ALLEN & OVERY

Key Regulatory Topics: Weekly Update

15 November 2019 – 21 November 2019

BREXIT

EC outlines plans for sustainable finance and proposes extension to the temporary equivalence regime for UK CCPs post-Brexit
On 15 November, the EC published a speech by Mr Dombrovskis, European Commissioner for Financial Stability, Financial Services and Capital Markets Union (CMU) on the EC's priorities for sustainability and green finance. Alongside outlining plans to finance the transition to a climate-neutral economy, the speech touches on plans for the treatment of UK CCPs post-Brexit. Central clearing was identified as a clear systemic risk in the event of a no-deal Brexit. This was addressed via a temporary equivalence decision last year which allows ESMA to recognise temporarily UK CCPs to allow these CCPs to continue to provide clearing services in the EU for a limited period after Brexit. However, this decision expires on 30 March 2020. Dombrovskis proposes to extend this decision, citing the belief that the risk to financial stability is still present due to the lack of preparation within the industry.
Read more

CONSUMER/RETAIL

Please see the Payment Services and Payments Systems section for an update on the BCBS report on open banking and application programming interfaces frameworks.

FINANCIAL CRIME

Please read our Investigations Insight publications on Anti-Money Laundering: HMRC raises its game and The UK FCA shines a light on personal account dealing.

FCA publishes questionnaire on cyber resilience
On 21 November, the FCA released a self-assessment questionnaire, created with the PRA, aiming to understand firm's cyber resilience capability. The questionnaire includes questions relating to firms' current cyber security strategy, the knowledge of cyber security at a senior level and an assessment of tools put in place to protect sensitive data.
Read more

FATF announces strategic review to improve implementation of FATF standards
On 19 November, FATF published a speech on plans to carry out a strategic review. David Lewis, FATF Executive Secretary outlined that FATF is currently conducting a round of mutual evaluations, whereby they assess the effectiveness of AML and counter terrorist financing (CFT) measures. Mr Lewis highlights that many countries are failing with regards to effectiveness and technical compliance. Given these findings FATF has made a strategic review the first priority of its term. FATF notes that the challenge of this review is not creating effective standards, but rather ensuring these standards are implemented correctly and effectively within countries. Whilst FATF evaluations can create meaningful results, often countries are motivated by the desire to avoid a bad reputation rather than the desire to reduce crime and terrorism. Consequently the strategic review will consider the following: (i) whether a 5th round of evaluations should

be introduced; (ii) how countries should be selected; (iii) how to encourage effective implementation of standards; (iv) how to enhance the methodology used to ensure effective implementation; (v) whether to treat all countries identically; and (vi) how to improve the quality and consistency of FATF's evaluations.
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FINTECH

UKJT publishes legal statement on Cryptoassets and Smart Contracts
On 19 November, the UK Jurisdiction Taskforce (UKJT) published a legal statement on its findings on cryptoassets and smart contracts. The findings of the legal statement include the following: (i) cryptoassets are capable of having the legal characteristics of property under the principles of English private law; and (ii) a smart contract can possibly satisfy the basic requirements of a legal contract under English private law and therefore be enforceable by the courts. The next step following this legal statement is for the Law Commission to consider whether any legislation is needed to address the issues in this area.
Read more

FUND REGULATION

Investment Association publishes report outlining its Responsible Investment Framework
On 18 November, the Investment Association (IA) published a final report on its Responsible Investment Framework. The Framework aims to bring clarity and consistency to the way investment management firms describe products to clients. The Framework categorises, and provides standard definitions for the different components of responsible investment. The aim of the report is to: (i) address the lack of common language when describing different investment approaches; (ii) outline the consultation conducted by IA at the beginning of 2019; (iii) provide detail on the intended uses of the Framework and the industry response to the consultation; and (iv) raise any further questions on the disclosure of sustainability indicators.
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INSURANCE

Finalised FCA guidance on general insurance distribution chain
On 19 November, the FCA published its finalised guidance on the general insurance (GI) distribution chain (FG19/5). The guidance provides further clarification on the expectations of firms in the GI and pure protection sector. In particular, firms should consider the value that the product and distribution arrangements present to the customer. The FCA also expects manufacturers to consider product value to their end customer regardless of the type of distribution strategy they use. Whilst there is no specific guideline related to direct sales by manufacturers, this does not prevent the FCA from considering enforcement action where poor practice leading to customer detriment is detected.
Read more

EIOPA establishes a consultative expert group on digital ethics in insurance
On 15 November, EIOPA announced that it had established a Consultative Expert Group on digital ethics in insurance, which aims to assist in the development of digital responsibility principles within the sector. The formation of the group follows EIOPA's thematic review on the use of Big Data Analytics (BDA) in motor and health insurance. The thematic review notes potential risks that arise from BDA, hence the need for the development of digital responsibility principles which will aim to address the use of new business models, technologies and data sources in insurance from the perspective of fairness whilst taking into account ethical considerations. Furthermore the Consultative Expert Group may also assist EIOPA in other policy initiatives within the area of InsurTech, such as promoting sound governance around the use of Artificial Intelligence and Machine Learning.
Read more

MARKETS AND MARKETS INFRASTRUCTURE

FCA's speech on next steps in LIBOR transition
On 21 November, the FCA announced the next steps in the transition from LIBOR. In sterling interest rate swap (IRS) markets, the FCA will be encouraging market makers to make SONIA the market convention from Q1 2020. Within the loan market the FCA recognises that this is a bigger challenge, nevertheless the sterling RFR Working Group has set a target of Q3 2020 to stop new lending using LIBOR.
Read more

European Central Securities Depositories Association provides update to CSDR settlement fail penalties framework

On 20 November, the European Central Securities Depositories Association (ECSDA) published an updated version of its settlement fail penalties framework. The purpose of the framework is to facilitate a unified set of rules for the creation and operation of settlement discipline cash penalties mechanisms. It applies to all central securities depositaries (CSDs) subject to the Regulation on improving securities settlement and regulating CSDs (Regulation 909/2014) (CSDR). The latest changes relate to matters including settlement fail penalties, the daily reference price required for penalty calculations, and the collection and redistribution of penalties.

Read more

FCA publishes statement and Q&As on conduct risk during LIBOR transition

On 19 November, the FCA announced its expectation that firms take appropriate steps to transition to alternative rates by 2021. Firms are expected to have a strategy in place, taking necessary action during the LIBOR transition, as well as ensuring rules and guidance regarding customer treatment are followed. In addition to this, the FCA published answers to key questions on conduct risk arising from the LIBOR transition. Firms are encouraged to read this, although the FCA notes that this is not an exhaustive list of risks that may arise.

Read more

FSB encourages ISDA to add pre-cessation trigger to reduce systemic risk and market fragmentation

On 19 November, the FSB published a letter to the International Swaps and Derivatives Association (ISDA). The Official Sector Steering Group (OSSG) co-chairs highlight the need to reduce systemic risk and market fragmentation by allowing the swaps market to fall back to alternative rates in a coordinated fashion. Therefore in order to facilitate this, it was recommended that ISDA includes a pre-cessation trigger as standard language in the definitions for new derivatives, and in a single protocol, without embedded optionality, for outstanding derivatives contracts referencing key Interbank Offered Rates.

Read more

EC announces creation of high-level forum on the Capital Markets Union

On 18 November, the EC announced the creation of a high-level forum on the future of the Capital Markets Union (CMU). This forum will provide support to the EC's goal of developing a CMU encompassing all Member States, so they can mobilise capital for businesses, offer better investment opportunities and boost economic growth in Europe. The EC has selected 28 candidates on the basis of personal expertise. The forum will be chaired by Thomas Wieser and will be split into the following sub-groups: (i) the creation of an ecosystem enabling greater capital raising, with special focus on innovative SMEs; (ii) the development of the European capital market architecture, with special focus on how new financial technologies can support this process; and (iii) investment choice and accessibility to capital markets services to promote greater retail investors' participation.

Read more

ESMA publishes updated Q&As on the Securitisation Regulation

On 15 November, ESMA published an updated version of its Q&A on the Securitisation Regulation. The updates provide guidance on how specific fields should be completed in the templates contained in ESMA's draft technical standards on disclosure requirements as well as guidance on notifications to ESMA of STS securitisations.

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PAYMENT SERVICES AND PAYMENT SYSTEMS

BCBS publishes report assessing open banking frameworks and application programming interfaces

On 18 November, the Basel Committee on Banking Supervision (BCBS) published a report on open banking and application programming interfaces (APIs). The report focused on the evolving nature of open banking in relation to customer-permissioned data sharing where the customer grants permission to a third party firm to access their data. The report found that while the use of digital devices has contributed to a transition from traditional banking towards open banking, many BCBS members have not had significant open banking developments in their jurisdictions. The BCBS also identified the following challenges for banks and supervisors: (i) banks will need to pay greater attention to the risks of sharing customer-

permissioned data; (ii) banks may need to adopt new strategies to remain competitive in a changing digital environment; (iii) cyber security will need focus due to increased data sharing; (iv) it may be challenging to regulate third parties under an open banking model; and (v) assigning liability in the event of financial loss is more complex with open banking due to the fact that more parties are involved.
Read more

EPC SEPA payment scheme rulebooks enter into force
On 18 November, the European Payments Council (EPC) announced that the following four Single Euro Payments Area (SEPA) rulebooks came into force on 17 November: (i) Credit Transfer (SCT); (ii) SEPA Instant Credit Transfer (SCT Inst); (iii) SEPA Direct Debit (SDD) Core; and (iv) SDD Business-to-Business (B2B). The rulebooks apply until 21 November 2021. The EPC has also invited stakeholders to submit a change request relating to the SCT and SDD rulebooks. The deadline for comments is 31 December. These requests will be considered in 2020 and any changes made will come into force in November 2021.
Read more

Pay.UK responds to change request from UK Finance regarding funding of APP fraud reimbursements
On 15 November, Pay.UK published its response to a change request from UK Finance which proposed the introduction of a requirement in the Faster Payments Service (FPS) Rules for Participants to pay a Contingent Reimbursement (CRM) Fee, which in turn would be used to fund the reimburse 'no-blame' customers that were victims of fraud under the CRM Code for Authorised Push Payment (APP) scams. The seven FPS Direct Participants who brought the request argued that the rule change would ensure consistent outcomes for customers who were victims of APP scams, thus creating shared incentives to reduce fraud which should support more widespread adoption of the Code. Whilst Pay.UK acknowledged these arguments, they were unable to back the change request for the following reasons: (i) given the lack of consensus amongst payment service providers it is unlikely that the proposal could be enforced in practice; (ii) making a voluntary initiative mandatory would be the wrong approach from a policy perspective; (iii) the creation of a shared fund could reduce individual incentives to invest in fraud controls; and (iv) requiring all parties to manage their fraud risk in the same way could cause an increase in cost for some participants, thus having adverse effects on competition in the market. Nevertheless, Pay.UK acknowledges that steps need to be taken to reach a consensus on the funding for innocent customers. Their recommendations to achieve this include: (a) continuing commitment to meet the standards set out in the APP CRM Code; and (b) adopting a 'self-funding' arrangement which would allow flexibility for firms to enter voluntarily into an arrangement which would fund 'no-blame' customers.
Read more

PRUDENTIAL REGULATION

EC publishes impact assessment on proposals to amend CRR and CRD
On 21 November, the EC published an inception impact assessment aiming to inform citizens and stakeholders about the EC's plans regarding its proposals to amend CRR and CRD to implement the final Basel III reforms in the EU. The EC identified the following issues with rules in the CRR and the CRD: (i) the wide variation in own funds requirements across institutions makes it difficult to compare capital ratios; (ii) strong incentives exist to minimise risk weights when using internal models to calculate own funds requirement which may reduce the accuracy of risk measurement; (iii) current approaches to calculating capital requirements do not take into account certain exposures; (iv) there are undue administrative burdens placed on small institutions; and (v) the ECB, acting in its supervisory capacity, sometimes undermines the level playing field in the single market. The EC aims to address these issues through new legislation which would be adopted in the second quarter of 2020.
Read more

EBA publishes roadmap on the risk reduction measures package
On 21 November, the EBA published a set of roadmaps outlining its approach and timelines for delivering the mandates stemming from the Risk Reduction Measures Package adopted by the Council of the EU and the EP on 20 May 2019. These mandates are mainly focused in the areas of: (i) governance and remuneration; (ii) large exposures; (iii) resolution; and (iv) reporting and disclosure. Besides clarifying the sequencing of mandates and the rationale behind their prioritisation, the roadmaps aim at providing a preliminary understanding of the mandates combined with some policy guidance. Through this work, the EBA will contribute to making the European Single Rulebook more comprehensive, proportionate and reflective of developments in the banking sector.

Read more

EBA consults on specific supervisory reporting requirements for market risk

On 21 November, the EBA published a consultation paper (EBA/CP/2019/13) on draft implementing technical standards (ITS) for specific supervisory reporting requirements for market risk, which are the first elements of the Fundamental Review of the Trading Book (FRTB) introduced by CRR II. The EBA aims to introduce a thresholds template, providing insights into the size of institutions' trading books and the volume of their business subject to market risk, and a summary template, reflecting the own funds requirements under the "Alternative Standardised Approach" for market risk (MKR-ASA). When doing this, the EBA aims to take a gradual approach to ensure that the reporting requirements resulting from the FRTB are expanded in a proportionate manner, as institutions will also continue to be subject to the current market risk framework and the associated reporting requirements.

Read more

PRA issues a statement on delegated regulation changes

On 20 November, the PRA issued a statement to firms reminding them of the Delegated Regulation changes to the following regulations from 1 January: (i) Standard Formula component loss-absorbing capacity of deferred tax (LACDT); (ii) segmentation of non-life insurance and reinsurance obligations; (iii) standard deviations for the non-life premium and reserve risk sub-module; (iv) segmentation of Not Similar to Life Techniques (NSLT) health insurance and reinsurance obligations; and (v) standard deviations for the NSLT health premium and reserve risk sub-module.

Read more

SUSTAINABLE FINANCE

Please see the Brexit section for an update on the EC's plans for sustainable finance.

OTHER DEVELOPMENTS

CMA's updates timetable for investigation of anti-competitive arrangements in financial services sector

On 20 November, the Competition and Markets Authority (CMA) published an updated timetable for its on-going investigation of anti-competitive arrangements in the financial services sectors under the Competition Act 1998 and Article 101 of the Treaty on the Functioning of the European Union. The CMA launched their investigation in November 2018, aiming to use their power to enforce competition law infringements in the financial services sector. Currently, the CMA has not come to a decision as to whether there is sufficient evidence of infringements of competition law. The CMA had previously indicated that its initial investigation would take until August 2019. It now states that the initial investigation, including a review and analysis of information gathered, will continue until April 2020.

Read more

Council of the EU releases texts of European Financial Stability Facility

On 21 November, the Council of the EU published the following texts: (i) the Regulation relating to the powers, governance and funding of the European Supervisory Authorities (ESAs); (ii) the Directive amending the MiFID II Directive (2014/65/EU) and the Solvency II Directive (2009/138/EC); and (iii) the Regulation amending the European Systemic Risk Board (ESRB) Regulation (1092/2010).

Omnibus Regulation (PE-CONS 75/19)
Omnibus Directive (PE-CONS 76/19)
Regulation amending ESRB Regulation