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EU Council adopts ELTIF2

The EU Council has adopted a regulation amending the European long-term investment funds Regulation (ELTIF2).

ELTIF2 is intended to make ELTIFs more attractive and overcome the limitations on the demand-side and supply-side posed by ELTIF1. It is also seeks to improve regulatory oversight and investor protection safeguards in order to accelerate the uptake of ELTIFs. The Council and the EU Parliament believe that, as they are designed to channel long-term investments, ELTIFs are well placed to help finance the green and digital transitions.

The EU Parliament formally adopted the regulation on 15 February 2023.

The regulation will enter into force 20 days following its publication in the Official Journal and apply from nine months after its entry into force.

Sustainable finance: EU Commission requests financial system climate stress test

The EU Commission has written to the European Supervisory Authorities (ESAs) requesting the development of a one-off scenario analysis exercise to test the financial system's resilience to stress.

In the Commission's 'Strategy for Financing the Transition to a Sustainable Economy' of July 2021, it laid out its plans for ensuring the resilience of the financial sector to climate risks and an orderly transition towards the EU's climate targets of reaching carbon neutrality by 2050 and reducing greenhouse gas emissions by at least 55% by 2030 compared to 1990 levels. The EU has developed a sustainable finance framework that aims to channel private financial flows into sustainable economic activities to aid with the financing of the plans.

The Commission has invited the ESAs to conduct a one-off exercise that should assess the resilience of the financial sector and highlight the extent to which early climate-risk related shocks could already generate significant stress for the financial system as a whole in the period up to 2030, taking into account contagion and second-round effects. The Commission has suggested two different scenarios which should be developed by the European Systemic Risk Board's Task Force on Stress Testing to ensure consistency across sectors and synergies with the scenarios used in other stress tests.

The Commission would ideally like to receive results by the end of 2024 but no later than Q1 2025.

CRR: RTS on calculation of risk-weighted exposure amounts published in OJ

Commission Delegated Regulation (EU) 2023/511 containing regulatory technical standards (RTS) for the calculation of risk-weighted exposure amounts of collective investment undertakings under the mandate-based approach has been published in the Official Journal.

The RTS specify:

- how institutions are to calculate the risk-weighted exposure amount referred to in Article 132a(2) of the Capital Requirements Regulation (CRR), where one or more of the inputs required for that calculation is not available;
- the steps to be taken to calculate the exposure value of collective investment undertakings' (CIUs') derivative exposures where the underlying is unknown; and
- what to do in cases where the calculation of the exposure value to the counterparty credit risk of a netting set of CIUs' derivative exposures is needed.

The Delegated Regulation will enter into force on 29 March 2023.

ECON Committee publishes report on MiFID3

The EU Parliament's Committee on Economic and Monetary Affairs (ECON) has published the text of the report it adopted on 1 March 2023 on the EU Commission's proposals for a Directive amending the Markets in Financial Instruments Directive (MiFID3).

The text of the report on the proposed Regulation amending MiFIR (MiFIR2) also adopted on 1 March 2023 is yet to be published.

The EU Council agreed its negotiating position on MiFID3 and MiFIR2 in December 2022 and the co-legislators will enter trilogue negotiations in due course.

ECON Committee publishes draft report on instant payments in euro

The ECON Committee has published its draft report on the EU Commission's legislative proposal to make instant payments in euro available to all citizens and businesses holding a bank account in the EU and in EEA countries.

The EU Commission's proposal fulfils a commitment in the Commission's 2020 Retail Payments Strategy. Among other things, the draft report welcomes the following aspects of the proposal:

- the EU-wide approach to cross-border instant payments in euro, including paper and bulk, on a 24/7/365 basis;
- the amendments to Single Euro Payments Area (SEPA) to bring the current legislation up-to-date;
- the non-discriminatory approach to instant payments as compared to other types of credit transfers;
- the provision of the international bank account number (IBAN) name check as a security feature and the free of charge aspect of it; and
- moving the EU sanctions list screening from a transaction-based to client-based approach.

The draft report also identifies a number of areas for improvement, including:

- clarifying the sanctions requirements and encouraging a move from transaction-based checks to client-based ones; and
- a call to re-visit the Settlement Finality Directive in an effort to broaden the scope of the payment service providers included in the current legislation, thereby reflecting the current payments landscape more accurately.

EBA reports on diversity practices and gender pay gap

The European Banking Authority (EBA) has published its report on diversity practices and the gender pay gap at the level of the management body.

According to the EBA, the figures in the report are based on a representative sample of 662 credit institutions and 129 investment firms selected by national competent authorities (NCAs) of all EU Member States, Lichtenstein and Iceland, on the basis of common criteria set out by the EBA.

Key findings from the report include that:

- 27.75% of non-executive directorships are held by women;

- 18.05% of executive directors are female;
- 27.05% of institutions still lack the mandatory diversity policy; and
- women earn on average 9.48% less than male executive directors and 5.90% less than male non-executive directors.

The report also concludes that gender balance in Northern and Eastern Europe is generally better than in other parts of the EU, and that a clear positive correlation between gender balance and return on equity (RoE) exists.

EBA publishes annual assessment of banks' internal approaches for calculation of capital requirements

The EBA has published two reports on the consistency of risk weighted assets (RWAs) across all EU institutions authorised to use internal approaches for the calculation of capital requirements. The reports cover credit risk and market risk.

The market risk report presents the results of the 2022 supervisory benchmarking and summarises the conclusions drawn from a hypothetical portfolio exercise (HPE) conducted in 2021/22. The results confirm that the majority of participating banks confirm a relatively low dispersion in the initial market valuation (IMVs) of most of the instruments, and a decrease in the dispersion in the value at risk (VaR) submissions compared to the previous exercise.

The credit risk report includes in-depth analysis of the observed and potential impact of the COVID-19 pandemic on the internal rating-based (IRB) parameters used to calculate own funds requirements. It concludes that the variability of RWAs remained rather stable, despite the pandemic and the different banks' pace in complying with the policies set out in the EBA IRB roadmap.

ESMA and ACER update MoU to strengthen cooperation

The European Securities and Markets Authority (ESMA) and the EU Agency for the Cooperation of Energy Regulators (ACER) have signed an updated Memorandum of Understanding (MoU) strengthening collaboration between the two institutions in relation to wholesale energy markets, which encompass energy derivatives and spot markets.

According to the institutions, continued cooperation will primarily be achieved through on-going consultations, exchange of information and cross-participation in joint meetings of working groups and task forces.

The updates to the MoU include, among other things:

- the new cooperation areas under the market correction mechanism (MCM) and benchmarks related to the energy sector;
- the role of the recently established ACER–ESMA Task Force created to strengthen oversight of energy and energy derivative markets;
- the coordinated approach to the market abuse framework under the Regulation on wholesale energy market integrity and transparency and the Market Abuse Regulation (MAR);
- the technical cooperation on data and knowledge with respect to the functioning of energy and energy derivative markets; and

- the LLNG price assessments and benchmarks administered by ACER and other energy-related benchmarks relevant for ESMA's or ACER's mandates.

HM Treasury publishes Investment Research Review terms of reference

HM Treasury (HMT) has published the terms of reference for the forthcoming Investment Research Review.

The Review was first announced as part of the Government's December 2022 Edinburgh Reforms and has the following two key objectives:

- to assess the link between levels of research and the attractiveness of the UK as a destination to list; and
- evaluate options to improve the UK market for investment research and to provide legislative and non-legislative recommendations.

Among other things, the Review is expected to consider the impact of UK MiFID2 unbundling rules on the levels and quality of investment research and to evaluate the likely impact of any proposed changes on investment and fees.

The Review, which is to be chaired by Rachel Kent and conducted on an independent basis, will formally commence on 13 March 2023 and is expected to conclude in June 2023.

BaFin publishes article on regulatory assessment of NFTs

The German Federal Financial Supervisory Authority (BaFin) has published an article explaining its regulatory assessment of non-fungible tokens (NFTs).

NFTs can be used in a variety of ways, including in the financial sector. In its supervisory review of NFTs, BaFin generally proceeds in the same way as with respect to fungible tokens, so that market participants can refer to BaFin's respective guidance notes.

In the article, BaFin discusses the criteria according to which NFTs may be classified as securities under the EU Prospectus Regulation, capital investments under the German Capital Investment Act (VermAnlG) or financial instruments (especially cryptoassets) under the German Banking Act (KWG) or the German Investment Institutions Act (WpIG).

Such classifications will always need to be made according to the individual circumstances, taking into account in particular the rights associated by the issuer with the NFT and how the NFT can be used after the issuance.

The article further discusses possible license requirements under the KWG for activities involving NFTs that qualify as financial instruments, especially with respect to secondary trading. Such activities would be subject to licence requirements in the same way as activities relating to traditional financial instruments. License requirements could also arise under the German Capital Investment Code (KAGB) provided there is a pooling of funds by various investors for the purposes of the NFT acquisition. By contrast, no license requirements should usually apply under the German Payment Services Supervision Act (ZAG).

Another focus of the article are the money laundering risks associated with NFTs.

The conclusion of the article is that NFTs currently need to be classified in a very differentiated manner for supervisory purposes. From BaFin's perspective, it will be crucial in the future to weigh up the opportunities NFTs offer to the financial system against the risks they pose to its stability and integrity.

CONSOB consults on new regulation governing crowdfunding service providers

The Commissione Nazionale per le Società e la Borsa (Consob) has launched a public consultation on a new draft regulation intended fully to implement Regulation (EU) 2020/1503 on European crowdfunding service providers for business.

The provisions included in the draft regulation are intended to define certain detailed elements of the European regulatory framework on the provision of crowdfunding services in view of the imminent completion of the process of adapting national legislation to Regulation (EU) 2020/1503.

In particular, the new regulation will regulate the following aspects:

- the procedure for granting and withdrawing clearances;
- the definition of disclosure requirements for crowdfunding service providers;
- the definition of domestic legislation applicable to marketing communications; and
- the definition of further obligations under the applicable legislation.

Comments are due by 17 March 2023.

HKMA issues circular on balanced and effective AML/CFT measures in private banking

The Hong Kong Monetary Authority (HKMA) has issued a circular on balanced and effective anti-money laundering and counter-financing of terrorism (AML/CFT) measures in private banking.

The circular sets out the HKMA's guidance and expectations with regard to AML/CFT requirements during account opening and ongoing monitoring of private banking customers. The HKMA notes that the three guiding principles, i.e. risk differentiation, proportionality, and not a 'zero failure' regime of the risk-based approach (RBA), which is central to the effective implementation of the international standards issued by the Financial Action Task Force, apply equally to private banking business.

The industry and customer feedback have indicated that private banks face challenges in customer onboarding and account maintenance, especially for three key areas, namely (i) establishment of source of wealth and source of funds; (ii) ongoing monitoring; and (iii) AML Regtech adoption. The HKMA has prepared a set of 'Do's and Don'ts' and good practices with the aim of helping private banks' AML compliance and customer-facing units appropriately to apply AML/CFT requirements to deliver customer outcomes.

The HKMA is also introducing supervisory technology to strengthen its risk-based and data-driven AML supervision. This includes an upcoming revamp of the way it obtains and analyses data collected from banks, to optimise supervisory and compliance resources as well as focusing on collaborative efforts and an ecosystem response to evolving money laundering and financial crime risks and supporting a safe and efficient platform for the development of private wealth management businesses.

Japanese Government consults on draft amendment to regulatory notices adding core business sectors of Foreign Exchange and Foreign Trade Act

The Japanese Government has launched a public consultation on a draft amendment to the regulatory notices adding the core business sectors of the Foreign Exchange and Foreign Trade Act of Japan (FEFTA).

The public consultation follows the recent designation of ‘specially designated critical commodities’, which are eligible for receiving support for securing stable supply chains under the Economic Security Promotion Act of Japan. The draft amendment proposes the following sectors to be added to the ‘core business sectors’ (which are business sectors where foreign investors are required to file a pre-closing foreign direct investment (FDI) filing for inward direct investment and the filing requirements are exempted in very limited cases) in order to secure stable supply chains and address the risk of technology leakage and diversion of commercial technologies into military use, among others:

- importing of fertilisers (potassium chloride, etc.);
- machine tools/industrial robots manufacturing, etc.;
- storage batteries manufacturing/material manufacturing;
- metals and mineral products refining;
- metal 3D printers manufacturing/metal powder manufacturing;
- permanent magnets manufacturing/material manufacturing;
- semiconductors manufacturing of manufacturing equipment, etc.;
- natural gas wholesaling; and
- marine equipment engine manufacturing, etc.

In addition, the proposed amendments will:

- clarify that drones are covered by Aircraft Manufacturing, which is a core business sector; and
- add manufacturing of antibacterial products and petroleum refining and others to the scope of specified acquisition.

The proposed amendments aim to ensure that ‘specially designated critical commodities’ under the Economic Security Promotion Act are fully covered as core business sectors.

Comments on the consultation are due by 8 April 2023.

RECENT CLIFFORD CHANCE BRIEFINGS

ELTIF2 – a new dawn?

On 15 February 2023, the European Parliament adopted the amending regulation to the ELTIF Regulation (ELTIF2) on which the EU Council and the

European Parliament had reached provisional agreement on 7 December 2022. These EU bodies believe that ELTIF2 will finally unlock untapped potential to mobilise capital for the financing of long-term projects (encompassing private equity, private debt, loans, infrastructure and real assets) by making such funds more attractive for asset managers and easier for retail investors, while ensuring strong investor protection.

This briefing paper discusses ELTIF2.

https://www.cliffordchance.com/briefings/2023/03/eltif2--a-new-dawn-.html

What are the governance and conduct rule implications of the new FCA Consumer Duty?

The FCA's new Consumer Duty regime will come into effect for new and existing products and services on 31 July 2023. As part and parcel of the planning for, and implementation of, the new Duty firms need to consider the implications of the regime's new governance requirements and the addition of the new 'Conduct Rule 6' to existing Senior Managers & Certification Regime (SM&CR) requirements – and how they equip their workforce.

This briefing paper discusses the Duty.

https://www.cliffordchance.com/briefings/2023/03/what-are-the-governance-and-conduct-rule-implications-of-the-fca.html