Now in its fifth year, BNY Mellon’s Tax & Regulatory Client Forum, EMEA, is just one way in which we help our clients to navigate their way through the many tax, regulatory and market infrastructure reforms. This year, over 230 delegates engaged in discussions with experts from BNY Mellon and other industry professionals over two days of panels, presentations and practical workshops – all with the aim of gaining a deeper understanding of the emerging tax and regulatory landscape and the priorities for 2017 and 2018.

For this year’s event, based on our ongoing dialogue with clients, we put together an agenda and speaker list that reflects the increased volume of regulations rolling out across Europe and the US that will impact financial institutions. As well as dedicated sessions on key topics – such as the Common Reporting Standard, MiFID II, Base Erosion and Profit Shifting and TARGET2-Securities (T2S) – the client forum provided an overall context for tax and regulatory changes, identifying the wider themes and ideas that will influence the financial services sector for decades to come.

In his opening remarks, Lawrence Langenhan, Segment Head for Asset Owners and MEA, EMEA Asset Servicing, noted that these changes present both opportunities and challenges, and BNY Mellon aims to provide clients with the insights and support to assist with their compliance and help to build long-term strategies for success in this reformed market for investment services in Europe.

From a regulatory reform perspective, the far-reaching and wide-ranging nature of ongoing changes can make compliance seem all-consuming, taking the firm’s attention from serving the client. Although issues such as investor protection and transparency rules introduced or strengthened over the past years will result in higher costs and margin compression, there are also upsides. These include new product opportunities created by the changes, such as European Long-Term Investment Funds (ELTIFs), and cost efficiencies through market infrastructure projects like T2S. At the same time, technology innovation is fast evolving with the potential to further reduce costs or bring new insights that may add new value for clients.

In terms of tax, the direction of travel is also largely to be welcomed, despite challenges to business models, and the increased costs and workload faced by individual firms. Indeed the scale of change in the tax environment is just as dramatic as that unleashed by post-crisis financial market reform if not more so. The emphasis on responsible, ethical tax planning is certainly having a major impact, but the new initiatives to achieve greater transparency – some of which are being pushed strongly by the G20 countries – are also causing the most significant reassessment of the relationship between domestic and international tax laws in a century.

In this time of change, it helps to discuss priorities and best practice with peers, but of course the hard work continues day in, day out. The Tax & Regulatory Client Forum is very much the tip of the iceberg when it comes to how BNY Mellon is working with clients on tax, regulatory and market structure issues. In the spirit of collaboration, we look forward to sharing our plans and understanding yours as they evolve over the coming year.

“While changes to the global tax framework are not yet in place, the direction of travel is clear. As such, we must anticipate change, rather than wait for it. Don’t fight the change, take it as an opportunity. As Heraclitus said, ‘If you do not expect the unexpected, you will not recognise it when it arrives.’”

Mariano Giralt, Head of Global Tax Services, BNY Mellon

“2017-2018 looks to be a busy and demanding period for regulatory changes across EMEA and the US which present both challenges and opportunities. Margin compression is likely to continue, alongside greater transparency and cost pressures. But shifts in the regulatory framework are creating new areas of demand too.”

Paul North, Head of Product Management, EMEA, BNY Mellon
Transparency topped the tax agenda on the first morning of this year’s BNY Mellon Tax & Regulatory Client Forum EMEA and with good reason. Seen by many as an overdue attempt by governments to ensure entities and individuals pay their ‘fair share’, greater transparency is firmly on the table for a wide number of institutions and investors.

The automatic exchange of information (AEOI) between governments under the OECD-led Common Reporting Standard (CRS) initiative and its efforts to coordinate a comprehensive harmonisation of the global tax framework – the Base Erosion and Profit Shifting (BEPS) project – are among the most prominent and far-reaching of recent reforms. As noted by the panel of tax experts at the Tax & Regulatory Client Forum, these are only the most high-profile examples of a broader shift toward a more ethical and transparent tax environment which will fundamentally change how financial institutions interact with their clients and the tax authorities. The shift will also alter the roles and responsibilities of tax professionals within those institutions.

CRS is the latest step toward greater information-sharing by tax authorities on an automatic basis, starting with the European Savings Directive (EUSD) in 2005 and more recently US and UK Foreign Account Tax Compliance Act (FATCA), but its potential scope is unprecedented. With more than 100 jurisdictions having signed up for AEOI, increased reporting requirements will ultimately lead to tax authorities having a more comprehensive view of an individual’s investments than that of the individual’s financial intermediaries or service providers. This will raise the bar considerably in terms of the due diligence and recordkeeping expected of institutions regarding the tax status of clients. Over time, tax authorities will likely ask more targeted questions of institutions about their clients, based on superior intelligence.

As financial institutions ramp up their data management and due diligence capabilities, there is concern that CRS is moving too fast for participating jurisdictions. Panellists noted that infrastructure and skills deficits could prevent tax authorities from exchanging sufficiently accurate information ahead of the first CRS date for information exchange in September 2017. For participating authorities, many issues need to be resolved at short notice, from different conventions for address names such as street and house numbers to peer reviews between jurisdictions to the resolution of data privacy and confidentiality issues. Going forwards, tax authorities will expect financial institutions to do likewise, requesting evidence of sound data management processes and governance.

Similar to CRS in motivation, BEPS is even broader in its strategic and operational impacts for investment managers and institutional investors. It stems from a common desire by governments to close gaps in domestic and international tax laws that allow multinational entities to shelter profits in low-tax jurisdictions. The 15 ‘BEPS actions’ – focused on three pillars: coherence, substance and transparency – could alter policies on location, structure and financing arrangements. Although not aimed primarily at the institutional investment sector, panellists suggested that BEPS could prompt further expenditure on data collection, analysis, storage and dissemination, as well as the introduction of new policies and controls to ensure local compliance and global coordination and oversight. Implementing the appropriate data governance model may be a huge challenge, but not the only one. Tax departments that were historically equipped for filing returns and planning may now need to acquire the skills and the technology to design and oversee automated onboarding processes and data management systems in order to comply with BEPS without negatively impacting the customer.

CRS and BEPS might be co-ordinated by the OECD, but many non-OECD member countries – specifically developing countries – have signed up too. At the same time, supra-national non-tax reforms, such as anti-money-laundering rules, are also aimed at increasing transparency and information sharing. Local legislature is also aimed at increasing transparency and information sharing. The UK’s incoming corporate criminal liability offence, which will punish failure to implement sufficiently robust anti-tax evasion policies, is being closely watched in other jurisdictions that may follow suit. It’s hard to avoid tax reform, so to speak. The sheer scale of the changes being formulated is overwhelming and the outcome as yet unknown. Through discussions and workshops such as those held at the BNY Mellon Tax & Regulatory Client Forum, we hope to breakdown the impacts of the reforms into manageable chunks to support our clients’ preparations and our own. As Socrates said, “To move the world, we must first move ourselves.”
Direction of travel: MiFID II and PRIIPs plenary session briefing

Of all the regulatory initiatives launched over the past decade, few have the reach across our industry clients and BNY Mellon as MiFID II (Markets in Financial Instruments Directive II). Indeed, I needed input from not one but two colleagues to outline key impacts in a dedicated session at BNY Mellon’s recent Tax & Regulatory Client Forum EMEA in London.

From the outset, the European Commission always intended to review and revise key elements of MiFID, as well as extending their scope to non-equity markets. But the financial crisis widened the new directive’s investor protection requirements and added derivatives market reforms, as part of Europe’s response to the G-20 mandate, alongside the European Market Infrastructure Regulation. As such, few links in the investment value chain will remain untouched when the directive and its accompanying regulation come into force in January 2018. Unsurprisingly, MiFID II is consistently cited as a key regulatory concern among BNY Mellon clients.

A major difficulty is that some of the finer details are still subject to confirmation in Level 3 or 4 texts from the European Securities and Markets Authority (ESMA), which can cause firms to delay their preparations. In live polling, just under a quarter forum delegates said they had already conducted their impact assessments and defined their budgets and plans for 2017, while three in 10 said they were still assessing impacts. This compared with pre-event polling in which just under a quarter of respondents said their firms had not yet finalised their MiFID II plan, while a third had already started implementing changes.

From an asset servicing perspective, MiFID II does not radically change how BNY Mellon provides services, but there are several areas in which we can help clients adjust to new rules, notably around investor protection and product governance. As highlighted by Trudie Embery, MiFID II clarifies the roles and relationships between product manufacturers and distributors, while also providing more detailed information to investors, for example on costs and risks. These changes throw up lots of questions: how do manufacturers and distributors identify and classify different customer types across European jurisdictions? Will fund providers issue new share classes in light of the ban on inducements for investment advice? How will firms meet new disclosure requirements on costs, as well as demonstration of best execution? And in parallel with MiFID II, will firms overhaul all their key information documents for the introduction of PRIIPs rules or will they postpone changes to UCITS KIIDs until 2019?

At the forum, Ross Whitehill, stressed the trading workflow implications of MiFID’s pre- and post-trade reporting and best execution requirements. Noting the benefits of increased transparency, Ross nevertheless pointed out the administrative challenge to price-makers from the obligation to provide demonstrably fair pricing across a diverse client base and a wide range of asset classes and instruments. Similarly, buy-side firms face increased post-trade reporting requirements as well as ensuring their trading processes achieve best execution for all transactions, not just equities.

As work intensifies on MiFID II’s challenges, Ross also reminded delegates to remain alert to other regulatory initiatives. In particular, he warned of the potential negative impact on securities market liquidity from ESMA proposals to segregate assets held by UCITS and alternative investment funds at sub-custodians and central securities depositories. This could significantly increase the number of transactions required to complete a securities lending transaction – thereby diminishing returns and ultimately volumes – without improving investor protection.

While dialogue with regulators continues on this proposal, so must discussions between service providers and market participants as MiFID II’s deadlines loom. As well as our forums across the globe, BNY Mellon will continue to engage with clients as these changes unfold in 2017 and beyond.

What is the current status of your MiFID II project?

- Don’t know (26%)
- Conducted an assessment and believe MiFID II does not impact us (2%)
- Begun to implement changes (10%)
- Conducted our assessment and have plans and budgets defined for 2017 (24%)
- Still assessing the impacts (29%)
- Have not started any material work but will do so before end of this year (5%)
- Will start work in 2017 (4%)

Source: BNY Mellon
Market infrastructure: T2S update

Allison Levy, T2S Product Manager, Global Product Management, BNY Mellon

Like many other securities market infrastructure and regulatory initiatives, TARGET2-Securities (T2S) has been discussed with increasing interest over the past few years; but its relevance and benefits, particularly to the buy-side, have not always been clear.

This major pan-European post-trade project is now live and service providers such as BNY Mellon have strategically chosen to establish direct connectivity with T2S and have upgraded their value propositions accordingly. As such, it is a good time to reiterate the rationale for T2S and the opportunities for efficiency and risk reduction that it may offer. For this reason, I provided an update at our recent EMEA Tax & Regulatory Client Forum in a joint presentation with my colleague, Mark Higgins, who put T2S’s potential benefits in the context of market participants’ growing collateral management needs.

T2S stems from the European Commission’s intention to create a unified, frictionless securities market to boost investment in the European economy. Under T2S, securities settlement is migrating from multiple national central securities depositories (CSDs) to a single settlement engine operated by the European Central Bank. This simplifies and strengthens Europe’s post-trade market infrastructure, bringing harmonisation to the settlement process and therefore reducing risks. We are roughly midway through the implementation of T2S with more than half of the 23 participating CSDs having successfully migrated.

Through the development being undertaken by BNY Mellon, the first indication of the benefits of T2S are becoming clear. We are using T2S to increase our direct connectivity to six primary European markets (Italy, France, Belgium, the Netherlands, Germany and Spain) which totals seven CSDs. The transaction volume in those markets accounts for 90% of BNY Mellon’s European activity. This reduction in BNY Mellon’s reliance on sub-custodians lowers third-party exposure, offering greater efficiencies to our clients. As we connect directly to each of these markets, we are extending our settlement cut-off times to within 30 minutes of market close as well as aiming to improve our current corporate action deadlines. Operationally, we are already seeing better settlement rates in the Netherlands and Italy where we have already migrated.

In addition, BNY Mellon has leveraged its TARGET2 Euro cash clearing capabilities to become a payment bank on T2S. This means that we will settle our clients’ activity in those primary markets in central bank money and expand our collateral and settlement service. Harmonisation of securities settlement in T2S also brings additional functionality to a wide range of European markets that was previously only available in some markets. For example, T2S will enable BNY Mellon to support ‘hold and release’ in more markets, which provides clients with greater flexibility by permitting trades to be sent for pre-matching before being released on receipt of assets. Further flexibility and efficiency benefits from T2S will include wider availability of night-time settlement and auto-collateralisation, which can minimise liquidity costs via access to euro-zone central banks’ intra-day credit services.

While there are many elements to achieving better collateral management – for example use of the new ISDA protocol to support compliance with variation margin rules planned for March 2017 – the role for T2S is clear. With the heightened importance of identifying and mobilising the cheapest-to-deliver collateral, the ability to efficiently access a robust, flexible and harmonised securities settlement infrastructure could play a central role in any firm’s collateral strategy.

A view from Markets

Mark Higgins, EMEA Business Development, Markets, BNY Mellon

The importance of flexibility and operational efficiency for buy-side securities market participants was underlined in the second part of the session at the EMEA Tax & Regulatory Client Forum, in which Mark Higgins sketched out the changing regulatory landscape.

As Mark explained, the scale of post-crisis regulatory change has been close to overwhelming, not helped by some conflicts, anomalies and unintended consequences. Though the impacts vary across asset classes and institutions, the big picture is of increased requirements for collateral, notably to facilitate trades in the OTC derivatives markets, but also impacting securities lending and repo trading with multiple factors making collateral availability far from certain.

Though banks and brokers have typically had to comply with the new rules before their sell-side counterparts (Basel III has also altered sell-side collateral needs) all market participants need to re-evaluate how they access and manage collateral to optimise its use. The challenge varies widely across institutions, but few have the capacity to take on the job in one go. As such, some firms are trying to first identify process efficiencies, then look to optimise collateral resources as inventory visibility increased, before migrating gradually to a holistic, enterprise-wide approach, Mark observed.
Despite the plethora of tax, regulatory and market structure changes facing financial institutions, there are still opportunities to develop new products and services to add greater value for clients. A willingness to innovate whilst also tackling compliance pressures was reflected in polling conducted for BNY Mellon’s Tax & Regulatory Client Forum EMEA.

Around 60% of poll respondents (vs 53% last year) expect to spend more on market infrastructure, tax and regulatory developments in 2017 than 2016, with around 30% predicting unchanged expenditure. While MiFID II, CRS and Brexit were the highest priority issues for respondents overall, a full 21 different topics selected were cited as being among firm's top three priorities.

Paul Gough, Senior Counsel, Office of Public Policy and Regulatory Affairs, EMEA at BNY Mellon, touched on many of these during a forward-looking summary at the client forum. As well as commenting on BNY Mellon’s ongoing investment on regulatory projects and their impacts on clients, Paul noted the many drivers of future change. Alongside planned reviews of existing legislation (AIFMD, UCITS and CRD) and the measures emerging from the Capital Markets Union, he pointed to the completion of the European Banking Union and EU Bank Structural Reform initiatives, the regulatory impact of fintech innovation, the uncertainty of the Brexit timetable, and the evolving priorities of a new commissioner in the second half of the Juncker presidency.

On tax, local political considerations are likely to influence the progress of the transaction tax, Paul observed, predicting nevertheless movement on VAT, withholding tax and transparency.

Co-presenter Paul North also highlighted the long-term effect on business models from the combined force of multiple reforms, with reference to a recent client workshop on liquidity. Whilst bank deleveraging is a primary driver, the broad concept of liquidity risk (market, funding and cash) is evolving quickly, encouraging buy-side firms to review counterparty policies, investment operations and strategies and even distribution arrangements.

The volume of regulatory change clearly has wide business implications. More than 40% of poll respondents admitted that compliance priorities are forcing them to delay some projects, a slightly higher proportion than recorded in last year’s survey. Nevertheless, for some, attention is turning to the opportunities presented by the emerging regulatory framework. A total of 46% of 2016 poll respondents expect regulation to

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### Compared to 2016 how much do you think your firm will spend on marketing infrastructure, tax and regulatory developments in 2017?

- Less than 2016 (3%)
- About the same (30%)
- More than 2016 (60%)
- Do not know (7%)

### Do you believe these regulations/issues will have material impact on your firm in the next few years?

- Only minor impacts (15%)
- Yes, material impacts in the next 1-3 years (82%)
- Yes, but in the longer term (3%)
create value for their businesses, through cost savings, new products or new revenues. For the moment, the focus would appear to be on the bottom line, with 40% seeing opportunities to pursue cost savings through legal entity consolidation or fund rationalisation. Although polling suggests limited bandwidth for new product development in the short term (40% of respondents have no plans for new products in 2017), a third voiced their interest in TTFs, which allow investors to access the double taxation treaty benefits that would have accrued from direct investment, while achieving the scale efficiencies of investing alongside others in a pooled fund. In the client forum's panel session on the development of tax transparent pooling vehicles led by Chris Mitchell, head of UK tax services at BNY Mellon, panellists suggested that the operational challenges of establishing new fund structures mean that tax transparency and efficiency gains should be carefully weighed alongside wider considerations.

Addressing the wider picture, the tax stream on the first day of the forum closed with a panel discussion by senior tax experts from diverse finance sector backgrounds on the current fundamental changes to the global tax system. Panellists noted that the taxpayer bailout that followed the financial crisis was one of several events to have placed tax reform firmly on the political agenda, meaning that engagement with policy-makers would continue to be a priority for some time to come. The growing involvement of developing countries in the development of corporation tax rules was cited as a potential source of unpredictability, but panellists also noted impacts from the digitisation of commercial activity. As new company structures evolve – e.g. based on digital service delivery rather than ownership of assets – the tax system will need to adjust accordingly.

As such, it seems clear that efforts by investment firms to add value will continue to be complicated by the sheer range of current tax, regulatory and market structure changes. In this evolving environment, BNY Mellon stands ready to help clients balance their compliance and client service priorities.

Visit BNY Mellon’s interactive timeline and explore certain past, present and future regulatory initiatives impacting financial services globally by going to www.bnymellon.com/theroadahead

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