**OFAC**") has initiated enforcement action with respect to transactions with a sufficient nexus in the U.S. These include dollar transactions involving non-U.S. parties, settled by an American bank. By way of example, in 2017, OFAC announced its first enforcement action against a non U.S., non-financial company for "causing" sanction violations. The Singaporean company, TransTel entered into contracts with multiple Iranian companies to deliver and install telecommunications equipment. TransTel engaged various third party vendors in connection with these contracts.

3.3. Ms Territt went on to give an overview of recent U.S. sanctions against Venezuela. She noted that sanctions had been levied against Venezuela since the 1970s; pre-2017, however, these were mainly aimed at protecting people. In 2017, Venezuela defaulted on a large government debt. Sectoral sanctions were subsequently introduced. These restrictions were very similar to those placed on Russia. A major difference, however, was the breadth

[1] Please see Appendix I below.

of licences made available which allowed substantial transactions to continue (e.g. trading with Citgo, a U.S.-based oil refinery owned by PdVSA). In May 2018, Venezuela started to sell off certain receivables and the U.S. reacted by expanding the scope of its sanctions to cover receivables.

3.4. In January 2019 PdVSA was itself designated under U.S. sanctions. Various general licenses were granted to allow certain transactions and activities related to PdVSA and its subsidiaries, some for specified wind-down periods, including an authorisation to import petroleum from PdVSA to end April 2019, which stipulated payments were to be made to a blocked U.S. account. Several U.S. companies with operations in Venezuela involving PdVSA were permitted to continue operating (through October 25, 2019).

3.5. In February 2019, guidance on secondary trading changed. U.S. investors prohibited from purchasing PdVSA bonds, but are permitted to hold previously purchased PdVSA debt and to sell PdVSA bonds to non-U.S. entities, solely for the purpose of divesting. Other Government of Venezuela bonds, which are not blocked, were initially unaffected. However, later the same day, OFAC announced amendments to an existing general license that essentially eliminated the distinction between U.S. investors' treatment of existing Government of Venezuela bonds and existing PdVSA bonds.

3.6. In August 2019 an "embargo" was effectively placed on the Venezuelan government. All Venezuelan government assets within the U.S. were frozen and transactions by U.S. persons with the Venezuelan government were prohibited, unless specifically exempted. Non-U.S. persons could be sanctioned if they are found to have "*materially assisted, sponsored, or provided financial, material, or technological support for, or services to or in support of*" the Government of Venezuela. There was a wind-down period to 4 September 2019 and exemptions for dealing with the Venezuelan opposition as well as certain other standard exemptions.

3.7. A discussion on the issues surrounding the sanctions followed, including on the impact of sanctions on ongoing debt restructuring talks (both initially with the Maduro government and subsequently with the transitional government under Guaido), and the impact on liquidity and pricing following guidance on secondary market trading. Forum members commented on their views of the specific aims and impact of the sanctions.

## 4. U.S. Office of Foreign Assets Control: amended reporting obligations regarding rejected transactions (Harriet Territt)

4.1. Ms Territt explained that OFAC has issued an interim final rule on 21 June 2019 which amended several regulations relating to reporting procedures and requirements. The revised guidance had caused much uncertainty both because its release had been unanticipated and because it appeared to substantially expand reporting obligations.

4.2. Previously, this regulation only required reporting by "[a]ny financial institution that rejects a funds transfer" where processing that transfer would violate or facilitate the violation of OFAC's proscriptions. The revised regulation, however, now requires "[a]ny U.S. person (or person subject to U.S. jurisdiction), including a financial institution, that rejects a transaction" that would otherwise violate OFAC's prohibitions to file a report with OFAC within 10 business days. Notably, the term "transaction" is defined in the regulation to include goods and services. Ms Territt observed that one area that could usefully be clarified is the extent to which this reporting requirement applied to majority owned or controlled subsidiaries of U.S. companies located outside the United States in respect of any rejected transactions.

4.3. Forum members then considered the impact of U.S. sanctions on sovereign debt transactions in the U.K. The group noted that Council Regulation (EC) No 2271/96 protecting against the effects of the extra-territorial application of legislation adopted by a third country, and actions based thereon or resulting therefrom (the "Blocking Regulation") protects E.U. operators from the effect of certain U.S. sanctions. In practice, however, market participants often try to comply with U.S. sanctions as well as the Blocking Regulations to the extent practical. The Blocking Regulation will be replicated in the U.K. after Brexit so the issue is likely to persist. A discussion followed as to OFACs aim for the increased reporting duties.

## 5. Transparency Principles from Private Debt (Deborah Zandstra)

5.1. Ms Zandstra provided an update on private sector principles for transparency in sovereign debt market, published by the Institute of International Finance ("**IIF**"). Ms Zandstra had introduced Forum members to the project at the Forum meeting on Tuesday 5 March 2019. The principles are yet to be implemented. At the heart of the principles is a new reporting requirement in which private sector lenders involved in a financial transaction, with the consent of the public sector counterparty, discloses certain "relevant" information to a Reporting Host. Ms Zandstra said that an institution had not yet been identified to

undertake the responsibilities of Reporting Host. Once a Reporting Host and platform are established, an implementation memorandum will be published.

5.2. Ms Zandstra recounted the development of the project. After the Mozambique debt crisis, the private sector had demanded greater transparency within the sovereign debt market, particularly in relation to derivative loans. The IIF therefore established the working group to consider a market-led response. Reaching consensus amongst working group members on the principles had proved quite difficult and negotiation was needed; the principles were drafted by committee.

5.3. In particular, the reporting obligation had been contentious. Members of the working group had differing views on the repercussions to be applied in event of non-compliance, whether derivatives and/or security repurchase agreements should be included, and whether only home currency or foreign currency debt should be included. The reporting requirement also raises competition-related issues with respect to the length of any cooling off periods and the disclosure of pricing information. As the reporting is voluntary, regulation will be through transparency and civil society rather than by enforcement.

5.4. Ms Zandstra ended by stating that the reporting requirements were likely to be accepted if states in the Group of 20 ("**G20**") adopt them. The G20 has not given the reporting principles full endorsement, but has expressed support. In the U.K., a government led by the Labour Party is likely to adopt the principles and, indeed, may deem them mandatory rather than voluntary. This would, however, only impact contracts governed by English law.

5.5. Forum members discussed the general trend of regulation by transparency.

## 6. Any other business[2]

6.1. No further business was raised at the meeting.

[2] The next meeting of the Sovereign Debt Scoping Forum is scheduled to be held on Tuesday 3 December between 8.30am and 10.00am.

# The FMLC's Public Education Function: Speeches

**Venessa Parekh**

Research and Communications Manager

# The FMLC's charitable remit

According to the charitable remit, the FMLC has a tripartite mission:

- to *identify* relevant issues (the **radar** function);
- to *consider* such issues (the **research** function); and
- to *address* such issues (the **public education** function).

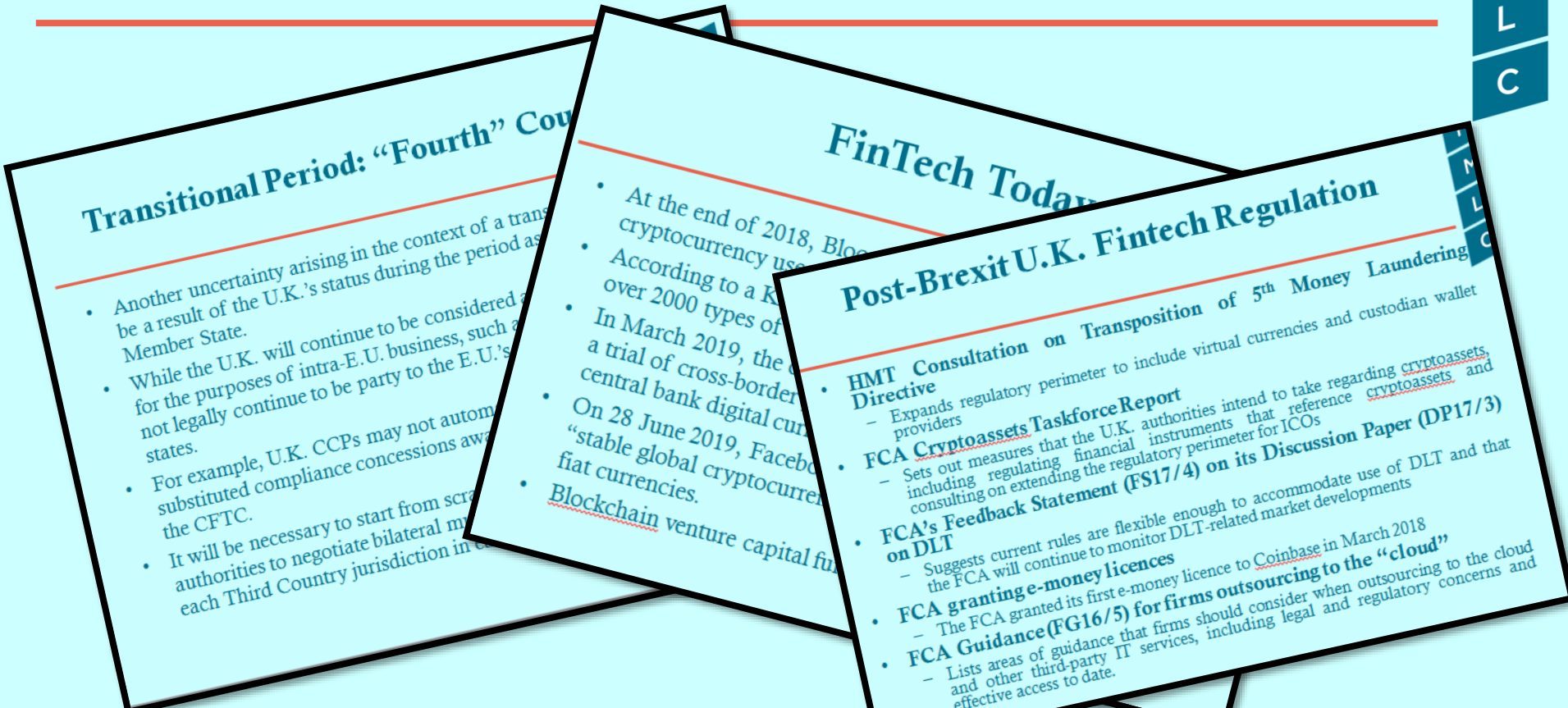
**Reduced legal uncertainty and risk is in the public good**; the ***radar*** and ***research*** functions are somewhat self-explanatory in this regard. The ***public education*** function is a key aspect of the FMLC's status as a charity, and is addressed in the following ways:

- All FMLC papers, presentations/speeches and correspondence are freely available via the FMLC website.
- The FMLC seeks to raise the profile of its research with those who are best positioned to implement solutions. This is achieved primarily through correspondence: the FMLC maintains active correspondence with regulatory and legislative groups around the world, particularly HM Treasury and the European Commission.
- Most FMLC events (with the exception of Patrons' events) are free to attend by members of the public.
- The FMLC also acts as a bridge to the judiciary, a task it carries out primarily by organising seminars to brief senior members of the judiciary on aspects of wholesale financial markets practice.

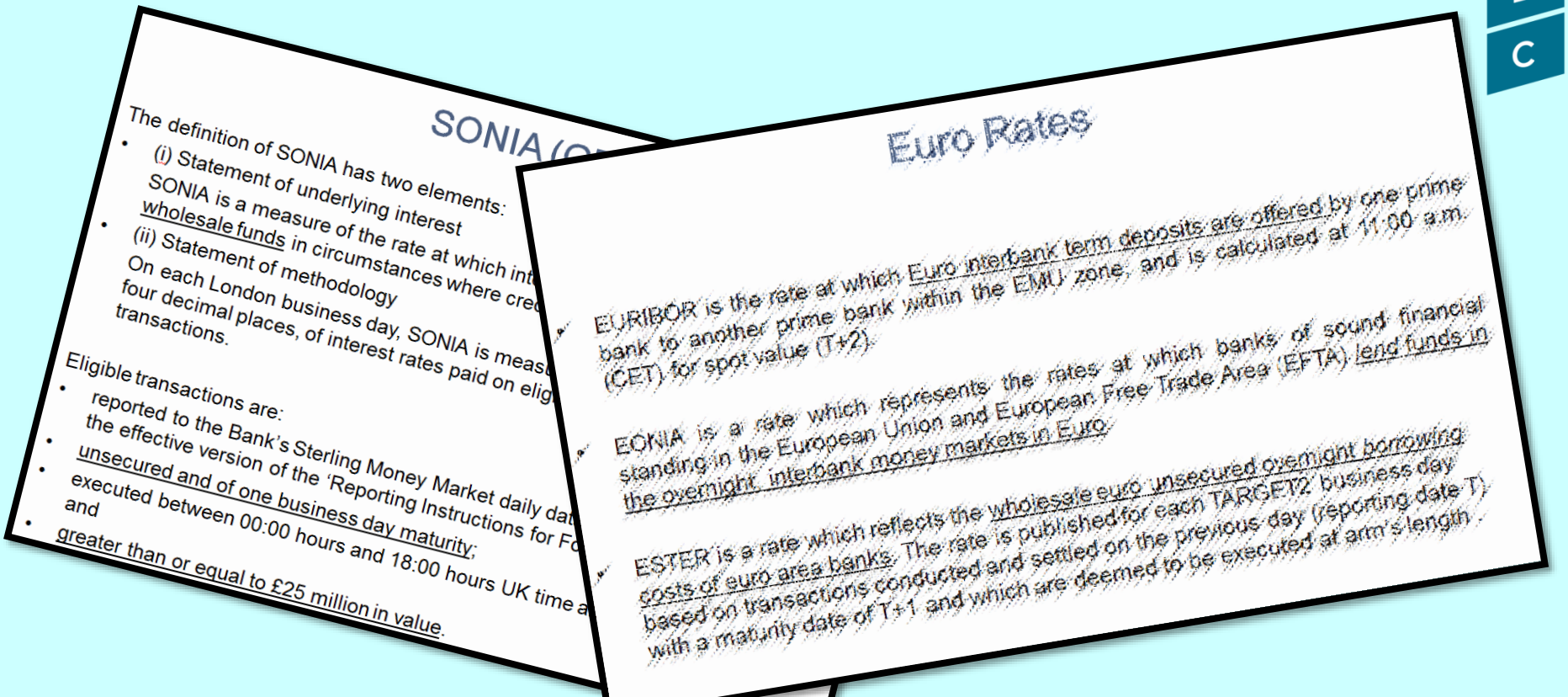
# The Public Education Function

- Along with publications and events, the FMLC Secretariat furthers the Committee's education function by giving speeches about legal developments and issues of legal uncertainty in the financial markets.
- These speaking engagements may be at high-profile events or at a smaller gathering of an interested audience at a stakeholder firm.
- Members of the Secretariat have presented to audiences, within law firms for example, which are interested in learning about current issues facing the financial markets.
- The FMLC used to be CPD-qualified and such talks presented excellent training opportunities.
- Example of topics on which the Secretariat has presented are set out in slides below.

# Brexit, FinTech and FinTech Regulation After Brexit



# IBOR Transition (at the P.R.I.M.E Finance Conference 2019)



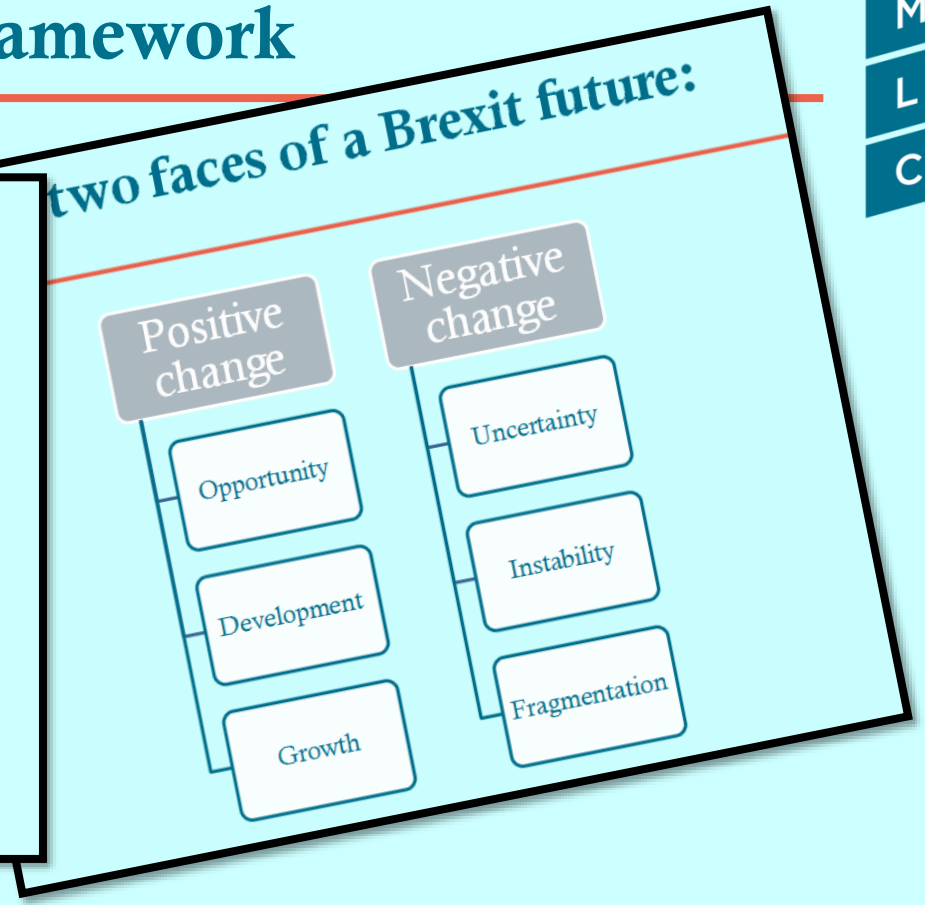
# Brexit and finance: the legal framework

**Covering note on the Financial Regulators' Powers (Technical Standards) (Amendment etc.) (EU Exit) Regulations 2018**

5 Following this model will mean that EU 'Level 1' legislation (which was developed by the European Commission and negotiated through the Council and European Parliament) and 'Level 2' legislation (apart from BTS and certain other technical elements of Level 2), will become the responsibility of the UK Parliament. This body of EU legislation includes provisions which set the policy direction for financial services, so it is appropriate that responsibility for deciding how deficiencies are fixed in this legislation should rest with Parliament. HM Treasury will propose amendments to this legislation, using the powers under the EUWB, ensuring that Parliament is able to scrutinise all of the changes. It is expected that the majority of the statutory instruments needed to correct deficiencies in this legislation will be laid under the affirmative procedure.

6 For certain EU 'Level 2' technical rules, known as Binding Technical Standards (BTS), HM Treasury proposes to transfer ongoing responsibility from the European Supervisory Authorities to the UK financial regulators – the Bank of England, the PRA, the FCA and the Payment Systems Regulator (PSR). BTS, running to several thousand pages, do not set overall policy direction but fill out the technical detail of how the requirements set at Level 1 are to be met. Having played an important role in the EU to develop these standards, through their membership of the Boards and working groups of the European Supervisory Authorities, UK regulators have the necessary expertise and resource to maintain them after the UK's exit from the EU. This allocation of responsibility would be consistent with the general rule-making responsibilities already delegated to the FCA and PRA by Parliament under FSMA.

7 As HM Treasury proposes to transfer ongoing responsibility for BTS to the UK regulators, it also makes sense that the regulators perform the task of making corrections to deficiencies in existing BTS so that these rules operate effectively in the UK at exit. HM Treasury therefore proposes to delegate to UK financial regulators the power to correct deficiencies in BTS arising from EU withdrawal.

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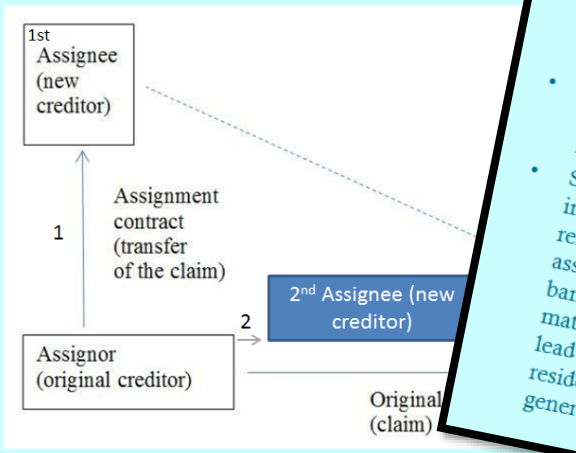
# Conflicts of laws on securities and claims: collateralisation

## Collateralisation and the assignment of claims




## Collateralisation and the assignment of claims

- The Commission proposal insures that retail deposits, whi
against banks by natural person depositors
- the law of the underlying cl
- This is the correct rule: hig
by a natural person, who is
habitual residence.
- Situations in which individu
include the taking of security
relationship, the assigning of
association to a company on t
bank account from one spouse
matters are excluded from the p
lead to competing entitlements a
residence, it may be that only the
generate a legally certain result.

## Collateralisation and the assignment of claims

- Further, with regard to bank accounts in general, it is often argued that banks should be able to take a charge over their own indebtedness *vis à vis* their clients under the law of the assigned claim and irrespective of any rule to the contrary in the law of the latter´s habitual residence.
- The question arose for consideration in the U.K. courts in two cases: *In re Charge Card Services Ltd* [1987] Ch 150, where it was held to be "conceptually impossible" that banks should take a charge in these circumstances, and *Re Bank of Credit and Commerce International SA (No 8)* [1998] AC 214, where the House of Lords settled the question and upheld the charge. In between these case decisions, legislation was enacted in several jurisdictions with common law influence (including the Cayman Islands, Bermuda, Singapore and Hong Kong) providing for the validity and enforceability of charges of this kind, which were common at the time and continue to be prevalent as a means of taking security today.

# Summary and Conclusion

- The Secretariat is happy to visit your organisation and introduce legal uncertainties in a relevant area of the financial markets.
- This helps us get reach a wider audience of stakeholders, learn about the questions occupying their time and fulfil our public education.
- If you are interested, get in touch with Debbie Hayes at: secretarial@fmlc.org or with Venessa Parekh at: research@fmlc.org