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stability

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Sustainable Finance: EU Commission consults on extending EU Taxonomy environmental objectives and on new social taxonomy

The EU Commission's Platform on Sustainable Finance expert group has published for consultation two draft reports on an extended taxonomy linked to environmental objectives and on a suggested new social taxonomy structure.

The draft report on taxonomy extension options linked to environmental objectives examines the premises, issues and options for and against extending the EU Taxonomy beyond green to include significantly harmful (SH) activities and no significant impact (NSI) activities, both relating to environmental sustainability within the overall EU sustainable finance framework.

The draft report on a suggested new social taxonomy explores the need to extend the scope of the EU Taxonomy to include social objectives. The report suggests vertical and horizontal social taxonomy structure dimensions. The vertical dimension focuses on products and services for basic human needs and basic infrastructure. The horizontal dimension considers the impacts on different groups of stakeholders affected by economic activities such as workers, consumers and communities and it also covers corporate governance.

Comments on both consultations are due by 27 August 2021. The Platform intends to submit final advice reports to the EU Commission in autumn 2021.

UCITS: EU Commission proposes amending directive on use of key information documents and extension of transitional arrangement under PRIIPs Regulation until 30 June 2022

The EU Commission has adopted a proposal for a directive amending Directive 2009/65/EC as regards the use of key information documents by management companies of undertakings for collective investment in transferable securities (UCITS). The proposal is intended to ensure that key information documents that comply with the Regulation on key information documents for Packaged Retail and Insurance-based Investment Products (PRIIPs) are considered as satisfying the requirements for key investor information for UCITS in Articles 78 to 82, and 94 of Directive 2009/65/EC, in order to avoid a situation where retail investors receive two different pre-contractual disclosure documents in respect of the same UCITS.

The Commission has also adopted a related proposal for a regulation amending the PRIIPs Regulation as regards an extension of the transitional arrangement whereby management companies, investment companies and persons advising on, or selling, units of UCITS and non-UCITS are temporarily exempted from the requirement to provide retail investors with a key information document. This transitional arrangement under Article 32 of the PRIIPs Regulation currently applies until 31 December 2021. The proposed regulation provides for an extension by six months to 30 June 2022. The purpose is to ensure legal certainty for the industry and the competent authorities as they prepare for the application of the new rules in Delegated Regulation (EU) 2017/653, which specifies the presentation and content of the key information document for PRIIPs, its standardised format, the methodology for presenting risk and reward and calculating costs, the conditions and minimum frequency for reviewing the information and conditions on providing the document to retail investors, and Directive 2009/65/EC, as amended.

The Commission has invited feedback on the proposed regulation by 9 September 2021. The feedback received will be summarised by the Commission and presented to the EU Parliament and Council with the aim of feeding into the legislative debate.

MiFID2: EU Commission adopts Delegated Regulation on criteria for establishing when an activity is to be considered to be ancillary to main business at group level

The EU Commission has adopted a Delegated Regulation supplementing MiFID2 by specifying the criteria for establishing when an activity is to be considered to be ancillary to the main business at group level.

MiFID2 exempts persons dealing on own account, or providing investment services to clients, in commodity derivatives, emission allowances or derivatives thereof, provided this is an ancillary activity to their main business on a group basis and the main business is not the provision of investment services within the meaning of MiFID2 or banking activities under CRD4. In this context, Article 2(4) of MiFID2 empowered the Commission to adopt regulatory technical standards (RTS) specifying the criteria for establishing when an activity is to be considered ancillary to the main business of a group.

Directive (EU) 2021/338 revisited the Ancillary Activity Exemption and empowered the Commission to adopt a Delegated Regulation that will replace CDR 2017/592 (RTS 20). The changes triggered by the amended Ancillary Activity Exemption are the deletion of the Overall Market Size Test of Article 2 of the CDR 2017/592 and the introduction of the new De-Minimis Threshold Test. The amended Ancillary Activity Exemption does not change the established calculation methodology of the Trading Test and Capital Employed Test as described in CDR 2017/592. The only change to these two tests is the level of the corresponding threshold as set out in Directive (EU) 2021/338. The new Delegated Regulation therefore continues to apply the established calculation methodologies and principles of the CDR 2017/592.

EU Commission consults on adjustment of threshold for notification of significant net short positions in shares

The EU Commission has published for consultation a draft Delegated Regulation on the adjustment of the threshold for the notification of significant net short positions in shares. The Delegated Regulation would adjust the threshold for the notification to competent authorities of significant net short positions in shares set out in Article 5, paragraph (2) of the Short Selling Regulation from 0.2% to 0.1% (and each 0.1 % above that). This follows an opinion published by the European Securities and Markets Authority (ESMA) on 13 May 2021.

Comments on the draft Delegated Regulation are due by 12 August 2021.

CRR: EBA publishes guidelines for data inputs in expected shortfall risk measure under Internal Model Approach

The European Banking Authority (EBA) has published its final guidelines clarifying the requirements that the data inputs used to determine the scenarios of future shocks applied to modellable risk factors should meet.

Institutions using the alternative Internal Model Approach (IMA) for market risk are required to compute the expected shortfall risk measure for their modellable risk factors. The guidelines clarify the conditions that the data inputs related to modellable risk factors should meet for their use in the expected shortfall calculations.

In particular, the guidelines set out criteria in relation to the accuracy, appropriateness, frequency for updating and completeness of the data inputs used by institutions for their modellable risk factors.

The guidelines will apply from 1 January 2022.

PSD2: EBA consults on draft limited network exclusion guidelines

The EBA has published a consultation on draft guidelines on the limited network exclusion (LNE) for certain payment instruments under the revised Payment Services Directive (PSD2).

The draft guidelines seek to provide clarity on the application of LNE requirements and address specificities for each type of LNE, including, where relevant, criteria and indicators on how to qualify a limited network of service providers and limited range of good and services as such.

The draft guidelines also set out the EBA's expectations on the use of payment instruments within a limited network, the application of the LNE by regulated payment service providers and electronic money issuers, as well as the submission of notifications to competent authorities.

The consultation closes on 15 October 2021.

CCP Recovery and Resolution Regulation: ESMA consults on draft RTS and guidelines

ESMA has launched seven consultations on draft RTS and guidance for its central counterparty (CCP) recovery mandates under Regulation (EU) 2021/23 (the CCP Recovery and Resolution Regulation).

ESMA's consultation papers (CPs) relate to the following:

- draft RTS on Article 10(12), Article 9(15), and Article 20(2); and
- draft guidelines on Article 18(8), Article 45a, Article 9(5), and Article 9(12).

Comments are due by 20 September 2021. ESMA intends to publish final reports by Q1 2022.

MAR: ESMA consults on amendments to guidelines on delayed disclosure of inside information

ESMA has launched a consultation on the review of its guidelines on delayed disclosure of inside information under the Market Abuse Regulation (MAR) in relation to its interaction with prudential supervision.

The consultation paper proposes to amend the current guidelines by:

- clarifying that in case of redemptions, reductions and repurchases of own funds, pending the prudential supervisor's authorisation, the institution has a legitimate interest to delay disclosure of inside information until authorisation is granted;
- clarifying that in case of draft SREP decisions and related preliminary information, the institution has a legitimate interest in delaying disclosure of inside information until that information becomes public; and
- adding a separate section clarifying that Pillar 2 Capital Requirements and Pillar 2 Capital Guidance contained in the Supervisory Review and Evaluation Process under the Capital Requirements Regulation and Directive package are likely to meet the definition of inside information under MAR and would therefore need to be disclosed as soon as possible, once final.

Comments are due by 27 August 2021. ESMA will consider the responses and expects to publish a final report including its amended MAR guidelines by the end of 2021.

EMIR REFIT: ESMA consults on derivatives reporting guidelines

ESMA has launched a consultation on draft derivatives reporting guidelines under EMIR as amended by Regulation (EU) 2019/834 (EMIR REFIT). The draft guidelines are intended to complement revised draft technical standards on reporting by counterparties, data quality and data access that ESMA submitted to the EU Commission in December 2020.

Amongst other topics, ESMA's consultation paper discusses reporting in the case of delegation and the correct population of fields for different products and reporting scenarios.

Comments are due by 30 September 2021.

EMIR/SFTR: ESMA publishes final advice to EU Commission on simplifying trade repository fees

ESMA has published a final report setting out technical advice to the EU Commission on simplifying and harmonising fees for trade repositories (TRs) under the European Market Infrastructure Regulation (EMIR) and the Securities Financing Transactions Regulation (SFTR).

ESMA's report follows a request for advice from the EU Commission in July 2020 and sets out proposals for the Commission, including in relation to the following:

- a single fixed fee for TRs (as opposed to two layers of fees);
- simplified TR turnover calculations for the purposes of supervisory fees;
- fees in the case of an extension of registration under SFTR or concurrent application under both regimes; and
- a single payment deadline of 31 March.

ESMA expects that the EU Commission will amend the Delegated Regulations on fees for TRs.

EMIR: ESMA reports on supervisory measures and penalties

ESMA has published its third annual report on competent authorities' supervisory measures and penalties under Articles 4, 9, 10 and 11 of EMIR.

The report takes into account changes introduced to EMIR by Regulation (EU) 2019/834 (EMIR REFIT), as well as developments including Brexit preparations and the outbreak of the coronavirus pandemic. Amongst other findings, the report details challenges in looking at group activities and an increase in the use of EMIR data for supervisory purposes.

EMIR: ESMA publishes methodology for assessing third-country CCPs' systemic importance

ESMA has published a methodology for assessing whether a third-country CCP, or some of its clearing services, are of such systemic importance that it should not be recognised to provide certain clearing services or activities in the EU. ESMA's CCP Supervisory Committee developed the methodology based on the requirements set out in Article 25(2c) of EMIR.

MiFIR: ESMA issues statement on access provisions for exchange traded derivatives

ESMA has published a statement setting out its expectation that national competent authorities (NCAs) not prioritise actions in relation to trading venues and CCPs benefitting from a temporary exemption from open access provisions for exchange traded derivatives (ETDs) under Article 54(2) of the Markets in Financial Instruments Regulation (MiFIR).

ESMA has issued the statement in light of the strong indication that the co-legislators intend to legislate to extend the transitional period for the temporary exemption, which expired on 3 July 2021, by two years to 3 July 2023.

MiFID: ESMA issues statement on payment for order flow

ESMA has published a statement warning firms and investors about risks arising from payment for order flow (PFOF) and certain practices by 'zero-commission brokers'.

ESMA states that PFOF raises serious investor protection concerns, and that in most cases, it is unlikely that the receipt of PFOF by firms from third parties would be compatible with MiFID2 and its delegated acts.

Noting a surge in retail client activity that has highlighted the use of PFOF, ESMA reminds firms that they must rigorously assess whether, by receiving PFOF, they are able to comply with relevant MiFID2 requirements, most notably those on best execution, conflicts of interest and inducements.

ESMA also reminds 'zero-commission brokers' that marketing services as 'cost-free' while receiving PFOF from third parties to compensate for the lack of direct commission will infringe the MiFID2 requirements to provide fair, clear and not misleading information and to provide information on all costs and charges to the client, as well as the MiFID2 inducements requirements.

ESMA requests that NCAs prioritise investor protection issues relating to PFOF in their supervisory activities for 2021 or early 2022.

SPACs: ESMA publishes statement on disclosure and investor protection

ESMA has published a statement on investor protection and prospectus disclosure issues raised by special purpose acquisition companies (SPACs).

Noting a significant rise in SPAC activity within the EU, ESMA has issued the statement to set out its expectations in relation to product governance requirements for manufacturers and distributors of SPAC shares and warrants under MiFID2 and disclosure requirements for SPAC prospectuses under the Prospectus Regulation. Among other things, ESMA:

- expects manufacturers and distributors carefully to scrutinise SPAC shares and warrants in their respective product approval process in order to assess whether retail clients should be excluded from the positive target market or included in the negative target market;
- expects NCAs to focus their scrutiny of the information provided in SPAC prospectuses on the following disclosure requirements: risk factor; strategy and objectives; escrow accounts and the reinvestment of proceeds; relevant experience and principal activities of the administrative, management and supervisory bodies; conflicts of interest; shareholder rights; major shareholders; related party transactions; material interests; the proceeds of the offer; the intention of certain persons to subscribe to the offer; and, on the offer price; and
- considers it appropriate that NCAs require the inclusion of additional disclosure in SPAC prospectuses for the purposes of investor protection, such as the future remuneration and shareholdings of the sponsors, the sponsors' possible role after the acquisition of the target company, possible changes to governance after the acquisition of the target company, and detailed information on possible scenarios should the sponsors fail to find a suitable target.

ESMA and NCAs intend to continue to monitor SPAC activity within the EU to determine if additional initiatives are necessary to preserve investor protection.

ECON Committee adopts report on pilot regime for DLT

The EU Parliament Committee on Economic and Monetary Affairs (ECON) has adopted its report on the proposal for a regulation on the establishment of a temporary common EU pilot regime for market infrastructures based on distributed ledger technology (DLT). The proposed regime would act as a regulatory sandbox, allowing market infrastructures to experiment with restricted uses of DLT under exemptions from the requirements of certain

financial services legislation. The proposal is part of the EU Commission's wider digital finance strategy which was published in September 2020.

In its report, the MEPs recommend that:

- the scope of the regime to be limited to shares with a market capitalisation of less than EUR 200,000,000 and bonds, exchange traded funds and UCITs with an issuance size of less than EUR 500,000,000;
- new entrants are required to comply with the same requirements as authorised investment firms or market operators in order to access the pilot regime;
- ESMA is granted a direct supervisory mandate to grant permissions and exemptions to DLT market infrastructures across the EU, after consulting with national competent authorities; and
- ESMA is required to publish annual interim reports during the lifecycle of the pilot regime on key trends, risks and vulnerabilities.

Trilogue negotiations with the EU Council will now take place, following which the EU Parliament plenary session and the EU Council will adopt a final text.

G20 Finance Ministers and Central Bank Governors publish communiqué

G20 Finance Ministers and Central Bank Governors have published a communiqué following the 9 and 10 July 2021 finance meeting in Venice, Italy.

The communiqué sets out issues discussed and actions decided at the meeting, including:

- a commitment to work together and with international financial institutions (IFIs) and relevant partners to develop proposals for sustainable financing to strengthen future pandemic preparedness and response;
- an agreement on a new international tax architecture, including endorsement of the two pillars on the reallocation of profits of multinational enterprises and an effective global minimum tax as set out in a 1 July statement by the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS);
- an intention to discuss at the October meeting the Sustainable Finance Working Group (SFWG) synthesis report and a multi-year G20 roadmap on sustainable finance, initially focused on climate, and to continue to promote implementation of disclosure requirements or guidance, building on the FSB's Task Force on Climate-related Financial Disclosures (TCFD) framework;
- a commitment to address gaps in the financial regulatory framework by completing the remaining elements of the G20 regulatory reforms, as well as to strengthen the resilience of the non-bank financial intermediation (NBFI) sector; and
- reiterating a commitment to a timely and effective implementation of the G20 roadmap to enhance cross-border payments by relevant authorities.

The next meeting is due to be held on 29 or 30 October 2021 in Rome.

Coronavirus: FSB reports on lessons learnt regarding financial stability

The Financial Stability Board (FSB) has published an interim report on the lessons learnt from the COVID-19 pandemic regarding financial stability. The FSB notes that the pandemic marks the first major test of the global financial system since the introduction of the G20 reforms following the 2008 financial crisis, and therefore offers a significant opportunity to review the functioning of the reforms.

The report notes that, so far, the global financial system has remained resilient throughout the pandemic as a result of both the post-crisis reforms and swift international policy response. National competent authorities took advantage of the flexibility within international standards to support financing to the real economy, and the FSB COVID-19 principles helped discourage actions that could have otherwise distorted the level playing field or led to harmful market fragmentation.

The FSB observes that resilience was greatest in those parts of the global financial system where implementation of the reforms was most advanced. It therefore emphasises the importance of completing the remaining elements of the reform agenda. It also notes that there were variations in resilience across financial sectors, and highlights the need to strengthen resilience in non-bank financial intermediation in particular.

Other areas that may require further focus include:

- risk and crisis management arrangements and preparedness;
- resilience in the context of rapid technological change;
- the functioning of capital and liquidity buffers;
- financial system procyclicality; and
- the ongoing impact of the pandemic, including the effect of the unwinding of support measures and the potential build-up of leverage and debt overhang in the non-financial sector.

Following this interim report, the FSB intends to engage with external stakeholders on its findings. It will then incorporate this feedback in a final report, due to be published in October 2021, which will set out recommendations for next steps.

Global Foreign Exchange Committee updates FX Global Code and reports on outcomes of three-year review

The Global Foreign Exchange Committee (GFXC) has published an updated version of its FX Global Code, alongside a report setting out the findings from a three-year review of its implementation. The review involved consultations with foreign exchange committees around the world and a public request for feedback.

Overall, responses suggested that the code remained fit-for-purpose, although the GFXC has identified a few areas that require amendment to ensure it reflects the evolution of the market. Among other things, the code has been updated to:

- encourage greater disclosure by those operating anonymous platforms, including of their policies for managing the unique identifiers of their users;

- require multi-dealer FX e-trading platforms (including anonymous platforms) to be transparent about their market data policies, including which user types such data is made available to and at what frequency, and to encourage them to disclose the mechanisms and controls by which they are managing or monitoring the credit limits of their users;
- place greater emphasis on the usage of payment-versus-payment (PvP) settlement mechanisms where they are available and provide more detailed guidance on the management of settlement risk where PvP settlement is not used;
- require providers of algorithmic trading or aggregation services to disclose any conflicts of interest that could impact the handling of client orders; and
- require market participants to make their clients aware of the basis on which trades might be rejected, and encourage them to keep records of the reasons behind electronic trade rejections.

Alongside the amended code, the GFXC has also published:

- an algorithmic trading due diligence template, designed to assist clients in understanding and comparing the services being offered;
- a transaction cost analysis data template, designed to assist users of algorithmic trading services in evaluating the quality of their trade execution; and
- a guidance paper on pre-hedging, designed to provide further clarity on the circumstances in which pre-hedging could be used in the FX market and the controls and disclosures that could help align it with the principles of the FX Global Code.

The GFXC also intends to issue standardised disclosure cover sheets for liquidity providers and FX e-trading platforms, and an additional guidance paper on 'last look' (the practice used in e-trading activities whereby a market participant receiving a trade request has a final opportunity to accept or reject it against the quoted price) in August 2021.

Benchmarks (Provision of Information and Documents) Regulations 2021 made and laid before Parliament

The Benchmarks (Provision of Information and Documents) Regulations 2021 (SI 2021/812) have been made and laid before Parliament.

SI 2021/812 relates to the giving of a notice or permission by the Financial Conduct Authority (FCA) to the administrator of a critical benchmark under Articles 22A, 22B, 23A and 23D of the UK Benchmarks Regulation (BMR) where the FCA is considering whether to wind-down a critical benchmark.

In particular, the Regulations:

- impose an obligation on the administrator of a critical benchmark to provide an address to which the FCA may send such a notice or permission electronically; and
- make provision for when a notice or permission sent in such a manner is deemed to have been received.

The Regulations come into force on 9 August 2021.

Basel III / UK CRR: draft Capital Requirements Regulation (Amendment) Regulations 2021 laid before Parliament

HM Treasury (HMT) has laid a draft copy of the Capital Requirements Regulation (Amendment) Regulations 2021 before Parliament.

The draft explanatory memorandum to the statutory instrument (SI) notes its primary purpose is to make use of a power under the Financial Services Act 2021 to revoke provisions in the Capital Requirements Regulation (CRR) so as to allow the Prudential Regulation Authority (PRA) to introduce prudential rules for credit institutions and PRA-designated investment firms.

The draft memorandum notes the PRA's near-final rules and sets out the following reasons for which, among others, certain CRR provisions are not to be replaced by the PRA's rules:

- the PRA has other powers by which it can achieve a similar effect;
- the provisions are not required in relation to the revised requirements;
- the provisions are subject to delayed commencement in the CRR and so do not currently impose requirements on firms;
- the provisions relate to powers for the PRA to make technical standards or HMT to make regulations in relation to matters where responsibility is to be transferred to the PRA; or
- the provisions are time-limited and will no longer be needed.

The Financial Services Act enables HMT to transfer responsibility for implementing the Basel Committee on Banking Supervision (BCBS)'s Basel III standards to the PRA. The Act also introduces a new accountability framework to provide oversight from Government and Parliament.

If approved by resolution in each House of Parliament, the draft SI would enter into force on 1 January 2022.

Basel III / UK CRR: PRA publishes policy statement on implementation of Basel standards

The PRA has published a policy statement (PS 17/21) on the implementation of Basel standards, which feeds back on responses to its consultation paper (CP 5/21) on the same topic. Near-final rule instruments, statements of policy (SoPs), supervisory statements (SSs) and reporting templates and instructions are appended to the policy statement.

In CP 5/21, the PRA proposed the following measures:

- new requirements to implement in the UK certain remaining Basel III standards; and
- rules that restate elements of the CRR and related onshored EU Level 2 legislation made under the CRR (CRR Level 2 Regulations) that are to be revoked by HMT.

PS 17/21 summarises those proposals and sets out changes to the PRA's draft policy following comments, which include the following in particular:

- changes to a number of required stable funding (RSF) factors under the net stable funding ratio (NSFR), including those applicable to certain centrally cleared derivatives transactions;

- postponed application of the mandatory substitution approach to large exposures that are secured by collateral issued to a third party;
- a new notification requirement to apply if firms' exposures to collective investment undertakings (CIUs) are material; and
- not implementing new reporting templates for the Fundamental Review of the Trading Book (FRTB) Alternative Standardised Approach (SA) in light of changes to HMT's approach to Basel III implementation.

The PRA indicates that its near-final policy material broadly corresponds to the EU's second Capital Requirements Regulation (CRR2), which implements the same set of Basel III standards.

The policy is intended to take effect on 1 January 2022. The PRA notes that HMT must revoke the relevant parts of the CRR before they can be replaced in final PRA rules, and that it does not intend to make changes to its policy or significant alterations to the text of its instruments before finalisation.

BoE publishes Financial Stability Report and conclusions on review of liquidity mismatch in open-ended funds

The Financial Policy Committee (FPC) of the Bank of England (BoE) has published its financial stability report.

The report sets out the FPC's views on the outlook for UK financial stability, including the resilience of, and main risks to, the banking system and market-based finance. Among other things, the FPC reports that:

- the UK banking sector remains resilient, and that the FPC expects banks to use all elements of their capital buffers as necessary to support the economy through recovery, with the UK countercyclical capital buffer rate expected to be maintained at 0% until at least December 2021;
- the interim results of the 2021 solvency stress test, together with the central outlook, are consistent with the decision of the Prudential Regulation Committee that the suspension on shareholder distributions is no longer necessary;
- risky asset prices have continued to increase, and in some markets asset valuations appear elevated relative to historical norms;
- to reduce the likelihood and impact of disruptions to market-based finance in the future, similar to the March 2020 'dash for cash', that international work focus on reducing the demand from the non-bank financial system for liquidity in stress, ensuring the resilience of the supply of liquidity in stress, and potential additional central bank liquidity backstops for market functioning;
- recently created credit sensitive rates are not robust or suitable for widespread use as a benchmark, and have the potential to reintroduce financial stability risks associated with LIBOR; and
- increasing reliance on a small number of cloud service providers (CSPs) and other critical third parties could, without greater regulatory oversight, increase financial stability risks.

In relation to market-based finance, the FPC also welcomes a report published by the BoE and FCA concluding their joint review into vulnerabilities

associated with liquidity mismatch in open-ended funds, which sets out a possible framework for liquidity classification and swing pricing.

FCA consults on LIBOR transition and derivatives trading obligation

The FCA has launched a consultation (CP21/22) on its proposals to modify the list of derivatives subject to the Derivatives Trading Obligation (DTO) in line with Articles 28 and 32 of UK MiFIR.

The FCA is reviewing the DTO in light of the interest rate benchmark reform and the recent Bank of England consultation on modifying the derivatives clearing obligation in line with Article 5 of UK EMIR. The proposals set out in CP21/22 are intended to support the FCA's strategic objective of ensuring that relevant markets function well, in particular the wholesale market for OTC derivatives and the other markets that depend on them.

Comments on CP21/22 are due by 25 August 2021.

FCA publishes business plan for 2021/22

The FCA has published its business plan for 2021/22. The plan sets out the FCA's key areas of focus in the coming year, including the following:

in relation to wholesale markets:

- plans to improve the functioning of primary and secondary markets, whilst maintaining standards, following Brexit;
- supporting the transition from sterling LIBOR to alternative risk-free rates (RFRs); and
- in relation to consumer markets:
- rules on financial promotions;
- pension advice standards;
- scams and high-risk investments; and
- proposals for a new 'Consumer Duty' intended to raise standards in firms' treatment of consumers.

The business plan also sets out the FCA's cross-cutting priorities, including in relation to fraud, diversity and inclusion, and a market-based transition to net-zero carbon emissions, as well as how it sees its future role and its plans to meet future challenges.

PRA issues statement on shareholder distributions by large UK banks

The PRA has published a statement setting out its revised approach to shareholder distributions by large UK banks.

In December 2020, the PRA published a statement in which it set out a framework of temporary guardrails that the boards of large UK banks should follow when making their decisions on capital distributions to ordinary shareholders in relation to full-year 2020 results. It also stated it would provide a further update ahead of the 2021 half-year results.

The PRA has now reviewed its approach. It observes that, in light of the interim results of the 2021 solvency stress test, banks remain well capitalised

and resilient to economic outcomes that are far more severe than the Monetary Policy Committee's current forecast. The PRA therefore judges that, despite continuing uncertainty around the evolution of the COVID-19 pandemic, the extraordinary guardrails are no longer required and have been removed with immediate effect. Bank boards are expected to follow the standard approach to capital-setting and shareholder distributions through 2021, making distribution decisions subject to the standard constraints of the regulatory framework, including the regular annual stress tests.

German Federal Government issues statement on impact of final Basel III implementation on banks' investment conduct regarding venture capital business

In its response (19/31320) to a minor interpellation (19/30768) of the FDP parliamentary group, the German Federal Government has stated that it will examine the effects of the EU Commission's forthcoming proposal for implementation of the final Basel III standards on banks' investment conduct in the venture capital business. The German Federal Government has stressed that it will continue to advocate for the implementation of the final Basel III standards not leading to equity investments with a long-term holding intention being classified as speculative.

The preliminary statement of the minor interpellation stated that the provisions affect banks' investments in venture capital funds with a corresponding impact on the financing conditions of German start-up companies.

BaFin and Bundesbank launch consultations on joint discussion paper on machine learning in risk models

The German Federal Financial Services Supervisory Authority (BaFin) and the German Federal Bank (Deutsche Bundesbank) have launched consultations on their joint discussion paper on machine learning (ML) in risk models (consultation 11/2021 on machine learning in risk models).

The paper deals with the use of ML in risk models of Pillars I and II of the regulatory frameworks for banks and insurers (Regelwerke für Banken und Versicherer). It is based on published principles of BaFin and Bundesbank for the use of Big Data and Artificial Intelligence (BDAI). Depending on the characteristics of certain models, the discussion paper defines supervisory priorities and describes starting points for the further development of the supervisory practice.

In the paper, BaFin and Bundesbank set out specific questions for potential developers and users of ML methods in Pillar I and Pillar II (i.e. credit institutions, insurers, and service providers) and request comments in order to understand what hurdles the industry believes prevent the adoption of ML methods in risk models and how they might be addressed.

Feedback on the questionnaire can be provided until 30 September 2021.

BaFin updates minimum requirements for compliance function and additional requirements governing rules of conduct, organisation and transparency

BaFin has published an update of its Circular 05/2018 (WA) on Minimum Requirements for the Compliance Function and Additional Requirements Governing Rules of Conduct, Organisation and Transparency (MaComp).

The update relates to the revised ESMA guidelines on certain aspects of the MiFID2 compliance function requirements of 6 April 2021, which BaFin included in special part BT 1 of MaComp.

The revised ESMA guidelines offer special guidance on product governance issues and the resulting changes for the compliance function. Thus, BaFin has supplemented BT 1 of MaComp with requirements for the monitoring and advisory activities and the compliance function's involvement in respective policies and procedures. Moreover, BaFin has comprehensively revised the requirements for annual compliance reports. The update reflects the ESMA guidelines in an almost unchanged manner.

Bank of Italy complies with ESMA guidelines on certain aspects of MiFID2

The Bank of Italy has announced its intention to comply with ESMA guidelines on certain aspects of the MiFID2 requirements relating to the compliance function. The guidelines specify certain application aspects relating to the requirements of the compliance function, which are governed by Delegated Regulation (EU) 2017/565 supplementing MiFID2 as regards, in particular, the organisational requirements of entities providing investment services. These guidelines apply to banks, investment firms and investment managers providing investment services and activities.

The guidelines apply from the day of publication of the Bank of Italy's note.

CONSOB complies with ESMA guidelines on outsourcing to cloud service providers

The Commissione Nazionale per le Società e la Borsa (Consob) has announced its intention to comply with ESMA guidelines on outsourcing to cloud service providers by incorporating them into its supervisory practice. The guidelines provide recommendations on identifying, managing and monitoring risks arising from arrangements for outsourcing activities and services to cloud service providers. The guidelines apply to competent authorities, which are given guidance on the supervision of such agreements in order to promote a convergent approach across the EU.

The guidelines will apply from 31 July 2021 to all outsourcing agreements to cloud service providers entered into or renewed from that date.

PSD2: Bank of Italy amends provisions on transparency of banking and financial transactions and services

The Bank of Italy has amended the provisions on transparency of banking and financial transactions and services. The intervention implements Article 106 of the Payment Services Directive (PSD2), where it provides that payment service providers shall make available in an easily accessible manner on their websites and in paper form the EU Commission's brochure illustrating consumers' rights within payment systems in the EU.

CSSF issues circular on conditions for application of alternative treatment of institutions' exposures related to tri-party repurchase agreements for large exposures purposes

The Commission de Surveillance du Secteur Financier (CSSF) has issued a circular to inform the public that, in its capacity as competent authority, it will apply the EBA's February 2021 guidelines (EBA/GL/2021/01) specifying the conditions for the application of the alternative treatment of institutions' exposures related to 'tri-party repurchase agreements' set out in Article 403(3) of the CRR for large exposures purposes.

The circular applies to Less Significant Institutions and to branches of non-EU credit institutions on an individual basis.

In-scope entities may replace the total amount of their exposures to a collateral issuer due to tri-party repurchase agreements facilitated by a tri-party agent, using as an alternative treatment the full amount of the limits that the institution has instructed the tri-party agent to apply to those exposures. When in-scope entities decide to carry out such a replacement, Article 403(3) of the CRR requires them to comply with specific conditions, which are further specified in the guidelines.

Where an in-scope entity intends to make use of the alternative treatment with a tri-party agent, it should notify the CSSF at least four weeks prior to the implementation of the alternative treatment. Further details on the notification and the related procedure are specified in the circular.

The circular applies with immediate effect.

CSSF launches survey of amount of covered deposits held on 30 June 2021

The CSSF has issued a circular launching a new survey on deposits, and more particularly on covered deposits, held by credit institutions incorporated under Luxembourg law, the POST Luxembourg for its provision of postal financial services, and Luxembourg branches of credit institutions having their head office in a third country as at 30 June 2021.

The CSSF also notes in its circular that a definition of 'covered deposits' and 'eligible deposits' can be found in Article 163 of the 2015 Law and that the provisions of Circular CSSF-CPDI 16/02 shall be taken into account, in particular with regard to the exclusion of structures assimilated to financial institutions, as well as the treatment of omnibus accounts.

Institutions are requested to provide the data at the level of their legal entity, consolidating data from branches located within other Member States, by 30 July 2021. The requested data shall be reported with utmost care, as it also constitutes the basis of determining the contribution to the Resolution Fund.

The circular further provides detailed guidance on the reporting procedure and it is noted that given the importance of this survey, a member of the authorised management, in this case the member in charge of the membership of the FGDL (the Luxembourg Deposit Guarantee Scheme) in accordance with section C of Circular CSSF 13/555, must review and approve the document prior to its transmission to the CSSF.

Polish Financial Supervision Authority adopts product intervention related to unit-linked insurance products

The Polish Financial Supervision Authority (KNF) has adopted a decision introducing a product intervention related to unit-linked insurance products (life insurance contracts if they are linked with an insurance capital fund). The KNF has introduced a prohibition on the marketing, distribution or sale of unit-linked insurance products:

- in the case of which the average return is lower than 50% of the interest rate for the period specified in the decision according to the relevant structure of the risk-free rate; or
- in the case of which the rules and investment restrictions set out in the rules of the insurance capital fund do not ensure that the funds of the insurance capital fund will not be invested in contingent convertibles.

The decision applies to both domestic and foreign entities offering unit-linked insurance products to customers in Poland. The decision is also to be complied with by Polish manufacturers of unit-linked insurance products offering unit-linked insurance products outside of Poland.

The decision applies to contracts concluded from 1 January 2022 (with the exceptions provided for in the decision).

Bank of Spain consults on draft circular to specialised lending institutions regarding liquidity, prudential requirements and reporting obligations

The Bank of Spain has launched a preliminary public consultation on a draft circular to specialised lending institutions (establecimientos financieros de crédito) regarding liquidity, prudential requirements and reporting obligations, amending Circular 1/2009 and Circular 3/2019.

The draft circular is intended to complete regulation of specialised lending institutions with regard to liquidity and reporting requirements in the area of solvency and shareholding structure (via an amendment of Bank of Spain Circular 1/2009), the guarantees that may be required from a person from a non-EU Member State who is to exercise control of a specialised lending institution and the specific cases in which specialised lending institutions must carry out the IAC and the Bank of Spain the SREP. The draft circular will also amend Circular 3/2019 to adapt it to the European Central Bank Guideline (EU) 2020/978 regarding the exercise of discretion by national competent authorities with regard to the threshold for assessing the materiality of credit obligations past due

The preliminary public consultation will be open for comments until 30 July 2021.

HKMA consults on practice code on contractual recognition of suspension of termination rights

The Hong Kong Monetary Authority (HKMA) has released a consultation draft on its new code of practice chapter ST-1 'Resolution Planning - Contractual Recognition of Suspension of Termination Rights'.

Section 196 of the Financial Institutions (Resolution) Ordinance (FIRO) empowers the HKMA as resolution authority in relation to banking sector

entities to issue a code of practice about any matter relating to the functions given to the HKMA as a resolution authority by the FIRO. Chapter ST-1 is intended to provide guidance on how the resolution authority intends to exercise certain discretionary powers under, and on the operation of certain provisions in, the Financial Institutions (Resolution) (Contractual Recognition of Suspension of Termination Rights – Banking Sector) Rules. The chapter does not seek to provide a comprehensive overview of requirements under the Stay Rules.

The consultation period will end on 9 September 2021.

MAS consults on proposals to refine tier structure requirements and introduce new requirements relating to remuneration

The Monetary Authority of Singapore (MAS) has launched a public consultation on proposals to refine the tier structure requirements under the Financial Advisers Act (FAA) and introduce new requirements relating to remuneration.

In particular, the MAS intends to:

- clarify its policy intent with respect to the tier structure requirements, and refine the requirements on tier structures, which includes defining overriding benefits and stipulating the circumstances under which payment of overriding benefits is allowed;
- consolidate and effect the tier structure requirements under the FAA and extend the application of the requirements to all financial advisers, including exempt financial advisers which operate tier structures, for consistency across the financial advisory (FA) industry; and
- introduce restrictions on the direct payment of remuneration to, and acceptance of remuneration by, representatives and/or supervisors of other FA firms.

The MAS expects FA firms to bear in mind the policy intent behind the MAS' rules when designing their remuneration arrangements and to comply with both the letter and the spirit of the rules. The MAS has indicated that it will also conduct a subsequent consultation on the legislative amendments to effect the proposals set out in this consultation paper.

Comments on the consultation are due by 13 August 2021.

MAS provides insurers with updates and FAQs on supervisory expectations for benchmarks transition

MAS has issued a circular to provide guidance to insurers on updates and frequently asked questions (FAQs) relating to supervisory expectations for benchmarks transition.

The MAS has extended the timeline for financial institutions (FIs) to cease new JPY LIBOR derivatives contracts that mature after end-December 2021, from end-June 2021 to end-September 2021. The extension is intended to align with the timelines announced by the Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks, and facilitate more efficient group wide management of LIBOR transition by global FIs.

Other supervisory expectations set out in the MAS' circular issued on 23 April 2021 regarding 'Supervisory Expectations for Benchmarks Transition' remain unchanged. The revised LIBOR transition timelines have been set out in Annex A to the circular. To help FIs better understand the expectations in Annex A and their application, the MAS has also appended a set of FAQs in Annex C to the circular.

With less than six months remaining to the cessation of non-USD LIBOR, FIs are urged to complete the tasks necessary to prepare for the benchmarks' discontinuation. The MAS has also indicated that it will step up the frequency of monitoring to track the progress of individual FIs as the end-December 2021 milestone approaches.

APRA consults on authorised deposit-taking institution's preparedness for zero and negative interest rates

The Australian Prudential Regulation Authority (APRA) has launched a public consultation on its draft expectations regarding authorised deposit-taking institution's (ADI's) preparedness for zero and negative interest rates.

APRA considers the risks arising from an ADI's lack of preparedness for zero and negative interest rates to be material since this could have significant implications for an ADI's risk management, hedging, operational processes, contracts, product disclosures, IT and accounting systems among other areas. Accordingly, APRA has set out its proposed expectations for ADIs' preparedness for zero and negative interest rates, after taking into consideration the responses received from ADIs to its December 2020 letter and international experience.

In particular, APRA expects ADIs, at a minimum, to develop tactical solutions to implement zero and negative market interest rates and cash rate by 30 April 2022. Tactical solutions are typically shorter-term fixes, involving workarounds on the periphery of existing systems, along with overrides in downstream systems.

Further, ADIs are advised to assess the associated operational risks and ensure that there are appropriate controls in place to manage them. ADIs should also consider any relevant conduct related issues, including the potential for conflicts of interest, fair treatment of clients, and asymmetry of information.

Comments on the consultation are due by 20 August 2021.

APRA consults on contingent liquidity reserves for locally-incorporated ADIs subject to liquidity coverage ratio requirements

APRA has launched a public consultation on contingent liquidity reserves for locally-incorporated ADIs, subject to APS 210 Liquidity Coverage Ratio (LCR) requirements.

Self-securitised assets are a key source of contingent liquidity in stress. APRA considers it is prudent for an ADI to maintain contingent liquidity reserves for use, if required, at short notice. APRA recognises self-securitised assets that are in excess of those used as collateral for the committed liquidity facility (CLF) as a form of contingent liquidity, and notes the risk that these assets may not be increased in a timely manner in a future stress due to operational issues and/or insufficient eligible loans.

Given this risk, Prudential Practice Guide APG 210 Liquidity (APG 210) states that for an ADI with a CLF with the Reserve Bank of Australia, APRA expects the level of the ADI's self-securitised assets would be well in excess of that used as collateral for the CLF. While the CLF has decreased materially, APRA maintains its view that it is prudent for an ADI to hold contingent liquidity reserves regardless of the size and presence of the CLF. Accordingly, APRA intends to revise its guidance for self-securitised assets, to de-link it from the CLF, by proposing guidance for the level of these assets to be maintained periodically.

In particular, APRA proposes to replace APG 210 paragraph 67 with the following: 'For a locally-incorporated LCR ADI, it would be prudent to hold self-securitised assets with a cash value equivalent to at least 30 per cent of group net cash outflows as contingency for periods of stress. APRA would expect the self-securitised assets to be unencumbered, and not held as collateral for any other purpose.'

Comments on the consultation are due by 20 August 2021.

RECENT CLIFFORD CHANCE BRIEFINGS

10 questions on the proposed carbon border adjustment mechanism

The European Commission has published a proposal for a Regulation on a Carbon Border Adjustment Mechanism (CBAM) to deal with the long-standing problem of 'carbon leakage' that impedes the EU's decarbonisation plans.

It is part of the Commission's 'Fit for 55' initiative that will help it achieve the EU's new target for a 55% reduction in greenhouse gas emissions by 2030 (against 1990 levels).

This briefing answers 10 key questions about the proposal.

https://www.cliffordchance.com/briefings/2021/07/10-questions-on-the-proposed-carbon-border-adjustment-mechanism.html

New German ownership control regime creates more onerous obligations in financial institutions M&A

On 11 June 2021, BaFin closed its consultation on substantial amendments to the German Ownership Control Regulation (Inhaberkontrollverordnung, 'InhKontrollV'). These amendments mainly serve to implement the Joint Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector published by the European Supervisory Authorities on 20 December 2016 ('Joint Guidelines') and to make further technical adjustments driven by recent changes to the German Insurance Supervision Act (Versicherungsaufsichtsgesetz, 'VAG') and in the German Banking Act (Kreditwesengesetz, 'KWG').

This briefing summarises the key changes which affect, in particular, investments by sovereign wealth, private equity and hedge funds as well as by investors from third countries outside the European Economic Area intending to acquire a qualifying holding in a credit institution, financial service institution, insurance or re-insurance undertaking or pension fund.

https://www.cliffordchance.com/briefings/2021/07/new-german-ownership-control-regime-creates-more-onerous-obligat.html

COP26 – nature-based solutions to climate change

COP26 – the United Nations' 26th conference on climate change is expected to focus not only on the global climate crisis, but also to highlight the interconnected loss of biodiversity. These issues will have a huge impact on all of us – including businesses.

At a recent Clifford Chance event, a panel of experts discussed nature-based solutions and the crucial role nature plays in combating climate change and sustaining national economies, as well as examining how state and private sector nature-based solutions could be financed.

This briefing provides a summary of the discussion.

https://www.cliffordchance.com/briefings/2021/07/cop26--nature-based-solutions-to-climate-change.html

Colorado joins California and Virginia with a comprehensive data privacy law

On 8 July 2021, Colorado Governor Jared Polis signed the Colorado Privacy Act, making his state the third to enact a comprehensive consumer privacy law. Although there are some key differences, the CPA largely parallels both the California Privacy Rights Act and the Virginia Consumer Data Protection Act, and will give Colorado consumers certain rights with respect to their personal data. The new law will go into effect on 1 July 2023.

This briefing examines the new privacy law.

https://www.cliffordchance.com/briefings/2021/07/colorado-joins-california-and-virginia-with-a-comprehensive-data.html

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