EUROPEAN REGULATORY PERSPECTIVE

2022

Alpha

CONTENTS

FOREWORD

The impacts of the Covid-19 crisis have shifted regulators' agendas with increased attention to new and exacerbated risks affecting financial stability. Regulation and risk management teams will thus be heavily mobilised in 2022 to address these concerns.

It cannot be said that the Covid-19 crisis is now behind us, but regulators are trying to take stock of it and mitigate the risks that have emerged or been amplified.

Those identified as posing the greatest threat to financial stability are treated as a priority, such as the embedded leverage in the financial system ; the potential liquidity mismatch in open-ended funds and the use of liquidity risk management tools ; the resilience of money market funds ; the valuation and risk management practices regarding illiquid assets, in particular real estate ; the physical and transition risks posed by climate change.

Asset and Wealth managers should therefore demonstrate they have robust risk management and reporting processes in these areas. They should also pursue the implementation of sustainable finance regulations.

New regulations are also emerging regarding crypto technology (crypto-assets, stablecoin and DeFi), where regulators try to strike the right balance between fostering innovation and ensuring stability.

Alpha’s European Compliance & Regulation Practice team is happy to share its views on some of the key concerns of asset and wealth management industry.

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2022 KEY TRENDS

Once again, the cadence of regulatory changes at the European-level is not slowing down. To help you navigate this ever-changing sea of changes, the Alpha Europe team zooms in three topics:

Sustainable Finance – Where we are ?

After a year dedicated to the implementation of European and local ESG regulations, asset and wealth managers have to maintain the effort to finalize their transformation program and anticipate regulators incoming requirements on the fight against greenwashing.

Operational Resilience & Cloud computing

With the reliance of asset management industry to “information and communication technologies” (ICT), a new set of regulations is arising around the world to mitigate operational resilience risks.

KYC-KYT

Leveraging on the KYC-KYT approach ensures a full risk overview, from proactive detection to effective de-risking management.

Sustainable Finance – Where we are?

BY ALEXANDRE LACAZE & DAMIEN DUPART

KEY TAKEAWAYS

ONGOING REGULATORY PRESSURE & ESMA'S BATTLE AGAINST GREENWASHING

The sustainable finance regulation was the key concern of the investment management industry in 2021, and it will likely be the same in 2022. You will find hereafter an overview of the incoming new regulations and update of the existing ones.

SFDR & Taxonomy :

Most of SFDR Level 1 and Taxonomy already entered into force in 2021 and early 2022. The second set of RTS Draft under SFDR, expected for a long time, has been published on the 22nd of October 2021*, and will be applicable in January 2023** for most of its provisions.

Requirements on product reporting shall enter into force sequentially in 2023 and 2024 for RTS requirements.

MiFID 2 :

Amendment of MiFID2 has been published and should enter into force in August 2022 for the integration of the sustainability risk and clients' sustainability preferences. On these specific topics, wealth managers are particularly impacted. They are currently working on the reshaping of their suitability test. At the same time, they must collect information on products sustainability. This will be certainly simplified by the new market standard developed by FinDatEx, the "European ESG Template" or "EET". The effort must not be undervalued in terms of data and process. In addition, update of client KYC document may be time consuming and will increase the sales workload.

UCITS & AIFM :

Those two Directive have been reviewed and new provisions may be applicable in October 2022. These new requirements are focused on the consideration of sustainability risk by asset managers. Thus, they must consider sustainability risk both at entity and product level. For that, asset managers must retain the necessary resources and expertise for the effective integration of these risks. In addition, they must identify and manage conflict of interests which may arise as a result of the integration of sustainability risks in their processes, systems and internal controls framework.

*https://www.esma.europa.eu/sites/default/files/library/jc_2021_50_-_final_report_on_taxonomy-related_product_disclosure_rts.pdf
** https://www.esma.europa.eu/sites/default/files/library/com_letter_to_ep_and_council_sfdr_rts-j.berrigan.pdf

What are the next steps:

The European Securities and Markets Authority (ESMA), has published a new Sustainable Finance Roadmap for 2022-2024. Following the entry into force of several new regulations in 2022 as described above, the EU securities markets regulator is now drawing its priorities for the coming years.

First key concern of the ESMA is the fight against greenwashing. For the EU regulator, "greenwashing is a complex and multifaceted issue which takes various forms, has different causes and has potential to detrimentally impact investors looking to make sustainable investments". Risk of Greenwashing arises from the combination of a growing client demand for ESG products and a fast evolution of this new segment. This risk must be in the coming years addressed with a coordinated actions across EU.

Second key concern is the National Regulators (NCAs) and ESMA capabilities on sustainable finance. All regulators need to further develop skills beyond their traditional areas of focus to understand and address the supervisory implications of ESG regulation and emerging market practices in this area.

Third key concern is the monitoring of ESG markets and risks. The aim is to identify new trends, risks and vulnerabilities impacting investor protection or financial market stability. ESMA can leverage on its data-analysis capabilities to do this work and coordinate actions among NCAs.

To address these priorities, ESMA has designed a comprehensive list of action impacting investment management, investment services, issuers' disclosure and governance, benchmarks, credit and ESG ratings, trading and post-trading and financial innovation. Several of these actions shall also contribute to fulfilling the European Commission's 2021 Renewed Sustainable Finance Strategy.

In a broader perspective, new regulations are expected to emerge in the coming months following the publications of the 10 IOSCO recommendations on ESG ratings and data products providers. If most of them are addressed to regulators and ESG ratings and data product providers, recommendation 7 aims to strengthen due diligence procedures or information gathering and review for market participants using ESG ratings and data products. This could result in new requirements from NCAs or ESMA to ensure market participants assess the published methodologies of ESG ratings and data products they use or refer to in their internal processes.

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Operational Resilience & Cloud computing

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KEY TAKEAWAYS

STRONG OPERATIONAL RESILIENCE AND CLOUD COMPUTING FRAMEWORK ENABLE ASSET MANAGERS TO THRIVE IN THE DIGITAL ERA

SPECIALIZED TEAM, ENHANCED PROVIDERS OVERSIGHT AND INDEPENDENT ICT TESTING ARE THE CORNERSTONES TO MITIGATE THIS NEW RISK

Operational resilience in asset management

In early 2021, the Asian subsidiary of a global insurer was hit by a cyberattack. The hackers threatened to leak a large amount of personal and financial data. The triggering of this attack was a fire in a Cloud building, which weakened the servers hosting the insurer's confidential client data.

This event is not a singular phenomenon. Cyber-attacks are on the rise and asset managers are not immune. For this reason, financial regulators seek to regulate IT flows and strengthen companies' business continuity systems to better mitigate operational risks. The concept of Digital Operational Resilience is now in the spotlights and is defined by the European commission as "the ability of a financial entity to build, assure and review its operational integrity from a technological perspective by ensuring, either directly or indirectly, through the use of services of ICT third-party providers, the full range of ICT-related capabilities needed to address the security of the network and information systems".

Many regulations on operational resilience came to light these past years, pushing financial institutions to review their internal information and technology systems, as well as their cloud/data management processes.

Digital Operational Resilience Act:

In 2020, the European Commission adopted a package listing general lines and strategies to help Financial institutions mitigate their risks while implementing digital transformation initiatives. In the context of this digital finance package, the European commission has published on September 2020 its final proposal on digital operational resilience for the financial sector aiming to create a European approach to better define and manage digital or information and communication technologies (ICT). One of the main subjects tackled by the DORA regulation is the "critical ICT Third party service providers including cloud service providers".

DORA regulation includes many requirements focusing on the following subjects:

- Information and Communication Technology (ICT) risk identification and management.
- Digital operational resilience testing and Business Continuity plans; Information and intelligence sharing in relation to cyber threats and vulnerabilities with reporting of major ICT-related incidents to the competent authorities;
- Oversight framework of critical ICT third party service providers.

Following the publication of this proposal, financial institutions should already start testing their operational resilience to anticipate the regulatory requirements to come. As operational resilience is becoming a central strategic theme within financial services, asset managers need to deploy the necessary means to comply with this regulation.

The final regulation should see the light by the end of 2022, but the draft proposal is already available online.

Cloud Computing:

ESMA tried to identify and mitigate the risks emerging from cloud outsourcing arrangements in its guidelines. The publication followed the European Banking Authority's guidelines on cloud outsourcing. The final guidelines were published in May 2021 with the objective of helping banks, investment companies and financial institutions identify, monitor and better mitigate the risks arising from cloud outsourcing.

Specific attention is required by ESMA on the definition and risk management of important or/and critical functions which are by definition "function whose defect or failure in its performance would materially impair a firm's compliance with its obligations under the applicable legislation; a firm's financial performance; or the soundness or the continuity of a firm's main services and activities".

The ESMA guidelines are built around 9 topics . The most relevant subjects to be tackled by asset managers include:

- Governance, oversight and documentation of cloud service providers with detailed due diligence and pre-outsourcing analysis.
- Key contractual elements with dedicated requirements on the outsourcing agreement and the obligation of implementing and testing the business continuity and disaster recovery plans.
- Sub-outsourcing of critical or important functions.
- Written notification to competent authorities regarding any change in the classification of functions or in case of planned cloud outsourcing arrangements for important or critical functions.

What will change for asset managers?

Asset management companies will be required by regulators to implement change management initiatives to strengthen digital security risk management processes and policies. In order to be ready, asset managers would need to work on three different aspects:

DORA Regulation: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52020PC0595
ESMA Regulation : https://www.esma.europa.eu/sites/default/files/library/esma_cloud_guidelines.pdf

Report on market practice & Regulatory requirements

Operational resilience is a key concern for most local / regional regulators.
If some rules apply mainly to bank activities, they can also be used as best practices for the investment management industry.

UK
- Outsourcing
- Guidance for firms outsourcing to the 'cloud' and other third-party IT services

Hong Kong
- Outsourcing
- Cloud Outsourcing

Singapore
- Outsourcing
- Cloud Outsourcing

Europe
- Delegation & Outsourcing: UCITS Directive, AIFM Directive, MiFID 2
- Cloud outsourcing / ESMA
- Cloud outsourcing / EBA

France
- Control of PSE (Banking Sector): Arrêté du 3 novembre 2014

Luxembourg
- CSSF Circular 18/698 Authorisation and organisation of Investment Fund Managers
- Circulaire CSSF 17/654 Outsourcing relying on a cloud computing infrastructure

Ireland
- Cross-Industry Guidance on Outsourcing

1. Specialized team

Regulators highly recommend the creation of a dedicated specialized team accountable for the oversight of cloud outsourcing.

European authorities are also keen on reviewing the existing business continuity plan, with a focus on its extension to technology management activities. To do so, collaborators involved in the process should be trained and well informed.

2. Enhanced providers oversight

Local and European regulators asked for enhanced communication between local authorities and market players regarding new arrangements with third party service providers, and new critical/ important functions. The creation of a dedicated register of all providers is necessary, and so is complying with the reporting requirements on incidents management related to technologies.

In addition, asset managers should ensure that due diligence analysis and final agreements define and better capture the terms, roles and responsibilities of third-party service providers. For that, strong due diligence processes (initial and ongoing) should be implemented, and an overhaul of the approach to the negotiation and signing of new and existing contractual arrangements should be overtaken when necessary.

3. Independent ICT testing

To make sure that every potential risk is tackled and mitigated by the processes and proper monitoring is implemented, asset managers should run several tests, among them digital operational resilience testing and penetration testing by independent internal or external parties, at least annually. These tests aim to ensure that companies are prepared for any event of ICT incident.

The new possibilities arising from cloud computing are an opportunity that asset management companies should seize. The global digitalization of the financial system creates new types of risks that endanger the sustainability of financial institutions. Complying with the operational resilience and cloud outsourcing regulations are a necessity for companies to thrive.

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At the core of Compliance Operating Model: the KYC-KYT approach

BY THIBAUT GALLINEAU

KEY TAKEAWAYS

LEVERAGING ON THE KYC-KYT APPROACH ENSURES A FULL RISK OVERVIEW, FROM PROACTIVE DETECTION TO EFFECTIVE DE-RISKING MANAGEMENT

COMPLIANCE OPERATING MODEL ARE REINFORCED WITH A HOLISTIC FRAMEWORK EMBEDDED WITHIN THE COMPLIANCE VALUE CHAIN

KYC-KYT: the two edges of the same blade

Since 2005-2010, the famous "Know Your Customers – KYC" approach has been widely promoted by regulators, audit firms, and even major players of the Financial Services. Focused at the very beginning on the Documentation aspects of the client relationship, KYC approach has grown to now have a deep understanding of the whole client information including his/her background in various domains (professional activities, revenue level, former contractual relationships, etc.).

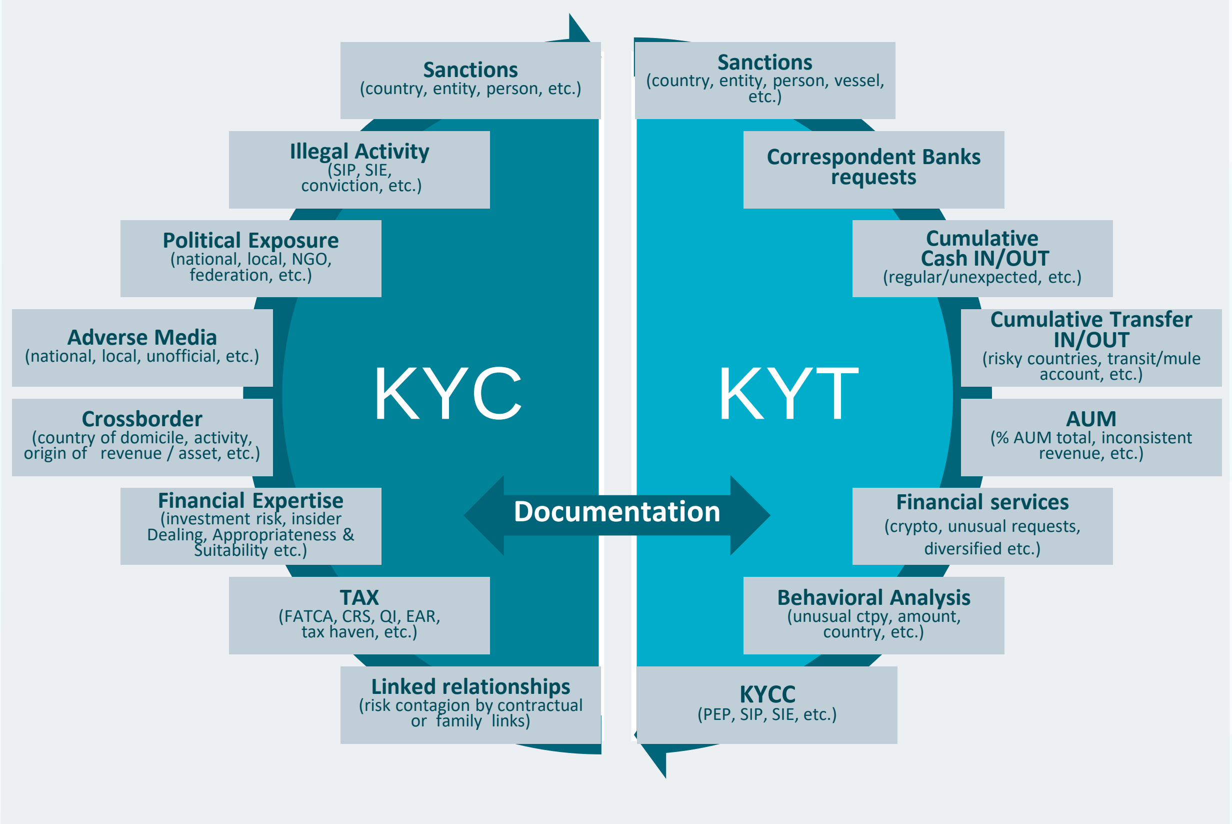
This first step has led to numerous remediations, task forces, and even long-term KYC dedicated team creations. The Financial industry has been urged to be much more diligent with the proper and adequate documents, the associated document management rules, flow and IT architecture. There is no denying that such activities allowed the detection of unknown risks, the legacy of risky or non-cooperating clients and the ultimate understanding that nothing can be hidden or forgotten in a digital-tracking world. Even if the data behind the KYC set of information is less subject to change, we decently cannot call it "static data" as the increasing number of "changes of circumstance" to be treated is revealing us it's in fact a semi-static data.

The more recent "Know Your Transactions –KYT" approach is in fact derived from the whole dynamic of all transactions and services initiated or received by the client. Thus, it mixes Anti-Money Laundering, Counter Financial Terrorism but can also include tax evasion and also country risk exposition.

Many regulators are now mentioning this KYT approach with the aim of defocusing only on the documentation aspect of the relationships to include a wider analysis on the financial trends and habits by cumulated flows so as the reach a so called "holistic vision of the relationship". Indeed, the semi-static KYC data enough is not sufficient to figure out if the way your client is using your financial institution constitutes or not a potential, suspected or proven risk.

Risk Profiling data based on KYC-KYT approach and supported by tangible documents and logs (sometimes called the KYD, Know Your Documents) has become now the core of the Compliance Operating Model.

KYC-T Approach by Alpha FMC



A leverage for de-risking:

The point of integrating the dynamic KYT side is also to play on both grounds:

- From a regulatory perspective, automatic cumulated flows per type of transaction or country, give the institution the expected self-confidence your client is not misusing your services by exorbitant amounts of cash, transitory accounts to hide some illegal financial scheme, not reported source of revenues coming from risky countries from a corruption or an economic point of view.
- From a business perspective, Front Officers can definitely leverage on these Key Business Indicators to propose tailor made services, to detect trends and associated business opportunities and to prevent client lassitude or exit.

KYT approach can even confirm or extend KYC approach with the "Know Your Customers' Customers –KYCC" that allows Compliance Officers to really qualify the adapted momentum of a risk.

To set an example, let's take a former PEP, Member of Parliament in a foreign county with no active mandates since she retired in Europe in 2014. If the KYCC details shows she is still actively transacting with active PEPs and State Owned Entities, it confirms the High-Risk PEP qualification even inactive as of PEP more than 5 years later.

KYC-KYT in Compliance Value Chain:

You will find below a proposition of the Compliance Value Chain definition. If the three first steps [Definition – Detection – Qualification] are similar to each control functions, the three other [Classification – Decision – Supervision] are really connected with the laws, the regulator expectation and the firm strategy.

The Decision chain is always the most challenging as it is on case-by-case analysis basis and involves other actors such as Front-Office, Central File, Legal or Tax Department. From risk acceptance to litigation, the number of concrete action to mitigate, prevent, reduce, delete a compliance risk is infinite.

That's the reason why a solid KYC-KYT holistic approach can support Client Risk Reviews and all decision-making processes when all Compliance value chain are integrating both KYC and KYT associated risks with their conditions (documentation, amount, threshold, client reminders, risk country matrix, etc.).

In the end, Financial Institutions that followed this KYC-KYT approach acquired an improved Compliance maturity to manage their risky client. Indeed, knowing your risky client has neither KYC intrinsic proven risk factors nor KYT suspicious activity but is at risk due to contractual relationships provoking a severe risk inheritance, is a key deciding factor to ensure an optimized Risk Management across all the value chain and the core activities of Compliance.

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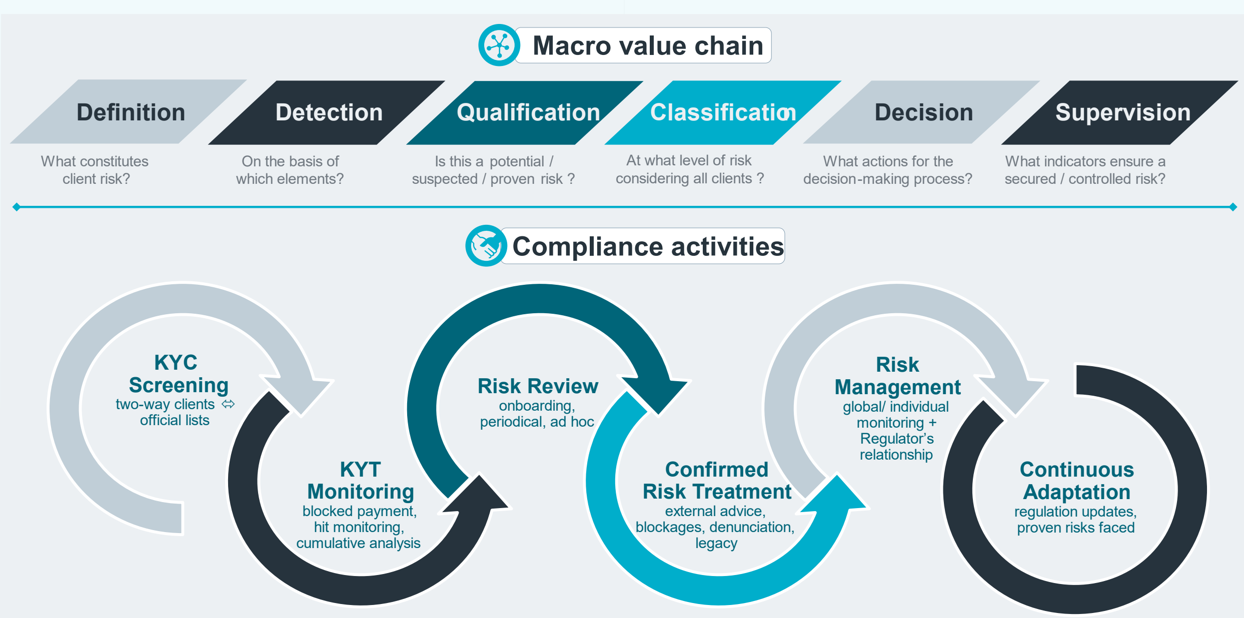

HOT TOPICS OVERVIEW

The purpose of this section is to present a holistic view of compelling topics frequently assessed by European NCAs and most likely exposed to controls or inspections. These topics shall be considered in the 2022 roadmap of Compliance & Risks Heads.

Regulatory Reporting

Regulatory reporting became a high priority for most of EU regulators. The main challenge for asset & wealth managers is the governance and data quality. As an illustration, the Autorité des Marchés Financiers (AMF), the French regulator has enshrined regulatory reporting into its supervision priorities for 2022.

REGULATORY REPORTING:

WHY THE REGULATOR IS LOOKING FOR BETTER DATA QUALITY IN 2022?

INTERVIEW MADE BY AÏCHA MAUDUIT

KEY TAKEAWAYS

Alpha is in touch with vendors providing solutions dedicated to asset and wealth management and has identified Kaizen Reporting as a potential tech solution for the monitoring of data accuracy and completeness of regulatory reporting

The regulatory reporting obligations that apply to the asset and wealth management industry have increased in complexity and volume in the past few years.

As the reporting regimes become more mature, data quality is increasingly becoming a higher priority for local regulators. Thus, the Autorité des Marchés Financiers (AMF), the French regulator has enshrined governance and data quality into its supervision priorities for 2022.

A new era begins, where the challenges for asset and wealth managers will not only be data production but governance and data quality with Investment Firms required by regulators to ensure reports are timely, accurate and complete. These issues cannot be solved by manual processes and require the implementation of technological solutions able to assess the data accuracy.

Regulatory technology firm Kaizen Reporting developed its ReportShield™ automated testing services to help investment firms improve the quality of their reporting.

Aïcha Mauduit: *Could you summarize Kaizen's ReportShield assurance services?*

Ian Rennie: Our quality assurance services for regulatory reporting are marketed under the umbrella name ReportShield. ReportShield comprises three testing services:

- Accuracy Testing
- Advanced Regulatory Reconciliation
- Reference Data Testing

Together these services act as a shield against regulatory scrutiny, providing the controls firms need to meet their regulatory obligations and effectively manage reporting risks.

Aïcha Mauduit: *Where did the idea come from ?*

Ian Rennie: Formed in 2013, Kaizen Reporting was established after CEO & Founder Dario Crispini witnessed first-hand while working at the UK regulator (the FSA, now the FCA) the problems many organisations faced with their regulatory reporting data quality.

Aïcha Mauduit: *What is Kaizen's story?*

Ian Rennie: Our mission is to make working with regulation easier for our clients, from initial researching and managing rules to improving confidence in the quality of their regulatory reporting.

We've combined regulatory expertise with advanced technology to develop our market-leading automated quality assurance services which are unique in providing our clients with full visibility of their regulatory reporting quality.

Over the last three years, Kaizen Reporting has identified approximately 3.09 billion errors/queries from 3.5 billion records tested across multiple regulatory reporting regimes: MiFIR, SFTR and multiple G20 regulations (EMIR, DFA, MAS, CSA, HKMA, ASIC & FinfraG).

In 2020, we launched two new services – an automated system for monitoring and reporting Shareholding Disclosures and Single Rulebook, a software solution that enables you to search, share and manage regulatory rules on one digital platform, taking our services deeper into the RegTech space and beyond regulatory reporting.

Today, more than 140 clients globally use Kaizen Reporting's ReportShield services to improve their data quality as well as manage regulatory change across their organization. *(cf chart P.19)*

Aïcha Mauduit: *As of today, what is your client portfolio ?*

Ian Rennie: Our services are used by some of the world's largest banks, asset managers, hedge funds, brokers and trading venues and have been recognized with multiple industry awards as well as by the UK government with a prestigious Queen's Award for innovation.

Aïcha Mauduit: *What is the expected added value for Asset and Wealth Managers brought by Kaizen ?*

Ian Rennie: Asset managers in particular are relatively new to the reporting space compared to the sell-side who have been obliged to report for a much longer period of time. For example, in 2018, MiFID II brought asset managers into the reporting scope for the first time. This means they have had to get up to speed more quickly and may not have the depth of expertise in house to adhere to the requirements. For wealth managers, although many have been reporting since MiFID I, their reporting obligations also increased significantly under MiFID II.

Kaizen's assurance services give asset and wealth managers full visibility of the quality of their reporting so that they meet their reporting requirements, allowing them to evidence where they are accurate and identify errors so that they can be quickly remediated.

Aïcha Mauduit: *How does Kaizen Reporting differ compared with other solutions, and what is your development plan for the next 5 years?*

Ian Rennie: Our ultimate goal and plan for the next five years is to provide best in class reporting assurance services that drive and

underpin the improvement in data quality which is vitally important for the industry as a whole as well as regulators across Europe.
Kaizen Reporting's ReportShield services differ from other solutions in a number of ways:

1. ReportShield's suite of services are underpinned by a unique and data led testing and reconciliation methodology.
2. Our approach is focused on ongoing testing to identify reporting errors before they become an issue and not just backdated testing when there's a problem or a regulatory fine.
3. "Deep testing" – we test all reported records (100% testing for all trades and fields) and detect all types of reporting errors - something that standard validations and reconciliations do not do.
4. We work in partnership with clients and regulators on the resubmission of reporting data.

Aïcha Mauduit: *Why should accuracy and completeness of regulatory reporting be a priority for 2022?*

Ian Rennie: Accuracy and completeness of regulatory reporting have always been a priority ever since global reporting rules were introduced post financial crisis. However, as we approach several years since the rules, including MiFID II, EMIR and SFTR, were implemented, the stance of regulators continues to toughen year on year.
Furthermore, it is a requirement under MiFID RTS 22, Article 15 to test and reconcile reports on a regular basis.
Ongoing testing is mandated to ensure a high level of reporting accuracy as well as the timely identification of reporting issues which can be remediated as required.
With Kaizen Reporting data showing that 88% of transactions reported are impacted by errors or queries over the last three years, it is apparent that many firms are still struggling with regulatory reporting and so the timely identification of reporting issues is essential to ensure that remediation costs and regulatory risk are managed.

Aïcha Mauduit: *Is there any technical pre-requisite for an asset or wealth manager to use a solution similar to Kaizen Reporting's?*

Ian Rennie: There is no technical pre-requisite. Clients just need to complete a business discovery questionnaire and give us permission to access their data from their ARM, Trade Repository or the regulator and Kaizen will take care of the rest.

Aïcha Mauduit: *What is a typical journey for your clients ?*

Ian Rennie: When working with new clients, we ensure we understand the client's problem statement, and this reflects the tailored solution that we provide.
We have vigorous on-boarding and Know Your Customer (KYC) processes. At the point of engagement, we outline our on-boarding process to prospective clients and begin to complete the KYC documentation in order to understand the client's business requirements and allocate internal resources appropriately. We initially offer a complimentary 'Proof of Concept', enabling prospective clients to trial our services by providing us with a sample set of data and in return receiving a redacted version of our testing results. In order to adhere to security and data protection rules and protocols, we set up a secure transfer (SFTP) to send and receive data securely. Prospective clients then complete a 'Business Discovery Questionnaire', so that we can collect the detail to be included in the scope of testing. We then input this information into our CRM system which feeds through to our Data Analysts via our Telemetry system, in order to prioritize and schedule delivery. During and post-delivery, clients have access to the Kaizen Helpdesk, allowing them to submit questions which are reviewed and responded to by our Regulatory Reporting Specialists. These queries could relate to business discovery queries or the results themselves.

Aïcha Mauduit: *Any insight on what ESMA and local regulators such as AMF and CSSF are prioritizing in relation to this topic?*

Ian Rennie: As mentioned above, regulators have toughened their stance in recent years as they seek to improve data quality. Firms should have demonstrable controls in place that allow them to monitor the accuracy, completeness and timeliness of transaction reports. Where issues are identified, they need to work with sufficient pace and effort to resolve them in appropriate timescales.
The complexity of transaction reporting has meant that the regulator has acknowledged that firms will encounter issues that require remediation. There is even a view that firms identifying and notifying the regulator of breaches have a stronger control framework in place than those who have not notified the regulators of anything.
One of the key reasons behind the implementation of MiFID II transaction reporting was to mitigate the risk of market abuse. Covid-19 and the subsequent changes to the working model have dramatically increased this risk (e.g. through reduced trade surveillance and monitoring as employees work remotely and increased risk of employees disclosing sensitive information). ESMA and national competent authorities across Europe have re-affirmed their expectations that firms should continue to take all steps required to prevent market abuse.
In its "Supervisory Priorities for 2022", the

Autorité des Marchés Financiers (AMF) highlighted data quality in the various reporting regimes introduced by MiFID II as a key theme for their supervisory activity this year.

Indeed, this theme was one of ESMA's first Union Strategic Supervisory Priorities (USSP) in 2021 and was communicated as a key priority to national competent authorities across Europe last year and again for 2022.

The AMF notes that:
"*The data reported to the AMF contribute to the knowledge and monitoring of market participants and regulated products and enable the regulator to detect situations requiring its attention.*"
It also states that, *"in order to check the quality of the data received, a SPOT inspection campaign will be launched in 2022 on governance and the process for gathering, calculation and transmission of the data submitted to the AMF.*"

In light of the continued focus on reporting accuracy by regulators not only in Europe, but across the globe, it remains vital that asset management firms test and remediate their reporting data on a regular basis to ensure the highest data quality. Would you also want to add - Similar trend occurs with the CSSF as noted by recent fines.

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REGULATORY WATCH

The purpose of this section is to highlight the most relevant regulatory evolutions for the asset and wealth management industry which occurred in 2021 and January 2022. Publications have been classified in alphabetical order.

A landmark year for sustainable finance

2021 was particularly significant in sustainable finance notably with the entry into force of the first SDFR provisions which involved huge workload for the industry (see *Sustainable Finance*).

However, efforts are far from over, with the forthcoming entry into force of the Taxonomy (which is still not stabilised), possible clarifications on the application of SFDR, and the discussions around CSDR. Not to mention the UK's development of its own sustainable finance package.

Increased attention by regulators to financial stability

The steady growth of so-called "non-bank financial intermediation" in the recent years and the risks raised by the COVID-19 pandemic led to greater vigilance from regulators regarding financial stability.

Public authorities, for instance, assessed the resilience of money market funds (see *MMFR*), the liquidity risk in open-ended funds (see *Initiatives of International Bodies*), or continued to build the regulatory framework for CCP Resolution (see *CCP RRR*).

Emerging regulatory frameworks for new practices and products

Competition between financial jurisdictions led to various developments in the regulatory landscape, such as the publication in the OJEU of the "Quick Fix" Directive amending MiFID 2 (see *MiFID II / MiFIR*) or emerging local regulations on alternative assets such as crypto (see *Initiatives of local regulator*).

REGULATORY WATCH

KEY TAKEAWAYS

THIS SECTION RECAPS THE MAIN REGULATORY UPDATES WHICH OCCURRED BETWEEN FEBRUARY 2021 AND JANUARY 2022.

AIFMD

- ESMA updated on 17/12/2021 its Questions and Answers on the application of the AIMD to clarify the scope of the Directive as regards to investments in crypto-assets.

- The European Commission released on 25/11/2021 its AIFMD review proposal introducing changes on delegation rules, liquidity risk management, provision of depositary and custody services and loan origination.

This proposal is following the ordinary European legislative process and the negotiations are expected to occupy most of 2022.

- AIFMD Level 2 amendment was published on 02/08/2021 in the Official Journal of the EU. It contains provisions on the sustainability risks and sustainability factors to be taken into account by AIFM.

BENCHMARKS REGULATION / IBORs

- The EUR RFR Working-Group published a statement on 13/12/2021 on preparedness for the cessation of EUR, GBP, CHF and JPY LIBORs and EONIA, and ceasing use of USD LIBOR in new contracts, at the end of 2021.

- The EUR RFR Working-Group published a statement on 09/12/2021 indicating it supports the CTFC MRAC initiative for cross-currency swaps and recommends the adoption of €STR for the EUR leg of EUR vs USD cross-currency swap in the EU interdealer market.

- ESMA published on 07/12/2021 its Guidelines on methodology, oversight function and record keeping under the Benchmarks Regulation.

- ESMA updated on 19/11/2021 its Questions and Answers on the Benchmarks Regulation clarifying disclosure requirements of the benchmark statement template and providing the European Commission answer on ESG factors and ESG objectives.

- ESMA released on 18/11/2021 its final report on draft RTS on the clearing and derivative trading obligations in view of the benchmark transition to risk free rates.

- The EUR RFR Working-Group published some recommendations on 26/07/2021 on the switch to risk free rates in the interdealer market.

- The European Commission, the ECB, the EBA and ESMA issued on 24/06/2021 a joint public statement on the forthcoming cessation of all LIBOR settings.

BREXIT

- The EU and the UK concluded technical negotiations on 26/03/2021 on EU-UK Memorandum of Understanding on financial services regulatory cooperation.

The MoU will establish the Joint EU-UK Financial Regulatory Forum that will meet at least twice a year to work on financial services issues.

- ESMA issued on 31/03/2021 a statement bringing clarifications on the application of the TD requirements by UK issuers with securities admitted to trading on regulated markets in the EU.

- ESMA issued on 09/03/2021 a statement on the impact of Brexit on the Benchmark Regulation.

CCP RRR

- ESMA launched on 18/11/2021 six consultations on the CCP Resolution Regime. These consultations contain proposals for draft RTS on resolution colleges; the valuation of CCPs' assets and liabilities in resolution; the safeguard for clients and indirect clients; and the content of resolution plans. They also contain proposal for draft guidelines on the valuation in termination of contracts and on the application of the circumstances under which a CCP is deemed to be failing or likely to fall.

CBDF

- ESMA released on 27/05/2021 its Guidelines specifying the requirements that funds' marketing communications must comply with under the CBDF Regulation.

- ESMA published on 01/02/2021 its final report on the draft ITS under Regulation EU/2019/1156 on the facilitation of cross-border distribution of collective investment undertakings, specifying standard forms, templates and procedures for the publication of information by NCAs on their websites and for NCAs to notify ESMA regarding national marketing requirements, regulatory fees and charges, and funds distributed on a cross-border basis.

CSDR

- ESMA updated on 22/12/2021 its list of key relevant provisions on national corporate or similar law under which the securities are constituted.

- ESMA updated on 17/12/2021 its Questions and Answers on the implementation of CSDR, amending its answer on settlement instructions sent by CCPs and adding an answer on Participant's settlement efficiency.

- ESMA released on 08/12/2021 a final report on the guidelines on settlement fails reporting under Article 7 of CSDR.

- ESMA released on 17/12/2021 a public statement calling on the NCAs not to prioritize supervisory actions in relation to the application of the CSDR buy-in regime.

CYBERSECURITY

- The Financial Stability Board published on 19/10/2021 a report on cyber incident reporting, existing approaches and next steps for broader convergence.

- The AMF published on 07/04/2021 a summary of the results of a new series of thematic inspections of the cybersecurity systems and processes of asset management companies.

EMIR

- ESMA released on 17/12/2021 a report and a statement on Tier 2 CCP assessment under Article 25(2c) of EMIR. The European watchdog concludes that it will not recommend to the European Commission to derecognise LCH Ltd and ICE Clear Europe Ltd, or one of its services, at this point of time.

- ESMA launched on 19/11/2021 a consultation on highly liquid financial instruments with regards to the investment policy of central counterparties (EMIR article 85(3a(e))).

- ESMA updated on 19/11/2021 its Questions and Answers on the implementation of EMIR, amending answers on the calculation of the clearing threshold and the hedging definition.

• ESMA updated on 13/10/2021 its Public Register for the clearing obligation under EMIR.

• ESMA published on 15/04/2021 its EMIR and SFTR data quality report 2020 which is the first review of the data quality of data reported by Trade Repositories (TRs) and contains an overview of actions taken by NCAs and ESMA to improve both EMIR and SFTR.

ECSPR

• ESMA published on 10/11/202 its final report on draft RTS under the European crowdfunding service providers for business Regulation.

IFR/IFD

• EBA and ESMA launched on 18/11/2021 a consultation on their guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) of investment firms.

• EBA launched a consultation on 18/11/2021 draft RTS on Pillar 2 add-ons for investment firms under Article 40(6) of Directive (EU) 2019/2034.

INSURANCE DISTRIBUTION DIRECTIVE

• EIOPA released on 21/12/2021 its annual report on sanctions under the IDD during 2020.

• EOPIA launched on 08/04/2021 its IDD Single Rulebook, that enables the navigation across different legal acts such as the Directive, Delegated and Implementing Regulations, as well as EIOPA Guidelines and IDD Q&A.

• EIPOA published on 23/03/2021 Questions and Answers on the IDD provided by the European Commission.

AML/CFT

• The FATF updated in June 2021 and in October 2021 its recommendations to, respectively, clarify the types of offences which fall within the 'environmental crime' category ; clarify obligations on DNFBPs to apply group-wide programmes ; and clarify that the definition of 'financial group is not limited to Core Principles institutions.

• AMF updated on 24/11/2021 its Position DOC-2019-14 its Guidelines on risk factors, applying the EBA revised Guidelines on money laundering and terrorist financing risk factors.

• The EC presented on 20/07/2021 an AML/CFT package consisting out of four legislative proposals: a regulation establishing an EU AML/CFT authority in the form of a decentralized EU regulatory agency; a new AML/CFT Regulation ("Single Rulebook") containing directly applicable AML/CFT rules, including a revised EU list of entities subject to AML/CFT rules (known as "Obliged Entities"); a sixth Directive on AML/CFT ("AMLD6"), replacing the current Directive 2015/849/EU (the fourth AML directive as amended by the fifth AML directive), containing provisions that will be transposed into national law; and a revamp of the Regulation on Transfers of Funds from 2015.

• EBA released on 01/03/2021 its revised Guidelines on money laundering and terrorist financing risk factors (EBA/GL/2021/02).

The revisions take into account changes to the EU Anti Money Laundering and Counter Terrorism Financing (AML/CTF) legal framework and address new ML/TF risks, including those identified by the EBA's implementation reviews.

MAD / MAR

• ESMA published on 28/10/2021 a statement on investment recommendations on social media.

• ESMA released on 20/10/2021 its report on administrative and criminal sanctions and other administrative measures imposed under MAR in 2020.

MiFID II / MiFIR

• ESMA launched on 04/01/2022 a call for evidence on the DLT Pilot Regime and review of MiFIR RTS on transparency and reporting. The "DLT Pilot" Regulation required ESMA to assess whether the MiFIR RTS need to be amended to fit with DLT.

• Directive 2021/338 called "Quick Fix" amending Directive 2014/54/EU (MiFID II) was published on 16/12/2021 on the Official Journal of the EU.

Provisions will apply on 28/02/2022 and modify, in particular, the product governance requirements, cost display, services granted to professional investor or the funding research regime.

• ESMA released on 16/12/2021 its annual report on the application of pre-trade equity and non-equity transparency waivers for 2020.

• The European Commission published on 25/11/2021 a proposal amending Regulation (EU) No 600/2014 on markets in financial instruments (MiFIR), and a proposal amending Directive 2014/65/EU on markets in financial instruments (MiFID II), aiming to empower especially smaller and retail investors, by tackling three priority areas; improving the transparency and availability of market data; improving the level-playing field between execution venues; and ensuring EU market infrastructures can remain competitive at the international level.

• ESMA updated on 19/11/2021 its Questions and Answers on MiFID II and MiFIR investor protection and intermediaries topics providing clarification on the exemption of the MiFID II product governance requirements for certain bonds embedding a make-whole clause.

• ESMA updated on 26/10/2021 its data validation rules for MiFIR transaction data. This document provides comprehensive description of all validation rules that are applied.

• ESMA updated on 01/10/2021 its Public Register for the trading obligations for derivatives under MiFIR.

• ESMA published on 30/03/2021 its final report on the obligations to report transactions and reference data under MiFIR to the EC, based on the feedback ESMA received from its consultation, that contained recommendations and possible legislative amendments to the MiFIR transaction reporting regime.

• Version 3.1 of the EMT (MiFID II template) was validated by FinDatEx on 12/02/2021, which included changes regarding SFDR level 1 requirements. This is a temporary template that went live on 10 March 2021 and would coexist with version 3, meaning both templates need to be disseminated.

MMFR

• ESMA published on 29/06/21 its annual update of its Guidelines on stress test scenarios under the MMF Regulation.

• ESMA launched on 26/03/2021 a consultation on potential reforms of the EU MMF Regulation after the stress caused by the COVID-19 crisis.

PRIIPs

• The ESAs updated on 17/12/2021 their Questions and Answers on the PRIIPs Key Information Document (KID).

• Three important EU texts as regards the PRIIPs Regulation were published on 15/12/2021 in the Official Journal of the EU.

The Regulation (EU) 2021/2259 amending Regulation (EU) 1286/2014 (PRIIPs Regulation) extended the transitional arrangement for ManCos, investment companies and persons advising on, or selling, UCITS and non-UCITS until 31/12/2022.

The Directive (EU) 2021/2261 amending Directive 2009/65/EC (UCITS Directive) stating that the PRIIPs KIDs may be given to any investor (including a professional investor) instead of the UCITS KIDs. This Directive must be transposed by Member States by 31/07/2022.

Finally, the Commission Delegated Regulation (EU) 2021/2268 amended the previous RTS for PRIIPs KIDs.

• The EP voted on 23/11/2021 to extend the UCITS exemption and postpone the PRIIPS RTS by six months, moving the go-live date and end of the exemption to 1 January 2023.

• The ESAs published on 20/10/2021 a call for evidence on the European Commission mandate regarding the PRIIPs Regulation.

PROSPECTUS REGULATION

• ESMA updated on 27/07/2021 its Questions and Answers on the Prospectus Regulation.

• ESMA released on 20/07/2021 its report on Prospectus activity and sanctions in 2020.

• ESMA issued on 15/07/2021 a Public Statement on SPACs prospectus disclosure and investor protections considerations.

• ESMA published on 04/03/2021 its Guidelines on disclosure requirements under the Prospectus Regulation.

SECURITISATION REGULATION

• The ESAs released on 10/12/2021 their Questions and Answers relating to the Securitisation Regulation.

• ESMA updated on 19/11/2021 its Questions and Answers on the Securitisation Regulation.

• ESMA published on 07/10/2021 its draft technical standards on content and format of the STS notification for on-balance sheet securitisations under the amended Securitisation Regulation.

• The ESAs released on 17/05/2021 a Report on the implementation and functioning of the Securitisation Regulation.

• ESMA published on 05/02/2021 its Guidelines on portability of information between securitisation repositories under the Securitisation Regulation.

SHAREHOLDER RIGHTS DIRECTIVE

• ESMA updated on 14/12/2021 its document listing the thresholds above which shareholders can be identified in the various Member States of the EU.

SHORT SELLING REGULATION

• ESMA issued on 26/01/2022 a statement on how to report the notification threshold of net short positions (NSPs) under the new reporting threshold of 0.1%.

SFTR

• ESMA updated on 14/12/2021 its Questions and Answers on SFTR data reporting and its Guidelines on calculation of positions in SFTs by Trade Repositories.

• AMF published on 11/06/22 a report on its initial assessment of SFTR reporting data and specified the various use cases already identified.

SUSTAINABLE FINANCE

• EC published on 25/11/2021 a letter to EP and Council stating that SFDR technical standards will apply on 1 January 2023.

• IOSCO published on 21/11/2021 a report on ESG ratings and data products providers.

• The ESAs published on 22/10/2021 their final report on draft RTS with regard to the content and presentation of disclosures under SFDR. These RTS come from provisions inserted in SFDR by the Taxonomy Regulation.

• G7 published on 05/06/2021 a Communiqué stating that G7 nations will mandate climate reporting in line with the recommendations of the TCFD.

• Delegated acts amending AIFMD, UCITS and MiF 2 Directive and Regulation were published on 21/04/2021 in the Official Journal of the EU. These changes aim to integrate sustainability preferences and risks into the organisational policies of asset managers and product governance arrangements as well as when assessing the product suitability with the client's ESG preferences.

• The ESAs published on 25/02/2021 a joint statement on the application of the SFDR, providing guidance during the interim period between the time SFDR Level 1 requirements will apply and the proposed application date of the draft RTS Level 2.

• The ESAs published on 02/02/2021 their final report on draft RTS with regard to the content and presentation of disclosures under SFDR.

UCITS

• ESMA launched on 06/01/2021 a Common Supervisory Action (CSA) with NCAs on the supervision of costs and fees of UCITS across the European Union (EU). It aimed to assess the compliance of supervised entities with the relevant cost-related provisions in the UCITS framework, the obligation of not charging investors with undue costs and the compliance to the requirements on Efficient Portfolio Management (EPM) techniques.

INITIATIVES OF INTERNATIONAL BODIES

• The FATF published on 28/12/2021 the Updated Guidance for a Risk-Based Approach to Virtual Assets (VAs) and Virtual Asset Service Providers (VASPs), mainly addressing ML/TF risk associations with VAs and VASPs.

• The European Council announced on 24/11/2021 that it reached an agreement on MiCA – creating a regulatory framework for crypto-assets markets – and DORA proposals, opening the trilogue negotiations with the EP which may end in 2022.

• The FSB published on 01/11/2021 its Progress Report on enhancing the resilience of Non-Bank Financial Intermediation (NBFI).

This report mainly focuses on MMF resilience, liquidity risk in open-ended funds, core government and corporate bond markets' liquidity during stress, margin calls in centrally and non-centrally cleared markets, and an assessment of the fragilities in USD cross-border funding.

• The Committee on Payments and Market Infrastructures (CPMI) and the International Organization of Securities Commissions (IOSCO) published on 06/10/2021 preliminary guidance for public consultation, confirming and clarifying that stablecoin arrangements (SA) should comply with international standards for payment, clearing and settlement systems according to the Principles for Financial Market Infrastructures (PFMI).

• ESMA published on 27/09/2021 its 2022 Annual Work Programme. The ESAs' Review and EMIR 2.2 – including the set up of the CCP Supervisory Committed – have had a considerable impact on ESMA's activities and organisation since 2020.

Main priorities for 2022 will be the development of a Capital Markets Union (CMU), Innovation and Digitalisation, and Sustainable Finance. ESMA will also exercise new mandates as regards the supervision of critical benchmark administrators and Data Reporting Service Providers (DRSP).

• The EC adopted on 04/06/2021 a new set of Standard Contractual Clauses (SCCs) to align them with the requirements of GDPR, market practices, and the Court of Justice of the European Union's (CJEU) "Schrems II" ruling.

• The EC proposed on 21/04/2021 the AI regulation, which is the first of its kind, including standardized rules for marketing, using, and deploying AI technologies, prohibition of some AI practices, specific requirements for high-risk AI systems, transparency standards that are consistent among AI systems that interact with natural persons, detect emotions, categorize biometrics, and generate or manipulate picture, audio, or video content and market surveillance and monitoring rules.

• IOSCO published on 26/02/2021 its work program for 2021-2022 adding two new priorities for the institution: financial stability and systemic risks of non-bank financial intermediation activities (NBFI); and risks exacerbated by the COVID-19 pandemic – misconduct risks, fraud, and operational resilience.

INITIATIVES OF LOCAL REGULATORS

• The AMF published on 05/01/2022 its annual supervisory priorities.

• The CSSF published on 22/12/2021 three new Circulars (CSSF 21/788, 21/789, and 21/790) concerning new regulatory reporting obligations for UCIs and IFMs, aiming to enlarge the scope of regulated entities under CSSF supervision, introducing a new electronic reporting tool enabling enhanced supervision, communicating key controls at the regulated entities, and reconciling the controls of the AML/CFT report.

• The CSSF published on 29/11/2021 Guidance and Questions and Answers on virtual assets which opens the way for AIF marketed to professional investors to invest in crypto.

• The CSSF published on 14/10/2021 a new Circular (CSSF 21/785), replacing the prior authorization obligation with a prior notification obligation in the case of material IT outsourcing, applying to credit institutions, professionals of the financial sector, payment institutions, electronic money institutions and investment fund managers subject to CSSF 18/698.

• The AMF released on 28/10/2021 its priority areas of actions for 2021 and its recent actions and contributions as regards sustainable finance.

• The CSSF published on 21/06/2021 its Circular 21/773, providing guidance on risk management related to the climate and the environment, which applies to all CIs, classified as less significant institutions (LSIs) and all non-EU Cis.

• The Chambre des Députés of Luxembourg published on 21/05/2021 Bill 7825 amending the Law of 22 March 2004 on securization, aiming to offer new methods for operators who want to conduct securization transactions under Luxembourg law.

• The CSSF published on 09/04/2021 its Circular 21/769 regarding governance and security requirements for supervised entities to perform tasks or activities through telework. The Circular applies to all CSSF supervised entities. Teleworking no longer needs approval from the CSSF and the Circular presents the requirements for entities using teleworking in a non-pandemic situation.

• The Internal Revenue Service (IRS) updated on 08/04/2021 its Quality Intermediaries (QI) FAQs, and hereby postponing the (QI) certification deadline. Meaning that IQs with periodic reviews of 2018, 2019 or with a waiver request from this date need a new IQ certificate by 1 December 2021, and IQs with periodic reviews of 2020, have a new deadline of 1 March 2022.

• The CSSF published on 18/02/2021 a revised notification form and an explanatory document, supplementing Circular CSSF 02/77. The form applies to UCITS and SIFs subject to the Law of 13 February 2007 and is aiming to provide the CSSF with information on non-compliance with the investment rules and NAV calculation errors.

• The Administration de l'Enregistrement, des Domaines et de la TVA published on 17/02/2021 Circular 804bis, presenting the new subscription tax rates for UCIs or individual compartments of UCIs with multiple compartments. The Circular is following the Budget Law 2021 and the Law of 19 December 2021.

• The law no. 7637 on dematerialized securities was published on 22/01/2021 in Luxembourg,

The law is seeking to update the current legal framework for dematerialized securities, by accepting the issuance of dematerialized securities using secure electronic registration mechanisms (including distributed electronic databases or registers). Also, this law extends the application of its predecessor, by opening the activity of central account holders for unlisted debt securities to European Union (EU) credit institutions and investment firms.

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