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Sustainable Architecture for Finance in Europe (https://safe-frankfurt.de/)

SAFE Finance Blog

The SAFE Regulatory Radar in June

06/28/2019

A pan-European pension product and new rules for investment funds, reforms in the Banking Union and guidelines on sustainable finance: a selection of regulatory developments from this month

New and from now on regularly in the SAFE Policy Blog: At the end of each month, the SAFE Regulatory Radar highlights a selection of important news and developments on financial regulation. Do you have feedback on the SAFE Regulatory Radar? Please send us an e-mail: Policy_Center@safe.uni-frankfurt.de

Capital Markets Union: reforms for a pan-European pension product and for the regulation of

Capital Markets Union: reforms for a pan-European pension product and for the regulation of investment funds.

The Council of the European Union (https://www.consilium.europa.eu/en/council-eu/) presented two key reforms (https://www.consilium.europa.eu/en/press/press-releases/2019/06/14/capital-markets-union-council-adopts-new-rules-facilitating-access-to-pension-products-and-investment-funds/) in the framework of the Capital Markets Union: The PEPP ("pan-European pension product") regulation and a package of measures aimed at removing existing barriers to the cross-border distribution of investment funds. On 20 June 2019, the new legislation was adopted by the European Parliament. The new measures for PEPP and cross-border distribution of funds will be published in the Official Journal shortly after signature and will enter into force 20 days later.

The PEPP regulation (http://data.consilium.europa.eu/doc/document/PE-24-2019-INIT/en/pdf) expands the market for personal pensions through the creation of a new type of voluntary personal pension product. It aims to provide greater choice for people who wish to save for their retirement. A wide range of providers, such as insurance companies, banks, occupational pension funds, investment firms, and asset managers can offer the new product. Due to the benefits from an EU passport, PEPPs will be selling throughout the EU under the same conditions and portable between the member states. That means savers will be able to continue contributing to their PEPP even if they move to another EU country. It is a new EU-wide saving option that will complement state-based, occupational and national personal pension schemes. It will allow consumers to voluntarily complement their savings for retirement whilst benefitting from solid consumer protection independent of their location in the EU.

In order to strengthen the existing legal framework, the agreement on cross-border distribution (https://data.consilium.europa.eu/doc/document/PE-54-2019-INIT/en/pdf) of investment funds removes regulatory barriers and decreases distribution costs. New measures (https://data.consilium.europa.eu/doc/document/PE-53-2019-INIT/en/pdf) aim to make it easier for EU alternative investment fund managers to test the appetite of potential professional investors in new markets as well as to align procedures and conditions for managers of collective investment funds to exit national markets when they decide to terminate the offering or placement of their funds. New rules clarify customer service obligations for asset managers and introduce increased transparency and the creation of a single online access point for information on national rules related to marketing requirements and applicable fees.

The contradictory regulations of the member countries hinder the development of the personal pension market. Because of the limited choice for products based on capital market instruments the customers' costs and lack of liquidity in the markets are increasing. Introduction of new EU-wide saving form prevents the market fragmentation and provide new opportunities for savers and pension plan providers.

Legislative package reforms reducing risks in the Banking Union enter into force

On May 20, 2019, the European Parliament adopted a comprehensive legislative package for the Banking Union. It aims to reduce risks in the banking sector and further reinforce banks' ability to withstand potential shocks. The package contains amendments to the capital requirement legislation (Capital Requirements Regulation II (https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R0876&from=EN) – CRR II) which strengthens the capital and liquidity positions of banks and improves the framework for the recovery and resolution of banks in difficulty (Capital Requirements Directive V (https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019L0878&from=EN) – CRD V). It is an important step in the deepening of the Economic and Monetary Union.

The new provisions also implement reforms agreed at the global level following the financial crisis. They include the measures agreed by the Basel Committee on Banking Supervision (https://www.bis.org/bcbs/) and by the Financial Stability Board (https://www.fsb.org/about/) (FSB) in November 2016 to strengthen the banking sector and consider remaining issues to financial stability.

The package introduced a set of key measures, including a leverage ratio requirement for all institutions as well as a leverage ratio buffer for all global systemically important institutions (G-SIIs). The new amendments present a new market risk framework for reporting purposes, including measures reducing reporting and disclosure requirements and simplifying market risk and liquidity rules for small non-complex banks in order to ensure a proportionate framework for all banks within the EU. Other changes relate to a net stable funding requirement, a requirement for third-country institutions with significant activities in the EU to have an intermediate EU parent undertaking and enhanced Minimum Requirement for own funds and Eligible Liabilities (https://eba.europa.eu/documents/10180/1132900/EBA-RTS-2015-05+RTS+on+MREL+Criteria.pdf/a0fc8387-e98e-4c3f-ae9d-11fb75511662) (MREL) subordination rules for G-SIIs and other large banks.

It also introduces a set of targeted measures to meet the EU specificities, such as incentives for investments in public infrastructures and small and medium-sized enterprises (SMEs) or a credit risk framework facilitating the disposal of non-performing loans (NPLs).

CRR II and CRD V entered into force on 27 June 2019. Most of the new rules will start applying from 28 June 2021.

The Banking Union (https://ec.europa.eu/info/business-economy-euro/banking-and-finance/banking-union/what-banking-union_de) is a system of European institutions which, since its inception in November 2014, has comprised a Single Supervisory Mechanism (https://ec.europa.eu/info/business-economy-euro/banking-and-finance/banking-union/single-supervisory-mechanism_en) (SSM) and, since the beginning of 2016, a Single Resolution Mechanism (https://ec.europa.eu/info/business-economy-euro/banking-and-finance/banking-union/single-supervisory-mechanism_en) (SRM). It aims to create a safer financial sector for the single market.

Sustainable finance: European Commission publishes reports on climate finance and guidelines on corporate climate-related information

On June 18, 2019, the European Commission presented the new guidelines on reporting climate-related information (http://ec.europa.eu/finance/docs/policy/190618-climate-related-information-reporting-guidelines_en.pdf) as a part of its Sustainable Finance Action Plan (https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097) which was published in March 2018. It aims to redirect capital towards sustainable investment, manage financial risks arising from climate change, and encourage transparency and a long-term view in financial and economic activities.

The guidelines give companies some practical recommendations on how to better report the impact of their activities on the climate as well as the effects of climate change on their business. According to the Commission, the disclosure of clear and usable sustainability, and climate-related information are critical to the success of the Action Plan and essential for formalizing the Commission’s proposed regulations on sustainable investment taxonomy, sustainability disclosures, and carbon-related benchmarks. Under the new guidelines disclosures on climate-related risks should include the information about how climate change impacts the business model, strategy, policies and due diligence processes as well as how a company identifies and manages principal risks.

The Commission awaits the companies will take advantages from better disclosure of climate-related information through increased awareness and understanding of climate-related risks and opportunities as well as improved risk management. Disclosure of climate-related information also leads to many benefits, such as more informed decision-making, strategic planning and more constructive dialog with stakeholders. As a result, the companies that disclose climate-related information get a higher corporate reputation and a more diverse investor base.

The guidelines are non-binding, and companies may report climate-related information differently provided the legal requirements are met. Nevertheless, it is an important step forward for the Commission in relation to its Action Plan which aims to promote further reforms in the European financial sector and constitutes the largest modern geographical policy framework for environmental activities. The document gives guidance to around 6,000 EU-listed companies, banks, and insurance companies that have to disclose non-financial information under the Non-Financial Reporting Directive (https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en).

In addition, the Commission welcomed three important expert reports published by Technical Expert Group on sustainable finance (https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en) (TEG). The first TEG report (https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/190618-sustainable-finance-teg-report-taxonomy_en.pdf) is a classification system (the Taxonomy) for environmentally sustainable economic activities that provides practical guidance for policymakers, industry, and investors on how best to support and invest in economic activities that contribute to a climate-neutral economy. A report on an EU Green Bond Standard (https://ec.europa.eu/info/files/190618-sustainable-finance-teg-report-green-bond-standard_en) (EU-GBS) recommends clear and comparable criteria for issuing green bonds. It suggests creating the EU-GBS voluntarily to enhance the effectiveness, transparency, accountability, comparability, and credibility of the green bond market, and encourage issuers to issue bonds as “EU Green Bonds”. The third expert report (https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/190618-sustainable-finance-teg-report-climate-benchmarks-and-disclosures_en.pdf) outlines the creation of two types of climate benchmarks: the EU Climate Transition Benchmark and the EU Paris-aligned Benchmark. It sets out the methodology and minimum technical requirements for indices that enable investors who wish to adopt a climate-conscious investment strategy to orient their choices.

The new guidelines on reporting climate-related information integrate the recommendations of the Taskforce on Climate-related Financial Disclosures (https://www.fsb-tcfd.org/) (TCFD) of the FSB and are based on proposals from Technical Expert Group (TEG) on Sustainable Finance (https://www.iasplus.com/en/news/2019/01/ec-teg-climate-disclosure) published in January 2019. The 2019 Guidelines supplement the general guidelines on non-financial reporting (https://www.iasplus.com/en/news/2017/07/eu-high-level-expert-group-sustainable-finance) published in July 2017, which continue to be applicable.

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