

**2018 Asia Securities Forum**

# **The Unintended Consequences of Global Regulations**

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# I. Key Details of EU Benchmark Regulation

- EU BMR regulates business conducts of benchmark related institutions **to prevent conflicts of interest**, establish control system, store data, etc.
  - **Administrators**: a natural and legal person providing of a benchmark  
ex) exchange, pricing agencies, market association
  - **Contributors**: a natural and legal person contributing input data
  - **Index providers**: a natural and legal person providing of an index
  
- Non-EU benchmarks administrators have to be authorized by a National Competent Authority (NCA) and benchmarks have to be registered with ESMA\* (by end-2019) in order to be used by EU financial institutions.
  - **Critical Benchmarks (Administrators):** CD rate (KOFIA), KOSPI 200 index (KRX)

## **II. KOFIA's CD rate registration related key issues**

**1. Registration Method**

**2. Legal Representative**

**3. Independence**

**4. Brexit**

## III. KOFIA's Plan and Difficulties

### 1. Registration Method

- Two-track approach (Equivalence or Recognition) among 3 methods
  - Equivalence : The legal framework is equivalent to that of the EU (Judged by the EC)
  - Recognition : A legal representative has to be established in EU (Recognized by competent Authority)
  - Endorsement : A Benchmark has to comply with the BMR requirement (Endorsed by the EU administrator)
- KRW IRS using 3 month CD rate is traded in EU trading platform (UK)
  - The FCA (UK) will be the National Competent Authority for the recognition

## 2. Legal Representative

- The review result for potential legal representatives
  - EU financial companies : express difficulties
  - Information vendors : express difficulties
    - due to the lack of EU guideline for 3rd countries' administrators and potential risk of legal responsibilities
  - Law firms : express positive intention
    - potential management cost is still unclear

### 3. Independence

- To prevent conflict of interest in calculating CD rate
  - Internally establishing an independent supervisory committee and separating the department that calculates the CD rate
  - Planning to gain recognition from the EU supervisory authority by the end of next year based on the legal advice and consultation provided by law firms in EU and Korea.
- Uncertain whether KOFIA's plan to retain independence will be accepted by EU NCAs

## 4. Brexit

### Hard Brexit Case

- Considering an alternative NCA (AMF in France) for the recognition in EU after the Brexit

### Soft Brexit Case

- Ensuring the FCA's recognition will be effective after the Brexit

→ KOFIA will continue to explore ways to minimize the impact on the industry

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- **Benchmark Regulations**
  - **MiFID II**
  - **GDPR**

# I. Understanding MiFID II

- The EU unveiled MiFID II in order to strengthen the competitiveness and transparency of the European financial market in 2018
  - The application scope is much larger than MiFID I
  - MiFID II is extensive, consisting of 1.7 million paragraphs
  - However, the implementation of the new regulations seems to be moving on smoothly
- Regulations have especially become stronger for the OTC market, which had investors mired in confusion during the financial crisis.

## II. Introduction of MiFID II and its impact on Korea

Key Agendas	Revised Details	Impact
Pre- & Post –Trade Transparency	- Obligation to manage, disclose and report quotes prior to trading and execution prices	X
Best Execution Obligation	- Establishment of a policy for order execution and reporting on the details in accordance with the best execution obligation.	X
Order Management · Data Analysis and Reporting	- Upon request by the regulatory authority, investment firms must immediately record, receive and provide all data necessary for monitoring and reconfiguring transactions.	X
Research Compliance and Management	- Research costs should they choose to pay using client commissions - Investment firms can pay for research directly from their own account or use a Research Payment Account (RPA)	O
KYC and Appropriateness	- Management of audit records · data access and data updates in accordance with the KYC policy - Identify institutional investors with the LEI* data - Digitalization of data related to the suitability rule, agreement, disclosure, etc.	X
Monitoring of Algorithmic Trading	- All institutions engaged in algorithmic trading must monitor orders and transactions	X

### III. Unintended impacts of MiFID II

- 'Research unbundling' may have some level of impact on the EU and the regional market.
  - Due to cost issues, asset managers are turning to a small number of large IBs for research.
  - The research functions of local small and medium sized brokers are dwindling.
  - Research will naturally focus more on blue-cap, large corporations than SMEs.
  - Negative impact on SME financing.
  
- Increasing compliance cost deterring Korean firms from venturing abroad.
  - Posing compliance cost burden as a new challenge.

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# I. Key Details of EU GDPR

- In May 2018, the EU introduced the GDPR in place of the existing Directive 95/46/EC to unify the different regulations across member states and provide a one stop shop mechanism.
  - The GDPR is intended to promote **the balance between data protection and data use**
- The three big changes from the GDPR
  1. Corporate accountability has been bolstered through **the designation of DPOs**
  2. New rights added such as **the right to data portability and right to restrict processing**
  3. **The same criteria for fines** will be applied across EU member states.



## II. Challenges to Non-EU Industry

- (Burden of fines)** According to the survey conducted by the Korea Internet & Security Agency on 500 companies, most of the companies replied that they had fears about the fines.
  - Max. (€20mn or 4% of total sales)
- (Difficulties in transferring personal information)** Under the GDPR, information of EU citizens can only be transferred when certain conditions are met.
  - Korean companies have to each establish their own binding corporate rules and standard agreements, which is quite cumbersome.
- (Restrictions to FinTech industry development)** The GDPR was enacted to strike a balance between personal information protection and use in the EU.
  - However, if the emphasis tilts too much towards protection of personal information, that could delay the development of the global Big Data industry.



### III. Preparation of Korean government and KOFIA

- **(Special Committee on the 4<sup>th</sup> Industrial Revolution)** The Korean government established the committee for effective policy and regulatory improvement
  - lessen regulations **to foster the data industry, and protect and use personal information**, because regulations pertaining to personal information protection in Korea are quite strong
- **(Promotion of MyData Industry)** The FSC is striving to allow the subject of personal information to be expanded to individuals by introducing the Right to Data Portability in the legal framework
  - This should lead to a paradigm shift, balancing the protection and use of personal information and strengthen the competitiveness of the Big Data industry in Korea
- **(Working Group and Guidelines)** KOFIA established a **working group** for personal information protection with more than 20 brokerage firms
  - **KOFIA provides guidelines** to almost 400 member companies

# Summary

- ✓ The EU regulations are introduced with unintended implications for the Asian governments and industries.
- ✓ The changes in EU regulations are closely connected to the transforming global financial regulatory landscape (ex. Benchmark transition plan, OTC market transparency)
- ✓ Asian markets are fully equipped to deal with such external changes, as we have had strict financial regulations

➔ **Close interaction regarding the negative impact** those regulations could bring and **cooperation for the development** of the Asian securities industry.



**THANK YOU**