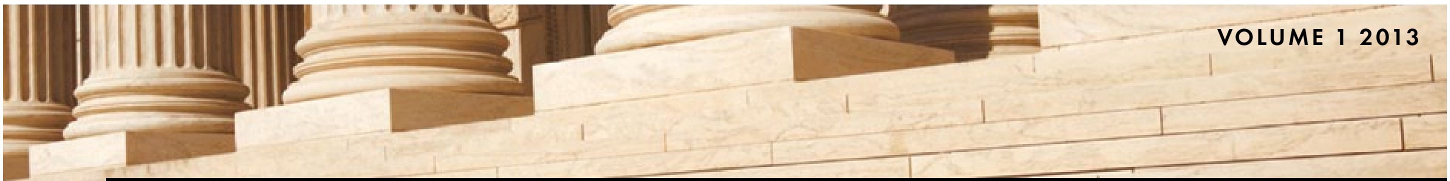

VOLUME 1 2013

EMEA AND APAC REGULATORY DEVELOPMENTS NEWSLETTER

Dedicated to helping you stay ahead of regulatory change, this newsletter summarises the latest regulatory developments affecting Europe and APAC and provides updates on how Northern Trust is evolving to support your requirements.

The regulatory calendar provides an overview of the main regulatory milestones for 2013 and beyond. Readers of the electronic version of the newsletter can use the links to the latest regulatory insights from Northern Trust.

REGULATORY CHANGE TIMELINE — EMEA AND APAC: KEY MILESTONES

2013			
Q1	**Q2**	**Q3**	**Q4**
	EU Solvency II Transposed into national law (likely to be delayed)		**EU RRP – non banks** Proposal Expected
	UK Depositor Preference FSA final rules originally expected. FSA to confirm new timeline		**EU Financial Transactions Tax** Expected directive implementation by 31 December 2013
	UK Regulatory Architecture Legal cutover 1 April		
US Dodd-Frank Title VII Mandatory clearing to be introduced in waves Q1, Q2 and Q3	**US Dodd-Frank** Reporting and record keeping rules become effective		
US FATCA Final rules issued 17 January			**US FATCA** FFI's to enter into agreement with the IRS by 25 October
EU CRD IV / Basel III Phased implementation 2013–2019. January 2013 implementation deadline will slip	**UK Living Wills** FSA's final rules expected	**EU AIFMD** Implementation into national law by 22 July 2013	
	EU Securities Law Regulation Proposed regulation expected April		**EU UCITS VI** Legislative proposal expected October
EU EMIR Entry into force of technical standards	**EU EMIR** Existing CCPs to apply for recognition H1 2013	**EU EMIR** ESMA starts process to determine products to be cleared. Reporting to trade repository for interest rate & credit derivatives starts	
	EU EMIR Trade repository registration begins April	**EU EMIR** Portfolio compression, dispute resolution procedures & portfolio reconciliation starts August	
EU Shadow Banking Follow up with Green Paper expected Q1		**EU Structural Reforms for Banks** Legislative proposal expected	
EU MMF Proposal for EU framework expected March			

REGULATORY CHANGE TIMELINE — EMEA AND APAC: KEY MILESTONES

2014				2015	2017 - 2019
Q1	**Q2**	**Q3**	**Q4**		
EU Solvency II Implementation likely to slip into 2015 and beyond			**EU Review of Market Abuse Directive** Expected implementation	**EU Target2- Securities** Operational 2015	
EU Financial Transactions Tax Comes into effect in the EU from January 2014			**EU Review of Transparency Directive** Expected implementation	**UK Independent Commission on Banking Proposals** Legislation to implement retail ring fence by May 2015	**UK Independent Commission on Banking Proposals** Fully phased in 2019
		US Dodd-Frank Volcker rule conformance period ends 21 July 2014	**EU PRIPS** Implementation expected end 2014	**EU MiFID II** Expected implementation	
US FATCA Withholding tax starts for fixed, determinable, annual or periodical income only				**US FATCA** All branches and affiliates of NT must be FFI's or covered by IGA by 31 December	**US FATCA** Withholding starts for gross proceeds and foreign pass thru payments January 2017
US FATCA New account documentation procedures begin					
US FATCA Review of pre-existing accounts phased in over 2014-16					
EU EMIR Reporting to TR for other derivatives		**EU EMIR** Clearing obligation starts			
				EU Data Protection Expected implementation	**EU CRD IV / Basel III** Fully phased in 2019
			EU Regulation of Central Securities Depositories Expected implementation before 2015	**EU Recovery and Resolution** Expected implementation January	**EU Recovery and Resolution** Expected implementation for bail-in 1 January 2018
			EU UCITS V Implementation expected end 2014		

LEGEND AND GLOSSARY

- UK Regulatory Changes
- EU Regulatory Changes
- US Regulatory Changes

AIFMD: Alternative Investment Fund Managers Directive
CRD: Capital Requirements Directive; DFA Dodd-Frank Act
EMIR: European Markets Infrastructure Regulation
FATCA: Foreign Account Tax Compliance Act
FFI: Foreign Financial Institutions
IGA: Intergovernmental Agreement
IORP: Institutions for Occupational Retirement Provision
MMF: Money Market Funds
MiFID: Markets in Financial Instruments Directive
PRIPS: Packaged Retail Investment Products;
TR: Trade Repositories
UCITS: Undertakings for Collective Investment in Transferable Securities

GLOBAL

1. Legal Entity Identifier (LEI)

Impacts

- *Any legal entity engaged in financial contracts, including banks, dealers/ brokers, corporations, pension funds and investment funds*

Key takeaway

- *LEI will act as a universal standard for uniquely identifying all entities related to a financial contract and will gradually be implemented across the industry*
- *First phase affects any entity trading swaps instruments that are subject to the jurisdiction of the U.S. Commodity Futures Trading Commission (CFTC)*

OVERVIEW

To monitor systemic risk and manage financial stability, the U.S. Office of Financial Research (OFR) and other G20 regulators will require financial institutions to report on information such as exposure and market risk. As a result, a new global identification standard, Legal Entity Identifier (LEI), has been established to set a universal standard for uniquely identifying all entities related to a financial contract. The LEI will persist over an entity's lifetime regardless of corporate actions or other business or structural changes.

As adoption evolves, LEI will enhance regulators' ability to monitor and analyse threats to financial stability. It will also enable financial institutions to improve their internal credit and exposure risk management capabilities.

KEY UPDATES

- The G20 approved the charter for the LEI Regulatory Oversight Committee at their November 2012 meeting, which led to the appointment of the Regulatory Oversight Committee (ROC) in January 2013. The ROC will now lead the further development of the Global LEI System, including the operational framework, relationship data, intellectual property, data privacy and confidentiality.
- By March 2013, the ROC is expected to establish the Global LEI Utility Central Operating Unit that will oversee global LEI utility issues and implementation deadlines.
- Once the global LEI utility is launched in 2013, the CFTC's interim solution, the CFTC Interim Compliant Identifier (CICI) code, will be grandfathered to become part of the new global LEI identification scheme.
- Under the CFTC's rules, Northern Trust is projected to begin data reporting and retention for non-deliverable forwards (NDFs), interest rate swaps, FX swaps and forwards, commodity swaps, and equity swaps by 10 April 2013.
- Other regulators, including in Europe and Hong Kong, are including the LEI in regulatory technical and consultation documents.

NORTHERN TRUST ACTIONS

- Northern Trust is preparing to generate the new Unique Swap Identifier code, which will be assigned by Northern Trust to uniquely identify every swap transaction for reporting purposes. Where applicable, this transaction identifier will be provided to clients.
- Currently, Northern Trust is required to register as a 'limited purpose' swap dealer for our NDF transactions only. This registration activity also requires adherence to the CFTC Business Conduct Standards and imposes other requirements related to our NDF transactions. These requirements are currently under review by our compliance and operations teams.
- Northern Trust is a member of the Private Sector Working Group, which advises and supports the FSB's global LEI Implementation Group, and we continue to work closely with industry peers to develop best practices for implementing the standard.

- Although at the early stages of adoption, more regulators are beginning to include LEI in their draft technical specifications. Northern Trust continues to monitor those developments closely and will communicate any perceived impacts to our clients.
- In December 2012, we informed our clients affected by the CFTC regulations of their obligation to register for a CICI/LEI and the process for registering. In some cases, for example where Northern Trust is a client's trustee, we can provide registration support and assistance.

HOW CAN I LEARN MORE?

For more information on which entities are required to register as counterparties, visit the CFTC's website at http://www.cftc.gov/index.htm.

To learn more about the CFTC's interim solution, the CFTC Interim Compliant Identifer (CICI) visit: https://www.ciciutility.org.

EUROPE

2. Alternative Investment Fund Managers Directive (AIFMD)

Impacts
- *Non-UCITS funds managed in, domiciled in, and/or distributed in the European Union*
- *Non-EU funds and managers wishing to sell in Europe*

Key takeaway
- *Managers can apply for a pan European marketing passport for alternative funds*
- *To secure the Passport, managers need to demonstrate new governance, reporting and structural requirements*
- *AIFMD provides for new duties, responsibilities and liability for the provision of a depositary function.*
- *Potential investors will need to consider the impact of AIFMD as it may raise costs and may drive managers to manage funds differently*

OVERVIEW

AIFMD imposes new regulatory provisions on non-UCITS that actively market to EU investors. Each member state is due to transpose the Directive into domestic law by July 2013.

Two further phases remain before AIFMD is fully implemented at the national level:
- 'Level 1' has already established the high level legislative framework
- 'Level 2' implementing measures issued 19 December 2012 provide clarity on how AIFMD is to be implemented
- 'Level 3' national legislative and regulatory guidelines are in progress

AIFMD formally comes into force in July 2013, and managers operating before July must submit an application for authorisation before July 2014. Any manager applying for authorisation after July 2013 needs to apply under, and be fully compliant with, the AIFMD regime.

Each member state is required to transpose AIFMD into national law and regulation before July 2013, and Northern Trust is participating in implementation and transition consultation processes in Ireland, the United Kingdom and other key jurisdictions.

NEXT STEPS

Managers should now be creating internal AIFMD projects, with a view to determining the optimal approach to compliance, taking into account the manager location, fund domicile, investor base, distribution strategy and operational environment.

NORTHERN TRUST ACTIONS

Northern Trust is actively engaged in the implementation and deployment of AIFMD across our business, and is working closely with our clients to review the implications and assess the strategic opportunities presented by the regulation.

We are holding a series of seminars to keep our clients updated on the latest developments in the Directive and provide an overview of our approach to AIFMD. At a recent seminar in London, we conducted a delegate survey of approximately 130 clients, prospective clients and consultants who stated that their AIFMD projects are in preliminary stages and that more clarity around the Directive is required.

Our next seminar will be held in Dublin on 10 April. If you are interested in attending the event, please contact your Northern Trust relationship manager or regular contact.

View further Northern Trust insights:
- AIFMD Implementation Checklist & Sample Implementation Timeframe
- Fund managers still have concerns around AIFMD, finds Northern Trust survey

3. European Markets Infrastructure Regulation (EMIR)

Impacts

- *All over-the-counter (OTC) derivatives users, even those granted a pension exemption for clearing, given the knock-on impacts to the bilateral market*

Key takeaway

- *The complexity of the collateral management will increase*
- *The requirement to finance margin requirements, together with clearing fees, may impact performance*

OVERVIEW

The regulation entered into force on 16 August 2012, and on 19 December 2012 the European Commission adopted nine regulatory and implementing technical standards underpinning EMIR. These standards came into force 15 March 2013 and 10 January 2013 respectively. However, this does not mean that the legislative process is quite over yet for EMIR as three technical standards remain to be finalised.

The first is with respect to risk mitigation techniques for OTC derivatives that are not centrally cleared. This technical standard is contingent on the outcome of the consultation paper launched by the Basel Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO). While the proposal made in the consultation paper allow a wide range of securities to be eligible for initial margin, the levels payable will be set higher than for the cleared initial margin (2% to 15% of notional, depending on asset class).

The second and third technical standards relate to colleges for central counterparties and to contracts that are considered to have direct substantial and foreseeable effect in the European Union to prevent evasion of EMIR. The European Commission will set a new deadline for the delivery of these standards in due course.

NEXT STEPS

The next step for policymakers is to finalise the above mentioned unfinished technical standards in addition to making steady progress towards a system where the EU and the US recognise the application of their respective derivative rules on both sides of the Atlantic as equivalent. A likely implementation timeline could look as follows:

Legislative	■ Likely entry into force of technical standards will be 15 March 2013
Clearing	■ Q1/Q2 2013: Existing central counterparties (CCP) to apply for recognition within six months of Commission's adoption of technical standards ■ Q3 2013: ESMA starts process to determine products to be cleared ■ Summer 2014: clearing obligation starts
Trade reporting	■ April 2013: Trade repository registration begins ■ 1 July 2013: Reporting to trade repositories for interest rate and credit derivatives starts (may be delayed) ■ 1 Jan 2014: Reporting to trade repositories for other derivative contracts starts
Risk mitigation rules for noncleared trades	■ Q1/Q2 2013: T+2 trade confirmation requirements start ■ August 2013: Portfolio compression, dispute resolution procedures and portfolio reconciliation starts ■ Q1 2015: Bilateral initial margin rules based on the BCBS/IOSCO paper start; however, ESMA may implement these earlier

NORTHERN TRUST ACTIONS

Northern Trust has enhanced its systems to provide operational support for central clearing of certain OTC derivatives. New capabilities allow us to electronically capture trade information on OTC derivatives and connect with external parties to route trades to electronic matching platforms, clearing firms and exchanges.

We are unaffiliated with particular clearing members or clearing houses and at every point in the central counterparty clearing process we will, therefore, be able to act as our clients' independent derivatives servicing agent to help them execute their trades efficiently and pursue their investment strategies.

We have developed and continue to develop solutions that build on our expertise in core custody and collateral management to provide transparent reporting, processing and margin solutions, helping investors manage the greater complexity of the central clearing environment.

4. Proposed EU Directive: Financial Transaction Tax Directive (FTT)

Impacts

- *Client purchases, sales and exchanges of financial instruments, the conclusion of derivative contracts, repos, and securities lending transactions*
- *Proposed tax will apply at a minimum rate of 0.1% on equities and bond transactions and 0.01% on derivatives*
- *Main exclusions include primary market transactions, transactions with EU central banks and public bodies*

Key takeaway

- *Effective date of 1 January 2014 proposed, but this is generally viewed as a very ambitious timeline*
- *Territorial scope of tax has been widened so it would not only apply to parties established in a participating member state (PMS), but also to parties established outside the PMS that are trading instruments originally issued in a PMS*
- *There are no details at this stage on the mechanisms and responsibilities for collecting and paying the tax*

OVERVIEW

The proposed Directive sets out the framework for a harmonized FTT within 11 participating member states: Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and Spain.

Transactions in scope	Include the purchases, sales and exchanges of financial instruments, the conclusion of derivatives contracts, repos and securities lending transactions.
Main exclusions	Include primary market transactions, transactions with EU central banks and public bodies and certain restructuring operations.
Instruments in scope	Include equities (and related depositary receipts), bonds, derivatives, as well as units in investment funds.

The territorial scope includes a "residence principle" and an "issuance principle." Under the residence principle, the tax applies whenever a party to the transaction (or a financial institution acting for the account of that party) is established in a PMS. For that purpose, "establishment" is defined very broadly and includes, for example, the authorization given by that PMS to a financial institution to operate within its borders. Under the issuance principle, the tax also covers transactions in instruments issued in a PMS.

France introduced its own version of FTT, effective 1 August 2012, limited to transfers of equities issued by French companies with market capitalization exceeding EUR1 billion.

Italy has also recently introduced its own FTT regime, which like French FTT, will apply to the transfer of equities, but also to derivatives referencing Italian equities. Italy's FTT regime is effective 1 March 2013 for equities and 1 July 2013 for derivatives, and we expect detailed implementation guidelines to be released shortly.

EU member states opposing the establishment of a FTT include the United Kingdom, Ireland, Sweden and Luxembourg.

NEXT STEPS

All 27 member states will discuss the proposed Directive, but only the 11 participating member states will have a vote. They must agree unanimously before the Directive can be implemented.

NORTHERN TRUST ACTIONS

Northern Trust is actively engaged in industry initiatives via associations representing the global custody industry, and is closely monitoring the new rules to understand the implications for our clients and our business.

5. Markets in Financial Instruments Directive (MiFID II)

OVERVIEW

MiFID II revises the initial MiFID Directive (implemented in November 2007) to promote further competition in the European securities market, modernise market structures, increase market transparency and enhance investor protection. It will be reinforced by other regulatory changes such as regulations on OTC and central counterparties (EMIR), short selling and credit default swaps together with upcoming reviews of the Market Abuse Directive and the Securities Law Directive.

MiFID II is making its way through the EU legislative process but the final text is yet to be agreed between the Council, the Parliament and the Commission. The European Parliament has almost unanimously voted in favour of changes to draft rules in the areas of transparency around trading rules, high frequency trading and limits on commodity derivatives trading.

NEXT STEPS

We anticipate that the Level 1 text of the Directive and the Regulation will be finalised during the course of this year. Implementation of MiFID II is not expected until 2015.

Impacts

- *Anyone operating in the European securities market including:*
  - *Broker dealers*
  - *Fund distributors*
  - *Traditional and alternative investment managers*
  - *Wealth management*
  - *Custodians*

Key takeaway

- *A key piece of regulation set to transform the way a range of instruments are traded in Europe*
- *Introduces a new passporting regime for non-European Economic Area (EEA) firms*
- *European Securities and Markets Authority (ESMA) and national regulators (in co-ordination with ESMA) given powers to intervene to protect investors from inappropriate products or services by banning products*
- *Increased transparency and reporting requirements for product classes such as OTC derivatives and fixed income*
- *Local authorities/ municipalities are to be treated as retail clients unless an opt-up procedure is followed to treat them as elective professional clients*

6. Shadow Banking

OVERVIEW

Shadow banking regulatory reform is spearheaded at the global level by the Financial Stability Board (FSB), which defines shadow banking as "credit intermediation involving entities and activities (fully or partially) outside the regular banking system." In Europe, the reforms will trickle down via the European Commission, the European Parliament and the European Council. This may result in the European Commission proposing EU-wide rules during 2013 with eventual local implementation by national regulators.

On 18 November 2012, the FSB published a consultation paper proposing an initial set of policy recommendations to mitigate the systemic risks associated with shadow banking. The paper focuses on five areas:

1. Mitigate the spill-over effect between the regular banking system and the shadow banking system
2. Reduce the susceptibility of money market funds to runs
3. Assess and mitigate systemic risks posed by other shadow banking entities
4. Assess and align the incentives associated with securitisation
5. Dampen risks and pro-cyclical incentives associated with secured financing contracts such as repos, and securities lending that may exacerbate funding strains in times of runs

On 20 November 2012, the European Parliament passed a non-legislative resolution on shadow banking suggesting how systemic risks posed by shadow banks could be minimised by, for example:

- Extending capital requirements to all unregulated entities
- Imposing limits on the complexity of financial products
- Considering whether shadow banking entities linked to a bank should be included in the bank's balance sheet

The resolution calls for the European Commission to adopt a consistent approach to collecting data centrally so it can map all financial service transactions in real time and identify the riskiest deals.

Meanwhile, debate continues in the United States over regulators' concern about the systemic risk posed by the potential for redemption runs on money market funds and this is covered in the 'Money Market Fund Reform' section later in the newsletter.

NEXT STEPS

The FSB will publish its final recommendations in September 2013. Thereafter it will work on procedures for the consistent implementation of its policy recommendations.

Impacts

- *Investors in, and sponsors of, money market funds as well as issuers of securities that rely on money market funds to help them meet their short-term financing needs*
- *Investors that provide financing to banks via repo or securities lending agreements*

Key takeaway

- *The FSOC has extended the comment period for its proposed recommendations on money market fund reform to February 2013. The FSOC will now consider the comments and may issue final recommendations*
- *The SEC is expected to issue recommendations on money market fund reform early in 2013*
- *The FSB recognises the value of secured financing, but it recommends greater levels of regulatory disclosure*

UNITED KINGDOM

7. Recovery and Resolution Planning 'Living Wills'

Impacts

- *All UK licensed deposit-takers*
- *Investment firms with assets exceeding GBP15 billion*

Key takeaway

- *Requires production of robust, detailed and credible recovery and resolution plans for financial institutions*

OVERVIEW

The 2008 banking crisis highlighted that firms had failed to implement effective recovery plans and needed to be better prepared to deal with periods of severe financial difficulty. In response to the crisis, the G20 has called for the rapid development of internationally consistent, firm-specific recovery and resolution plans (RRPs). Under the Financial Services Act 2010, all UK deposit-takers are required to put RRPs in place.

Recovery Plans are intended to enable firms to plan for how they would recover from severely adverse conditions that could cause their failure. It should set out in advance a firm's 'menu of options' for dealing with a range of severe stress events. These stresses may be caused by an idiosyncratic problem, a market-wide problem or a combination of both, and extend beyond the firm's current regulatory stress testing scenarios and remedies.

Resolution Plans are intended to provide a strategy and detailed roadmap to resolve a failed firm or group in a way that minimises the impact on financial stability without recourse to taxpayer funds, while at the same time limiting the social disruption that could occur from widespread interruption to deposit, insurance or securities accounts.

NORTHERN TRUST ACTIONS

Northern Trust is required to complete a UK Recovery Plan & Resolution Pack (UK RRP) covering the activities of all three of its FSA authorised firms. A dedicated team of subject matter experts across our business have coordinated the preparation of the UK RRP as part of a global integrated approach. A full-time UK programme manager is in place and the regional chief risk officer has been appointed as the UK RRP executive director. The first four modules (of six) were supplied to the FSA at the end of 2012 and the remaining two modules will be completed once we have agreed with the FSA as to which of our services or "economic functions" are considered critical.

As part of our resolution planning we were also required to create a Client Asset Resolution Pack (CASS RP). The CASS RP, which must be maintained at all times, is intended for use by an insolvency practitioner to facilitate the timely return of client assets where a firm has failed.

In response to the need to keep resolution plans current, we have recently established a resolution office as part of our corporate risk management function. This team is responsible for the development and maintenance of Northern Trust's resolution planning and coordination with the various supervisory authorities both in the United Kingdom and in the United States.

NEXT STEPS

We must determine with the FSA which of our services or "economic functions" are considered critical, and then complete the remaining elements of our UK RRP. We expect the FSA to publish a Policy Statement to include final rules during the second quarter of 2013.

We also must complete our US Resolution Plan, which is due to the Federal Reserve Bank of Chicago and the Federal Deposit Insurance Corporation by December 2013.

8. New Regulatory Architecture

Impacts

- *Financial services firms, including fund managers and insurance companies. In short all firms currently regulated by the FSA*

Key takeaway

- *The new regime poses both strategic and practical challenges that regulated firms need to consider*
- *The majority of firms (including fund managers) will be supervised by the Financial Conduct Authority for both conduct and prudential issues*

OVERVIEW

As part of the significant reforms taking place to the way in which financial services firms are supervised in the United Kingdom, the regulation of prudential and conduct supervision – both currently regulated by the Financial Services Authority – will be carried out by two new organisations: the Prudential Regulation Authority (PRA), which will be a subsidiary of the Bank of England, and the Financial Conduct Authority (FCA), which will replace the FSA and officially come into existence on 1 April 2013.

Financial Conduct Authority	■ The core objective of the FCA will be to ensure that consumers get a fair deal through a well-functioning market. To achieve this, new intervention powers will allow the FCA to ban products and financial promotions if it believes they create risks to consumers and to promote competition that is in consumers' best interest. ■ The FCA will be responsible for regulation in conduct in retail as well as wholesale, financial markets and infrastructure that supports those markets. With responsibility for the prudential regulation of firms that do not fall under the PRA's scope, the FCA will regulate approximately 27,000 firms
Prudential Regulation Authority	■ The PRA will have one objective: to enhance the financial stability of the overall financial system. It will do this by promoting the safety and soundness of firms and minimising the adverse effects of a firm's failure. Supervisors will take a closer look at firms' business models including revenue projections, examining in detail if a firm's business model exposes it to concentration and market risk. ■ The PRA will supervise approximately 2,000 firms for prudential matters. This includes all deposit-takers, insurance companies and a small number of 'investment firms' that could present significant risks to the financial system's stability. All firms within the PRA's remit will be subject to the FCA for conduct supervision.

NORTHERN TRUST ACTIONS

The new regime poses both strategic and practical challenges that we are considering. As we will be a 'dual regulated' firm under the new regulatory architecture we will be supervised by two independent groups of supervisors one for prudential (PRA) and one for conduct (FCA)) and responding to two sets of different supervisory requests. All other firms (for example the large majority of investment firms) will be supervised by one supervision area for both conduct and prudential issues.

Negotiating and interacting with the regulator will feel different irrespective of whether we are dealing with the FCA or the PRA. In addition to being required to answer to a range of new issues on our business model (as set out above) the new authorities will want to see a willingness to comply. Although we will still be able to challenge the regulators, the FSA has

made it clear that a firm dragging its feet in complying with supervisory requests when it is obvious that the outcome is in the best interest of society as a whole, is not a behaviour that would meet the regulators' expectations. In addition the FCA's new product intervention powers will put the pressure on product design and the product approval process.

The practical impacts should also not be underestimated. This includes updating any documentation with references to the FSA and getting accustomed to two separate sets of rulebooks.

UNITED STATES

9. Dodd Frank, Over the Counter Derivatives and Swaps (Title VII)

Impacts

- *Any investor trading in derivatives*

Key takeaway

- *Investors need to understand their obligations under the final rules and determine what actions they will need to take based on the dates to be regulatory compliant*
- *Northern Trust will continue to support asset managers in post-trade operational activities for clearing swaps*
- *Clients who engage in or plan to engage in OTC derivatives transactions should discuss their intentions with their Northern Trust relationship manager, including how they are preparing to meet the mandatory clearing requirements*

OVERVIEW

The provision of the Dodd-Frank Act pertaining to over the counter (OTC) derivatives and swaps is designed to provide a framework for transparency and accountability given the volume and the intricate role derivatives play in financial markets.

KEY IMPACT

Clearing Requirements

The U.S. Commodities Futures Trading Commission (CFTC) has issued final regulations which establish a schedule to phase in compliance with new clearing requirements. Under the new requirements, clearing will be phased in based on the type of market participant entering into swaps subject to the clearing requirement. The compliance schedule identifies categories of market participants and provides a compliance timeframe for each as follows:

Category 1 Entities	Includes swap dealers, security-based swap dealers, major swap participants, major security-based swap participants and active funds.
Category 2 Entities	Includes commodity pools; private funds (other than active funds); or entities predominantly engaged in activities that are in the business of banking, or in activities that are financial in nature, provided the entity is not a third-party subaccount.
Category 3 Entities	All other swaps, including those involving third-party subaccounts, ERISA plans and those not excepted from the clearing requirements.

Swaps Subject to Mandatory Clearing in First Wave

Certain types of swaps will be subject to mandatory clearing in the first wave, including:

- Interest rate swaps (fixed-to-floating rate swaps, basis swaps, overnight index swaps and forward rate agreements on certain common indices); and
- Credit default swaps on common indices

Swaps Exempt From Mandatory Clearing

The U.S. Treasury Department finalised its determination that foreign exchange (FX) swaps and forwards (as defined in the U.S. Commodity Exchange Act) should not be regulated as "swaps" under Title VII of the Dodd-Frank Act.

TIMELINE FOR MANDATORY CLEARING OF SWAPS

28 November 2012	CFTC published final clearing determination for certain credit default swaps and interest rate swaps
11 March 2013	Category 1 Entities to begin clearing swaps
10 June 2013	Category 2 Entities to begin clearing swaps
9 September 2013	Category 3 Entities to begin clearing swaps

OTHER KEY DATES FOR REPORTING AND REGISTRATION

31 December 2012	Earliest date for required registration for swap dealers and major swap participants, and for reporting and record-keeping requirements for interest rate and credit swaps
28 February 2013	Reporting for equity, foreign exchange and other commodity swaps begins
10 April 2013	End users subject to reporting and recordkeeping requirements for all swaps

NORTHERN TRUST ACTIONS

Northern Trust has invested significantly in our capabilities to support post-trade operational functions for cleared swaps as follows:

- Connected downstream platforms (accounting, client reporting, valuations, margin management, etc.) to support cleared swaps
- Developed a link to route trades to a third-party industry standard intermediary, MarkitSERV, to have client trades confirmed and submitted to an exchange and to clearing firms for acceptance
- Implementing a collateral management service to achieve margin optimisation

NEXT STEPS – WHAT SHOULD CLIENTS CONSIDER?

Understand and Prepare to Meet Mandatory Clearing Requirements

Investors need to understand their obligations under the final rules and determine, based on the timeline, what actions they will need to be regulatory compliant, and what steps they will need to take to be operationally compliant. If you currently transact, or plan to engage in OTC derivatives transactions, we encourage you to discuss your intentions with your Northern Trust relationship manager, including how you are preparing to meet the mandatory clearing requirements.

Post-Trade Activities for Clearing Swaps

Asset managers and outsource providers alike will continue to significantly invest in their derivative systems to support the new workflow required for mandatory clearing. This development has been a major area of focus for Northern Trust. We will continue to support asset managers in post-trade operational activities for clearing swaps.

HOW CAN I LEARN MORE?

To learn more about Dodd-Frank regulations pertaining to OTC derivatives and swaps, see the following:

- Implementing Mandatory Clearing of Swaps Under the Dodd-Frank Act
- Central Clearing of Over-the-Counter Derivatives
- Frequently Asked Questions: Centrally Cleared Swaps

10. Foreign Account Tax Compliance Act (FATCA)

OVERVIEW

On 17 January 2013, the U.S. Internal Revenue Service (IRS) and the U.S. Treasury Department issued final regulations for the implementation of the U.S. Foreign Account Tax Compliance Act (FATCA). Northern Trust is currently analysing the full impact of the final regulations and intergovernmental agreements (IGAs) on its businesses and entities, as well as on its clients. Northern Trust will be releasing updated FATCA FAQ documents and related client material to reflect the changes set out in the final regulations and in the IGAs concluded so far.

Following the conclusion of a Model I IGA with the UK on 12 September 2012, the US Treasury Department has signed additional Model I IGAs with Denmark, Mexico and Ireland. IGAs with Spain, Norway and Germany also have been announced, but not yet published. On 14 February 2013, the Treasury Department signed the first Model II IGA with Switzerland. Model II IGAs require financial institutions of the partner jurisdiction to report information regarding their US accounts directly to the IRS; Model I IGAs require reporting to the tax authorities of the partner jurisdiction.

The IGAs with the United Kingdom and Ireland will impact Northern Trust subsidiaries, funds and clients organised in those jurisdictions. Under the IGAs, UK and Irish financial institutions will be relieved of the requirement to enter into an agreement with the IRS, and the requirements are generally less onerous than those provided in the regulations. However, IGA financial institutions will retain significant due diligence, reporting and other responsibilities and will be required to register either with the IRS or locally. The publication by the UK tax authorities (HMRC) of draft FATCA regulations and guidance on 18 December 2012 provides insight into how the regulations will be applied in the UK and may also provide a template for other jurisdictions concluding Model I IGAs with the United States. Note that the UK rules are in draft form only and subject to change.

NORTHERN TRUST ACTIONS

In the United Kingdom, Northern Trust is working with HMRC through the British Bankers Association and other industry bodies, such as the Investment Management Association's (IMA) FATCA Implementation Working Group, to agree an appropriate method of submitting the required FATCA reporting.

Globally, Northern Trust is participating in industry organisations, and sharing perspectives with other industry participants to identify and resolve challenges. Northern Trust is modifying systems and operations to support Northern Trust's FATCA obligations and to assist fund managers in meeting FATCA obligations on their funds.

Impacts

- *Foreign financial institutions (FFIs) (including non-US banks, brokers, custodians, investment funds and insurance companies) and US financial institutions that make payments to FFIs or other foreign entities*
- *Institutional investors that will need to provide evidence of compliance to financial service providers*

Key takeaway

- *FFIs will need to provide evidence of FATCA compliance to financial service providers. To comply, FFIs (unless exempt under the regulations or an IGA) must conduct due diligence on account holders, report on US account holders and (at a later stage) withhold from non-compliant account holders*

NEXT STEPS

The IRS and U.S. Treasury Department are expected to publish additional guidance and revised forms over the course of 2013. The IRS will launch a new web-based FATCA Registration Portal for FFIs no later than 15 July 2013. FFIs must register on the portal by 25 October 2013 to be included on the IRS list of compliant FFIs before the 1 January 2014 effective date and thus to avoid FATCA withholding on US payments they receive.

More IGAs are expected to be concluded over the course of 2013; countries concluding IGAs also will be transposing the IGA provisions into their domestic legislation.

11. Money Market Fund Reform

Impacts

- *Affects investors in, and sponsors of, money market funds, as well as issuers of securities who rely on money market funds to help meet their short-term financing needs*

Key takeaway

- *The FSOC has extended the comment period for its proposed recommendations on money market fund reform until February 15, 2013. Afterwards, the FSOC will consider the comments and may issue final recommendations*
- *The Securities and Exchange Commission (SEC) is expected to issue recommendations on money market fund reform early in 2013*

OVERVIEW

On 13 November 2012, the Financial Stability Oversight Council (FSOC) issued a proposal for comment on three alternatives to reform money market funds:

1. Floating net asset value (NAV)
2. Stable NAV with a capital buffer and "minimum balance at risk"
3. Stable NAV with a risk-based capital buffer and other measures

- In addition to the FSOC's proposal, cash investments, like money market funds, currently face other challenges: the European Central Bank has lowered interest rates to zero and low interest rates in the United States are expected to persist through 2015.
- Fund sponsors face the possible need to maintain a capital buffer, enforce redemption restrictions, implement a floating NAV or some combination of the foregoing. These proposals could significantly change the way cash investments are managed.

NORTHERN TRUST ACTIONS

Our cross-functional team is evaluating the effects of the FSOC's recommendations on our clients and our business; our goal is to continue to offer to clients the safety and liquidity benefits they seek from money market funds.

We are closely monitoring the situation and actively participating in various industry group efforts pertaining to money market fund reform. On January 14, 2013, Northern Trust submitted a letter in response to the FSOC's request for comments. In that letter, Northern Trust encouraged the use of increased disclosures, gating and liquidity fees under certain circumstances.

For the past two years we have provided a link on our sites to the SEC site where market-based NAVs are published.

We continue to seek feedback from clients so that we can continue to understand and respond to their concerns.

NEXT STEPS

The FSOC extended the comment period for its proposed recommendations on money market fund reform until 15 February 2013. Comment letters to FSOC are being reviewed and next action steps from FSOC and/or the SEC are undetermined at this time.

HOW CAN I LEARN MORE?

Given recent developments, we will continue to educate partners and our clients about the changes the FSOC is proposing. We remain committed to offering our clients solutions to assist them with their liquidity needs.

To learn more about the effects of the economic environment, ultra-low interest rates and money market fund reform, read:

- Rethinking Cash Portfolios
- Market and Economic Commentary

APAC

12. Stronger Super

Impacts

- *Superannuation funds regulated by APRA will be required to comply with the new requirements*

Key takeaway

- *The reporting requirements are in draft form. The regulator is engaging with the industry to finalise requirements.*
- *The proposed start date for reporting is 1 July 2013, with reporting for the quarter ended 30 September 2013 as the first deliverable.*

OVERVIEW

In line with the global theme of "transparency," the Stronger Super legislation has been introduced progressively since 2011. Similar to the Dutch Financial Assessment Framework and the US Regulatory Reporting Requirements, the Stronger Super legislation is designed to improve the transparency of superannuation. Measures to achieve this goal include ensuring the Australian Prudential Regulatory Authority (APRA) is able to publish comparable data on the fees, costs and net returns of MySuper products and providing new data collection powers for the regulator in relation to superannuation.

The Stronger Super reforms stem from the government's wholesale review of the superannuation industry and are the most significant reforms to the Australian superannuation system in more than 20 years. The components of Stronger Super are covered by different tranches of legislation, which are in various stages of passing through Parliament. There are four components to Stronger Super:

1. **MySuper** – (members' interests, includes investments) will replace default investment options
   - A simple, low-cost product for members who do not exercise choice
   - Prescribed standards regarding fee structure, investment, insurance and disclosure
2. **SuperStream** – (Superfund administrators, back office)
   - Measures designed to enhance the back office
   - Data and e-commerce standards for transactions
3. **Self-managed superannuation funds**
4. **Governance**
   - New prudential standards
   - Heightened trustee and regulatory oversight
   - Will require a higher standard of care, skill and due diligence

NORTHERN TRUST ACTIONS

The Stronger Super legislation provides APRA with standard-setting powers. The new prudential standards bring the superannuation regulatory framework more into line with the banking and insurance sectors. These standards have passed through Parliament and will have effect from 1 July 2013 for the most part. APRA released drafts of the reporting that supports these standards for industry review and comment. Final reporting requirements were subsequently issued by APRA at the end of March, which are currently under review and are being compared to previous draft reports.

Northern Trust is highly engaged with and is lobbying through industry bodies such as the Australian Custodial Services Association (ACSA), who have submitted a response to APRA. Some key components of the response included a request for clarification for certain terms and definitions including liquidity, investment costs, netting methodology, materiality for investment option reporting, asset class definitions and also highlighted potential duplication between the Australian Bureau of Statistics (ABS) and APRA reporting data. In addition, the ACSA submission stated that the changes in the "fair value" accounting methodology to be applied when preparing APRA reports are not aligned to the implementation of the revised accounting standards for superannuation funds (currently "net realisable value" moving to International Financial Report Standards).

Based on the draft form of reports released, Northern Trust has undergone a detailed gap analysis of our existing capabilities and is well placed to assist superannuation funds in meeting the new requirements through our market leading global technology platform, which enables us to provide data in multiple formats to our clients. Northern Trust has been investing in technology to meet similar requirements in other regions, as we have experienced a global trend towards the provision of data over the past few years.

NEXT STEPS

Northern Trust is analysing the final reporting requirements recently released and is working in close collaboration with our clients to ensure the new requirements are met and will continue to engage with industry bodies such as ACSA.