



# Regulatory Insights

August - September 2024



# Anti-Money Laundering

FATF updates methodology for assessing compliance and effectiveness of AML/CFT/CPF systems

On 29 August 2024, the Financial Action Task Force (FATF) updated its [methodology for assessing countries' technical compliance with FATF Recommendations and the effectiveness of AML/CFT/CPF systems](#). This revised methodology will guide FATF's fifth round of evaluations and emphasises a comprehensive understanding of countries' risks, contexts, and effectiveness in achieving AML/CFT/CPF outcomes. The assessment process focuses on two main areas:

*Effectiveness:* evaluations will prioritise the effectiveness of laws and policies in protecting the financial system from abuse. Countries must show they have robust frameworks tailored to their specific risks. The assessment team will examine 11 key areas to assess how effective a country is in combating these issues.

*Technical compliance:* assessments will also review whether countries have established the necessary legal frameworks and regulations aligned with the FATF's 40 recommendations. This framework is essential for preventing criminals from profiting from their activities and stopping terrorist financing.

The updated methodology includes refined criteria for technical compliance, prioritisation of effectiveness outcomes, and enhanced guidance for assessors. This ensures a more nuanced assessment that better reflects the evolving complexities of global financial systems and the threats posed by money laundering, terrorist financing, and the proliferation of weapons of mass destruction. The methodology aims to provide a more accurate and practical framework for evaluating and improving national AML/CFT/CPF regimes, ensuring that countries not only comply with technical standards but also effectively combat financial crimes. The FATF began its fifth round of evaluations under this updated methodology in 2024, and regional bodies will adopt the methodology once they finish their current evaluations. The previous 2013 FATF Methodology will still be used for countries undergoing earlier evaluations and related follow-ups.



# Asset Management

## EFAMA publishes Insights on sustainable equity UCITS

On 24 September 2024, the EFAMA released its latest edition of the Market Insights series, titled “[Sustainable Equity UCITS: Promoting sustainable business models](#)”. This report provides a comprehensive analysis of the trends and dynamics in the sustainable equity UCITS market, highlighting the substantial growth in net assets and the evolving landscape of investor preferences in recent years.

### Key findings:

- ❑ In 2023, sustainable equity UCITS represented 24% of all sustainable UCITS, up from 15% in 2019. Over the past five years, the net assets of these funds have more than doubled, rising from EUR 0.6 trillion to EUR 1.3 trillion.
- ❑ Despite market volatility and economic challenges, sustainable equity UCITS have shown remarkable resilience, particularly in 2021 when net inflows reached EUR 231 billion. Although net inflows declined in 2022 and 2023, demand for these funds remained strong compared to global trends, reflecting investor confidence in sustainable investments.
- ❑ Nearly 20% of sustainable equity UCITS are classified as Article 9 funds, while 70% fall under Article 8. This classification indicates cautious investor sentiment amid ongoing regulatory uncertainties. The upcoming review of the Sustainable Finance Disclosure Regulation (SFDR) is expected to clarify definitions and enhance support for transition finance.
- ❑ On average, sustainable equity funds have consistently delivered positive net performance, comparable to that of non-sustainable equity UCITS. Additionally, these funds tend to be cost-effective, making them attractive options for sustainability-conscious investors.

## EFAMA Expands European Fund Classification System

As per the EFAMA publication the [European Fund Classification](#) (EFC), a comprehensive pan-European classification system for investment funds overseen by the EFAMA, has significantly expanded its reach. It now covers nearly 180,000 fund share classes across most European countries, meaning that the majority of European funds are now classified under the EFC.

The latest update introduces several new fund categories to reflect evolving market trends. The EFC now includes over 880 fund subcategories, with recent additions such as: (i) Crypto asset funds, (ii) FX funds and (iii) Ultra-short bond funds.

The EFC is entirely owned and managed by the fund industry. It is provided free of charge to both fund managers and data users. The classification process operates on a non-commercial basis, with results accessible to all interested parties via the EFC webpage or tailored data feeds.

# Banking & Finance (1)

## EBA launches 2024 EU-wide transparency exercise

On 9 September 2024, the EBA initiated its annual EU-wide transparency exercise, providing key insights into the health and stability of Europe's banking sector as we approach the 2025 stress tests. The findings from this exercise will be published at the end of November, coinciding with the release of the Risk Assessment Report (RAR).

This year, the EBA is collaborating with over 100 major EU banks to gather data exclusively from supervisory reporting. The exercise will examine various aspects, including capital positions, profitability, financial assets, risk exposure amounts, sovereign exposures, and asset quality.

Since its inception in 2011, the EU-wide transparency exercise has played a vital role in overseeing the EU banking sector. It aims to enhance transparency and bolster public confidence in the resilience and stability of the EU financial system by providing detailed data and innovative visualisation tools. This exercise works in tandem with the EBA's biannual stress tests, utilising supervisory reporting data to present a comprehensive overview of banks' capital strength and risk profiles. Notably, in 2019, the EBA expanded this initiative to include quarterly disclosures, significantly increasing the amount of information accessible to the public.

## Q2 2024 Risk Dashboard (RDB), providing summary statistics for major EU/EEA banks

On 19 September 2024, the EBA published its [quarterly Risk Dashboard](#) (RDB) for Q2 2024, providing aggregated statistical data for the largest banks in the EU and EEA. The return on equity (RoE) for EU/EEA banks remained relatively stable year-on-year at 10.9%, a decrease of just 10 basis points from the previous year. However, on a quarterly basis, RoE saw a 30 basis point increase, primarily due to a rise in other operating income. The net interest margin (NIM) experienced a slight decline, falling to 1.68% in Q2 from 1.69% in Q1 and 1.60% a year earlier, suggesting it may have peaked in Q1 2024.

Despite some growth in volumes, this did not fully offset the negative effects of the NIM, leading to a minor decrease in net interest income for the quarter.

Additionally, the common equity tier 1 (CET1) ratio for EU/EEA banks rose by 10 basis points on a fully loaded basis, reaching 16.1% in Q2 2024. Both the liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) also saw improvements during the second quarter, increasing from 161.7% to 163.2% and from 127.3% to 127.8%, respectively.

Within the LCR's numerator, the proportion of cash and reserves held by banks decreased, while the share of central government assets increased. Loans to households and non-financial corporations showed a slight increase over the quarter. Sovereign exposures grew by approximately EUR 200 billion (+5.5%) since the end of the previous year, accompanied by a higher share of exposures recognised at fair value and a shift toward shorter-term maturities.

The non-performing loan (NPL) ratio remained stable at 1.9%, although there were significant variations across different segments.

# Banking & Finance (2)

## Delegated Regulation on 2021 update of ESEF taxonomy

On 30 November 2021, the EU Commission published a [Delegated Regulation](#) amending the 2019 regulation on the single electronic reporting format (ESEF). This update introduces technical changes to the taxonomy that issuers on EU-regulated markets must use when marking up IFRS consolidated financial statements in their annual financial reports. Key changes include amendments to Annex I and Annex VI of the existing ESEF regulatory technical standards, as outlined in the newly issued delegated act.

## The EBA and ECB release a joint report on payment fraud

On 1 August 2024, the EBA and the ECB released a [joint report](#) on payment fraud data in the European Economic Area (EEA). The report reveals that payment fraud totaled €4.3 billion in 2022 and €2.0 billion in the first half of 2023, highlighting the positive impact of strong customer authentication (SCA) in reducing fraud. The report includes an analysis of total payment transactions alongside fraudulent ones, categorising them by payment types such as credit transfers, direct debits, card payments, cash withdrawals, and e-money transactions. It finds that SCA-authenticated transactions have significantly lower fraud rates compared to non-SCA transactions, particularly for card payments. Notably, fraud rates for card transactions are ten times higher when the transaction is with parties outside the EEA, where SCA is not legally required. These findings underscore the effectiveness of the SCA requirements established by PSD2 and the technical standards developed by the EBA and ECB in 2018. The report also notes that fraud losses vary depending on the payment instrument used. Going forward, the EBA and ECB will continue to monitor fraud data and publish aggregated figures annually. This initial report presents descriptive observations, while future editions will include analyses of trends and explanations of the data.

## The EBA amends technical standards specifying the data collection for the 2025 benchmarking exercise

The EBA released on 9 August 2024 its final [draft Implementing Technical Standards](#) (ITS), which amend the Implementing Regulation concerning the benchmarking of credit risk, market risk, and IFRS 9 models for the 2025 exercise. The most notable change is within the market risk framework, where the EBA plans to extend the alternative standardised approach (ASA) validation portfolios to all asset classes, differing from the 2024 exercise. For credit risk, only minor adjustments have been suggested. Regarding market risk, templates based on the alternative internal model approach (AIMA) have not been implemented due to a Delegated Act from the EU Commission that delays the Fundamental Review of the Trading Book (FRTB) in the EU. As a result, both the content and sample of banks for data collection in market risk remain unchanged from the 2024 exercise. The data collection deadlines have been postponed to provide banks with additional time in light of the delay in publishing this amending ITS. In terms of credit risk, the minor amendments clarify the mandatory reporting of probability of default (PD) and loss given default (LGD) risk parameters, where applicable, in relation to the margin of conservatism (MoC), regulatory add-ons, and downturn components. Additionally, the amendments address the use of internal model IDs utilised by the competent authorities.



# Banking & Finance (3)

The EBA responds to the EU Commission's Delegated Act postponing the application of the market risk framework in the EU

EBA releases final draft technical standards on market risk for EU Banking package Implementation

Following the EU Commission's adoption of a Delegated Act to delay the application of the revised market risk framework in the EU, known as the Fundamental Review of the Trading Book (FRTB), the EBA published a [no-action letter](#) addressing the boundary between the banking book and the trading book. The letter outlines the EBA's views on technical questions and issues arising from this postponement. In the no-action letter, the EBA advises that competent authorities should not prioritise any supervisory or enforcement actions related to the amendments concerning the boundary between the banking and trading books or those that define internal risk transfers between them. The EBA clarifies that the points made in a previous no-action letter on this topic issued in 2023 still apply. The EBA believes that implementing the revised provisions on the boundary and internal risk transfers ahead of the rest of the FRTB framework would create operational complexity and unnecessary costs for institutions. It also notes that no jurisdictions globally plan for such a two-step implementation of the FRTB framework. This could result in global institutions facing vastly different regulatory requirements based on their risk management locations, leading to fragmentation of the regulatory framework. Additionally, the EBA addresses several [technical questions and implementation issues](#) arising from the postponement that are crucial for achieving a harmonised implementation of the market risk framework across institutions during this period. The letter also clarifies aspects related to the supervisory benchmarking exercise.

On 13 August 2024, the EBA published [final amendments to its Regulatory Technical Standards \(RTS\) on the Fundamental Review of the Trading Book \(FRTB\)](#). These revisions primarily aim to align the RTS with the Capital Requirements Regulation (CRR3) and maintain stability within the regulatory framework. The RTS form part of the broader banking package roadmap. The CRR3 introduced several changes to the FRTB and mandated the EBA to update existing RTS to conform to the new Level 1 text. Specifically, the EBA has been tasked with reviewing the RTS concerning the treatment of foreign exchange and commodity risk in the banking book, the RTS on profit and loss attribution tests, and the RTS on risk factor modellability assessments. Regarding the profit and loss attribution test, the RTS eliminates the aggregation formula used to calculate total own funds requirements for market risk for institutions employing the alternative internal model approach, as this formula has now been incorporated into CRR3. In terms of risk factor modellability assessments, the RTS ensure that institutions can clearly identify their reliance on third-party vendors when assessing the modellability of a risk factor. Lastly, concerning the treatment of foreign exchange and commodity risk in the non-trading book, the RTS confirm that translation risk is adequately captured by institutions.

# Securities & Markets (1)

**The future of EU competitiveness : report by Mario Draghi**

On 10 September 2024, the EU Commission has released [a report](#) prepared by Mario Draghi, former President of the European Central Bank, which addresses the challenges industries and businesses face within the Single Market and outlines Draghi's vision for the future of European competitiveness. This report, along with Enrico Letta's [in-depth analysis and recommendations](#), on the Single Market, will shape the EU's strategy for promoting sustainable prosperity and competitiveness. Draghi emphasised the need for outward-looking industrial policies, focusing on ten key sectors, and highlighted the importance of scalability, public goods investment, and securing essential resources. His insights will be critical in guiding the development of the forthcoming Clean Industrial Deal, aimed at strengthening competitive industries and creating quality jobs, to be unveiled within the first 100 days of the new Commission's mandate. Both reports are set to influence the EU's strategic agenda for 2024-2029, focusing on green and digital transitions, competitiveness, and the Capital Markets Union.

**ESMA announces next steps for the selection of Consolidated Tape Providers (CTPs)**

ESMA has announced further details on selecting Consolidated Tape Providers (CTPs) for bonds, shares, and ETFs. ESMA will begin the selection process for bond CTPs on 3 January 2025, the first working day after 29 December 2024, as per MiFIR Article 27da(1). A decision on the chosen provider is expected by July 2025. The selection process for shares and ETFs will follow in June 2025, with a decision anticipated by the end of the year. Contract notices and procurement documents will be available on the EU Funding & Tenders portal, and ESMA will provide guidance and answer questions throughout the application period. These timelines align with MiFIR regulations and aim to foster healthy competition and strong proposals.

For further background information, please visit ESMA's announcement on the next steps for CTP selection [here](#).



# Securities & Markets (2)

## ESMA publishes second risk monitoring report for 2024

ESMA has released its [second risk monitoring report for 2024](#), highlighting key risk drivers affecting EU financial markets. The report indicates that external events are significantly influencing market trends, leading to high overall risks within ESMA's jurisdiction. Despite a period of reduced volatility earlier this year, recent developments reveal that markets are sensitive to interest rate changes, credit risks, and political events. ESMA Chair Verena Ross noted that market anxiety has increased due to economic uncertainties and political developments, which has resulted in a dip in equity valuations and heightened volatility.

### Key Insights:

**Market conditions:** The market appears to be experiencing a 'gentle slowdown,' with signs in early 2024 indicating that investors are actively seeking yield. However, weak market liquidity raises the risk of sudden corrections.

### Structural developments:

- ❑ **Market-based finance:** Capital availability remains stable, but equity issuance is challenging. Corporate bond issuance peaked in Q1 but declined in Q2, leading to concerns about corporate debt sustainability.
- ❑ **Sustainable finance:** Interest in sustainable investments remains strong, but the recent slowdown in green bond issuance and fund outflows has raised concerns about mobilising private capital.
- ❑ **Financial innovation:** The crypto-assets market surged, with a total global market valuation reaching €2.2 trillion by June. However, recent market volatility has affected crypto valuations.

### Market monitoring:

- ❑ **Securities markets:** Asset prices initially trended upward, but market volatility was observed during recent elections and economic indicators in August. High-yield corporate bond spreads have decreased, yet the credit quality of high-yield non-financials, particularly in real estate, continues to decline.
- ❑ **Asset management:** Overall fund performance was positive, with inflows into bond funds. However, deteriorating credit quality raises concerns about a potential disorderly repricing of risky assets, particularly in open-ended real estate funds.



# Sustainable Finance

**EU Commission releases FAQs on EU corporate sustainability reporting rules**

On 7 August 2024, the EU Commission published a set of FAQs on the implementation of the EU Corporate Sustainability Reporting Directive (CSRD) and the interpretation of key provisions in related directives, such as the Accounting Directive, Transparency Directive, and Sustainable Finance Disclosure Regulation. These FAQs address topics like scope, timing, and exemptions, with tools like a flowchart to help determine an entity's reporting obligations and a table outlining application dates for different undertakings. Additionally, the FAQs touch on elements of the European Sustainability Reporting Standards (ESRS). EFRAG, which developed the ESRS, has also released the latest implementation guidance, available since May 2024. For more information, you can access the FAQs [here](#) and the ESRS guidance [here](#).



# Glossary

AIF	Alternative Investment Fund (EU)
AIFMD	Directive 2011/61/EU on Alternative Investment Fund Managers
AIFMs	Alternative Investment Fund Managers
AML/CFT	Anti-Money Laundering/Countering the Financing of Terrorism
CSRD	Corporate Sustainability Reporting Directive
CySEC	Cyprus Securities and Exchange Commission
EBA	European Banking Authority
ECB	European Central Bank
EIOPA	European Insurance & Occupational Pensions Authority
EFAMA	European Fund and Asset Management Association
ESG	environmental, social, and governance
EMIR	European Market Infrastructure Regulation
ESAs	European Supervisory Authorities (EBA, EIOPA and ESMA)
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board EU European Union
ICT	Information and Communication Technology
MiCA	Regulation of the European Parliament and of the Council on markets in crypto-assets
MiFID	Markets in Financial Instruments Directive
NCA	National Competent Authority
RTS	Regulatory Technical Standards
SFDR	Sustainable Finance Disclosure Directive
OECD	Organisation for Economic Co-operation and Development
OJ	Official Journal
UCITS Directive	directive 2009/65/EC on Undertakings for Collective investments in Transferable Securities
UCITS	Undertakings for Collective investments in Transferable Securities (EU)



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