Financial Markets Law Committee ("FMLC")

Securities Markets Scoping Forum

Date: Wednesday 10 February 2021

Time: 2.00pm to 3.00pm

Virtual meeting

Attendees:

Ferdisha Snagg (Moderator)	Cleary Gottlieb Steen & Hamilton LLP
Andrew Bryan	Clifford Chance LLP
Leland Goss	International Capital Market Association
Mindy Hauman	White & Case LLP
Matthias Lehmann	University of Bonn
Eleanor Ley	Allen & Overy LLP
Kristina Locmele	Slaughter and May
Tim Morris	Ashurst LLP
Michael Sholem	Cadwalader, Wickersham & Taft LLP
Christina Tarnanidou	Athens University of Economics and Business
Madeleine Wanner	Linklaters LLP
Robert Williams	NatWest Markets Legal
Venessa Parekh	FMLC Secretariat
Chhavi Sinha	FMLC Secretariat
Katja Trela-Larsen	FMLC Secretariat

Guest Speaker

Brandon Hammer	Cleary Gottlieb Steen & Hamilton LLP
Marc Rotter	Cleary Gottlieb Steen & Hamilton LLP

Minutes:

1. Introductions

1.1. Ms Snagg opened the meeting and introduced the guest speakers.

2. FMLC Scoping Forums (Venessa Parekh)

2.1. Ms Parekh explained that the FMLC's remit covers the entirety of the wholesale financial markets. To identify issues of legal uncertainty, the FMLC Secretariat operates ten Scoping Forums, each focused on a specific area of the financial services. Ms Parekh provided an overview of the Scoping Forums' role in the FMLC's architecture and their conduct of business rules.

3. GameStop/Robinhood: U.S. Securities Law Implications of the Recent Volatility for Market Participants (Marc Rotter and Brandon Hammer)

3.1 Mr Rotter provided an account of the recent events related to the trading in the shares of GameStop, whose stock prices surged recently. The trading frenzy in the shares of GameStop, and select other so-called "meme stocks", which was widely attributed to the trading activities of retail investors on a Reddit subforum and action by Robinhood and certain other retail brokers to restrict trading in these stocks, has raised many questions around the unlawful manipulation of the market as well as the efficacy of regulatory and risk disclosure obligations. Mr Rotter explained that these events may have widespread ramifications, including impacts on issuers and insiders, potential enforcement action and the role of market intermediaries.

3.2 With respect to the impact on issuers, Mr Rotter noted that issuers should consider the possibility that they could they be targeted by a similar campaign. Mr Rotter added that an issuer might be faced with the question of when and how to make a public offer and what information to disclose. He noted that the Securities and Exchange Commission, ("**SEC**") has issued guidance with respect to disclosure that issuers should make if conducting a registered offering during times of extreme price volatility.[1] Mr. Rotter noted that when an issuer decides to make a public offer, the SEC generally has the power to review the prospectus/registration statement and decline to declare it effective or, if the registration

[1] SEC, *Guidance*: *Sample Letter to Companies Regarding Securities Offerings During Times of Extreme Price Volatility* (February 2021); available at https://www.sec.gov/corpfin/sample-letter-securities-offerings-during-extreme-price-volatility

statement is automatically effective or already declared effective. issue an order requiring the issuer to stop using it.

3.3 Next, Mr Rotter noted that officers and directors of a company, as well as 10% shareholders, are considered to be insiders under Section 16 of the Securities Act. While insiders may in some cases be able to rely on exemptions allowing them to sell their shares without registration, they are required to file information about the purchase and sale of their shares. He remarked that not many directors and officers of "meme stocks" have recently filed information in connection with sales of "meme stocks", indicating that they have not sold shares of the issuer during the recent run-up in prices.

3.4 Moving on to the potential enforcement actions by the SEC, Mr Rotter explained that it is not clear what actions the SEC will take at this stage, but there is expected to be substantial pressure on the regulator to act. He noted that it appeared that it would be difficult for the SEC to prosecute actions for "pump and dump" schemes or violations of certain market manipulation provisions of the Securities and Exchange Act in this context. Mr Rotter further explained the steps that the SEC might consider taking and the contours of a potential investigation. He noted that it will be interesting to monitor the steps/actions that SEC will finally take.

3.5 Mr Hammer turned to the role of intermediaries in the clearing system. He explained the "payment for order flow" practice that has come under additional scrutiny in connection with the GameStop volatility. Under this kind of arrangement, a broker like Robinhood agrees with another broker to route customer orders to such broker in exchange for a fee. This practice is permissible under SEC regulations if disclosed to customers and consistent with the broker's best execution obligations. Mr Hammer explained that, in December of 2020, the SEC commenced an enforcement action against Robinhood for both disclosure and best execution failures. Mr Hammer also discussed some possible reasons why Robinhood began limiting the ability of customers to execute certain trades on GameStop and other names. Mr Hammer added that the SEC might consider providing guidance on the margin methodology used by U.S. clearing organisations and/or imposing liquidity requirements on intermediaries like Robinhood.

3.6 Members discussed the impact of GameStop manipulation on the U.K. market. They noted that the increased participation by the retail investors in the financial market is something that the regulators should consider examining. It will be important to see how the rules on market manipulation, financial promotions, liquidity requirements and operational resilience will apply to retail investors who are not professionals. Another member added that these events demonstrate the role of social media in creating price volatility. Mr Rotter remarked that it is hard to see how the SEC will bring out actions against the retail investors. A member asked if there are rules which allows intermediaries to use margin as a tool and re-hypothecate them. Mr Hammer explained that the broker is permitted to re-hypothecate margin within specified limits.

3.7 Members agreed to monitor regulatory developments on the GameStop case in the U.S.

4. The effect of the Non-Performing Loans Credit Servicers' Directive on securitisations (Andrew Bryan)

4.1. Mr Bryan remarked that, over past two decades, economic difficulties have meant that an increasing number of E.U. companies and citizens have been unable to repay their loans. Consequently, E.U. banks have accumulated high volumes of non-performing loans ("**NPLs**") in their balance-sheets. The loans extended by E.U. banks remain historically high when measured against the ratios of other advanced economies. High levels of NPLs require banks to hold higher amounts of regulatory capital and pay a risk premium on liquidity markets, as a result of which their profitability and growth prospects diminish. To address this issue, several different initiatives have been adopted both at national and E.U. level. In March 2018, the European Commission adopted a proposal for a directive on credit servicers, credit purchasers and the recovery of collateral (hereinafter referred to as **"the Proposed Directive"**).[2] The stated aim of the Proposed Directive is to foster a secondary market in NPLs and ease collateral recovery from secured loans. Among other measures, it would require NPL loan servicers to acquire a license in order to service loans. This scope of the Proposed Directive would include non-credit institution purchasers and servicers of credit originally issued by a credit institution or its subsidiaries. The Commission had also proposed an accelerated extrajudicial collateral enforcement procedure, but this has not been progressed by the co-legislators.

4.2. Mr Bryan noted that the Proposed Directive would require Member States to ensure that a creditor provides all necessary information to a credit purchaser to enable the latter to assess the value of the credit agreement and the likelihood of recovery prior to entering into a contract for the transfer of that credit agreement. He further added that, under the Proposed Directive, the European Banking Authority (the "**EBA**") would be required to develop draft implementing technical standards that specify the formats to be used by credit institutions, in their role as creditors to provide detailed information on their credit exposures in the

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2 European Comission, *Proposal for a directive on credit servicers, credit purchasers and the recovery of collateral* (14 March 2018); available at: https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX%3A52018PC0135

banking book to credit purchasers for the screening, financial due diligence and valuation of the credit agreement. Mr Bryan noted that the Proposed Directive has been progressed through the Council and the European Parliament Committee on Economic and Monetary Affairs ("**ECON**") and will likely become law in the coming months.

4.3. Mr Bryan noted that, with respect to securitisation, there were important differences between the Commission, Council and ECON versions of the Proposed Directive. These differences include the types of loans included in the scope of the any new legislation, whether the legislation would have any effect on the secondary markets in performing loans and whether any substituted compliance would be possible in respect of transparency obligations (e.g. allowing an exemption to the information disclosure requirements where equivalent requirements are already being complied with under the Securitisation Regulation regime). He further added that, if the final version of the Proposed Directive were to include a ban on transferring performing credit agreements that would render it extremely difficult for market participants to securitise such loans – which would be likely to have a significant negative impact on consumer finance. Another effect on securitisation highlighted by Mr Bryan was with respect to the information requirement under Article 14 and 15 of the Directive which refers to a template, with respect to securitisation, information on credit exposures, financial due diligence and valuation of the credit agreement. Similar information would also be required to be disclosed under Regulation (EU) 2017/2402 for laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, (the "**E.U. Securitisation Regulation**") and the RTS made thereunder. Mr Bryan added that any double reporting should be avoided and the EBA might consider reviewing Article 14 requirement to ensure the consistency.

4.4. Members agreed that this is a good example of in-flight proposal and agreed to monitor developments in this regard.

5. Any other business

5.1. Members agreed that the U. K.'s future regulatory framework should be on the agenda for the next meeting.