



Regulatory insights

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European updates

ESG & Sustainability Finance

First Set of ESRS published in EU's Official Journal

On 22 December 2023, [Delegated Regulation \(EU\) 2023/2772](#) (Delegate Regulation) was published in the EU's Official Journal. It contains the first set of European sustainability reporting standards ("ESRS") specifying the information that undertakings are required to report in accordance with the Accounting Directive (2013/34/EU) as amended by the Corporate Sustainability Directive ((EU) 2022/2464).

The ESRS will help investors understand the sustainability impact of the companies in which they invest. There are twelve ESRS, covering the full spectrum of sustainability concerns, comprised of two cross-cutting standards and ten topical standards.

Annex I to the Delegated Regulation sets out the following ESRS applicable to all in-scope undertakings, namely large undertakings, small and medium-sized undertakings with securities admitted to trading on EU regulated markets, and parent undertaking of large groups:

- cross-cutting standards covering general requirements (ESRS 1) and general disclosures (ESRS 2);
- specific standards on environmental disclosures covering climate change (ESRS E1), pollution (ESRS E2), water and marine resources (ESRS E3), biodiversity and ecosystems (ESRS E4) and resource use and circular economy (ESRS E5);
- specific standards on social disclosures covering own workforce (ESRS S1), workers in the value chain (ESRS S2), affected communities (ESRS S3) and consumers and end-users (ESRS S4); and
- specific standards on governance (ESRS G1).

Annex II sets out acronyms and a glossary of terms.

The Delegated Regulation entered into force on 25 December 2023 and applies from 1 January 2024 for financial years beginning on or after 1 January 2024.

Draft RTS on the review of Principles Adverse Impact (PAI) and financial product disclosures under SFDR

The ESAs published on 4 December 2023 their [Final Report](#) amending the draft Regulatory Technical Standards (RTS) to the delegated regulation supplementing the SFDR. The purpose of the ESAs' review is to extend and simplify sustainability disclosures.

The proposed changes to the SFDR RTS in the Final Report can be grouped in four main categories:

1. Changes related to the PAI framework:

These include (i) the addition of new mandatory and opt-in social indicators (e.g. "Exposure to companies active in the cultivation and production of tobacco" and "Employees earning less than an adequate wage", among others) and (ii) the modification of existing social and environmental indicators (e.g. "Rate of recordable work-related injuries" or "Exposure to companies active in the fossil fuel sector", among others).

Other changes encompass the basis to be used for PAI calculation, which remains "all investments"; the disclosure of the share of PAI that is estimated (or reasonably assumed) which becomes mandatory; the treatment of derivatives which should be converted to economic exposure, and the treatment of companies' value chains which only need to be included in the PAI calculations where the investee company reports on that value chain.

2. Changes related to the GHG emissions reduction targets:

These include new disclosures for financial products on GHG emissions reduction targets, including intermediary targets and milestones, where relevant, and actions pursued. The said disclosures apply to products having GHG emissions reduction as their investment objective under article 9(3) of SFDR, although simplified disclosures still apply to products that passively track EU Climate Transition Benchmark (EU CTB) or EU Paris-aligned Benchmark (EU PAB).

The technicalities in terms of metrics, baseline, and calculation methodologies for such GHG emissions targets are further specified.

3. Changes related to the SFDR templates:

Various propositions are put forward to simplify the templates for pre-contractual and periodic disclosures.

Significant changes include revising the front page to introduce a dashboard, restructuring the information provided to avoid repetition, removing the green color, and generally refocusing the templates on their four essential elements (according to the ESAs): (i) Sustainable investments; (ii) Taxonomy-aligned investments; (iii) PAI; and (iv) GHG emissions reduction targets

The new proposed templates have also been designed to be delivered electronically, meaning that sections can be extended by clicking.

4. Other notable changes include:

- Improvements to the disclosures on how sustainable investments "Do No Significant Harm" (DNSH) to the environment and society;
- Simplification of the pre-contractual and periodic disclosure templates for financial products; and
- Other technical adjustments concerning, among others, the treatment of derivatives, the calculation of sustainable investments, and provisions for financial products with underlying investment options.

The EU Commission will study the draft RTS and decide whether to endorse them within three months. These draft RTS would be applied independently of the [comprehensive assessment](#) of SFDR announced by the EU Commission in September 2023 and before changes resulting from that assessment would be introduced.

The revised SFDR RTS are not expected to enter into effect before Q2 2024 at the earliest.

Political Agreement on the Corporate Sustainability Due Diligence Directive

On 14 December 2023, the Council of the European Union (the “Council”) and the European Parliament each issued a press release announcing that a “provisional agreement” regarding the draft Corporate Sustainability Due Diligence Directive (“CSDDD”) has been reached.

While the final wording of the provisional agreement between the European Parliament and the Council has not been published, an overview of the expected content has been provided in a press release. This includes:

1. Scope

For EU companies, it has been agreed to fix the scope of the directive as large companies that have more than 500 employees and a net worldwide turnover of more than EUR 150 million. The directive will also apply to EU companies with more than 250 employees and with a turnover of more than EUR 40 million if at least EUR 20 million is generated in certain high-risk sectors, such as textiles, clothing, footwear, forestry, fishery, mining construction.

For non-EU companies, the scope will be non-EU companies and parent companies with equivalent turnover in the EU, albeit that the Council’s press release states that non-EU companies are within the scope only if they have such net turnover in the EU, three years after the entry into force of the CSDDD.

The financial sector will be excluded from the scope of the directive temporarily but will be subject to inclusion depending on impact assessment.

2. Penalties

Each EU member state will be obligated to designate a supervisory authority to monitor companies’ compliance with the directive, launch inspections and investigations, and impose penalties on non-compliant companies, including fines of up to 5% of the violators’ net worldwide turnover.

3. Definitions

The agreement contains a list of specific rights and prohibitions that shall be deemed to constitute an adverse human rights impact when they are abused or violated. The list refers to international instruments that have been ratified by all EU member states and that set sufficiently clear standards that can be observed by companies. It also refers to UN conventions such as the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural rights, and the Convention on the Rights of the Child.

In terms of the environment, the directive will cover measurable environmental degradation, such as harmful soil change, water or air pollution, harmful emissions, excessive water consumption, or other impacts on natural resources.

The provisional agreement needs to be endorsed and formally adopted by the Council and the European Parliament. The concrete timeline is not clear based on the press release.

Fact sheet published by the ESAs on Q&A on sustainable finance

The ESAs published an [interactive factsheet](#) entitled “*Investments, Loans, Insurance or Pensions with a Sustainable Focus: What do you need to know?*” that answers consumers’ most frequently asked questions about sustainable finance.

The factsheet provides tips to consumers considering buying financial products with sustainability features, including loans, investments, insurances, and pensions. The factsheet provides answers to frequently asked questions and steps consumers can take to understand how their financial choices could contribute to a more sustainable future. In addition, the factsheet provides four tips consumers should take into account before choosing financial products with sustainability features.

Consumers are encouraged to:

- i. decide how important sustainability is for them and what financial goals they want to achieve before they choose a product;
- ii. pay attention to the conditions and the sustainability features, to avoid being misled by ‘greenwashing’;
- iii. keep in mind that financial products with sustainability features are not risk-free;
- iv. for investments and life insurance policies, take their time before deciding and, if need be, seek further clarification from the firm or person that can advise them on and sell them such products.

Asset Management

ESMA publishes draft RTS pursuant to ELTIF 2.0

ESMA published on the 19 December 2023 the [final report](#) setting out the draft Regulatory Technical Standards (RTS) for the European Long-Term Investment Fund (ELTIF) Regulation (EU) 2015/760 as amended by Regulation 2023/606/EU.

The draft RTS provide, among others, a detailed framework for the following areas that are relevant where an ELTIF's rules or instruments of incorporation provide for the possibility of redemptions during the life of the ELTIF.

Minimum holding period:

ESMA suggest allowing the ELTIF manager to select the minimum holding period that is best adjusted to an individual ELTIF, based on criteria set in the RTS, and upon justifications to the competent authority.

Maximum redemption frequency:

ESMA proposes to include a common standard (maximum quarterly redemption frequency), while allowing the ELTIF manager to deviate from it, upon justifications to the competent authority.

Choice of liquidity management tools:

It is suggested the mandatory implementation of at least one anti-dilution mechanism, which could be anti-dilution levies, swing pricing or redemption fees (in addition to the notice period), as well as redemption gates (in exceptional circumstances only), while allowing the ELTIF manager to deviate, in specific circumstances, and upon justifications provided to the ELTIF's competent authority.

Notice period and maximum percentage of liquid assets that can be redeemed:

In addition to applying varying lengths of the notice period (from 12 months to less one month) calibrated depending on the minimum percentages of liquid assets, different percentages of maximum amount of liquid assets that can be redeemed are also applied. In its press release, ESMA states that the draft RTS seek to reach a balance by proposing prescriptive rules, while allowing ELTIF managers to deviate from these rules under specific circumstances.

ESMA submitted the draft RTS to the EU Commission for endorsement and final approval. From the date of submission, the EU Commission shall take a decision on whether to adopt the RTS within three months. The EU Commission may extend that period by one month. Once the EU Commission adopts the draft RTS, the EU Parliament and the Council of the EU will have a period of three months to scrutinise the adopted draft RTS.

Given the importance of the RTS entering into force as soon as possible after the date of application of the ELTIF 2.0 regime, that is 10 January 2024, ESMA proposes that the RTS enter into force on the day following their publication in the Official Journal of the EU.

Delegated Acts relating to Cross-Border Activities of AIFMs and UCITS ManCos

The EU Commission has adopted Regulatory Technical Standards (RTS) and Implementing Regulatory Standards (ITS) in relation to the cross-border marketing and management of funds in the EU under the Undertakings for the Collective Investment in Transferable Securities (UCITS) Directive and Alternative Investment Fund Managers Directive (AIFMD).

In particular, the Commission has adopted:

- [RTS](#) specifying the information to be notified in relation to the cross-border activities of managers of alternative investment funds (AIFMs);
- [RTS](#) specifying the information to be notified in relation to the cross-border activities of UCITS management companies and UCITS;
- [ITS](#) with regard to the form and content of the information to be notified in respect of the cross-border activities of AIFMs and the exchange of information between competent authorities on cross-border notification letters; and
- [ITS](#) with regard to the form and content of the information to be notified in respect of the cross-border activities of UCITS, UCITS management companies, and the exchange of information between competent authorities on cross-border notification letters.

ESMA publishes

On 19 December 2023, ESMA published two “risk articles” regarding [the impact of climate-related risks in the fund sector](#) (1) and [risks derived from greenwashing controversies](#) (2).

Key elements of both publications are detailed below.

1. *Dynamic modelling of climate-related shocks in the fund sector*

The article discusses a method for modeling climate-related shocks in the fund sector, considering factors like investor actions and portfolio adjustments. It highlights that when investors withdraw funds, it can worsen the impact of initial shocks on fund values.

This modeling work is part of ESMA's efforts in climate stress testing. The EU Commission has instructed the ESAs to conduct regular climate change stress tests, providing methods for supervisors. The ESAs are also set to coordinate a one-time climate change stress test across the financial sector, working with the ECB and ESRB and reporting results by Q1 2025.

2. *Financial impact of greenwashing controversies*

The article highlights how data on ESG controversies can be useful to monitor potential reputational risks around greenwashing. It also outlines the challenges involved in using such data. The number of greenwashing controversies involving large European firms increased between 2020 and 2021 and tended to be concentrated within a few firms belonging to three main sectors, including the financial sector. Growing public scrutiny highlights the importance of clear policy guidance by regulators and efforts by supervisors to ensure the credibility of sustainability-related claims.

Studying the financial effects of greenwashing controversies is crucial for the shift to a low-carbon economy. Trust in companies' commitment to climate goals is vital, but greenwashing risks erode this trust, affecting confidence among consumers and investors. It emphasizes the need to monitor and address the issue.

ESMA is organising a public webinar on the articles' findings. The webinar will be held online via Teams on 7 February 2024 from 11:00 to 12:00.

During the webinar, authors of the articles will have a presentation about the articles, which will be followed by a Q&A session. Interested persons may register by 2 February 2024 using the [registration link](#).

The Financial Stability Board (FSB) and IOSCO publish policies to address vulnerabilities from liquidity mismatch in open-ended funds

The FSB on 20 December 2023 has published [revised policy recommendations](#) (Revised FSB Recommendations) to address structural vulnerabilities from liquidity mismatch in open-ended funds (OEFs). At the same time, IOSCO has published its [final guidance](#) on anti-dilution liquidity management tools (LMT Guidance) for the effective implementation of the recommendations for liquidity risk management for collective investment schemes. The measures are intended to provide greater clarity on the redemption terms that OEFs could offer to investors, based on the liquidity of their asset holdings, and to ensure greater use and consistency in the use of anti-dilution LMTs.

The Revised FSB Recommendations provide greater clarity on the redemption terms that OEFs can offer to investors, based on the liquidity of the OEF asset holdings. This would be achieved through a categorisation approach, where OEFs would be grouped depending on the liquidity of their assets (e.g., liquid, less liquid, illiquid). OEFs in each category would then be subject to specific expectations in terms of their redemption terms and conditions. Authorities should set expectations for OEF managers to use a mixture of quantitative and qualitative factors when determining the liquidity of OEF assets in normal and stressed market conditions within the context of the domestic liquidity framework set out by authorities. The Revised FSB Recommendations seek to achieve (i) greater inclusion of anti-dilution LMTs in OEF constitutional documents and (ii) greater use of, and greater consistency in the use of, anti-dilution LMTs in both normal and stressed market conditions.

IOSCO's LMT Guidance provides detailed guidance on the design and use of anti-dilution LMTs by OEF managers. The LMT Guidance aims to support the greater use of anti-dilution LMTs by OEFs to mitigate investor dilution and potential first-mover advantage arising from structural liquidity mismatch in OEFs. The LMT Guidance sets out key operational, design, oversight, disclosure and other factors and parameters that responsible entities should consider when anti-dilution LMTs are used, to promote greater, more consistent, and more effective use of these tools. For example, responsible entities should have appropriate internal systems, procedures and controls in place at all times in compliance with applicable regulatory requirements for the design and use of anti-dilution LMTs as part of the everyday liquidity risk management of their OEFs. Furthermore, anti-dilution LMTs used by responsible entities should impose on subscribing and redeeming investors the estimated cost of liquidity. This encompasses the explicit and implicit transaction costs of subscriptions or redemptions, including any significant market impact of asset purchases or sales to meet those subscriptions or redemptions.

The FSB and IOSCO will both review progress by member jurisdictions in implementing their respective revised recommendations and guidance. This will begin with a stocktake, to be completed by the end of 2026, of the measures and practices adopted and planned by FSB member jurisdictions. IOSCO will aim to coordinate a stocktake of its recommendations and guidance with the FSB's stocktake to provide a comprehensive picture. The FSB and IOSCO will, by 2028, assess whether implemented reforms have sufficiently addressed risks to financial stability.

Digital Finance

DORA: ESAs consult on second set of technical standards and guidance

The ESAs launched on 8 December 2023 a public consultation on the [second set of policy mandates](#) under the Digital Operational Resilience Act (DORA).

DORA aim to ensure a consistent and harmonised legal framework in the areas of major ICT-related incident reporting, digital operational resilience testing, ICT third-party risk management and oversight over critical ICT third-party providers.

Through DORA the ESAs are mandated to jointly develop a total of 13 policy instruments, presented in two sets. This second set comprises the following:

- ❑ draft RTS on the elements which a financial entity needs to determine and assess when subcontracting ICT services supporting critical or important functions ([here](#));
- ❑ draft RTS on the harmonisation of conditions enabling the conduct of the oversight activities ([here](#));
- ❑ draft RTS on the content of the notification and reports for major incidents and significant cyber threats and determining the time limits for reporting major incidents and draft ITS on the standard forms, templates and procedures for financial entities to report a major incident and to notify a significant cyber threat ([here](#));
- ❑ draft RTS specifying elements related to threat-led penetration tests ([here](#));
- ❑ guidelines on the oversight co-operation and information exchange between the ESAs and the competent authorities ([here](#)); and
- ❑ guidelines on the estimation of aggregated annual costs and losses caused by major ICT-related incidents ([here](#)).

The consultation runs until 4 March 2024.

Anti-Money Laundering

MOKAS issues its strategic analysis report 2020-2022

On 30 November 2023, the Financial Intelligence Unit of Cyprus ('Mokas') issued its ('Report'). [Strategic Analysis Report 2020 – 2022](#)

The Report aims to provide the regulated sector with important information and feedback addressing money laundering and terrorist financing trends and patterns, as these emerge from the context and nature of the Suspicious Transaction Reports (STRs) / Suspicious Activity Reports (SARs) submitted to Mokas by obliged entities during 2020-2022, requests and spontaneous disclosures from foreign Financial Intelligence Units as well as requests from Cyprus Police Authorities and from the Cyprus Customs and Excise Department.

The Report is considered to be of assistance to regulated entities, especially in regard to enhancing their understanding of SARS and STRs, so as to further improve the quality of information provided to Mokas and Law enforcement authorities-police.

EU Commission updates list of high-risk third countries to remove Cayman Islands and Jordan

On 12 December 2023, the EU Commission adopted a [draft Delegated Regulation](#) amending the list of high-risk third countries with strategic AML/CFT deficiencies, by deleting the Cayman Islands and Jordan from the list.

The Delegated Regulation was submitted to the Council of the EU and the European Parliament for scrutiny. If neither objects, it will be published in the EU's Official Journal and enter into force on the twentieth day thereafter.

EBA proposes Voluntary EU Green Loan Label

The EBA has published its [response](#) to the EU Commission's call for advice on green loans and mortgages. The EBA is proposing the introduction of a voluntary EU label for green loans based on a common EU definition and the integration of the concept of green mortgage and its key sustainability features in the Mortgage Credit Directive.

In particular, the EBA proposes that:

- the EU definition and labelling framework for green loans, while based on the Taxonomy, should incorporate a degree of flexibility to facilitate market participants' credible efforts in contributing to environmental objectives;
- the labelling framework for green loans should provide the necessary information and transparency for prospective borrowers, including information on the long-term benefits of investing in energy-efficient solutions, documentation requirements and availability of financial support schemes; and
- when reviewing the Mortgage Credit Directive, the EU Commission should consider integrating the concept of green mortgages as well as the expected features of these loans.

EBA publishes final guidelines on assessing the knowledge and experience of the management or administrative organ of credit servicers

The EBA has published a [final report](#) on guidelines on the assessment of adequate knowledge and experience of the management or administrative organ, as a whole, of credit servicers under Directive (EU) 2021/2167 on credit servicers and credit purchasers. This report encompasses the criteria used in the assessment and outlines the assessment process.

The guidelines are intended to ensure that the management or administrative organs are suitable to conduct the business of the credit services in a competent and responsible manner and set out, among other things:

- the common criteria to assess the collective adequate knowledge and experience of the management or administrative organ based on the individual knowledge and experience of the members of the organ;
- the requirements of the assessment process and specify when an assessment should be performed; and
- the requirement for credit servicers to take appropriate corrective measures where shortcomings are identified.

The guidelines apply to credit servicers and competent authorities across the EU and do not apply to credit institutions or other entities listed in Article 2(5)(a) of the NPL Directive.

The guidelines will apply three months after their publication on the EBA's website in the official languages of the EU.

Glossary

- AIF Alternative Investment Fund (EU)
- AIFMD Directive 2011/61/EU on Alternative Investment Fund Managers
- AIFMs Alternative Investment Fund Managers
- AML Anti-Money Laundering
- CSRD Corporate Sustainability Reporting Directive
- CySEC Cyprus Securities and Exchange Commission
- CP Consultation Paper
- EBA European Banking Authority
- EC European Commission
- ESG environmental, social, and governance
- EMIR European Market Infrastructure Regulation
- ESAs European Supervisory Authorities (EBA, EIOPA and ESMA)
- ESMA European Securities and Markets Authority
- EIOPA European Insurance & Occupational Pensions Authority
- EU European Union
- 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
- 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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