EU Public Policy Update
Financial Services and Taxation

Selected Developments from H1 2020

INTRODUCTION

The European Commission (i.e. the European Union's Executive Body) has started a new 5-year political mandate on 1 December 2019 under the leadership of its new President, the German Ursula von der Leyen. Three overarching priorities are woven into the EC policy agenda 2019-2024: (1) sustainability/climate neutrality (under the new European Green Deal), (2) digitalization and (3) supporting the European economy. The COVID-19 outbreak in Q1 2020 has inevitably had a strong impact on these policy priorities – but it did not change the planned direction of travel, quite on the contrary: many of the planned policy initiatives now play a major role in the COVID-19 economic recovery efforts. At the forefront of these recovery efforts is the EU Recovery Instrument, (overview available here) aiming at revitalizing the suffering European economies in the years to come.

In this European Commission term, Executive Vice-President (EVP) for an Economy that Works for People, Valdis Dombrovskis (Latvian) and the Commissioner for Economy, Paolo Gentiloni (Italian), lead the financial services and taxation portfolios. It is worth noting that EVP for A Europe Fit for the Digital Age, Margrethe Vestager (Danish) leads on the Digital Taxation file and EVP Frans Timmermans (Dutch) the European Green Deal portfolio. The EC has revised its work program for 2020 on 27 May, and we set out below the revised timelines for the selected policy initiatives.

This overview provides selected EU policy developments in the area of financial services and taxation – and indicates how SPB can support clients in managing and shaping these policy discussions to their advantage. SPB has been recognized as one of the leading public policy law firms in Brussels in 2019 and 2020.

Recently Published Initiatives in Financial Services

A. Action Plan on Anti-Money Laundering and Counter-Financing Terrorism

On 7 May 2020, the EC published its much anticipated Anti-Money Laundering (AML) and Counter-Financing Terrorism (CFT) Action Plan. A public consultation was simultaneously launched for stakeholder input until 29 July 2020. The Action Plan is built on six pillars:

I. **Ensuring the consistent implementation and application of EU AML/CFT rules** across the 27 EU Member States

II. **Establishing an EU single rulebook on AML/CFT**: A legislative proposal turning AML Directives into Regulations (i.e. direct application of EU law throughout Member States) is one possible strategy.

III. **Establishing EU level AML/CFT supervision:** The possibility of establishing a standalone EU Supervisory Body for AML/CFT purposes have been discussed in recent months. The EC will come forward with legislation to set-up an EU-level supervisor in Q1 2021.

IV. **Establishing a support and cooperation mechanism for Financial Intelligence Units (FIU):** Actions include a legislative proposal by Q1 2021 and a change of technical management of FIU.net by Q4 2020.

V. **Enforcing EU-level criminal law provisions and information exchange:** guidelines and monitoring systems for the criminal law enforcement (e.g. through public-private partnerships) and information/data sharing to be published by Q1 2021.

VI. **Strengthening the international dimension of the EU AML/CFT framework:** The highly political AML "blacklist of third countries" has been published together with the Action Plan, including a new methodology used to assess high-risk third countries . A series of delegated acts are tentatively planned to be published every quarter of 2020.

The EU's revised AML high-risk third country list (AML blacklist) follows once more the approach taken by the Financial Action Task Force (FATF). The high-risk third country list includes the following jurisdictions: **Afghanistan, Bahamas, Barbados, Botswana, Cambodia, Ghana, Iraq, Jamaica, Mauritius, Mongolia, Myanmar/Burma, Nicaragua, Pakistan, Panama, Syria, Trinidad and Tobago, Uganda, Vanuatu, Yemen, Zimbabwe.**

The earlier version of the blacklist has created a lot of political reaction, especially from Saudi Arabia and the United States, as some of their territories such as the US Virgin Islands were on that list. This led to a public rejection of the blacklist by the Council (i.e. the body representing the 27 EU Member States). The EC was tasked with revising the methodology which leads to a country being listed as high risk. The EC Staff Working Document outlines the revised methodology and criteria in line with EU law. The EU will use the public list of the FATF as a basis and will conduct an autonomous assessment based on Article 9 of the 4th Anti-Money Laundering Directive. Member State experts are expected to actively engage and be consulted at every stage of the process.

B. EU Green Deal Investment Plan and Just Transition Mechanism

The European Green Deal is one of the flagship initiatives of the EC, which will determine future growth initiatives in a range of policies aimed towards the EU's climate neutrality goal. To facilitate the necessary investment into Green Deal projects, the EC published on 14 January 2020 a Communication on a Sustainable Europe Investment Plan together with a proposal for a Regulation establishing the **Just Transition Fund**.

The Sustainable Europe Investment Plan details how the EC envisages to raise **investments of € 260 billion per year** by 2030. To that end, these proposals are aiming to create a single policy framework for sustainable investment, to ensure that instruments and regulatory principles are in place. Public administrations would be supported to identify, structure and execute sustainable projects. 25% of the EU budget would contribute to climate investment. Together with InvestEU guarantees and the European Investment Bank (EIB) adapting to become a **climate bank**, this should activate **€ 1 trillion in private investments**.

In order to create an enabling framework that facilitates public and private investments, sustainable finance is put at the center of the financial system. Policy initiatives outlining how this will be achieved include:

- The Action Plan on financing sustainable growth;
- The EU taxonomy (analyzed on section below);
- A renewed strategy for sustainable finance (public consultation ongoing, see below entry);
- An EU Green Bond Standard.

Additionally, the Just Transition Mechanism is to raise € 100 billion to finance the social aspect of the European Green Deal. The Mechanism consists of three pillars: (i) The Just Transition Fund, (ii) a dedicated just transition scheme under InvestEU, and (iii) a new loan facility of the EIB. Advisory and technical assistance and state aid facilitation should be supporting these three pillars.

A **Communication** on the Just Transition Fund is expected to be published soon.

C. Sustainable Finance

The EC has been focusing its efforts on financing sustainable growth, since it laid out its initial perspectives with the 2018 Action Plan. Under the **climate neutrality ambition**, the EC will pursue renewed efforts for the sustainable finance strategy. A public consultation is launched until 15 July 2020, to gather stakeholder input in that context. As a complementary to the input by the financial sector on making the economy more sustainable, the consultation seeks input on strategic questions for sustainable finance, namely:

- Strengthening the foundations for sustainable investment by creating an enabling framework, with appropriate tools and structures;
- Increasing opportunities to have a positive impact on sustainability for citizens, financial institutions and corporations; and
- Managing and integrating climate and environmental risks into financial institutions and the financial system as a whole.

A **renewed sustainable finance strategy is expected** to be published **in Q4 2020**.

D. Digital/Cyber Resilience of the Financial Services Sector

The EC launched a public consultation on the cross-sectoral digital operational resilience in the area of financial services, which concluded on 19 March 2020. This aimed to gather stakeholder input prior to the development of a **legislative initiative**, **foreseen for Q3 2020**, on the following issues:

- targeted improvements of ICT and **security risk management** requirements;
- harmonisation of ICT **incident reporting**;
- the development of a digital **operational resilience** testing framework;
- better oversight of certain **critical ICT third-party providers**, including outsourcing;
- identify areas where EU Action may be needed (e.g. information sharing needs of different financial entities); and
- demonstrate the interaction with the Network and Information Security (NIS) Directive (of note, credit institutions are listed as an operator of essential services under the NIS Directive, which is foreseen to be amended in Q4 2020).

The public consultation is connected to the consultation on crypto-currencies (see below). It is worth noting that the consultation is linked to the broader digital agenda of the EC published in the Communication on the actions to shape digital Europe. A **legislative proposal is expected in Q3 2020**.

E. Cryptocurrencies

The EC launched a public consultation on the establishment of a European Framework for markets in crypto-assets, which concluded on 19 March 2020. The EC has been planning for some time to **establish a legislative framework for cryptocurrencies** more broadly, to ensure that the regulatory framework adequately addresses the risks inherent to these assets and related services. The public consultation included general questions on the use or potential use of crypto-assets but also targeted feedback on the following issues:

- Whether or not those crypto-assets falling under the existing EU legislative framework should be classified;
- Whether an EU regulatory framework for the crypto-assets that currently fall outside the scope of the EU

legislation is needed. The input should help identify the main risks raised by **unregulated crypto-assets** and specific services relating to those assets, as well as the priorities for policy actions; and
- The preferred approach crypto-assets that currently fall within the scope of EU legislation. This included a request for input about whether any further regulatory impediments to the use of DLT in the financial services.

The public consultation is connected to the consultation on the digital resilience of the financial services sector. A **legislative proposal is expected end Q3 2020**.

F. Retail Payments Action Plan

The COVID-19 outbreak underlined the importance of digital payments and digitalized retail finance services overall. The EC recently launched a public consultation on its Retail Payment Strategy and on Digital Finance/Fintech Action Plan. The **first public consultation relates to a Retail Payment Strategy** and is open until 26 June 2020.

The strategy on retail payments is expected to cover all payment aspects such as **instant payments**, **pan-European payment solutions**, **open data sharing**, **e-money** related issues etc. The consultation is touching on various work streams in particular on strategic domain such as contactless payments.

The public consultation will feed into the EC's reflection to prepare the **strategy on payments expected in Q3 2020**.

G. Fintech/Digital Finance Action Plan

Building on the work carried out in the context of the FinTech Action Plan, and the contribution of digital financial services during the COVID-19 outbreak, the EC launched a **second public consultation on the Digital Finance/FinTech Action Plan**, open until 26 June 2020.

The EC has identified the following four priority areas to stimulate the development of digital finance in the EU:

- ensuring that the EU financial services regulatory framework is fit for the digital age;
- enabling consumers and firms to benefit from the opportunities offered by the EU-wide Single Market for digital financial services;
- promoting a data-driven financial sector for the benefit of EU consumers and firms; and
- enhancing the digital operational resilience of the EU financial system (a separate public consultation is described above).

The public consultation seeks feedback on the following issues:

- how to ensure the financial services regulatory framework is technology neutral and innovation-friendly.
- ways to remove fragmentation of the Single Market for digital financial services.
- how best to promote a well-regulated data-driven financial sector.

The public consultation is linked with the Retail Payments Consultation and will feed into the **EC's preparation of the Digital Finance/FinTech Action Plan, currently foreseen for Q3 2020**.

H. Review of the Regulatory Framework for Investment firms and market operators

The EC proposes a review of the regulatory framework for investment firms and market operators, which will include amendments to the Markets in Financial Instruments Regulation (EU/600/2014) (MiFIR) and the Markets in Financial Instruments Directive II (2014/65/EU) (MiFID II). A public consultation to gather stakeholder input on both legislative instruments closed on 18 May 2020. The consultation document seeks stakeholder input on the following issues:

- Stakeholders experience of the two years of application of MiFID II/MiFIR. Stakeholders were also asked whether a targeted review would be appropriate to address the most urgent shortcomings.
- Input on certain technical aspects of the current MiFID II/MiFIR regime to allow the EC to assess the impact of possible changes to EU legislation based on that input, previous public consultations and studies and based on exchanges with experts.

It is expected that **legislative proposals** with amendments to the MiFIR and MiFID II **will be published in Q3 2020**.

I. Review of the Capital Requirements legislation

In the context of the COVID-19 pandemic, the EC adopted on 28 April a **COVID-19 banking package aiming to provide flexibility in bank lending to businesses and households.** The banking package consists of a proposal for a Regulation, which provides adjustments to maximize the capacity of **credit institutions to lend and to absorb losses** linked to the COVID-19 and an interpretative Communication explaining the proposed to the **EU's accounting and prudential frameworks.**

The proposed regulation includes targeted amendments to the Capital Requirements Regulation (CRR) (EU) 575/2013 (which requires banks and investment firms to improve the quantity and quality of their capital) and the Regulation (EU) 2019/876, (CRR II, which aims to ensure financial institutions' resilience). The proposed revision would amend the regulatory framework as follows:

- adjust the transitional arrangements allowing credit institutions to alleviate the impact from expected credit-loss (ECL);
- adjust the rules on the minimum loss coverage for non-performing exposure (NPEs);
- temporary exclusion of exposures from the calculation of the leverage ratio;
- defer the application date of the new leverage ratio buffer requirement; and
- delay the application dates of the capital benefits envisaged in the CRR.

The Interpretative Communication issued alongside the proposed amendments, outlines the flexibility in the regulatory framework for banks. It also provides the flexibility in the International Financial Reporting Standard IFRS 9 and the classification of non-performing loans. **Further targeted amendments on the CRR are expected in Q4 2020.**

J. Protection and facilitation of investment within the EU

The EC launched a public consultation on the **protection and facilitation of cross-border investment within the EU**, open until 8 September 2020. As announced in the Renewed Industrial Strategy for Europe, the new Action Plan on Capital Markets Union, **foreseen to be published in Q4 2020**, will include an initiative to strengthen intra-EU investment protection and efforts to unlock more diverse sources of funding for European businesses, especially SMEs. **Mobilizing private funding will be particularly important to cope with the negative economic impact of the COVID-19 pandemic.** The consultation seeks input on the strengths or weaknesses of cross-border investing in the EU. This is particularly timely, considering that **Member States have recently terminated the intra-EU Bilateral Investment Treaties**. The input of stakeholders will feed into a **broad list of upcoming policy initiatives incorporated in the New Capital Markets Union Action Plan.**

Outstanding Policy Initiatives in Financial Services

EU Taxonomy for Sustainable Investment

The proposal for a **Regulation on the establishment of a framework to facilitate sustainable investment** ('Taxonomy') was published on 24 May 2018, focusing on sustainable finance and development. The aim of the proposal on Taxonomy is to set out the uniform criteria for determining whether an economic activity is environmentally sustainable, involving a multi-stakeholder platform to establish such a unified EU classification.

After a few years of negotiations, on 16 December 2019, the two EU **co-legislators (i.e. the Parliament and Council) reached a political agreement** on the proposal for a Regulation on Taxonomy. EU Ambassadors endorsed the compromise agreement, followed by the Environment and Food Safety (ENVI) and Economic and Monetary Affairs (ECON) Committees of the Parliament on 23 January 2020.

The Council approved the revised compromise agreement **on 15 April 2020** alongside a statement. The European Commission welcomed the revised compromise agreement, reiterated that it fully reflects the political agreement previously reached and called the European Parliament to approve the revised text. The ENVI and ECON Committees are due to approve the revised text on 28 May 2020.

The proposed Taxonomy Regulation lists the **financial products and screening criteria applicable for sustainable investments**. It is closely linked to Regulation (EU) 2019/2088 on disclosures relating to sustainable investments and sustainability risks, addressed to investors and asset managers.

The Regulation determines **six underlying environmental objectives** and the level in which the economic activity can substantially contribute to these objectives. These cover:

1) climate change mitigation;
2) climate change adaptation;
3) sustainable use and protection of water and marine resources;
4) transition to a circular economy;
5) pollution prevention and control;
6) protection and restoration of biodiversity and ecosystems.

The Regulation also **clarifies the criteria for enabling activities** (contributing to one or more of the environmental objectives) as well as the **environmental objectives** to consider an economic activity that could be **significantly harming.**

Technical screening criteria, which would identify the contributions based on the environmental objectives, specify the sustainability indicators, possible scientific evidence, among others, are also introduced in the compromise agreement. The **EC would assess the implementation of the screening criteria** taking into account the outcome of their application by financial market participants and impact on capital markets, including challenging investments into sustainable economic activities.

The EC will also be tasked to **review the technical screening criteria** for those activities **at least every 3 years**. The Member States Expert Group on Sustainable Finance would advise the EC on the appropriateness of the technical screening criteria.

Member States would designate competent authorities for supervising the compliance with disclosure obligations. Member States should also introduce rules on **measures and penalties** applicable to the transparency of **environmentally sustainable investment, financial products that promote environmental characteristics and other financial products** in pre-contractual disclosures and periodic reports, on the use of the criteria for environmentally sustainable economic activities.

Selected Outstanding Policy Initiatives in Taxation

Digital Taxation

The EU has been at the forefront of the digital taxation debate by issuing in March 2018 two legislative proposals: a proposal for a Directive establishing a significant digital presence and a proposal for a Directive on the Digital Service Tax. At the early stages of EU negotiations, the Council focused on the latter proposal. Member States were nonetheless not able to reach consensus, especially considering the ongoing negotiations taking place at the OECD level for a global consensus for the taxation of the digital economy. Thus, the EU-level negotiations have stopped for the moment, as the focus of negotiations shifted at the OECD level.

The EC remains however keen to advance this policy forward. EC President von der Leyen has mandated Commissioners Vestager and Gentiloni to come forward with a revised EU legislative proposal, should the OECD fail to deliver on its mandate until the end of 2020. As the OECD negotiations on a global consensus have been delayed, it is likely that a **revised EU proposal on taxing the digital economy** will be put forward in Q1 2021.

Outstanding corporate taxation files

There are a few **key legislative proposals** that continue to be negotiated from the previous EC term:

- **Public Country-by-Country Reporting (CbCR):** The proposed Directive introduces a **mandatory obligation for multinational companies to publically disclose their annual accounts.** This proposal is exceptionally following the co-decision process, whereby the European Parliament has a co-legislator role. The Council has been advocating for years that the legal basis of the proposal is not correct and should change[1]. Negotiations are now at an impasse.

- **Common (Consolidated) Corporate Tax Base Directives (CCTB and CCCTB):** In October 2016, the EC published two proposed Directives that would allow for an **EU-wide harmonized calculation of the corporate tax base**, and then a consolidation of the common elements of the tax base calculation. The proposals were not introducing an EU-wide corporate tax rate. Thus far, only the Directive on CCTB has been negotiated; Member States have been however unable to agree on any substantial changes. This is the second effort of the EC to establish such a harmonized approach, but failed due to the unwillingness of Member States to compromise. The EC and Member States in favor of this scheme (e.g. France, Germany) have been advocating to advance the negotiations by sending strong political messages. It is unlikely that the negotiations will be concluded any time soon, considering it requires unanimity to approve this file.

- **Proposal for amending the VAT system:** The EC has come forward with a package of legislative proposals that would **amend the currently fragmented VAT system** across the EU towards a definitive VAT system. The definitive VAT regime will be completed in **two steps**: by (1) establishing a VAT regime for intra-Union B2B supplies of **goods**, and (2) by establishing a VAT regime for cross border **services**. The proposals issued so far only cover the first step (i.e. they focus on goods). Some legislative proposals have already been approved, however, the largest and most crucial proposal for a Directive, detailing the technical elements of how such a definitive regime would function, is still under negotiation. Member States are unable to reach an agreement in this very complex file.

[1] By changing the legal basis of the proposal, the European Parliament will not have a legislative role. The legislative proposal would be required only in Council to be adopted by unanimity vote.

How We Can Help Clients

Despite COVID-19, the EU lawmaking machinery in the financial services sector and on taxation is in full swing. As is customary in the first year of the new 5-year mandate of the EC, it is putting forward a range of new legislative and non-legislative proposals, which will be the subject of intense regulatory debates.

Now is the best time for clients to engage in these discussions, and SPB has a strong track record of supporting clients in shaping EU legislation and other policy initiatives in their favor.

Please reach out to us so we can discuss how we can help you manage any of the EU policy initiatives mentioned.

Contacts

Wolfgang A. Maschek
Partner, Brussels
T +322 627 11 04
E wolfgang.mascheck@squirepb.com

Matthew Kirk
International Affairs Advisor, London
T +44 207 655 1389
E matthew.kirk@squirepb.com

Christina Economides
Public Policy Advisor, Brussels
T +322 627 11 05
E christina.economides@squirepb.com