



FINANCIAL REGULATION

Investment services, asset management
and market infrastructure

April - May 2020

INTRODUCTION

Thank you for your interest in Uría Menéndez's *Newsletter on Financial Regulation*.

As a result of an evolving regulatory landscape, it is very important for institutions to identify, assimilate and implement changes in a timely and proper manner. The purpose of this newsletter is to assist financial institutions in this monitoring exercise. It will periodically compile regulatory developments at an international, EU and Spanish level that affect investment services, asset management and market infrastructures. It will also include a section on other matters of general interest.

For the April to May period, we highlight the ESMA's advice to the European Commission on inducements and costs and charges disclosures under Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (MiFID II). Also, the ESMA issued a public statement to clarify issues regarding the publication by execution venues and firms of the general best execution reports required under Regulatory Technical Standard (RTS) 27 and 28 of MiFID II, in light of the COVID-19 pandemic.

Finally, we highlight that the ESMA published its final guidance on performance fees in investment funds, applicable to Undertakings for the Collective Investment in Transferable Securities (UCITS) and certain types of Alternative Investment Funds (AIFs). The aim of these guidelines is to harmonise the way fund managers charge performance fees to retail investors, as well as the circumstances in which performance fees can be paid.

We hope you find this newsletter interesting and that it helps you to stay up-to-date on the financial regulatory framework applicable to the areas mentioned above.

INVESTMENT SERVICES

EU

ESMA

ESMA advises the European Commission on inducements and costs and charges disclosures

ESMA published on 1 April 2020 its advice to the European Commission (EC) on inducements and costs and charges disclosures under Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (MiFID II).

In relation to the disclosure of costs and charges, ESMA has found that the MiFID II disclosure regime generally works well and that it helps investors make informed investment decisions. However, ESMA advises that some disclosure obligations vis-à-vis eligible counterparties and professional investors be scaled back.

ESMA completes review of MiFID II commodity derivatives regime

On 1 April 2020, ESMA published a review report on the impact of position limits and position management on commodity derivatives markets, following over two years of MiFID II.

The report contains proposals to make the commodity derivatives framework operate more efficiently for market participants and competent authorities. This includes refocusing the position limit regime on the most important commodity derivatives contracts, and improving convergent implementation of position management controls by trading venues through Level 2 measures.

ESMA has also published new Technical Advice to the EC on the weekly aggregated information to be published by trading venues on open positions per category of stakeholders.

ESMA provides clarifications for best execution reports under MiFID II

ESMA issued a public statement to clarify issues regarding the publication by execution venues and firms of the general best execution reports required under RTS 27 and 28 of MiFID II, in light of the COVID-19 pandemic. ESMA recommends that National Competent Authorities (NCAs) take into account these circumstances by considering the possibility that:

- execution venues unable to publish RTS 27 reports due by 31 March 2020 may only be able to publish them as soon as reasonably practicable after that date but must do so no later than by the following reporting deadline (i.e. 30 June 2020); and
- firms may only be able to publish the RTS 28 reports due by 30 April 2020 on or before 30 June 2020.

In view of the exceptional circumstances, ESMA encourages NCAs not to prioritise supervisory action against execution venues and firms in respect of the deadlines of the general best execution reports for the periods referred to above.

 **ESMA consulted on standardised information to facilitate cross-border funds distribution**

ESMA launched a consultation on the standard forms, templates, and procedures that NCAs should use to publish information on their websites to facilitate cross-border distribution of funds, covering national laws, regulations and administrative provisions governing marketing requirements for AIFs and UCITS and regulatory fees and charges they levy for carrying out their duties in relation to the cross-border activities of fund managers.

 **ESMA report stresses impact of costs on retail investor benefits**

On 6 April 2020, ESMA published its second annual statistical report on the cost and performance of retail investment products in the European Union (EU).

The analysis contained in this report complements ESMA's risk assessment and supervisory convergence work within its investor protection mandate, and contributes to the EC's project on the cost and performance of investment products under the Capital Markets Union Action Plan.

 **ESMA reminds firms of business obligations under MiFID II**

ESMA issued a public statement on the risks for retail investors when trading under the highly uncertain market circumstances due to the COVID-19 pandemic. ESMA also reminds investment firms of their key conduct of business obligations under MiFID when providing services to retail investors.

In the current environment, ESMA believes that firms have even greater duties when providing investment or ancillary services to investors, especially when these investors are new to the market, or have limited investment knowledge or experience. ESMA therefore reminds firms of their obligation to act in accordance with the best interests of their clients, and points to the most significant conduct of business obligations under MiFID II, namely product governance, information disclosure, suitability and appropriateness.

 **ESMA supports ESRB actions to address COVID-related systemic vulnerabilities**

ESMA published a statement supporting the recommendations issued by the General Board of the European Systemic Risk Board (ESRB). These recommendations are part of a set of actions to address the COVID-19 emergency from a macroprudential perspective.

ESMA expresses its support for the ESRB recommendation, which suggests that relevant NCAs across the EU, coordinated by ESMA, undertake focused supervisory engagement with investment funds that have significant exposure to less-liquid assets, focusing on corporate debt and real estate. In this context, ESMA also welcomes the ESRB public communication regarding the importance of the timely use of liquidity management tools by investment funds and insurers with exposure to less-liquid assets.

CNMV

 **CNMV comments on certain aspects of MiFID II in the context of the public consultation launched by the European Commission in February 2020**

The EC launched an open public consultation on 17 February 2020 to gather stakeholders' views on the experience of two years of application of MiFID II and Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (MiFIR) and to seek views from stakeholders on technical aspects of the current MiFID II/MiFIR regime.

The CNMV's comments cover different areas, such as inducements, client profiling, investment services and activities, market structure and trading obligations.

ASSET MANAGEMENT

EU

ESMA

ESMA publishes guidance on performance fees in UCITS and certain AIFs

On 3 April 2020, ESMA published its final guidance on performance fees in investment funds, applicable to UCITS and certain types of AIFs.

ESMA's guidelines aim at harmonising the way fund managers charge performance fees to retail investors, as well as the circumstances in which performance fees can be paid. The common requirements will enable convergence in how NCAs supervise performance fee models and disclosure across the EU. The guidelines are applicable to both UCITS and certain types of AIFs, in order to ensure a level playing field and a consistent level of protection for retail investors.

ESMA announces update to reporting under the MMFR

ESMA announced that the first reports by Money Market Fund (MMF) managers under Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds (MMFR) should be submitted in September 2020. The original date for submissions was April 2020.

This change in timeline is because there will be an update to the XML schemas that should be used for the reporting, and MMF managers will need additional time to comply with the reporting obligation.

ESMA sets out supervisory expectations on publication of investment funds' periodic reports

On 9 April 2020, ESMA issued a public statement directed at fund managers concerning their obligations to publish yearly and half-yearly reports.

ESMA is of the view that the burdens on fund managers associated with the COVID-19 outbreak should be taken into account by NCAs in a coordinated way. In the current situation, ESMA expects NCAs to adopt a risk-based approach and not prioritise supervisory actions against these market participants in respect of the upcoming reporting deadlines.

ESMA Decision (EU) 2020/525 of 16 March 2020

This ESMA Decision requires natural or legal persons who have net short positions in relation to a share admitted to trading on a regulated market to notify to a competent authority details of any such position if the position reaches or exceeds 0.1% of the issued share capital.

The measure imposed by the ESMA Decision addresses the necessity for NCAs and ESMA to be aware of the net short positions that market participants have entered into in relation to shares admitted to trading on a regulated market, given the recent exceptional developments in financial markets.

 **ESMA announces open hearing on Benchmarks consultation paper**

ESMA held an open hearing for its consultation paper on draft RTS under Regulation (EU) 2016/1011 of the European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds (BMR) on 29 May 2020 via conference call.

The consultation paper seeks the views of interested parties on the proposed draft RTS covering the governance of administrators, methodology of benchmarks, reporting of infringements, mandatory administration of critical benchmarks and the compliance statement. The consultation period will end on 8 June 2020.

 **ESMA consults on guidance to address leverage risk in the AIF sector**

ESMA launched a public consultation on its draft guidance to address leverage risks in the AIF sector. The consultation is part of the ESMA response to the recommendations of the ESRB in April 2018 to address liquidity and leverage risk in investment funds.

ESMA's draft guidelines aim to promote supervisory convergence in the way NCAs assess how the use of leverage within the AIF sector contributes to the build-up of systemic risk in the financial system, as well as how they design, calibrate and implement leverage limits.

 **ESMA published the guidelines on stress test scenarios under MMF**

ESMA published on its website the guidelines on stress test scenarios under the Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on MMF.

International

IOSCO

 **IOSCO report provides new data on global hedge fund industry**

On 15 April 2020, the Board of the International Organization of Securities Commissions (IOSCO) published its 'Report on the Fifth IOSCO Hedge Fund Survey', which provides regulators new insights into the global hedge fund industry and the potential systemic risks this industry may pose to the international financial system.

The report explains the results of the fifth IOSCO survey and provides an overview of the hedge fund industry based on data as of 30 September 2018. Since the first survey was conducted in 2010, data collection has expanded due to enhanced regulatory reporting regimes in some jurisdictions.

LEGISLATION

 **The Council of Ministers approves Royal Decree-Law 11/2020 of 31 March**

Royal Decree-Law 11/2020 of 31 March was approved, adopting urgent complementary measures in the social and economic sphere to address COVID-19 and amending Article 71 septies of Law 35/2003 of 4 November on Collective Investment Institutions, on the supervision of leverage limits, the adequacy of credit evaluation processes and liquidity risk.

The amendment allows the management companies of collective investment institutions to authorise, individually or in respect of a plurality of them, the establishment of notice periods for redemptions in one or more collective investment institutions managed by them without subjecting them to the requirements of term, minimum amount and prior record in the management regulations applicable on a regular basis.

MARKET INFRASTRUCTURES

EU

ESMA

ESMA publishes advice on fines and penalties for third country CCPs

ESMA published its final technical advice to the EC on procedural rules for imposing fines and penalties on third country central counterparties (TC-CCPs) and alignment of those for trade repositories (TRs) and credit rating agencies (CRAs).

ESMA included advice on specific aspects, including the right to be heard by the independent investigation officer, access to the file, and the procedure for imposing fines.

ESMA extends MiFID II/MiFIR transparency review report consultation to 14 June 2020

ESMA decided, in view of the effects of the ongoing COVID-19 pandemic on stakeholders and market participants, to further extend the response date for the consultation on the MiFID II/MiFIR review report on the transparency regime for non-equity instruments and the trading obligation for derivatives to 14 June 2020.

ESMA clarifies position on SFTR backloading

ESMA issued a revised version of its 19 March public statement on coordinated supervisory actions on the application of Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse (SFTR).

The revised statement clarifies that SFTs concluded between 13 April 2020 and 13 July 2020 and SFTs subject to backloading under SFTR are also issues which competent authorities are not expected to prioritise in their supervisory actions towards counterparties, entities responsible for reporting and investment firms in respect of their reporting obligations under SFTR or MiFIR and recommends that they generally apply their risk-based approach in the exercise of supervisory powers in their day-to-day enforcement of applicable legislation in this area in a proportionate manner.

ESMA publishes annual bond transparency calculations, systematic internalisers calculations and new bond liquidity data

ESMA has made available, under MiFID II and MiFIR:

- the annual transparency calculations of the large in scale (LIS) and size specific to the instruments (SSTI) thresholds for bonds;
- systematic internaliser calculations for equity, equity-like instruments and bonds; and
- new data for bonds subject to the pre-trade and post-trade requirements of MiFID II and MiFIR.

ESMA consulted on SME Growth Market

ESMA launched a consultation on the functioning of the Small and Medium-sized enterprises (SME) Growth Market regime in the EU and on two draft technical standards, introduced by the amendments to Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (MAR) for the promotion of the use of SME Growth Markets.

ESMA aims to promote and facilitate access to capital markets for SMEs, acknowledging their key role in the economic growth of the EU. In the context of the MiFID II review on the functioning of SME Growth Markets in the EU, ESMA seeks stakeholders' views on proposed amendments to the regime which aim to further improve it.

ESAs published a joint new draft RTS on the risk mitigation techniques for OTC derivative contracts not cleared by a CCP under EMIR in response to the COVID-19 outbreak

In response to the COVID-19 outbreak, the European Supervisory Authorities (European Banking Authority, European Insurance and Occupational Pensions Authority and ESMA) have published joint draft RTS to amend the Commission Delegated Regulation (EU) 2016/2251 of 4 October 2016 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories (EMIR) with regard to RTS for risk-mitigation techniques for over the counter (OTC) derivative contracts not cleared by a central counterparty (CCP), to incorporate a one-year deferral of the two implementation phases of the bilateral margining requirements.

International

IOSCO

Basel Committee and IOSCO announce deferral of final implementation phases of the margin requirements for non-centrally cleared derivatives

In light of the significant challenges posed by COVID-19, including the displacement of staff and the need for firms to focus resources on managing risks associated with current market volatility, the Basel Committee on Banking Supervision (BCBS) and IOSCO have agreed to extend the deadline for completing the final two implementation phases of the margin requirements for non-centrally cleared derivatives by one year. This extension will provide additional operational capacity for firms to respond to the immediate impact of COVID-19 and, at the same time, assist covered entities to act diligently to comply with the requirements by the revised deadline.

OTHERS

EU

EUROPEAN COMMISSION

Consultation on a new digital finance strategy for Europe / FinTech action plan

As set out in the EC work programme, given the broad and fundamental nature of the challenges ahead for the financial sector, the EC will propose in the third quarter of 2020 a new digital finance strategy / FinTech action plan that sets out a number of areas that public policy should focus on in the next five years.

This new strategy will build on the work carried out during the previous mandate, in particular in the context of the FinTech action plan. It will take into consideration all the recent market and technological developments that are likely to impact the financial sector in the near future.

Responses to this consultation will inform forthcoming work on a digital finance strategy / FinTech action plan.

Statement by the EU Technical Expert Group on Sustainable Finance

The EU Technical Expert Group on Sustainable Finance (TEG), established to advise the EC on implementation of the Action Plan on Financing Sustainable Growth, believes the Sustainable Taxonomy, EU Green Bond Standard, and Paris-Aligned and Climate Transition Benchmarks can guide public and private sector plans for recovery from the COVID-19 pandemic, including the European Council's recently announced Roadmap to Recovery.

Action plan for a comprehensive EU policy on preventing money laundering and terrorism financing

On 7 May 2020, the EC adopted an action plan for a comprehensive EU policy on preventing money laundering and terrorism financing.

The action plan builds on six pillars:

- Effective implementation of existing rules
- A single EU rulebook
- EU-level supervision
- A support and cooperation mechanism for financial intelligence units
- Better use of information to enforce criminal law
- A stronger EU in the world

ESMA

ESMA updates its risk assessment in light of the COVID-19 pandemic

On 2 April 2020, ESMA updated its risk assessment to account for the impact of the COVID-19 pandemic.

The pandemic, in combination with existing valuation risks, has led to large equity market corrections since mid-February, driven by a sharp deterioration of the economic environment and in the outlook for consumers and businesses. Corporate bond and government bond markets and a number of investment funds show signs of stress. Market infrastructures have continued to function in an orderly manner despite significant surges in trading activity, the use of circuit breakers and increases in derivatives margins.

ESMA issues a no-action letter on the new ESG disclosure requirements under the BMR Regulation and an opinion regarding relevant Delegated Acts

ESMA issued a no-action letter to promote coordinated action by NCAs regarding the new environmental, social and governance (ESG) disclosure requirements for benchmark administrators under the BMR Regulation. It also issued an Opinion to the EC on the need for prompt adoption of the relevant Delegated Acts.

ESMA considers that it is necessary for NCAs to address the absence of the Delegated Acts through consistent risk-based supervisory and enforcement practices.

ESRB

Policy measures in response to the COVID-19 pandemic

The ESRB pointed out that the dialogue between macroprudential authorities and fiscal authorities is of utmost importance to assess the implications for financial stability, including cross-border and cross-sector aspects, as well as stressed that, if used in a timely manner, liquidity management tools may in particular help those funds that invest in less-liquid assets or assets that become temporarily illiquid and have short redemption periods.

Regarding the corporate bond sector, which has been impacted by the weak economic outlook due to the coronavirus pandemic, the ESRB is assessing the impact of a common scenario of large-scale ratings downgrades across the financial sector.

The making of a cyber crash: a conceptual model for systemic risk in the financial sector

Building on the work carried out by the European Systemic Cyber Group, this paper, published in the Occasional Paper Series of the ERSB, describes a conceptual model for systemic cyber risk and tries, among other aims, to provide a structured approach to describe cyber incidents and to demonstrate the link between the crystallisation of cyber risk in a firm-specific context and the possible ramifications for the financial system.

Spain

CNMV

CNMV decides not to renew the current prohibition on creating or increasing net short positions

The CNMV has decided not to extend the ban on creating or increasing net short positions, in force since 17 March 2020, which was extended on 15 April 2020 and on which the CNMV published a question-and-answer paper on 17 April.

Consequently, the ban ceased to apply from 18 May 2020 at 23:59.

International

IOSCO

IOSCO reprioritises its work programme to address the impact of COVID-19

IOSCO agreed to pause or delay some of its work in 2020 in order to redirect its resources to focus on the multiple challenges securities market regulators are facing as a result of the COVID-19 crisis.

In view of these principles, IOSCO agreed to redeploy resources to focus primarily on matters that are directly impacted by COVID-19. Among other things, substantial resources are being devoted to addressing the areas of market-based finance that are most exposed to heightened volatility, constrained liquidity and the potential for pro-cyclicality.

FSB

The 17th meeting of the FSB MENA group discusses regional financial stability and the impact of COVID-19

The Financial Stability Board (FSB) Regional Consultative Group (RCG) for the Middle East and North Africa (MENA) held its 17th RCG MENA meeting via a conference call on 2 April 2020 to discuss recent macroeconomic and financial market developments, including the financial stability implications of COVID-19.

Members discussed the current strains on the global financial system and financial sector tensions in some member jurisdictions and the measures taken by national authorities to mitigate the economic and financial stability effects of COVID-19. RCG MENA members agreed that, as a result of the post-crisis reforms, the global financial system is now in a better position to withstand shocks, maintain market functioning and sustain the supply of financing to support the real economy.

 **FSB consults on regulatory, supervisory and oversight recommendations for “global stablecoin” arrangements**

On 14 April 2020, the FSB published for consultation 10 high-level recommendations to address the regulatory, supervisory and oversight challenges raised by “global stablecoin” arrangements.

The FSB’s recommendations call for regulation, supervision and oversight that is proportionate to the risks, and stress the need for flexible, efficient, inclusive, and multi-sectoral cross-border cooperation, coordination and information-sharing arrangements that take into account the evolution of “global stablecoin” arrangements and the risks they may pose over time. They apply the principle of ‘same business – same risks – same rules’, independent of the underlying technology.

The report also highlights key international financial regulatory standards from the Basel Committee, the Financial Action Task Force, the Committee of Payments and Market Infrastructures and the International Organization of Securities Commissions that could apply to “global stablecoins”.

 **FSB publishes report on effective practices for cyber incident response and recovery**

On 20 April 2020, the FSB published a consultation report on ‘Effective Practices for Cyber Incident Response and Recovery’, which was sent to G20 Finance Ministers and Central Bank Governors for their virtual meeting on 15 April. The toolkit of effective practices aims to assist financial institutions in their cyber incident response and recovery activities.

The toolkit lists 46 effective practices, structured across seven components (among them, governance, analysis, mitigation and restoration).

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