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AN UPDATE ON EU FINANCIAL SERVICES LEGISLATION & ASSOCIATED INITIATIVES

Dr David Doyle, Board Member, Kangaroo Group & EU Policy Director, The Genesis Initiative

Webinar

Thursday, 21 January at 10am GMT

A WORD FROM TODAY'S CHAIRMAN



Professor Michael Mainelli

Executive Chairman

Z/Yen Group



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TODAY'S AGENDA



- 10:00 – 10:05 Chairman's Introduction
- 10:05 – 10:30 Keynote Address - Dr David Doyle
- 10:30 – 10:45 Questions & Answers

TODAY'S SPEAKER



Dr David P. Doyle

Board Member, **Kangaroo Group** (EU Parliament)

EU Policy Director, **The Genesis Initiative**

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POST-BREXIT AND EQUIVALENCE

- ❑ Trade & Cooperation Agreement (24th December): no financial services provisions
- ❑ EC extends the Temporary Equivalence Decision allowing EEA counterparties to continue accessing UK-based CCPs until to mid-2022
- ❑ No access relief for UK under the Share Trading Obligation and the Derivatives Trading Obligation

- ▶ EU revised equivalence assessment built around a “forward-looking model, i.e. interconnectedness with the UK, protecting financial stability, investor protection .
- ▶ EU Equivalence regime not comprehensive: mortgage lending, deposit-taking UCITS and insurance mediation not covered.
- ▶ EC seeks regular EU/UK ‘regulatory dialogue’ combined with equivalence... based on a ‘forward-looking and re-balanced relationship’...
- ▶ EU introduces regulatory access model for 3rd country CCPs, i.e. US & UK entities, seeking to clear derivatives in the 27EU: ESMA empowered to conduct comparable compliance assessment of 3rd country CCPs to verify organisational requirements, business conduct rules, prudential requirements and interoperability arrangements
- ▶ New ECB powers under EU Investment Firms Directive/Regulation from June 2021 to supervise large, systemic EU and 3rd country investment firms (+€30bn assets) required to apply for bank licence. Third-country investment firms branches excluded
- ▶ More granular equivalency assessment of 3rd country firms, under MiFIR with ‘operational conditions’ added by the EC



A QUICK POLL



What in your view are the prospects of an EU Equivalence decision for UK financial services?

- a) In the next 6 months?
- b) Over the next year?
- c) Not at all?
- d) Don't know?

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TOP 6 EU REGULATORY PRIORITIES IN 2021

- **Recovery & Resilience Package** (€750bn), covering workers, businesses and sovereigns
 - Allocated based on National recovery & resilience plans , applicable in in 3Q 2021
 - 37% to be spent on EU climate and green transition activities - 20% on digital innovation
 - EC to raise funds on capital markets on behalf of EU, repayment 2058
 - New funding: 0.2% tax on multinational firms' turnover, digital tax, plastics tax (2021), carbon border tax (2023), FTT (2024)

- Creation of centralized, independent **EU anti-money laundering supervisor** , with direct oversight powers, initially over banks; transform AMLDs into one consolidated EU Regulation

- Application of **regulation on disclosures relating to sustainable investments and sustainability risk** (10 March): disclosure by manufacturers of financial products + financial advisers to end-users. **Taxonomy Regulation**: overarching conditions of economic activity qualifying as environmentally sustainable

- ▶ Completion of **prudential capital Basel III Reforms** (end 2021) , dependant on effectiveness of 'CRR Quick Fix' pandemic prudential measures launched in spring 2020
- ▶ **Relaunched Capital Markets Union action plan**: promotion/facilitating equity financing, reducing reliance on bank funding: support green, digital and resilient economic recovery...
- ▶ **Launch of EC Digital Finance** and a renewed **Retail Payments Strategy**: licensing, artificial intelligence and machine learning (AI/ML), retail payments, cryptocurrency/assets and digital operational resilience, and oversight of 3rd party providers



DE-REGULATION FROM BRUSSELS? THE MIFID « QUICK FIXES »

- ❑ Phase-out of paper-based in favour of **electronic investor communications**, with retail investors to opt-in for paper information
- ❑ Exemption from **cost and charges disclosure** for ECPs and professional investors (ancillary services, costs of advice and financial instruments, including third-party payments) but not cover **investment advice and portfolio management**, nor retail investors
- ❑ For “**distance communication**“, option for all investors (professional and retail) to be suspended on ex-post delivery of costs and charges disclosures — speed critical
- ❑ **Periodic loss reports** — triggered by 10% portfolio losses — dis-applied for ECPs and professional clients (with opt-in), but retained for retail clients on a biannual rather than quarterly basis. Threshold increased to 20% with subsequent reporting after 10%.
- ❑ Exemption from “**complex products**“ in MiFID product governance rules - simple corporate bonds with make-whole clauses , Non-structured UCITS
- ❑ Removing unbundling rules for research/trading commissions for small and mid-cap issuers, ie, SMEs with market capitalization up to €1bn

- ▶ Suspend **best execution reports**, pending 2022 full MiFID assessment on value of these reports
- ▶ Targeted exemption of **a priori** cost-analysis in the case of **product switching** for professional clients

- New definition of professional investor:
 - 20 transactions per year and 2 transactions per year in case of illiquid instruments
 - Portfolio exceeds €350,000
 - Experience also incorporates relevant degree or management portfolio of more than €500,000
 - Undertaking a single transaction of over €100,000



THE LIQUIDITY CHALLENGE IN THE FUND MANAGEMENT SPACE

Securities Markets

- ▶ ESMA warns investment firms of risk to retail clients in heightened trading activity during C-19 crisis (6 May): “under unstable, volatile financial market conditions, provoking increase in market, credit and liquidity risks”
- ▶ Some 80 EU-based funds managing assets over €40b forced to suspend redemption policies, lending weight to ESMA and IMF concerns about adequacy of fund liquidity — even before C-19
- ▶ ESMA consultation on leverage risks in AIF space (March), asking NCA to probe AIF’s that pose risks to financial stability:
 - i. Employ leverage on a substantial basis,
 - ii. have assets under management of €500 or more
 - iii. "unusually high use of leverage", i.e., when compared with the average value of leverage of AIFs of the same type, i.e., hedge funds or funds of funds

European Systemic Risk Board

- ❑ Fund market illiquidity held by asset managers and insurers with unit-linked products: two vulnerable areas of exposure :
- ❑ **Corporate debt** – short redemption periods/open-ended ...Impact of large-scale corporate bond downgrades on markets & financial system
- ❑ **Real estate** - drop in transactions and valuation uncertainty

Action

- System wide restraints on dividends, share-buybacks, other pay-outs
- Liquidity management tools, swing pricing, redemption gates...but huge variation across the EU in availability



Financial Institutions most vulnerable to COVID-19

- ▶ Regional banks in affected areas/highly exposed to affected sectors
- ▶ Select life insurers
- ▶ Trade credit insurers
- ▶ Aircraft lessors and fuel/transport service providers
- ▶ Interest rate or equity market-sensitive service providers
- ▶ Prime money-market funds and closed-end equity/high yield funds

Moody's outlook 2020

ALIGN THE AIFMD, UCITS FUND FRAMEWORKS...ESMA REITERATES TO THE EC

- ❑ Harmonized UCITS and AIF reporting – covering manager & fund-specific data
- ❑ Delegation and substance of tasks: inconsistencies between AIFIM and UCITS lists
- ❑ Supervisory mis-alignment of seconded staff at Manco level, esp. 3rd-country arrangements
- ❑ Where do 'supporting tasks' fit in the AIFMD and UCITS delegated rules?
- ❑ White-label service structures: fund manager Vs business partner conflicts
- ❑ Liquidity testing rules – make it rules-binding!

- ❑ Supervision of cross-border AIF branches
- ❑ Loan origination in AIFMD: types of funds, admitted investors
- ❑ Semi-professional investors: divergent EU approaches, EU Passporting eligible only for professional investors
- ❑ Supervision of sub-thresholds' AIFMs
- ❑ Clarity on definition and application for reverse solicitation



QUESTIONS AND ANSWERS



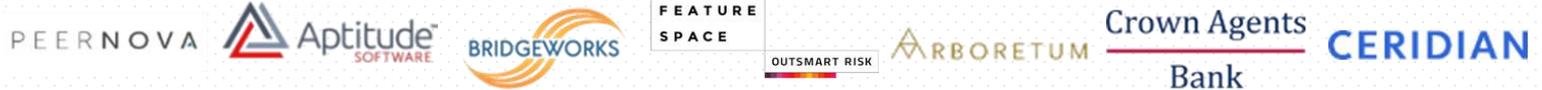


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Forthcoming Events

- Friday 22 Jan (12:00) Owing Your Place In A 21st Century Economy
- Wednesday 27 Jan (11:00) Passion & Purpose – What EU Insurance Mutuals & Cooperatives Have Been Doing Well During Covid-19
- Thursday 28 Jan (10:30) ESOP Centre Webclave
- Friday 29 Jan (16:30) Fully Grown: Why A Stagnant Economy Is A Sign Of Success
- Wednesday 03 Feb (11:00) ESOP Sofa

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