

2018 Asia Securities Forum

The Unintended Consequences of Global Regulations

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Table of Contents

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

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

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



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 4th 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