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GANADO
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BANKING AND FINANCIAL INSTITUTIONS
NEWSLETTER

INTRODUCTION

Dear colleagues and friends,

It is a pleasure for us to send you the 5th edition of the BANKING AND FINANCIAL INSTITUTIONS newsletter by the Banking and Finance team at GANADO Advocates.

Following on the heels of the results of the comprehensive assessment tests, we saw the European Central Bank (ECB) formally assuming responsibility for the euro area banking supervision as from the 4th November, 2014. This represents a major watershed in the financial services regulatory landscape of Malta. GANADO Advocates is collaborating closely with major law-firms in Frankfurt who are familiar with the workings of the ECB to cater for any of our clients who might have dealings with the ECB. It must be remembered that any authorizations of changes in shareholdings need to be approved by the ECB, even in the case of non-significant banks.

I am also pleased to announce that the 2nd Annual Banking and Finance Law Seminar being organized by GANADO Advocates, in collaboration with Malta Bankers' Association, will be held on Thursday 5th March, 2015. Please save the date.

I do hope you will find this newsletter of use. Should you have any queries or suggestions to make or should you know of anyone who might be interested in receiving this newsletter in the future, please do not hesitate to contact me at cportanier@ganadoadvocates.com or Dr Leonard Bonello at lbonello@ganadoadvocates.com. We would be more than pleased to hear from you.

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Single Resolution Mechanism

The banking union was a response to the financial crisis and comprises various initiatives and instruments which are intended to produce a sounder banking system and provide a more effective and consistent resolution regime for certain banks and financial institutions within the eurozone area. The three main pillars of the banking union are single supervision, single resolution and the common deposit protection scheme which has now been placed on the backburner.

Banking union measures which are in place and/or underway address the different stages of dealing with a bank which may potentially fail and hence cover crisis prevention, early intervention and crisis management. The single resolution mechanism (SRM) together with the single resolution fund (SRF) is one of the main pillars of the banking union and comes into play when single supervision has not been sufficient to prevent a crisis.

The SRM will implement the Bank Recovery and Resolution Directive (BRRD) which provides for a common framework for bank recovery and resolution throughout the European Union. The SRM sets out a mechanism which is intended to ensure efficient and prompt resolution and which aims to provide a single process for dealing with failing banks which are subject to single supervision. The fact that the SRM applies to those banks which are established in Member States participating in the Single Supervisory Mechanism (SSM) (and hence subject to the supervision of the European Central Bank and the national authorities within the framework of the SSM) highlights the close link between supervision and resolution in banking union. Below are some main points which are worth noting in respect of the SRM:

- It sets out a uniform procedure and rules for the resolution of banks and certain other entities.

- The legislative instrument chosen is a regulation (Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolutions Fund and amending Regulation (EU) No 1093/2010) (the "SRM Regulation"). This choice reflects the desire to avoid a situation where the instrument requires transposition into national law and may give rise to insufficient

FATF guidance on the risk based approach (banking sector)

At its plenary meeting in October 2014 the Financial Action Task Force adopted and published guidance on the risk based approach for the banking sector. The document is split into three main segments: an explanation of FATF's risk based approach to AML and CFT, specific guidance for banking supervisors and specific guidance for banks. This guidance is welcome in view of the general shift in favour of a risk based approach following FATF's revision of its recommendations. This approach is also reflected in the proposed Fourth EU AML Directive and hence it would be useful to become familiar with the concept even at this stage.

harmonisation. Accordingly, the SRM will have direct effect and consequently produce a rise to a more consistent approach.

- It provides for centralised resolution and establishes a Single Resolution Board (the "Board"). The determination that a bank is failing / likely to fail is made by the ECB, although it is possible for the Board to make such a determination where the ECB does not do so. In order for resolution to kick in, the following three conditions must be satisfied: (a) a bank is failing or likely to fail, (b) there are no alternative private solutions, and (3) resolution action is necessary in the public interest. In the event that these conditions are satisfied, the Board will proceed to adopt a resolution scheme, including resolution tools and any use of the single resolution fund. Having a centralised resolution process allows for effective and timely action to be taken (allowing a bank to be resolved over the weekend). Although the focus is on centralised decision taking, the national authorities are involved in the resolution process, assisting the Board and implementing the resolution decisions (monitored by the Board). The Commission and the Council also have roles to play in the process.

- It is supported by a single resolution fund which will be equal to 1% of covered deposits of all banks in Member States participating in the banking union. The fund will be built up over a number of years and will consist of ex ante contributions and ex post contributions. Undoubtedly this a major consideration for those Maltese banks which fall within the scope of the SRM.

- The SRM Regulation enters into force in January 2015 however is planned to be operational from January 2016, together with the BRRD bail-in provisions. Until then, national regimes will apply. Nevertheless it would be in the interest of those entities which will fall within the scope of these instruments to be fully prepared for the changes and challenges they will bring.

Securities Financing Transactions

We refer to the proposal for a Regulation of the European Parliament and of the Council on reporting and transparency of securities financing transactions which contemplates reporting of all securities financing transactions to a central repository, detailed reporting on securities financing transaction activity by investment funds and specific requirements in relation to rehypothecation of assets. While this instrument is still at proposal stage and there are still a number of steps which must be taken before it becomes a legislative instrument, we wished to bring this to your attention with an invitation to follow this development in order to anticipate the direction being taken and the obligations which will accompany this Regulation once adopted.

The Whistleblower Act

The Protection of the Whistleblower Act, 2013 (the "Act") came into force towards end of last year and it protects an employee who makes a protected disclosure about an improper practice committed by his employer from detrimental action. The whistleblower is someone close enough to the organisation to potentially suffer retaliation – the protections afforded under the Act therefore do not extend to the general public but are afforded to those who fall within the definition of "employee" in the Act.

In terms of the Act, an employer is required to have procedures in place for receiving and processing reports of "improper practices" made by employees. Each employer must have internal whistleblowing procedures and a whistleblowing reporting officer i.e. a person to whom a protected disclosure may be made internally within the employer. The Act promotes the making of internal disclosures before escalation to external disclosures by requiring an employee to first make a disclosure internally – this aims to minimise the impact of the improper practice being committed.

An "employer" is defined as a "natural person, legal organisation or statutory body whether forming part of the public administration or the private sector who: (a) enters into a contract of service with an employee; or (b) who employs or engages or permits any other person in any manner to assist in the carrying on or conducting of his business; or (c) who seeks to employ other persons." This also includes voluntary organisations in relation to volunteers who render services to such voluntary organisation on a voluntary basis or otherwise.

The Second Schedule to the Act further clarifies the employers who are subject to the requirements of the Act and who are required to have in place internal whistleblowing procedures. Within the private sector, any organisation which, according to its last annual or consolidated accounts, meets at least two of the following criteria: (i) an average number of employees, during the financial year, of more than 250; (ii) a total balance sheet exceeding forty-three million euro (€43,000,000); and (iii) an annual turnover exceeding fifty million euro (€50,000,000), is required to comply with the provisions of the Act.

It is noted, therefore, that the obligation to have in place internal whistleblowing procedures and to appoint a whistleblowing reporting officer would only apply to the largest banks in Malta. The Act, however, empowers the Minister of Justice to amend the Schedule for the better implementation of the Act and therefore the Minister may at any time extend the thresholds set out in the Second Schedule.

Although the requirement of having internal whistleblowing procedures is mandatory only in those organisations which satisfy the thresholds set out above, a

whistleblower within an organisation not falling within those parameters is still able to make a protected disclosure as defined in the Act. This protection would apply to all credit and financial institutions licensed under Maltese law. If there are no internal procedures established for receiving and dealing with information about an improper practice, the whistleblower may in terms of the Act make an internal disclosure to the head or deputy head of the organisation. Furthermore, if the whistleblower reasonably believes that the head of the organisation is or may be involved in the wrong-doing alleged in the disclosure, then the whistleblower may make a protected disclosure to the whistleblowing reports unit of the authority within whose remit the activities carried out by the organisation fall (as set out in the First Schedule of the Act).

Although as per the above, the whistleblower is protected even if his employer does not fall within the categories set out in the Second Schedule of the Act, all organisations – even those who do not fall within the thresholds set out in the Second Schedule of the Act – should consider introducing and putting into place internal whistleblowing procedures. Internal whistleblowing procedures are a very effective internal tool for detecting and rectifying wrong doing being done within the organisation. These procedures can also potentially minimise the impact of the wrong doing being committed by having the wrong doing solved internally before escalation to external supervisory authorities.

We would be glad to discuss any assistance which you might require in this regard.

EMIR – Updated Q&A

On the 24 October 2014 the European Securities and Markets Authority published its eleventh update of its Q&A document which provides answers and guidance on the implementation of the European Markets Infrastructure Regulation (EMIR).

Repayment of a debt – not an automatic assumption of a liability

In the case "Lombard Bank Malta plc vs. RJ Attard & Company Limited, Richard Attard, and his wife Tania Attard", the First Hall Civil Court, presided over by Mr. Justice Joseph Zammit McKeon, held, on September 15, 2014, that, inter alia, the fact that the Lombard Bank Malta plc (the "Bank") was aware that certain payments were not made directly by Mr. Richard Attard nor by RJ Attard & Company Ltd (the "Company") but by Herman Depasquale, did not render Mr. Depasquale in any way an obligor towards the Bank. Mr. Attard and the Company remained bound to repay the outstanding amount under the loan and no third party, including Mr. Depasquale in his own name or on behalf of the firm R. Attard & Co, had assumed the debt in their place.

In this case, the Company took out a loan facility from the Bank, accumulating a debt of €41,395 with interest. Richard Attard and his wife Tania Attard stood as guarantors, jointly and severally for the repayment of this loan, and granted a general hypothec over all their assets as well as a special hypothec over two immovable properties. As the balance on the loan was not repaid, the Bank proceeded to file legal proceedings against the above-mentioned parties, requesting the Court to condemn them jointly and severally to pay to the Bank €41,395 together with interest.

In reply, the defendants disputed liability and asked the Court to call Mr. Depasquale into the proceedings. It was stated that when Mr. Depasquale became a partner in the audit firm RJ Attard & Co, it was agreed that he would pay all debts of the Company, including any outstanding amounts due to the Bank in terms of the loan.

The Court considered that Mr. Depasquale had no legal relations with the Bank. The Bank only had relations with Mr. Attard and his Company and it was not involved in the agreement between Mr. Attard and Mr. Depasquale. Mr. Depasquale did not formally assume the debt nor did he accept to be co-guarantor. During the proceedings, Mr. Depasquale testified that he would pay the Bank with funds of the partnership, but he had not signed any loan agreement with the Bank nor was he involved in any sanction letter issued by the Bank.

Mr. Attard, on the other hand, pleaded that Mr. Depasquale should be called into the proceedings, due to the fact that the Bank had accepted payment from him and furthermore since he was aware of the existence of the loan agreement. The Court

distinguished between a person who was called into the proceedings from a person who joined the proceedings in statu et terminus, as the former was deemed to be a defendant who could either be condemned by the court or discharged.

The institute of 'calling a person into the suit' (kjamata fil-kawza) served the purpose of avoiding a multiplicity of lawsuits regarding the same merits, and with the same persons. It was important that such a person to be called into the proceedings had juridical interest, required by law and that he could be sued and or oppose the legal action. To appear as a claimant/defendant in the proceedings, a person had to have (a) judicial interest – the request had to be based on the existence of a right or its violation; (b) the interest had to be direct and personal; (c) as well as actual - it had to arise from the actual violation of the right or infringement of the law. If it results that a person who was to be called into the proceedings could not be condemned as he had no judicial interest, then he was not a legitimate defendant, and the claimant's action could not be made against him.

Here the Court noted that Mr. Depasquale's interest was not direct and personal. Mr. Depasquale had never assumed the debt and it was irrelevant for the Bank as to who paid the loan. The Bank had always sent the statements to the Company. Even though there was an agreement between Mr. Attard and Mr. Depasquale in terms of which Mr. Depasquale would pay the debts of the Company, this was irrelevant since the Bank was not party to this agreement. In fact, as far as the Bank was concerned, this agreement was a res inter alios acta and not binding upon it.

The fact that the Bank was aware that some payments were not made directly by Richard Attard or the Company but by Mr. Depasquale, did not render Mr. Depasquale in any way an obligor toward the Bank. Mr. Attard and the Company remained bound to repay the outstanding amount under the loan account and no third party, including Mr. Depasquale in his own name or on behalf of the firm R. Attard & Co, assumed the debt in their place.

For these reasons, the First Hall Civil Court dismissed the plea to call Mr. Depasquale into the proceedings and ordered the case to be continued.

QUERIES & SUGGESTIONS

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We trust that this issue of our **Banking & Financial Institutions Newsletter** was of interest to our readers, however, should you have any queries or suggestions to make, please feel free to contact **Dr Conrad Portanier** at **cportanier@ganadoadvocates.com** or **Dr Leonard Bonello** at **lbonello@ganadoadvocates.com**. We would be pleased to hear from you.

Further, should you wish to stop receiving this newsletter please click **unsubscribe** on the email sending this newsletter, or by contacting **rmizzi@ganadoadvocates.com.**

Disclaimer

This update is not intended to impart advice; readers are advised to seek confirmation of statements made herein before acting upon them. Specialist advice should always be sought on specific issues.

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