



Overview of the CSSF Annual Report 2022: On-site Inspections

This newsletter marks the beginning of a six-part series, offering an overview of the CSSF Annual Report for the year 2022. The initial edition of this series is dedicated to highlighting the outcomes of on-site inspections.

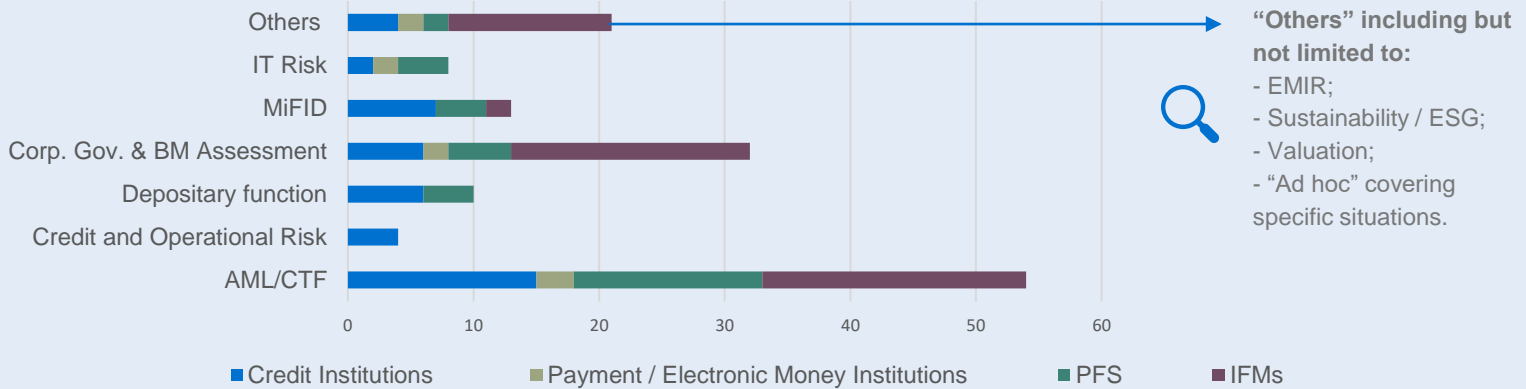
On the 25 August 2023, the CSSF published its annual report focusing on the overview of the CSSF activities and initiatives in 2022. This publication aims to provide valuable information to assist relevant entities in gaining an understanding of areas requiring attention based on the CSSF observations.

In upcoming publications, we will firstly deliver an overview of the key institutions under CSSF supervision, offering insights into various dimensions of CSSF supervision practices. Additionally, we will highlight significant past and forthcoming priorities, along with key findings from off-site inspections. Secondly, our focus will shift to the noteworthy regulatory changes that unfolded in 2022, providing a glimpse into anticipated developments for the years ahead.



This section provides an overview of key topics, and when disclosed, significant weaknesses and deficiencies identified by the CSSF during its on-site inspections.

Breakdown of the on-site inspections in 2022 by topic



Credit risk

Verifying the soundness and prudence of credit risk

- Lack of independent credit analysis by the risk control function covering the creditworthiness of the borrower;
- Significant delays and a lack of formalization were identified about credit monitoring;
- Methods used to calculate the expected Credit Loss was simplistic and lacked economic or statistical justification;
- Erroneous implementation of the regulatory framework on forbore exposures;
- Incorrect calculation of the amount of Risk Weighted Assets.



Operational risk

Verifying how operational risk is identified, controlled and managed

- Absence of a harmonized definition of operational risk;
- Absence of systematic quantification of operational risk based on concrete elements.



ICAAP (Pillar II)

Verifying that the credit institutions have established a suitable procedure for maintaining a sufficient capital level

- As of today, no results have been disclosed.



Pillar I

Verifying the correct application of the requirements for the computing of own funds

- As of today, no results have been disclosed.

Depository function

Verifying compliance with laws and regulations

- Absence of accurate and complete formalisation of ownership verification;
- Lack of risk-based approach concerning the monitoring of activities directly managed by the UCIs' leadership, applying to both the due diligence process of the different parties involved in the UCI management and the permanent control processes;
- Deficiencies in the internal control system of specialized PFS acting as depositaries, along with issues related to the allocation of their technical and human resources for task execution and documentation.

UCI Administrations

Ensuring proper implementation of CSSF Circular 22/811 on the authorization and organisation of entities acting as UCI administrators

- As of today, no results have been disclosed.

Business Model & profitability assessment

Checking how institutions' business and risk strategies are linked while pursuing their financial interests

- Absence of analyses of reliable performance factors;
- Inaccurate pricing methodology and profitability analyses of financial products;
- Lack of structures guidelines and systematic in-depth analyses with regard to financial planning.

On-site Inspections – Key Findings III/II



Corporate Governance



Evaluating the governance arrangements of some supervised entities pursuant to the regulatory and legal requirements.



The number of inspections and findings regarding Corporate Governance highlighted the focus on these regulations. Further developments in this respect might be expected.



- **Internal Policies and Procedures:** Lack of formal approval and / or weaknesses in the implementation;
- **Outsourcing:** Shortfalls in risks' identification and materiality level's assessment;
- **Board of Directors and Specialized Committees:** Lack of: (i) Physical or video meetings; (ii) Involvement of the board members with the internal control assessment;
- **Authorised management and management committees:** Shortcomings related to authorized management functioning and responsibilities: (i) Deficiencies in the supervision of the implementation of group policies within subsidiaries; (ii) Formalisation / communication of management decisions; (iii) Monitoring of the proper implementation of the recommendations issued by the control functions;
- **Compliance function:** (i) Weaknesses concerning the completeness and updating of the compliance programs; (ii) Implementation of controls that these documents define; (iii) Lack of specific budget, and sufficient resources allowing it to achieve its tasks;
- **Risk control function:** (i) Shortcomings in the definition and comprehensiveness of the limits system and risk appetite indicators; (ii) Absence of a risk management strategy;
- **Third line of defense:** (i) Deficiencies about the establishment of an audit plan; (ii) Weaknesses regarding the quality of the internal audit' function work, or the independence and objectivity of some internal auditors; (iii) The internal audit plans do not incorporate a risk-based approach;
- Deficiencies identified in the contractual framework and quality of the supervision of the outsourcing of some activities related to **EMIR**.



MiFID



Assess whether the implemented MiFID framework is compliant with the legal and regulatory requirements



- Major weaknesses identified on the **following themes:** (i) Suitability assessment of investment products or services; (ii) Product governance; (iii) Identification and management of conflicts of interest; (iv) Provision of information and reports to clients;
- Additionally, specific shortcomings were identified with regard to the **ex-post disclosure of costs and charges**, namely: (i) Some costs and charges elements were missing; (ii) Errors were noted in classifying different types of costs and charges; (iii) Incomplete cost impact illustration; (iv) Lack of client notifications when ex-post reports are made available electronically.



IT Risk



Assessing whether the implemented IT framework is compliant with the legal and regulatory requirements



- **IT Security:** Deficiencies in managing outdated IT systems and in configurations for protection against cyber threats;
- **IT Asset Management:** Weaknesses in the control and oversight of management of IT changes and incidents;
- **IT Risk Management:** Lack of adequate risk coverage by the second line of defense;
- **Internal Audit:** Incomplete coverage of IT activities, low-quality audit work, competence issues assessing IT risks, ineffective monitoring of corrective actions after audit findings;
- **Outsourcing deficiencies:** Weaknesses related to the contractual aspects and operational follow-up.



On-site AML/CTF supervision



Assessing whether the implemented AML/CTF framework is compliant with the legal and regulatory requirements



- **Name Matching Tool Efficiency:** Absence of controls for efficient name matching tools, leading to delays in official list updates and oversight;
- **Customer Review Delays:** Delayed periodic reviews of high-risk customer relationships;
- **Incomplete Risk Assessment:** Failure to consider all risk factors when assessing ML/TF risk, resulting in inappropriate due diligence measures;
- **Ongoing Transaction Monitoring Deficiencies:** (i) Scenarios employed did not effectively address risky situations (ii) Insufficient handling of alerts;
- **Customer File Information:** Insufficient information in customer files, especially regarding the source of funds and origin of wealth;
- **Reporting Failures:** Failures to promptly report ML/TF suspicions and associated predicate offenses to the Financial Intelligence Unit (FIU).



In 2022, administrative fines and prudential enforcement measures totaled EUR 5,880,931.8, marking a **36% increase** from the previous year's total of EUR 4,311,250.

Publication Timeline

This newsletter, the first in a series of 6 publications.



On-site Inspections

Published 13/09/2023



Credit Institutions

By 20/09/2023



IFMs and UCIs

By 27/09/2023



PFS

By 04/10/2023



Payment, Electronic Money Institutions and VASPs

By 11/10/2023



Challenges for the next years

By 18/10/2023

Why Mazars for you?

Joined-up Mazars engagement team



As a truly integrated partnership and firm, we operate seamlessly across borders. Our commitment to clients is absolute – we furnish you with a seasoned senior team well-versed in the intricacies of the field. You will benefit of senior leaders ‘on the ground’, poised to deliver not just insights but transformative, value-enhancing recommendations.



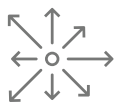
Tailored, pragmatic, joined-up approach



In these challenging times, Mazars is committed to support you navigating the regulatory challenges. As a service provider, our work is practical, and our conclusions and action plans will be pragmatic and fine-tuned to our clients’ needs. We will tailor our approach to ensure our work meets each and every client's specific requirements.



Personal and personable approach



We strongly believe that this sets us apart from the competition. Our commitment is to invest time and effort in truly understanding the unique environment of each entity we engage with. We approach every interaction with a willingness to listen, to empathize, and to adapt.

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