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Sustainable Finance: ESMA publishes supervisory briefing on investment funds

The European Securities and Markets Authority (ESMA) has published a supervisory briefing on sustainability risks and disclosures in the area of investment management.

The briefing aims to further enhance convergence among national competent authorities (NCAs) via common practices with a view to increasing transparency for investors and avoiding greenwashing, and sets out guidance for:

- the supervision of fund documentation and marketing materials, as well as guiding principles on the use of sustainability-related terms in funds' names; and
- the supervision of the integration of sustainability risks by AIFMs and UCITS managers.

ESAs report on withdrawal of authorisation for serious breaches of AML/CFT rules

The Joint Committee of the European Supervisory Authorities (ESAs), comprising the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and ESMA, has published a joint report on the completeness, adequacy and uniformity of the applicable laws and practices on the withdrawal of license for serious breaches of the rules on anti-money laundering and countering the financing of terrorism (AML/CFT).

The report advocates for the introduction in all relevant EU sectoral laws of a specific legal ground to revoke licences for serious breaches of AML/CFT rules. The report also calls for the inclusion of assessments by competent authorities of the adequacy of the arrangements and processes to ensure AML/CFT compliance as one condition for granting authorisation or registration.

The ESAs highlight the importance of the appropriate integration of AML/CFT issues into prudential regulation and supervision, including in the proposal for the Markets in Crypto-Assets Regulation (MiCA), currently under negotiation.

The report clarifies the nature of the decision to revoke licenses as a last resort measure, subject to a discretionary and proportionality assessment. It also lays down uniform criteria for the notion of serious breach of AML/CFT rules, highlighting that the identification of a serious breach is subject to a case-by-case assessment by the AML/CFT supervisor.

The report also provides a preliminary analysis of the interaction between serious breaches of AML/CFT rules and the crisis management and resolution frameworks as well as a first mapping of operational and legislative criticalities.

Investment funds: ESMA reports on common supervisory action on costs and fees

ESMA has published a final report setting out its analysis and conclusions on the 2021 common supervisory action (CSA) on the supervision of costs and fees of UCITS across the EU/EEA.

Key findings following the CSA include:

- there being room for improvement regarding the development of structured pricing processes, particularly for smaller management companies;

- questions concerning compliance with delegation rules where portfolio managers exercise significant influence over or decide the level of costs and fees;
- some divergent market practices on the notion of 'undue costs', noting that it should be primarily assessed against what should be considered the best interest of the fund and its investors, bearing in mind the applicable national requirements;
- some instances of conflicts of interest in related-party transactions, noting the importance, from an investor protection perspective, of the potential for intragroup/related-party transactions resulting in higher costs;
- in some instances, a lack of policies and procedures on efficient portfolio management (EPM) techniques and unclear disclosures;
- in light of divergent market practices and uncertainties, a need to further investigate the issue of fee-split arrangements; and
- the importance of ensuring that investors are adequately compensated in all cases where they were charged with undue costs/fees or there were calculation errors that resulted in a financial detriment for investors.

ESMA invites NCAs to consider enforcement actions in cases where a significant regulatory breach has been identified and intends to continue working on the topic.

NGFS publishes 2022 – 2024 work program

The Network for Greening the Financial System (NGFS) has published its new work program, detailing its priorities for the next two years. The NGFS will focus on:

- supervisory practices with respect to managing climate-related risks;
- design and analysis of climate scenarios;
- implications of climate change for monetary policy;
- guidance for central banks on transition to net zero;
- nature-related financial risks; and
- capacity building for its membership.

The new work program will be undertaken by four workstreams and two task forces:

- workstream on supervision;
- workstream on scenario design and analysis;
- workstream on monetary policy;
- workstream on net zero for central banks;
- task force on nature-related risks; and
- task force on capacity building and training.

Primary Market Bulletin No. 40: FCA reports on response to consultation on changes in Knowledge Base in relation to prospectus regime

The Financial Conduct Authority (FCA) has published the latest edition of its Primary Market Bulletin (PMB), which contains feedback on the responses it received to a consultation published in PMB 34. The consultation set out the FCA's proposals to amend its Knowledge Base to reflect changes in the UK prospectus regime. In particular, it proposed to:

- create a new technical note to adapt, as FCA guidance, ESMA's guidelines on disclosure requirements under the Prospectus Regulation;
- create a new technical note to cover the measures on specialist issuers contained in the ESMA update of the Committee of European Securities Regulators (CESR) recommendations, which are currently on the FCA's Handbook Level 3 Materials site; and
- incorporate certain elements of the Level 3 Questions and Answers, Prospectuses (PD Q&As), currently in the FCA Handbook, into existing and new procedural and technical notes.

PMB 40 summarises the feedback the FCA received on these proposals and the changes it has made as a result. Overall, the FCA has only made minor amendments to the proposals as consulted upon, largely to improve clarity or to better reflect its intent. The FCA notes that many of the issues raised by respondents are outside the scope of the current proposals but will be considered as part of the ongoing review of the prospectus regime.

FCA publishes Dear CEO letter to data reporting services providers

The FCA published a letter to the CEOs of data reporting service providers (DRSPs) providing services to approved reporting mechanisms (ARMs) and approved publication arrangements (APAs). The letter sets out the FCA's view of the key risks posed by the DRSP portfolio, and the steps it expects firms to take to mitigate them. It also sets out the FCA's supervisory priorities with regard to DRSPs.

Key risks to the sector identified by the FCA include:

- market concentration;
- inadequate systems and controls for the identification of incomplete or incorrect trade or transaction reporting data; and
- insufficient operational resilience.

Other risks identified include:

- a lack of focus on DRSP business when DRSPs form part of a wider group;
- the offering of unregulated services;
- differing levels of business oversight; and
- a lack of tailored policies and procedures around conflicts of interest.

To address these, the FCA expects firms to:

- review their services and fees to ensure clients are getting good value for money and are able to meet their regulatory reporting obligations;
- ensure they have appropriate monitoring systems and controls in place to ensure reporting data is complete, accurate and timely, including systems to check that the data published by the firm matches the data submitted by clients; and
- ensure they have arrangements in place to mitigate the impact of any disruption to their services and review their reliance on data vendors.

HMT consults on management of failures of systemic digital settlement asset firms

HM Treasury (HMT) has launched a consultation on proposed amendments to the Financial Market Infrastructure Special Administration Regime (FMI SAR) to include provisions on the management of failures of non-bank systemic digital settlement asset (DSA) firms.

HMT defines DSAs as stablecoins or other forms of digital assets that are used for payments and/or settlement. It notes that it is exploring the potential of the FMI SAR as a vehicle for addressing the risks posed by the failure of non-bank systemic DSA firms, before it considers the need for a bespoke legal framework. It also notes that bank DSA firms are outside the scope of the consultation, as they are covered by separate pre-established regimes.

In particular, HMT is seeking stakeholders' views on proposals to:

- appoint the FMI SAR as the primary regime for non-bank systemic DSA firms;
- establish an additional objective for the FMI SAR focused on the return or transfer of customer funds in the event of the failure of a systemic DSA firm, similar to the provisions included in the Payment and E-Money Special Administration Regime;
- introduce specific regulations to support the application of the FMI SAR to systemic DSA firms, including measures to ensure that the customer funds objective can be effectively managed by administrators;
- grant the Bank of England (BoE) powers to direct administrators as to which objective should take precedence in an administration; and
- require the BoE to consult with the Financial Conduct Authority before seeking an administration order for a systemic DSA firm that is subject to both regulators' requirements.

Responses are due by 2 August 2022.

Bank of Italy complies with EBA guidelines for institutions and resolution authorities on improving resolvability

The Bank of Italy has confirmed its decision to comply with the EBA guidelines for institutions and resolution authorities to improve resolvability under the Bank Recovery and Resolution Directive (BRRD), as amended by BRRD2. These guidelines therefore acquire the status of supervisory guidelines applicable to entities supervised by the Bank of Italy. Entities under resolution

mechanisms – in line with the guidelines – are required to ensure that their core activities shall continue to be provided during the application of the resolution process, including in the event of a reorganisation plan.

The guidelines will enter into force on 1 January 2024.

CSSF issues circular on application of EBA guidelines on monitoring of threshold on establishment of intermediate EU parent undertakings

The Luxembourg financial sector supervisory authority, the Commission de Surveillance du Secteur Financier (CSSF), has issued Circular 22/814 on the application of the EBA guidelines on the monitoring of the threshold and other procedural aspects on the establishment of an intermediate EU parent undertaking (IPU) under Article 21b of the Capital Requirements Directive 2013/36/EU (CRD 4) published on 28 July 2021 (EBA/GL/2021/08).

The circular is addressed to all credit institutions designated as Less Significant Institutions under the Single Supervisory Mechanism (SSM), to investment firms, to all Luxembourg branches of credit institutions or of investment firms incorporated in a third country, as well as financial holding companies, mixed financial holding companies and investment holding companies incorporated in Luxembourg.

The purpose of the circular is to inform them that the CSSF applies the guidelines and has integrated them into its administrative practice and regulatory approach in order to promote supervisory convergence in this field at European level. The guidelines are attached to the circular and available on the EBA's website.

An IPU is required if two or more credit institutions and/or investment firms established in the EU are part of the same third-country group (TCG) which has (considering also all third country branches authorised in the EU) a total value of assets in the EU equal to or greater than EUR 40 billion. The guidelines specify a common methodology to calculate the total value of assets in the EU of the TCG and clarify the period of reference to consider regarding that threshold.

The CSSF reminds the relevant entities that they are required to:

- assess whether the IPU threshold has been exceeded on a quarterly basis;
- monitor annually on a forward-looking basis whether the TCG has exceeded the IPU threshold against the strategic planning and the forecast of assets of that TCG for a time horizon of at least three years;
- exchange information necessary for the calculations to be made; and
- notify the CSSF, where the CSSF is the consolidating supervisor or group supervisor, if they expect that their TCG will reach the IPU threshold within the next three years and submit their quarterly assessment.

The circular applied with immediate effect.

MAR: CNMV adopts ESMA guidelines on delay in disclosure of inside information and interactions with prudential supervision

The Spanish National Securities Market Commission, the Comisión Nacional del Mercado de Valores (CNMV), has notified the ESMA of its intention to

comply with the revised guidelines on the delay in the disclosure of inside information and interactions with prudential supervision, in accordance with the Market Abuse Regulation (MAR).

Therefore, the CNMV will take these criteria into account and will endeavour, within the scope of its supervisory competences, to ensure that they are complied with by the issuers to which they apply.

Bank of Japan publishes review of JPY LIBOR transition and future initiatives

The Bank of Japan has published a document setting out its review of the JPY LIBOR transition and future initiatives.

The review paper first briefly reviews the events leading up to the cessation of LIBOR publication, and then focuses on responses to the transition away from JPY LIBOR in the Japanese financial markets, summarising the initiatives to achieve a smooth transition and explaining points to note and medium-to long-term efforts to be made.

In its review, the Bank of Japan has observed that, after the publication of JPY LIBOR ceased at the end of December 2021, practical deliberations on the transition from JPY LIBOR have been carried out mainly by the 'Cross-Industry Committee on Japanese Yen Interest Rate Benchmarks' established in August 2018 and, on this basis, a range of market participants have been working on the transition. During this period, the Financial Services Agency (FSA) and the Bank of Japan have supported market participants' efforts through surveys and monitoring of the use of JPY LIBOR by financial institutions and their progress in the transition.

The Bank of Japan notes that, due to this cross-sectoral cooperation in the Japanese financial markets, a smooth transition from JPY LIBOR has been achieved. Future challenges include the transition from USD LIBOR, for which the publication of some of the tenor settings will be ceased at the end of June 2023, and the development of infrastructure to facilitate the smooth use of JPY interest rate benchmarks to replace LIBOR.

The FSA and the Bank of Japan will continue to work together to support the efforts of market participants in cooperation with overseas authorities.

PRC Supreme People's Court issues opinions on strengthening blockchain application in judicial field

The Supreme People's Court of the People's Republic of China (PSC) has issued the 'Opinions on Strengthening Blockchain Application in the Judicial Field', which set out a framework on the application of blockchain technology in judicial practice.

The opinions set out a vision of building a blockchain system that connects and serves the judicial sector by 2025. According to the opinions, blockchain technology could be used to fulfil functions including, among other things:

- enhancing judicial credibility by ensuring security of judicial data, trustworthiness of electronic evidence, compliance of enforcement actions and the authenticity of court documents;
- improving efficiency by connecting mediation procedures, trial procedures and enforcement procedures;

- enhancing judicial collaboration by facilitating the verification of lawyers' qualifications and improving the capability of taking joint and collaborative actions by different authorities; and
- facilitating economic and social governance in the areas of, among others, intellectual property rights protection, business environment improvement, data development and utilisation, enterprise bankruptcy and restructuring and the construction of credit systems.

It is expected that additional innovations based on blockchain technology will be used in China's judicial system in the near future.

SFC and CSRC announce implementation details of ETF Connect

The Securities and Futures Commission (SFC) and the China Securities Regulatory Commission (CSRC) have jointly announced the implementation details concerning the inclusion of eligible exchange-traded funds (ETFs) in Stock Connect.

In 2016 the SFC and the CSRC reached a consensus to include ETFs as eligible securities under Stock Connect (ETF Connect). An overall proposal was agreed by the Shanghai Stock Exchange, Shenzhen Stock Exchange, Stock Exchange of Hong Kong Limited, China Securities Depository and Clearing Corporation Limited and Hong Kong Securities Clearing Company Limited in 2021.

According to the joint announcement, the principal arrangements for ETF Connect are made with reference to those under Stock Connect and follow existing fund operations, as well as the laws, regulations and operational models governing trading and clearing in the Hong Kong and Mainland China markets.

The Hong Kong Exchanges and Clearing Limited (HKEX) has also published a press release to welcome the joint announcement. The HKEX invites the public to its designated webpage and circular which set out the detailed arrangements concerning the inclusion of ETFs in Stock Connect.

A further announcement of the official launch date will be made in due course.

MAS announces commencement of Project Guardian

The Monetary Authority of Singapore (MAS) has announced the commencement of Project Guardian, which is a collaborative initiative with the financial industry that aims to explore the economic potential and value-adding use cases of asset tokenisation.

Project Guardian is set to test the feasibility of applications in asset tokenisation and decentralised finance (DeFi) while managing risks to financial stability and integrity. The MAS aims to develop and pilot use cases in four main areas:

- open, interoperable networks;
- trust anchors;
- asset tokenisation; and
- institutional grade DeFi protocols.

The first industry pilot will explore potential DeFi applications in wholesale funding markets. The pilot aims to carry out secured borrowing and lending on a public blockchain-based network through execution of smart contracts. The MAS welcomes further industry initiatives that addresses Project Guardian's four areas of interest.

MAS revises guidelines for operation of wholesale banks

MAS has revised its existing guidelines for the operation of wholesale banks relating to the requirements a bank needs to adhere to when operating under a wholesale bank licence in Singapore. The guidelines broadly cover specifications pertaining to allowable banking business, conditions for issuing bonds and negotiable certificates of deposit, and place of business.

Amongst other things, the guidelines have been revised to:

- remove (through a deletion of paragraph 2(a)) the requirement to obtain prior MAS approval when a wholesale bank operates savings accounts denominated in Singapore dollars for persons that are not approved financial institutions;
- allow (through amendments to paragraph 2(d)) a wholesale bank to operate savings accounts and/or current accounts; however, any such account denominated in Singapore dollars should not be interest-bearing without prior MAS approval, where the customer is a natural person and a resident in Singapore, and not acting in the capacity of a sole proprietor or a partner of a partnership (other than a limited liability partnership); and
- update the definitions of 'accredited investor', 'approved financial institution', and 'residents in Singapore'.

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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