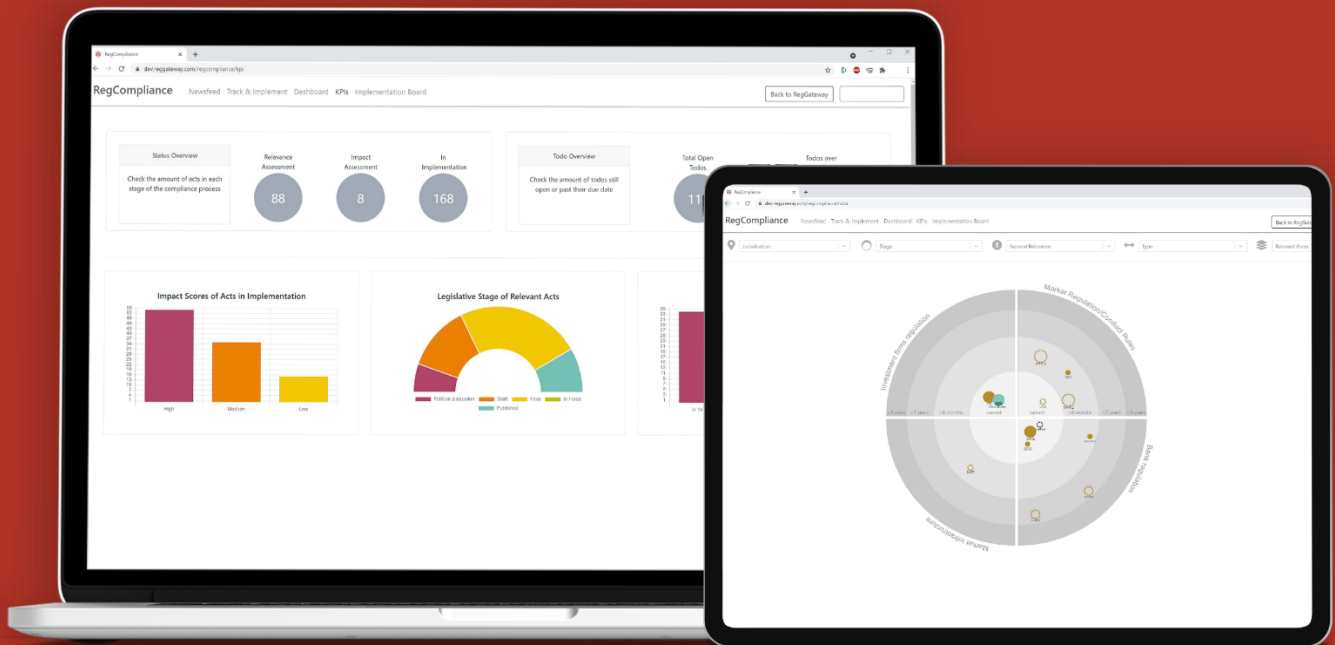


Regulatory monitoring: EU Version

Newsletter

August 2022





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CHANGE ANALYSIS AND PREVIEW OF RULES

Read the future versions of a law early, including the official explanatory memorandum, and identify any legislative changes.

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1. Bank regulation

1.1 Prudential regulation

(a) Solvency/Own funds issues

(i) EU

EC: Commission Delegated Regulation (EU) .../... supplementing the CRR with regard to RTS specifying exotic underlyings and the instruments bearing residual risks for the purposes of the calculation of own funds requirements for residual risks

Status: Adopted by the EC

The EC has adopted a Delegated Regulation supplementing the CRR with regard to RTS specifying exotic underlyings and the instruments bearing residual risks for the purposes of the calculation of own funds requirements for residual risks under the alternative standardised approach for market risk. In particular, the final draft RTS: (i) specify that longevity risk, weather, natural disasters and future realised volatility should be considered as exotic underlyings; (ii) set out a non-exhaustive list of instruments bearing residual risks; and (iii) set out a list of risks that, in themselves, do not constitute residual risks.

Date of publication: 16/08/2022

EC: Commission Delegated Regulation (EU) .../... supplementing the CRR with regard to RTS specifying the calculation methods of gross jump-to-default amounts for exposures to debt and equity instruments and for exposures to default risk arising from certain derivative instruments, and specifying the determination of notional amounts of instruments other than the instruments referred to in Article 325w(4) of the CRR

Status: Adopted by the EC

The EC has adopted a Delegated Regulation containing RTS on gross jump-to-default (JTD) amounts for exposures to debt and equity instruments and for exposures to default risk arising from certain derivative instruments, and specifying the determination of notional amounts of instruments other than the instruments referred to in Article 325w(4) of the CRR. The draft RTS specify how institutions are to determine prescribed components, and the notional amounts of instruments, when calculating gross JTD amounts for different types of instruments in accordance with the formulae in Article 325w of the CRR. In addition, the draft RTS specify which alternative methodologies institutions are to use for estimating the gross JTD amounts of exposures to default risk arising from derivative instruments whose pay-offs in the event of default of the obligor are not related to the notional amount of a specific instrument issued by that obligor, or to the LGD of the obligor or an instrument issued by that obligor. In this regard, the draft RTS provide specifications for the determination of those components, and methodologies, aimed at ensuring that gross JTD amounts calculated in accordance with Article 325w of the CRR are equivalent to those calculated under international standards for equivalent positions. In accordance with the provisions in the draft RTS, gross JTD amounts are determined as the change in market value of the instrument from which the exposure arises following an instantaneous default event of the debt or equity instrument, or of the obligor.

The Council and the EP will scrutinise the Delegated Regulation, and, if neither object, it will enter into force on the twentieth day following that of its publication in the OJ.

Date of publication: 11/08/2022

(b) Securitisation

(i) EU

EBA: Consultation on draft RTS specifying the determination by originator institutions of the exposure value of synthetic excess spread pursuant to Article 248(4) of the CRR

Status: Consultation

Deadline for the submission of comments: 14/10/2022

The EBA has launched a consultation on draft RTS on the determination by originator institutions of the exposure value of synthetic excess spread (SES) in securitisations under the CRR. The Capital Markets Recovery Package sets out that SES shall be considered a securitisation position by the originator institution with regard to a synthetic securitisation, and further requires the EBA to submit draft RTS specifying the determination of the exposure value to the EC. The proposals set out in the consultation paper will contribute to a more risk-sensitive prudential framework in the area of synthetic securitisation. The draft RTS address arbitrage opportunities, which can occur when an originator institution provides credit enhancement to the securitisation positions held by protection providers by contractually designating certain amounts to cover losses of the securitised exposures during the life of the transaction. These amounts, which encumber the originator institution's income statement in a manner similar to an unfunded guarantee, were not previously risk weighted.

These draft RTS specify the calculation of the exposure value of the elements that should be included in the exposure value of SES, taking into account the relevant losses expected to be covered by SES. These elements include: (i) any income from the securitised exposures recognised by the originator institution in its income statement under the applicable accounting framework that the originator institution has contractually designated to the transaction as SES that is still available to absorb losses; (ii) any SES contractually designated by the originator institution in any previous periods that is still available to absorb losses or for the current period; and (iii) any SES contractually designated by the originator institution for future periods.

Date of publication: 09/08/2022

2. Investment firms regulation

(i) EU

Corrigendum to IFR Delegated Regulation (EU) 2022/1159 on public disclosure of investment policy by investment firms

Status: Published in the OJ

The Corrigendum to Commission Delegated Regulation (EU) 2022/1159 supplementing the IFR with regard to RTS for public disclosure of investment policy by investment firms has been published in the OJ. The Corrigendum inserts two tables in Annex I of the Delegated Regulation related to voting behaviour in general meetings.

Date of publication: 25/08/2022



3. Market regulation/Conduct rules

3.1 Benchmarks

(i) EU

ESMA: Response to the Commission's consultation on the regime applicable to the use of benchmarks administered in a third country

Status: Final

ESMA has published its response to the EC's consultation on the regime applicable to the use of benchmarks administered in a third country (TC). Key points highlighted by ESMA include: (i) the restrictions on the use of TC benchmarks should be removed following a risk-based approach while ensuring a level playing field between EU and TC administrators; (ii) the proposal to create a new category of 'strategic' benchmarks is supported by ESMA. This category would be the only category of benchmarks subject to mandatory restrictions of use, similar to the current rules; (iii) the introduction of an EU ESG benchmark label would be an extra supporting tool against greenwashing; and (iv) ESMA emphasises that while the BMR covers a wide range of benchmarks used in the EU, so far very few jurisdictions have followed a similar regulatory approach regarding the provision and use of benchmarks. Therefore, the wide scope of the BMR would lead to the undesirable outcome of limited availability of TC benchmarks to EU investors as opposed to their non-EU peers.

The EC is required to complete its review and submit a report to the EP and the Council by 15 June 2023.

Date of publication: 19/08/2022

3.2 Consumer protection rules

(i) EU

EC: Final report on the disclosure, inducements, and suitability rules for retail investors study

Status: Final

The EC has published a final report on disclosure, inducements and suitability rules following the retail investors study that it commissioned to feed into the development of its retail investment strategy. The methodology for the study was designed to capture the whole process of retail investor decision-making, from searching for information and reviewing information documents to undergoing a suitability assessment and demands and needs test and receiving advice. The objective was the study and analysis of the investment environment the investors are in, with an analysis of the product costs, current practices in advice and product provision. The primary data collection focused on 15 EU member states to cover a wide range of situations regarding levels of take-up of retail investment products, market characteristics and geographical diversity. The findings relating to disclosure, inducements and advice, and suitability, demands and needs test are each set out in different chapters, with the findings then analysed under the light of the Better Regulation criteria to understand whether the current legal framework on disclosure, advice, inducements and suitability assessments is relevant, coherent, effective, efficient and has added value for consumer protection. Eight overarching conclusions arise from the study, and these are set out in Chapter 8.

Date of publication: 02/08/2022

3.3 MiFID/MiFIR

(i) EU

ECON: Draft report on proposed Regulation amending MiFIR

Status: Draft

The European Parliament's Economic and Monetary Affairs Committee (ECON) has published a draft report on the EC's proposal for a Regulation amending MiFIR as regards enhancing market data transparency, removing obstacles to the emergence of a consolidated tape, optimising trading obligations and prohibiting receipt of payments for forwarding client orders. The draft report, dated 26 July 2022, contains a draft EP legislative resolution which sets out suggested amendments to the proposed Regulation, as well as an explanatory statement.

The explanatory statement details the amendments to the legislation – these include: (i) consolidated tape (CT). The rapporteur agrees with the EC that a CT should be introduced across all asset classes. The various CTs should be introduced in a phased approach – starting with bonds, then equities/ETFs and derivatives – and with no longer than six months between the initiation of the process for appointing the CTP in each asset class; (ii) transparency waivers. The rapporteur proposes a rebalancing of the rules governing capital markets by limiting the use of the waivers to pre-trade transparency obligations under Article 4 of MiFIR. The threshold for the use of those waivers should be determined by ESMA, and not be higher than twice the standard market size. This proposal introduces greater flexibility than the EC's proposed fixed threshold, allowing ESMA to factor in different elements when determining the threshold; (iii) transparency: non-equities deferrals. To simplify the current regime and ensure end-investor transparency, the rapporteur believes that the deferral regime for non-equities should be harmonised. The price and the volume of a non-equity transaction should be published as close to real time as possible, and the price should only be delayed until, at most, the end of the trading day; (iv) systematic internalisers (SIs) definition and reporting requirements. ESMA should establish a register of all SIs and data reporting entities (DREs), specifying their identity and the instruments or classes of instruments for which they are either an SI or a DRE; (v) derivatives trading obligation (DTO) suspension. The EC proposal addresses the impact of the dealer-to-customer market by allowing for temporary suspension when receiving client quotes from counterparties with no active membership on an EU trading venue. However, this solution does not address the dealer-to-dealer market for credit default swaps in Europe. The ECON's amendment introduces the possibility for DTO suspensions in favour of dealer-to-dealer platforms that have established links to CCPs established in the EU, directly supporting the EU agenda to support the competitiveness of EU CCPs and clearing in the EU; and (vi) forwarding and execution of client orders. The rapporteur believes that the problems identified by the EC with the practices related to the so-called payments for order flows (PFOF) are symptomatic of a broader issue related to the best execution regime. In particular, the wording of the best execution requirements under Article 27 of MiFID II has led to widely divergent supervisory interpretations, of which PFOF is the starkest example. While the rapporteur maintains the initial proposal regarding PFOF, the amendments seek to implement changes to the best execution requirements with a view to ensuring a harmonised approach to best execution.

Date of publication: 29/07/2022

4. Market infrastructure

4.1 Custody rules

(i) EU

ESMA: Q&A on the implementation of the CSDR

Status: Final

ESMA has updated its Q&A on the implementation of the Central Securities Depositories Regulation (CSDR). Both changes relate to the section in the Q&A on settlement discipline. ESMA has updated a question on the calculation of cash penalties, and added a new question on the bilateral cancellation facility.

Date of publication: 03/08/2022

4.2 EMIR

(i) EU

ESMA: Memorandum of Understanding on CCPs established in South Africa

Status: Final

ESMA has published a memorandum of understanding (MoU) it entered into with South Africa's Financial Sector Conduct Authority, Prudential Authority and the South African Reserve Bank relating to CCPs established in South Africa that applied to ESMA for recognition under EMIR. This MoU: (i) ensures the fulfilment of the condition set out in Article 25 of EMIR, which is that cooperation arrangements have been established as regards the covered CCPs, including as regards information sharing related to the covered CCPs and to regulatory and supervisory developments in South Africa; and (ii) provides ESMA with adequate tools to assess compliance and to monitor the ongoing compliance by the covered CCPs with the recognition conditions in Article 25. This MoU also recognises the role of the ECB and other central banks of issue under EMIR. This MoU will take effect on the date that it is signed by the authorities. It will substitute the MoU entered into between ESMA and the FSCA (formerly known as Financial Services Board) dated 30 November 2015.

Date of publication: 10/08/2022

EC: Report on the treatment of central counterparty equity in the write-down and conversion tool under the CCP Recovery and Resolution Regulation

Status: Final

The EC has published a report, directed to the EP and Council, on the treatment of central counterparty (CCP) equity in the write-down and conversion tool under the CCP Recovery and Resolution Regulation. Under Article 27(7) of the CCP Recovery and Resolution Regulation (CCP RRR), the resolution authority must write down and convert any instruments of ownership, debt instruments and other unsecured liabilities immediately before or together with the application of another resolution tool, unless a different sequence is applied that would minimise deviations from the 'no creditor worse off' principle and better achieve the resolution objectives. The EC was mandated to publish a report on the application of Article 27(7) under Article 96 of the CCP RRR. Since technical work is still ongoing and practical experience is limited, the EC concludes that no recommendation to amend Article 27(7) can be made at this time. The EC states that more work is needed to ensure that the principle of CCP equity absorbing losses first and being fully loss-absorbing in resolution can be applied. It urges conclusions to be shared with the EP and the Council as soon as possible and no later than 12 February 2026, when the EC should submit the general CCP RRR assessment report.

Date of publication: 10/08/2022

(ii) International

IOSCO/CPMI: Discussion paper on CCPs' practices for addressing non-default losses

Status: Final

Deadline for the submission of comments: 04/10/2022

The International Organization of Securities Commissions (IOSCO) and the Committee on Payments and Market Infrastructures (CPMI) have published a discussion paper on central counterparty (CCP) practices to address non-default losses (NDLs). CPMI/IOSCO explain that NDLs can threaten a CCP's viability as a going concern and its ability to continue providing critical services. Therefore, under the CPMI-IOSCO Principles for financial market infrastructures (PFMI), CCPs must take action and have policies, procedures and plans for addressing NDLs, in addition to a sound risk management framework to mitigate and manage those risks. The discussion paper is intended to help advance industry efforts and foster dialogue by facilitating the sharing of existing practices CCPs employ to address NDLs, and by highlighting opportunities and challenges for CCPs to improve their planning for management of NDLs. It focusses on the key concepts and processes used by CCPs in four areas: (i) developing methodologies and practices for: (a) identifying scenarios in which NDLs may occur (NDL scenarios); (b) quantifying potential NDLs; and (c) assessing the sufficiency of resources and tools available to address NDLs; (ii) achieving the operational effectiveness of plans to address NDLs; (iii) reviewing, exercising, and testing plans for addressing NDLs; and (iv) providing effective governance of, and transparency regarding, plans for addressing NDLs, both in advance of, and during, an NDL event, and engaging with participants (e.g. clearing members and clients) and authorities.

Date of publication: 04/08/2022



5. Anti-money laundering

(i) International

FATF: Report on Germany's measures to combat money laundering and terrorist financing

Status: Final

The FATF has published a report evaluating Germany's measures to combat money laundering and terrorist financing. It found that Germany has implemented significant reforms in the last five years to strengthen its system and more effectively combat money laundering and terrorist financing. Furthermore, it found that some of these new measures are already delivering results, but that Germany needs to continue to implement reforms and take steps to make sure that there is resourcing and prioritisation at the operational level to combat illicit financial flows. The report also addresses BaFin and, for example application where suggests further improvement regarding money laundering prevention supervision in the non-bank financial sector and the elimination of deficiencies in individual financial institutions, especially large banks.

Following this publication, BaFin has published a statement expressing its delight that the FATF recognises BaFin's progress in the area of anti-money laundering and its agreement with the recommendations issued by the FATF. BaFin has also declared that it will implement these recommendations within its efforts to intensify its money laundering supervision.

Date of publication: 25/08/2022

6. Payments

6.1 Payment services/E-money

(i) EU

EC: Commission Delegated Regulation (EU) .../... amending the RTS laid down in Delegated Regulation (EU) 2018/389 as regards the 90-day exemption for account access

Status: Adopted by the EC

The EC has adopted a Delegated Regulation amending the RTS laid down in Delegated Regulation (EU) 2018/389 as regards the 90-day exemption for account access. This document aims to introduce into Delegated Regulation 2018/389 a new mandatory exemption from the requirement to apply strong customer authentication (SCA). Under the exemption, account providers must not apply SCA when customers use an account information service provider to access their payment account information, if certain conditions aimed at ensuring the safety and security of the payment service user's data. This includes that data must be limited in scope, the account service payment service provider (ASPSP) has to apply SCA for the first access and periodically renew it, and the ASPSP may at any time decide to apply SCA if it has objectively justified and duly evidenced reasons for unauthorised or fraudulent access. The Delegated Regulation aims to limit in parallel the scope of application of the voluntary exemption in Article 10 of Delegated Regulation (EU) 2018/389 to instances where the customer accesses the account information directly. It also extends the timeline for the renewal of SCA from every 90 days to every 180 days where the above-mentioned exemptions apply. ASPSPs that offer both a dedicated interface and a contingency mechanism are not required to implement the SCA exemption in the contingency mechanism, provided that they do not apply the SCA exemption in their direct customer channels.

The Council and the EP will scrutinise the Delegated Regulation, and, if neither object, it will enter into force on the twentieth day following that of its publication in the OJ.

Date of publication: 03/08/2022

7. Investment funds

7.1 Product regulation

(a) AIF

(i) EU

ECB: Opinion on a proposal for a directive as regards delegation arrangements, liquidity risk management, supervisory reporting, provision of depositary and custody services and loan origination by alternative investment funds

Status: Draft

The ECB has published an opinion on the EC's legislative proposal for a directive amending the AIFMD and the UCITS Directive as regards delegation arrangements, liquidity risk management, supervisory reporting, provision of depositary and custody services and loan origination by alternative investment funds (AIFs). In the opinion, the ECB focuses on the proposed amendments to the AIFMD, and sets out its views on the following: (i) liquidity management and macroprudential tools. The ECB generally welcomes the proposed directive's aim to harmonise the obligations of AIF managers (AIFMs) as regards the management of liquidity risks. However, the proposed directive should also aim to limit the liquidity mismatch between the assets and liabilities of AIFs, by means of measures that specifically target either assets or liabilities; (ii) reporting. The ECB stands ready to cooperate with ESMA in the preparation of a report for the development of an integrated supervisory data collection. The ECB stresses, however, that the integration of the underlying reporting infrastructure must not interfere with or otherwise prejudice the ECB's competence to adopt statistical regulations for its own purposes or to continue to include the full set of relevant statistical reporting requirements in relevant ECB regulations; and (iii) European System of Central Banks (ESCB) access to detailed data on the AIF sector. The proposed directive should require ESMA, which currently receives individual AIF data from the competent authorities, to also make that data available to the ECB and to other relevant ESCB central banks, to enable them to fulfil their tasks, including those under the Treaty, of defining and implementing monetary policy and contributing to the stability of the financial system.

Where the ECB recommends that the proposed directive is amended, specific drafting proposals are set out in a separate technical working document and accompanied by an explanatory text.

Date of publication: 09/08/2022

(b) UCITS

(i) EU

ECB: Opinion on a proposal for a directive as regards delegation arrangements, liquidity risk management, supervisory reporting, provision of depositary and custody services and loan origination by alternative investment funds

Status: Draft

The ECB has published an opinion on the EC's legislative proposal for a directive amending the AIFMD and the UCITS Directive as regards delegation arrangements, liquidity risk management, supervisory reporting, provision of depositary and custody services and loan origination by alternative investment funds (AIFs). For more information, please see section 7.1(a) above.

Date of publication: 09/08/2022

8. Special topics

8.1 Sustainable finance

(i) EU

ESMA: Response to EFRAG's consultation on first draft of European Sustainability Reporting Standards

Status: Final

ESMA has provided comments on the first draft of the European Sustainability Reporting Standards (ESRS), as suggested by the European Financial Reporting Advisory Group (EFRAG). The draft ESRS are a key element to achieve the Corporate Sustainability Reporting Directive's (CSRD) ambition of ensuring sustainability reporting which is relevant, reliable, comparable and understandable. This document highlights ESMA's support for a strong materiality assessment but expresses its concern with the suggested 'rebuttable presumption' approach. ESMA also encourages EFRAG to keep engaging with the International Sustainability Standards Board to ensure further alignment of the ESRS and the IFRS Sustainability Standards to benefit both users of sustainability reporting and the companies that prepare the reporting. In addition, ESMA sets out several technical remarks on the details of the draft standards.

EFRAG is expected to deliver its final draft ESRS to the European Commission in November 2022, on which ESMA, EBA and EIOPA are mandated to deliver opinions.

Date of publication: 08/08/2022

EC: Summary report on targeted consultation on the functioning of the ESG ratings market in the EU and on the consideration of ESG factors in credit ratings

Status: Final

The EC has published a summary report on a targeted consultation on the functioning of the ESG ratings market in the EU and the consideration of ESG factors in credit ratings. The report focuses on: (i) use of ESG ratings and dynamics of the market. The vast majority of respondents declare that they do use ESG ratings and among these, 77% use them 'very much', while a smaller share use them 'a little'. Almost all respondents replied that they value and need transparency in data sourcing and methodologies and timeliness, accuracy and reliability of ESG ratings. The majority of respondents, in total and within each main user group, expect to increase their usage of ESG ratings, at least to some degree but often to a large degree; (ii) functioning of the ESG ratings market. The large majority of respondents (over 84%) consider that the market is not functioning well today. A large majority of respondents consider that the lack of transparency on the methodologies used by the providers is a problem in the ESG ratings market, and that there are significant biases with the methodology used by providers, with the market prone to potential conflicts of interests; (iii) intervention in the ESG ratings market. Almost all respondents (94%) consider that intervention is necessary, of which the large majority (80%+) support a legislative intervention with the remainder supporting the development of non-regulatory intervention in the form of guidelines or a code of conduct. The vast majority of respondents (82%) consider that ESG rating providers should be subject to some form of authorisation/registration regime in order to offer their services in the EU; (iv) incorporation of ESG factors in credit ratings. Credit ratings are used by the large majority of respondents for investment decisions (48 out of 55), but they are only decisive for 9% of respondents; they are rather one of many sources of information (for 51%) or a starting point (for 13%). On the other hand, most respondents do find that the level of disclosures as to which credit ratings actions have been influenced by sustainability factors has improved sufficiently, with some laggards; and (v) intervention in the credit ratings market. Slightly more respondents consider that the current trends in the market are sufficient to ensure that CRAs incorporate relevant ESG factors in credit ratings (52 out of 101), than those who disagree. As far as enabling users' understanding of how ESG factors influence credit ratings is concerned, the majority (72%) do not consider market trends and ESMA guidelines to be sufficient. However, out of those who do not consider the current situation sufficient, the majority favour a non-legislative approach.

Date of publication: 03/08/2022

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