

Keynote Speech at the IFX EXPO 2023 9:00 - 18:00 - Expo Day 1 - City of Dreams Mediterranean Integrated Resort, Limassol

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CySEC's Chairman

New trends and developments in regulation and investor protection

Distinguished Guests,

Ladies and Gentlemen,

Good morning,

I am delighted to be here with you today to give the opening address to the iFX Expo 2023.

INTRODUCTION

By way of introduction, CySEC is the independent public supervisory Authority for the investment services market in Cyprus, regulating transactions in transferable securities and the collective investment and asset management sector. It also supervises the firms offering administrative services which fall outside the remit of ICPAC and the Cyprus Bar Association, as well as Crypto-Asset Services Providers.

While we are committed to encouraging financial innovation, it is imperative that we balance the adoption of new technologies against the threats that are inherent in innovation and the challenges they can pose to market participants.

Our vision is to enhance the Cyprus securities market, to make it one of the safest and most reliable investment destinations in Europe, and internationally. We do this by fostering trust amongst the firms we regulate and the investors they serve.

While the markets in which we operate are moving through some of the greatest upheavals that we have seen in recent years, whether through war, rising inflation, or the energy crunch, but we have also seen emerging sectors of the financial market face their own problems creating further volatility.

Added to these challenges is the simple fact that financial markets are becoming more accessible to retail investors. And with this rising level of retail activity, regulators must be able to respond to emerging threats, notably the rising influence on trading of social media and online messaging platforms exacerbated by aggressive marketing practices.

It is, therefore, incumbent upon us as regulators to act swiftly and to utilise the most advanced technological solutions to ensure that regulated entities remain compliant with enhanced regulatory requirements. In addition to this advanced monitoring and surveillance, CySEC plays an important role in improving investor education on the risks posed by crypto-asset investment and remains vigilant through the European Union's implementation of the Regulation on Markets in Crypto-Assets (MiCA) will provide more comprehensive regulatory supervision of the sector.

The new rules under MiCA introduce provisions for supervision, consumer protection and environmental safeguards for crypto assets, including

crypto currencies. But as Europe becomes the first continent to regulate crypto, greater attention must also be placed on financial literacy.

CySEC has seen the consequences of a lack of financial literacy at first hand. A few weeks ago, I came across an advert promoting investment in crypto. Featuring a celebrity influencer and promising to give away free crypto, it was clearly targeted at younger – and inexperienced – investors, playing on that very common human fear of missing out, a trend so common that the crypto world has coined its own acronym, FOMO! Promotion to inexperienced investors is the scourge of the investment industry and, of course it is not limited to the crypto space. But it is for these reasons that we have been proactive in launching our investor protection campaign which aims to improve the level of financial literacy amongst new investors.

NEW TOOLS AND SUPERVISION

In the ever-evolving landscape of the financial industry, the rapid emergence of the digitalization trend has been nothing short of evolutionary. The financial sector, once bound by traditional norms and practices, now finds itself at the forefront of technological renaissance. Big Data, AI, Fintech, RegTech, Cybersecurity, Cloud Computing, Robotic Process Automation, DLT, blockchain technologies. These are buzzwords in the financial industry that not so long ago barely existed outside the imagination of the writers of sci-fi. We have seen so many changes and disruptions, but none more so than in the past few years. These technologies are transforming our economic and financial systems and converting the landscape of the world of finance. Yet we are only starting to scratch the surface of what the prementioned terms can innovate in the way that we interact with the market.

Sustainable finance and digitalisation have already made a deep impact in the EU capital markets and they will continue to drive the reshaping of the financial regulatory landscape for years to come - building upon the momentum we have seen in the last decade or so in financial services as we see more migration to online and mobile platforms.

It is the role of regulators to identify future trends and to anticipate the potential risks and unintended consequences – and the known knowns! This means that not only do we need to keep pace and move swiftly to protect investors from new and emerging risks, but we are also harnessing technology to drive innovation that increases the efficiency of our own operations. The continuous upgrading of the Cyprus Securities and Exchange Commission's operations and procedures remains a priority, to make the Cyprus securities market a safe and secure place to do business, by maintaining high standards of investor protection, investor confidence and supporting the healthy development of the market with new products and services.

The commitment for continuous improvement remains paramount for CySEC. The goal is to create an environment where CySEC stands as a secure and trustworthy arena for the financial sector. This commitment revolves around upholding high standards of investor protection and confidence, while simultaneously fostering the healthy growth of the market with the introduction of new products and services.

This also addresses ESMA's strategic priority to protect retail investors in financial markets. Specifically, we are addressing the need to manage Big Data with the introduction of advanced RegTech systems, which use Artificial Intelligence and Cloud Computing. These systems have the capacity to quickly screen data from a large and varied volume of trading

activity in order to automatically detect risks and irregularities at an earlier stage and, thus, take proactive action against them.

As part of this, CySEC has also implemented a transaction data, processing, storage and reporting system that was designed based on Cloud Infrastructure and is able to generate business insights which can be used to supervise market entities. This system can connect to the ESMA hub and is able to download and store associated data securely, helping us to support ad-hoc queries and generate reports on both the aggregations and base data.

Other new procedures and methodologies, currently underway, will enhance our ability to oversee the compliance of regulated entities with regulations such as EMIR, MIFIR and SFTR, by automatically detecting potential risks and irregularities at an early stage.

Furthermore, given the international, and largely web-based nature of the activities of CIFs, a key acquisition made by CySEC is the specialised system that analyses and monitors the online marketing materials and social media activities of Cyprus investment firms.

INNOVATION HUB

Ladies and gentlemen,

It has been five years since CySEC established its Innovation Hub, to explore the growth and uses of FinTech developments like blockchain and DLT, AI tools, virtual/digital currencies, crypto exchanges, and RegTech solutions. The hub serves as a knowledge-sharing platform for both supervised and non-supervised entities, to enhance understanding about new and evolving financial technologies.

We are in the process to transform the Innovation Hub into a Regulatory Sandbox, to provide a controlled environment, for fintech start-ups and other entities which will be able to test their products or services in real conditions under the regulator's supervision.

INTRODUCTION OF MiCA

Distinguished guests,

The recent EU approval of this landmark crypto authorisation law for Europe represents a major step forward for the protection of investors in financial markets. More so now, because trading in crypto “assets” has drawn many new, often young, and sometimes financially illiterate investors to these newly emerging markets, where significant risks remain.

While the EU's forward-thinking initiative is to be applauded, the global market for crypto and digital assets remains volatile and largely unregulated. Outside of the EU, approaches to cryptocurrencies, speed of action, services, and products and even terminology differ significantly, creating a heavily fragmented system.

ESMA is shaping its Markets in Crypto Assets Regulation (MiCA) as part of its Digital Finance Strategy to increase consumer protection, establish clear crypto-industry conduct, and introduce new licensing requirements.

Importantly, MiCA covers classes of crypto-assets that currently fall outside of existing EU financial services legislation, as well as e-money tokens. The first consultation has been launched and based on its current timetable; MiCA will be fully adopted across Europe by the end of 2024.

Once implemented, existing investment firms will have a “passport scheme” for the pan-European provision of crypto digital asset services, operating under the guidelines and strict supervision that MiCA provides.

As I see it, technology is the bedrock for growth of the financial services industry and MiCA is an important, timely and reflective suite of legislation that reflects the new and emerging challenges. However, I would like to emphasise that such is the pace of digitalization in the market that MiCA should only be considered a starting point. MiCA will not cover the full spectrum of crypto assets, such as NFTs, which will remain outside its scope. Additionally, the issuance of stable coins will fall under central bank regulation, while trading and service provision will fall under ESMA and Securities and Exchange Commissions.

It is the role of regulators to recognise future trends and to anticipate potential risks and side effects. Better cooperation and coordination arrangements between financial supervisors and other authorities still need to be developed – not just to ensure that we follow the same rules under MiCA, but also on matters of consumer protection, AML/CFT, cyber and our engagement with digital platforms.

OTHER REGULATORY CHALLENGES

As I have said, regulators have a need to understand the challenges to financial markets posed by the growth of technology, in all its forms and be ever vigilant to the new and emerging risks. Amongst these is the rise of retail activity and increased market accessibility, which has led to aggressive marketing practices as well as false claims which include

“greenwashing”, practices that give consumers the impression that the product or service they are using prioritises ecology and green initiatives.

CySEC has itself invested in financial tools to help identify misleading adverts and the firms behind them. Our monitoring of the market has shown that the number of fraudulent advertisements has increased dramatically, with young investors now being the most vulnerable to potentially overly aggressive marketing strategies.

These emerging challenges related to technological innovation are expected to be addressed through new legislations that are under the way.

DORA

The European Regulation on digitalization and operational resilience in the financial sector, known as DORA (Digital Operational Resilience Act) came into force this year and will become applicable in 2025. The aim of the Regulation is to ensure that all participants in the financial system have the necessary safeguards in place to mitigate cyber-attacks and other risks.

DORA establishes uniform requirements concerning the security of network and information systems supporting the business processes of financial entities. There are actions to be taken both at EU and National level. CySEC participates in the Joint Committee Sub-Committee on Digital Operational Resilience Act (JC SC DOR). CySEC has also undertaken a mapping exercise examining the provisions of DORA to identify issues that require further attention from our side. Also, we are

planning to launch a platform where relevant entities will be required to report any incidents.

DLT Pilot Regime

Also, the DLT Pilot Regime came into effect. The DLT Pilot Regime is part of the Digital Finance Package introduced by the European Commission in 2020 to further enable and support the potential of digital finance while mitigating associated potential risks. The Regulation on a pilot regime for market infrastructures based on the DLT Pilot aims at developing the trading and settlement for DLT financial instruments.

AML PACKAGE

In addition, a package of legislative proposals on combating money laundering and terrorist financing is currently under review at EU level and it takes into account new and emerging challenges related to technological innovation. A key part of the package is the establishment of a European Anti-Money Laundering and Terrorist Financing Authority (AML Authority (AMLA)), and a plan to extend existing rules on funds transfer services to crypto-asset transactions. These new rules will ensure both the sender and beneficiary of these transactions are recorded by the crypto-asset service providers.

RETAIL INVESTMENT STRATEGY

In May 2023, the European Commission adopted the Retail Investment Strategy as part of its 2020 capital markets union action plan. The primary objective is to reinforce investor protection within the European Union, foster trust in the financial sector and promote participation in capital markets. This package proposal targets the Investor protection rules which are currently established across various pieces of EU legislation

through an Omnibus Directive covering MiFID II, the Insurance Distribution Directive, the Solvency II Directive, the AIFMD and UCITS Directive. The package also encompasses a proposal to amend the Packaged Retail and Insurance-based Investment Products Regulation (PRIIPs Regulation) which focuses on revisions to the general product disclosure rules. Among other aims to:

- Amend the rules on product oversight and governance, safeguarding investors against malpractices of marketing communications;
- Protect retail investors from excessive costs and ensure they receive value-for-money investments (i.e. efficient and effective financing);
- And considering the evolution of digital channels, promote stronger supervisory and enforcement practices.

This proposal is currently under negotiation at the Council level.

MiFIR Review

There is also the MiFIR review proposal focused on improving market transparency and structure which will have the most impact on firms and venues engaged in the wholesale trading markets. The review creates a mandatory framework for the so-called ‘consolidated tape provider (CTP)’. The consolidated tape will bring together the prices and volumes of financial instruments, such as shares and bonds, from hundreds of execution venues across all Member states into a single stream of information, equally accessible for everybody.

The review also includes a prohibition of the practice of ‘payment for order flow’ (PFOF) to increase the quality of execution and the amount of retail orders being performed on transparent and competitive public markets.

In addition, the MiFIR review provides for improved rules on transparency of 'non-equity instruments' such as bonds and derivatives as well as a set of rules aimed at making robust markets for commodity derivatives.

Overall, the new rules increase global competitiveness, better integrate EU capital markets and are a significant step towards a true capital markets union. A political agreement was reached in June with the EU Parliament, but technical meetings are still taking place.

Emir Refit

Another proposal which is under negotiations at the EU Council level is the Emir Refit. This proposal aims to modify the current framework that applies to EU central counterparties (CCPs) and market participants who use their services. They include measures to enhance EU CCPs' liquidity and strengthen the EU's CCP supervisory framework.

CAPITAL MARKETS UNION

Regarding the adoption of the actions of the Capital Markets Union (CMU) among other in May 2023 the Council and Parliament negotiators reached a provisional agreement on the proposal for a single access point for investors (the European single access point, ESAP). Under the provisional agreement, the ESAP platform is expected to be available from summer 2027 and will be phased in gradually to enable a robust implementation.

In addition, in June 2023, the Council and Parliament reached a provisional agreement in the creation of an EU-wide consolidated tape for trading and post-trading data via a review of the markets in financial

instruments regulation (MiFIR) and the markets in financial instruments directive (MiFID II).

CLOSING REMARKS

In conclusion, I would like to stress that whilst financial technology is creating new challenges, it also provides enormous opportunity for businesses to increase transparency, reduce costs and make information more accessible to Investors.

CySEC is fully committed to supporting these exciting developments. At the same time, we are also dedicated to ensuring that these applications are delivered in a prudent and compliant manner, and that investors are protected.

We also continue to contribute at National, EU and Global level to give Cyprus a strong voice, and we do this within the framework of EU regulation through ESMA and through our continued participation at various decision making and discussion forums.

I would like to re-iterate CySEC's strong commitment towards the responsible growth of the investment sector, one that is underpinned by rigorous supervision to safeguard investor protection, consistent with ESMA's mission to "Enhance investor protection and promote stable and orderly financial markets".

With these thoughts, I would like to thank you all for your kind attention.