

REGULATORY & COMPLIANCE

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REGWATCH SQUARE MANAGEMENT REGULATORY NEWSLETTER

PRESENTATION

Square Management offers a quarterly regulatory watch newsletter, providing you with an overview of the latest updates related to compliance and regulatory requirements. RegWatch covers the following topics :







INSURANCE

NEW PROTECTIONS FOR FRAGILE CLIENTELE

The new directive¹ on insurance distribution and its implementing texts have introduced new requirements for insurance product designers and distributors, with the aim of safeguarding customers' interests.

A series of inspections carried out by the French supervisory authority, the ACPR², showed that, for life insurance products in particular, practices were heterogeneous and not always respectful of customer interests. The inspection reports led to a recommendation of best practices in terms of governance, supervision, remuneration, and conflicts of interest.

The recommendation applies mainly to insurance companies, health insurance funds, provident institutions or unions governed by the Social Security Code, supplementary pension schemes, and insurance intermediaries, and encourages them to: - Better analyse and justify significant product adaptations;

- Better define their target market;

- Plan a strategy and distribution channels in line with this target market;

- Carry out tests to ensure that product costs are proportionate to expected benefits;

- Regularly monitor and review products to better map their characteristics, risk coverage, and guarantees;

- Not introduce a remuneration policy that could influence the (non)proposal of certain products;

- Better interpret and manage conflict of interest situations.

This recommendation takes effect on January 1st 2024.

For further information: <u>ACPR</u>

^{1 :} Directive (UE) 2016/97.

^{2 :} French Prudential Supervision and Resolution Authority



PUBLICATION OF THE 4TH MUTUAL EVALUATION REPORT OF LUXEMBOURG BY THE FATF

On 27 September 2023, the Financial Action Task Force (FATF) published Luxembourg's Mutual Evaluation Report as part of the 4th round of mutual evaluations. The previous evaluation report on Luxembourg dates back to 2010. The new report, covering the period from 1 January 2017 until 18 November 2022, reflects the considerable progress made since then by Luxembourg, which continues on the path of transparency and compliance.

Today, the signal is therefore clear to criminals who would like to take advantage of the system and financial players in Luxembourg. The report highlights the objective of removing all means to illegal money laundering through financial institutions, financial instruments, and investments.

Luxembourg obtains a good overall result and is among the best evaluated countries. The FATF recognises the quality of Luxembourg's system in the fight against money laundering and the financing of terrorism (AML/CFT), considers that Luxembourg has achieved a high level of technical compliance and that its AML/CFT regime provides good results. In its report, the FATF makes a certain number of recommendations in order to further improve the effectiveness of the national system:

- Significantly strengthen detection, investigations, and prosecutions;

- Strengthen the capacity of the competent national authorities so that they can better fulfill their mandates;

- Further develop and disseminate its understanding of Terrorist Financing (TF) risks and vulnerabilities, including the misuse of legal entities for TF purposes, arising from its exposure as an international financial center.

For further information: FATE



BANKING AND PRUDENTIAL

A QUARTER MARKED BY REVISION FOR THE CAPITAL AND PAYMENTS MARKET

Over the last quarter, the European trilogue³ participated in the revision of two major directives: the Payment Services Directive (also called PSD2) and the Second Markets in Financial Instruments Directive (MiFID II).

On 28 June 2023, the European Commission published and proposed its plan to reform the Payments Services Directive. The Commission presents two sets of measures aimed primarily at preventing fraud and better informing consumers. This renovation of the PSD2 aims in particular to:

- Further standardise the conditions of competition between banks and non-banks and improve the functioning of open banking;

- Strengthen the harmonisation and enforcement of payment rules.

On 29 June 2023, the European Council and Parlia-

ment reached a revision agreement after the work initiated at the beginning of 2021 on the reform of the MiFID II directive. Thus, two main areas of improvement are predominant:

- The establishment of a consolidated database, allowing investors to execute their transaction at the best European price. This development supports the desire for a market accessible to all;

- A Stricter supervision of Payment for Order Flow (PFOF), in particular to contribute to greater vigilance in matters of conflicts of interest.

Furthermore, the Commission is also putting forward a legislative proposal relating to a framework for access to financial data. This proposal responds in particular to the objectives of the European strategy relating to digital finance.

For further information: <u>Agefi</u>; <u>European Council</u>

^{3 :} CCR : Counterparty Credit Risk.

ECB CONSULTS ON COUNTERPARTY CREDIT RISK GOVERNANCE AND MANAGEMENT

The European Central Bank (ECB) has identified exposures to Counterparty Credit Risk (CCR) as a supervisory priority for 2022-2024.

In the last quarter of 2022, the ECB conducted a targeted horizontal review of governance and risk management of 23 institutions involved in derivatives and securities financing transactions with non-banking counterparties. The review also assessed how some banks met PBS (Prime Brokerage Services) expectations.

The document provides a collection of good practices in CCR governance and management, aiming to encourage institutions to improve their risk management capabilities. Good practices should be adapted to the specific characteristics of institutions and the size and complexity of their CCR portfolio, which may change over time. Developments in business practices may affect CCR governance and management practices.

For further information: <u>European Central Bank 1</u>; <u>European Central Bank 2</u>

IMPLEMENTING EU REGULATION AIMED AT BETTER INFORMATION ON THE CREDIT EXPOSURE OF BUYERS' BANK PORTFOLIOS

Commission Implementing Regulation⁴ of September 26th 2023 sets out implementing technical standards for the application of the directive⁵ of the European Parliament and of the Council as regards the models to be used by credit institutions for the provision of information to buyers on credit exposures in their banking book. It applies to sales and assignments of credit contracts classified as non-performing exposures that credit institutions hold in their banking book.

The Commission emphasises potential buyers' right to information in terms of contract, counterparty, collateral, history, etc., and formulates the need to do so using formalised transaction data models in order to reduce information asymmetry between potential buyers and sellers of credit contracts. The obligation to use models is limited to the assignment of non-performing credit contracts, and therefore does not apply to complex transactions involving credit contracts, or to sales or assignments of securities, derivatives, or other financial instruments.

For each type of information, a different model must be used:

- 1. The counterparty;
- 2. The credit agreement;
- 3. Security, guarantee, and performance;
- 4. Mortgage collateral;
- 5. Repayment history.

The information must be provided prior to the conclusion of a contract of sale or assignment, in electronic format and in compliance with the rules governing data confidentiality and banking secrecy.

These regulations came into force on 19 October 2023.

For further information: European Commission

^{4 : (}EU) 2023/2083.

^{5 : (}EU) 2021/2167 (art. 16, par. 1).



CRYPTOCURRENCIES BLOCKCHAIN

THE UNCERTAIN FUTURE OF CRYPTO REGULATIONS IN THE USA

US regulators are grappling with the regulation of crypto-assets, with the Financial Accounting Standards Board (FASB) proposing guidance for certain assets. The current ambiguity in US crypto regulation is due to the lack of a single regulator overseeing crypto-currency or its trading brokers. The House Financial Services Committee and the House Agriculture Committee have split oversight of the financial industry and regulators. The Federal Reserve (Fed), the FDIC⁶, and the OCC⁷ have issued joint statements urging cau-

tion and coordination on crypto-assets.

FED, FDIC, AND OCC JOINT STATE-MENTS

The Federal Reserve, the FDIC, and the OCC have issued several joint statements urging caution on this asset class, focusing on the safety, soundness, and compliance within the banking system. The Fed continues to regulate and enforce those crypto-assets under its authorization purview, but regularly signals the need for more coordinated oversight at a higher level.

FDIC AND OCC

The PWG (President's Working Group), the FDIC, and the OCC report on stablecoins suggests they could facilitate faster, efficient, and inclusive payment options. However, concerns about destabilizing runs, disruptions, and economic power concentration arise. The report recommends Congress to enact legislation to ensure consistent federal regulatory framework for payment stablecoins and arrangements.

The SEC[®] and CFTC⁹ are divided on how to regulate digital assets, with the SEC focusing on securities, and the CFTC on derivatives. Enforcement actions are expected to accelerate, but piecemeal regulation will continue until Congress passes legislation.

For further information: <u>Le Monde</u> ; <u>Global Com-</u> <u>pliance News</u> ; <u>Baker McKenzie</u> ; <u>Thomson Reu-</u> <u>ters</u>

6 : FDIC: Federal Deposit Insurance Corporation.

7 : OCC: Office of the Comptroller of the Currency.

8 : SEC: Securities and Exchange Commission.

9 : CFTC: Commodity Futures Trading Commission.



DATAPRIVACY CYBERSECURITY

DORA

The European Supervisory Authorities (the EBA¹⁰, the EIOPA¹¹, and the ESMA¹²) published two reports at the end of September with regard to DORA (Digital Operational Resilience Act) regulation that provide further information on the management of ICT¹³ Third-Party Service Providers (TPPs).

The first report, which is a response to a Call for Advice (CfA) from the European Commission, focuses on the criticality criteria to define these 'critical' TPPs – called the 'CTPPs' – and how to manage the oversight fees perceived through the relation between the financial entities and these CTTPs.

- On the criticality criteria, 11 quantitative and qualitative indicators are proposed to determine, in a two-step process, which service providers fall in the CTTPs category. The 6 quantitative indicators are given with minimum relevance thresholds (for example, if TPPs provide 10% or more of the financial entities support ICT functions). The 5 qualitative indicators on the relations between these CTTPs (e.g. interdependencies, impact of customers in case of discontinuity of services, market shares). The underlying procedures and methodologies are not in the scope of this report and will be published at a later stage.

- On the oversight fees, the goal is to define the types of expenditures in scope, the appropriate method (i.e. the way they are perceived), and the basis and available information to cover their calculation method.

The second report, prepared in collaboration with the national Competent Authorities (CAs) in 2022, was used to help prepare the first report summarised here above. It was a data collection exercise which aims to map the ICT TPPs landscape and the use of their services by the financial entities.

The main findings indicate that the TPPs cover as expected a wide range of services and they frequently support critical and important functions where (lack of) service continuity would have a critical impact on the financial entities' business continuity for which they operate.

For the valuable lessons, this exercise highlighted the importance of a well-prepared data collection and analysis, the use of actual data (through unique identifiers), and the need to further develop a dedicated taxonomy.

For further information: <u>EBA 1</u>; <u>EBA 2</u>

10 : EBA : European Banking Authority

11 : EIOPA : European Insurance and Occupational Pensions Authority

12 : ESMA : European Securities and Markets Authority

13 : ICT: Information and Communication Technology.



SUSTAINABLE FINANCE

THE EU ENDORSES NEW STANDARDS AIMED AT IMPROVING INFORMATION ON CORPORATE SUSTAINABILITY

The European Commission adopted the European Sustainability Reporting Standards (ESRS) on 31 July 2023. Indeed, European Union law requires that all listed companies (except listed microenterprises¹⁴) must provide information relating to what they consider to be the risks and opportunities arising from social and environmental issues. This public information helps investors evaluate companies' sustainability performance.

However, the information currently provided is very often fragmented and, therefore, it is difficult to compare one company with another. This directive will therefore improve both the quality and reliability of the data provided by companies. In this way, investors will also be able to comply with their reporting obligations required by the SFDR directive.

In addition, on 2 October 2023, the European Parliament presented the new green bond standards. The aim is to improve the environmental credibility of issuers, but also of the European market. These high-quality bonds will finance projects aimed at accelerating the ecological transition in order to achieve the objectives of the Paris Agreement and the European Green Deal.

For further information: European Council

SUSTAINABLE FINANCE DISCLOSURE REGULATION (SFDR)

The European Commission has launched a consultation from 14 September to 15 December 2023 aimed at revising the regulation on sustainability information, applicable partially since March 2021 and completely since June 2023 for asset managers and life-insurance companies.

This consultation aims to allow financial market participants and financial advisors subject to the regulation to give their opinion on the following points:

- Difficulties encountered in the implementation of the text and the effectiveness of the text in

terms of transparency, investor protection, or opinions on costs (among others);

- Consistency and interactions of SFDR with other texts in the sustainable finance regulatory corpus (Benchmark, Taxonomy, CSRD, MiFID, ESG, PRIIPs);

- Information to be published regarding financial products;

 Product classification system according to SFDR ('Article 8' and 'Article 9' type products).
For further information: <u>European Commission</u>

14 : Not completing at least two of the following criterion: balance sheet with over 350k euro; net revenue over 700k euro; more than 10 salaried persons (over the fiscal year).

LIST OF CONTRIBUTORS







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