Institute of International Bankers

*Advancing the Interests of the International Banking Community in the United States*

# Global Survey 2016

## Regulatory and Market Developments

**Banking - Securities - Insurance**
**Covering 23 Countries and the EU**

**October 2016**

# OVERVIEW

The Institute of International Bankers represents internationally headquartered banking/financial institutions from over 35 countries in connection with U.S. legislative, regulatory, compliance and tax issues that affect their banking, securities, insurance and other financial activities in the United States. In the aggregate, IIB members' U.S. operations have more than $5 trillion in assets, fund 27% of all commercial and industrial bank loans made in the U.S. and contribute to the depth and liquidity of U.S. financial markets. IIB members also contribute more than $50 billion each year to the economies of major cities across the country in the form of employee compensation, tax payments to local, state and federal authorities, and other operating and capital expenditures.

This 29th annual *Global Survey of Regulatory and Market Developments in Banking, Securities and Insurance* is part of the IIB's ongoing efforts to contribute to the understanding of global trends in financial regulation and markets. This year's Global Survey covers developments during the period from July 1, 2015 to June 30, 2016 in 23 countries and the European Union (EU). We are very grateful to the banking associations and financial services supervisory authorities from those countries and the EU that have contributed to this year's Survey and without whose participation this publication would not be possible.

This year's Survey focuses on remaining implementation of regulatory reforms by various countries in regard to increased capital and liquidity safeguards, over-the-counter derivatives, resolution authority and risk restraints similar to the proprietary trading restrictions contained in the U.S. "Volcker Rule", as well as anti-money laundering efforts and how government authorities around the world are addressing cybersecurity threats to financial institutions operating in their jurisdictions.

In describing the diversity of initiatives undertaken in these areas by countries around the world, the Global Survey provides a useful point of reference for assessing these developments and their impact on the international financial community.

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## AUSTRALIA

The Australian economy has grown steadily over the past year, although income growth has slowed markedly as commodity prices have fallen. The most recent data shows the Australian economy grew by 3.1 per cent over the year to March 2016 in volume-adjusted terms, which is above-average growth reflecting strong growth in Australia's exports of mining commodities as well as service exports like education and tourism. But nominal income growth has been very weak as Australia contends with large falls in commodity prices and weak domestic demand. These headwinds led the Reserve Bank of Australia (RBA) to lower the official cash rate in May to 1.75 per cent, its lowest rate on record.

Subdued business investment, both in the mining sector and outside it, have significantly dampened growth and are yet to respond to lower cash rates. Household spending has been stronger, and the bright spot of the economy in recent years has been housing construction. Historically low interest rates, together with solid population growth have underpinned residential construction but the cycle looks to have peaked with forward indicators suggesting construction will slow in the coming years.

Overall, official forecasters predict the economy will expand by 2.5 per cent in both 2015-16 and 2016-2017 before strengthening to 3.0 per cent in 2017-18.[1]

Australia's economic growth, healthy financial system, and strong regulatory framework have underpinned continued sound performance by the Australian banks.

Australian banks' business models focus on lending, and the strong asset performance over the past year means profits remain strong as non-performing loans remain low. Major banks noted in their recent half-year updates that there had been some pick-up in non-performing loans in recent months; concentrated in housing loans in mining regions and some business-related impairments in the mining and dairy sectors. Overall these impairment charges are very small and while they are expected to pick up, the rise will be limited by stable employment and low interest rate environment. The most recent official data shows the quality of bank lending in Australia is high with non-performing loans at 0.6 per cent.[2]

Australia's banks, in their recent half-yearly updates, reported returns on equity had eased slightly, back below recent averages, to 13.8 per cent. This is due to Australia's banks lifting capital positions further above their minimum regulatory requirements in anticipation of the Basel requirements, as well as a pick-up in impairment charges booked. Looking ahead, analysts suspect a slight pick-up in impairment charges along with the maturation of the residential property market cycle which will see profitability ease further but remain firm by international standards.

Australia's four major banks continue to be well regarded by the ratings agencies. Australia's four major banks all hold an AA- rating, the highest rating any top 100 bank holds. However, S&P recently placed the banks on a negative watch which it attributed to its decision to

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[1] Department of Treasury and Department of Finance (May 2016), Pre-Election Fiscal and Economic Outlook; http://www.treasury.gov.au/PublicationsAndMedia/Publications/2016/PEFO-2016

[2] Reserve Bank of Australia (April 2016), Financial Stability Review; http://www.rba.gov.au/publications/fsr/2016/apr/pdf/financial-stability-review-2016-04.pdf

place Australia's AAA sovereign rating on a negative watch given sustained federal budget's deficit forecasts.

**Financial Regulation Developments**
*Australia's Housing Market*

Concerns over the strength of the housing market and perceived decline in lending standards, especially in the investor market in late 2015, prompted the Australian Prudential Regulatory Authority (APRA) and the RBA to introduce changes to pricing and underwriting criteria aimed at bringing investment lending within regulatory guidelines of 10 per cent annual growth a year.

These measures have been successful, with the most recent statistics from the RBA indicating investor housing credit has slowed dramatically over the past year slowing to 5 per cent growth over the year to June 2016, from a peak growth rate of 11 per cent growth over the year to June 2015. APRA data also reveals that growth in interest-only mortgage products favoured by investors has also slowed and the loan-to-valuation ratios on new mortgages have fallen.[3] Consequently, the RBA recently noted that "the performance of housing lending remains strong and some of the concerns associated with banks' mortgage portfolios have lessened", over the past six months.[4] APRA also noted that serviceability assessment standards have also been lifted across the industry.[5]

The RBA's concerns are now concentrated on lending to residential property developers given concerns about a building oversupply in some apartment markets.[6] These projects have been concentrated in small areas of several capital cities and have been directed at meeting the demand of offshore buyers. The anticipated price falls in these markets pose settlement risk to the developers if their buyers walk away from purchasing the property. Development is typically financed through presales to purchasers, who agreed on a purchase price before construction began, and who may be compelled to walk away from purchase on completion if the price falls are significant and/or their access to mortgage finance is reduced due to tighter lending requirements by the banks.

The measures to slow growth in lending to investors were introduced by APRA in late 2014, are likely to have tempered these risks somewhat. Furthermore, Australian banks have pulled back from lending to developers by tightening lending criteria especially in the areas considered most at risk of oversupply.[7]

[3] Australian Prudential Regulatory Authority (February 2016), Quarterly Authorised Deposit-taking Institution Property Exposures; http://www.apra.gov.au/adi/Publications/Pages/Quarterly-ADI-Property-Exposures-statistics.aspx

[4] Reserve Bank of Australia (April 2016), Financial Stability Review; http://www.rba.gov.au/publications/fsr/2016/apr/pdf/financial-stability-review-2016-04.pdf

[5] Byres, Wayne (Chairman of APRA), (5 April 2016), "From Strength to Resilience," Speech given to AFR Banking & Wealth Summit, Sydney, http://www.apra.gov.au/Speeches/Documents/04%20From%20Strength%20to%20Resilience%20-%20AFR%20Banking%20and%20Wealth%20Summit%20-%205%20April%202016.pdf

[6] Reserve Bank of Australia (April 2016), Financial Stability Review; http://www.rba.gov.au/publications/fsr/2016/apr/pdf/financial-stability-review-2016-04.pdf

[7] Reserve Bank of Australia (April 2016), Financial Stability Review; http://www.rba.gov.au/publications/fsr/2016/apr/pdf/financial-stability-review-2016-04.pdf

## The Financial System Inquiry

In late 2015, the Australian Government announced its response to the Financial System Inquiry's (FSI) Final Report. The government-appointed FSI panel had been tasked with laying out a direction for the future of Australia's financial system and their Final Report contained 44 recommendations focused on building the resilience of the banking sector. The government responded supporting all but one of the final report's 44 recommendations and made six additional recommendations.

Notably, APRA has been charged with building the resilience of the banking sector through lifting capital ratios to be "unquestionably strong" by international standards, as recommended by the FSI. Australia's authorised deposit-taking institutions (ADIs) have lifted their capital ratios in anticipation of the new APRA requirements, which are yet to be finalised. APRA is currently consulting on the standards required to achieve an "unquestionably strong" capital position, with the framework expected to be finalised by the end of 2016.

The FSI also included recommendations aimed at clarifying the powers of the Australian Securities and Investments Commission (ASIC) and the RBA to regulate new payments systems, like digital currencies. Another recommendation was to reintroduce the non-statutory Financial Sector Advisory Council who will be charged with providing advice on government financial sector policy. In May, the government announced ten appointments to this panel drawing on chief executives from banks, funds management, insurance, and financial services.[8]

## Basel III Implementation

The FSI's "unquestionably strong" capital requirements come at a time when the Basel III standards are also being finalised. Australia's banks raised $5 billion in equity capital over the six months to April 2016 in anticipation of these requirements.[9]

Furthermore, Australian banks using the internal ratings-based approach to credit risk are meeting the requirements of holding sufficient Tier 1 capital to total exposure, known as the leverage ratio. While the leverage ratio framework is yet to be finalised by the Basel Committee, Australian banks have reported a leverage ratio close to 5 per cent at December 2015, well above the minimum 3 per cent so far indicated by the Basel Committee.

APRA is currently consulting with industry on the implementation of the Net Stable Funding Ratio (NSFR); another Basel initiative that is aimed at reducing banks' reliance on short-term funding of long-term products. In the past, Australian ADIs have traditionally been reliant on offshore funding, but have shifted to a greater reliance on deposit funding. The NSFR is likely to continue this trend.

APRA is consulting with industry ahead of the implementation of another Basel initiative, the margining and risk mitigation requirements for over-the-counter derivatives. APRA has indicated that it plans to follow the internationally agreed standards, with some small local

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8 http://kmo.ministers.treasury.gov.au/media-release/067-2016/

9 Reserve Bank of Australia (April 2016), Financial Stability Review; http://www.rba.gov.au/publications/fsr/2016/apr/pdf/financial-stability-review-2016-04.pdf

modifications. These new margining requirements will be phased in from September 2016 and will apply to all APRA-regulated organisations, apart from private health insurers.

**Conduct and Culture in the Banking Industry**

In May 2016, Australia's banks committed to a package containing several reforms and inquiries, which are aimed at strengthening consumer and stakeholders trust in banks. This follows several issues of culture and conduct in the financial services sector.

The package announced by the Australian Bankers' Association (ABA) includes the following measures:

- Reviewing product sales commissions through an independent review.
- Strengthening complaints handling processes, including working with regulators on appropriate remediation for poor financial advice.
- Strengthening whistle blower protection within banks.
- Implementing an industry register to prevent individuals who have breached laws or codes of conduct from working in the industry.
- Strengthening commitment to customers through the Code of Banking Practice; and
- Supporting ASIC through the implementation of a "user pays" industry funding model. [10]

These reforms will be implemented over the coming months subject to regulatory and legislative approval. Issues of conduct and culture within financial services have also been highlighted by Australia's opposition party in the federal parliament. The Coalition conservative government was returned following a national election on July 2. If the opposition Labor Party had been elected, they would have commenced a Royal Commission into the financial services industry, and while they were defeated at the election, it remains part of their platform.

**Robo Advice**

ASIC is consulting on the regulation of digital financial product advice, or 'robo advice'. Overall, the corporate regulator welcomes the development of a healthy and robust digital advice market and agrees that this has the potential to offer convenient and low cost advice to clients. ASIC has taken the view that the law should be technology neutral and the legal obligations which apply to the provision of traditional (i.e. non-digital) financial product advice and digital advice, should be the same. The ABA has been advocating to ensure that regulations around adviser training and registration, best interest tests and ethical standards also applies to robo advice, the same way they apply to traditional financial advice.

**Other Regulatory Developments**

The RBA recently announced new rules following the Review of Card Payments regulation. The RBA has made a series of recommendations focused on the regulation of card payments covering interchange and surcharge fees. Most notably, retailers will be limited in the fees they charge associated with card use so that the surcharges only cover the cost of processing

[10] http://www.bankers.asn.au/media/media-releases/media-release-2016/banks-act-to-strengthen-community-trust

the transaction. Interchange fees charged between the retailer's bank and the customer's bank will also be curbed through limits to be introduced from September.

APRA is progressing the work on improving its crisis resolution powers in line with the Financial Stability Board's (FSB) international standards. APRA is consulting with the larger ADIs to ensure their plans to deal with stressed operating conditions are credible, and is also assessing the efficacy of its own resolution powers.

APRA's work program also includes the introduction of the FSI's recommendations around total loss absorbing capital (TLAC) standards recommended by the FSB for global systemically-important banks (G-SIB). No Australian-headquartered bank is currently identified as a G-SIB, so the requirement to conform to the TLAC standard is not necessary. However, the FSI recommended that APRA implement such a framework to deal with minimum loss-absorbing and recapitalisation capacity in line with emerging international practice, which was endorsed by the Government. APRA indicated they will observe the range of approaches emerging internationally before designing the framework and will "hasten slowly".[11]

### How Australian Government Authorities are Addressing Cyber Security

The Australian Government recently announced its new strategy on cyber security, which focuses on partnering with industry to reduce the risks of cybercrime. The Australian Government's Cyber Security Review, which is the government's first cyber security update since 2009, included significant increase in spending to the Defence Department focused on monitoring and preventing foreign cyber-attacks and increasing intelligence sharing. The government will also boost funding to initiatives aimed at cooperating with industry, including a Cyber Security Growth Centre which will focus on innovation in the cyber security space. Australia's financial sector is the second most prone to attack, behind the energy sector.

## CANADA

### Executive Summary

The banking system in Canada was one of the most successful in dealing with the global financial crisis and the Canadian banks have been ranked as the most sound in the world for eight years in a row by the World Economic Forum. Canada's banks are regulated by a number of federal agencies. Prudential regulation is conducted by the Office of the Superintendent of Financial Institutions (OSFI), while consumer-facing market conduct is regulated by the Financial Consumer Agency of Canada (FCAC). Deposit insurance is provided by the Canada Deposit Insurance Corporation (CDIC). The Bank of Canada and OSFI are active members of the Basel Committee on Banking Supervision. Canadian regulators have been active in adopting new and revised global regulatory standards.

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[11] Byres, Wayne (Chairman of APRA), (5 April 2016), "From Strength to Resilience," Speech given to AFR Banking & Wealth Summit, Sydney, http://www.apra.gov.au/Speeches/Documents/04%20From%20Strength%20to%20Resilience%20-%20AFR%20Banking%20and%20Wealth%20Summit%20-%205%20April%202016.pdf

Federal financial services legislation, including the *Bank Act* that governs the activities of banks in Canada, is required to be reviewed every five years, and the most recent review was in 2012. The next comprehensive review was scheduled to occur in 2017, but the 2016 federal budget postponed the review till 2019. The Canadian banks are currently discussing what modifications to the bank legislative and regulatory regime to propose to the government in the context of the 2019 review. Proposals by stakeholders to the government are expected to be submitted in late 2017.

**Federal Financial Legislation and Regulations**
***2016 Federal Budget Measures***

The 2016 federal budget measures reiterated the federal government's intent to have a system of exclusive rules to ensure an efficient national banking system. The budget also stated that a new consumer chapter of the *Bank Act* will bring together disparate provisions in the Act to create a comprehensive, consolidated framework and provide a set of guiding principles, reflecting that banks should act fairly and responsibly.

***AML/ATF Measures***

Legislative amendments to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (PCMLTFA) were passed on June 19, 2014. However, the changes have not yet come into force, pending the passage of the Regulations that will be required to fully implement the new requirements. Draft regulations were published in July 2015 and should be published in final form in the near term. The proposed Regulations included the following:

- The circumstances under which a reporting entity must make a determination that a client is a domestic politically exposed person or the head of an international organization, or a close associate or family member of such a person, and the measures to be taken as a result. The Regulations currently contain requirements with respect to politically exposed foreign persons.
- An update to the existing list of methods that reporting entities must use to verify the identity of their clients. The new methods would be more flexible and allow for a broader range of reliable and independent sources to be used. In particular, the amendment would identify the specific types of sources that are deemed reliable enough to be used on a standalone basis (e.g. government-issued photo identification documents), and broadly allow other types of sources that are reliable and independent to be referred to on a dual-method basis (i.e. in combination).
- An amendment would expand the definition of a signature to more broadly include electronic signatures, which would facilitate account openings in a non-face-to-face environment.
- An amendment would clarify that a reporting entity that relies on an agent (e.g. deposit broker) to verify client identity on its behalf could use identification measures that were previously undertaken by that agent on behalf of another reporting entity or itself with respect to the same client.
- An amendment would add an element to the list that should be considered in a reporting entity's risk assessment that requires reporting entities to assess and document the risks posed by the impacts of new developments and technologies on the existing risk assessment criteria (business relationships, products, delivery channels or geographic locations).

A second package of regulations, covering virtual currencies, prepaid access products, simplified customer due diligence for low risk entities and foreign money services businesses, is expected in the near term.

**Cybersecurity Threats to Financial Institutions Operating in Canada**

Cyber risk is a growing concern in today's world and particularly so for financial institutions. Given the reliance on technology and the growing interconnectedness of networks and systems, cybersecurity has been identified as a top priority for the Canadian government and OSFI.

- The Canadian government is expected to undertake a cybersecurity review in the near future. In the Prime Minister's mandate letter to the new Minister of Public Safety and Emergency Preparedness, the Prime Minister directed the Minister to "Lead a review of existing measures to protect Canadians and our critical infrastructure from cyber-threats, in collaboration with the Minister of National Defence, the Minister of Innovation, Science and Economic Development, the Minister of Infrastructure and Communities, the Minister of Public Services and Procurement, and the President of the Treasury Board."

- OSFI introduced a cyber-risk management self-assessment tool for federally-regulated financial institutions in 2013.

**Housing**
***Canada Mortgage and Housing Corporation (CMHC)***

The federal government announced several changes in December 2015 with the stated objectives to strengthen the resiliency of the housing finance system and promote long-term stability as well as balanced economic growth. The measures introduced were a coordinated effort by the Department of Finance, CMHC and OSFI. The changes included the following:

- Mortgage Insurance: The minimum down payment for newly insured mortgage increased from 5% to 10% for the portion of the house price between $500,000 and $999,999. The 5% minimum down payment for properties up to $500,000 remains unchanged and so does the 20% minimum down payment on properties over $1,000,000. This change was effective February 15th, 2016.

- Mortgage Securitization: CMHC revised its fee structure for the timely payment guarantee for NHA MBS and CMB securities. In addition, CMHC also announced that all NHA MBS sold into CMBs are subject to guarantee NHA MBS fees. The allocation methodology for new guarantees of Market NHA MBS was also revised. These changes will be effective July 1, 2016.
- Capital requirements for Mortgages: OSFI announced updates to regulatory capital requirements for loans secured by residential real estate. Capital will be tied to increases in local property prices and/or to house prices that are high relative to borrower incomes. Consultations with key stakeholders and the broader public have been taking place this year and the goal is to implement the final rules by 2017.

The federal government also finalized regulations that limit the extension of portfolio insurance through the substitution of mortgages in insured pools, tie the use of portfolio insurance

to CMHC securitization vehicles, and prohibit the use of government-backed insured mortgages as collateral in securitization vehicles that are not sponsored by CMHC. These new regulations also come into effect on July 1, 2016.

**Finance Canada Payments Advisory Committee (FinPay)**

In 2012, the federal government established a multi-stakeholder forum known as the Finance Canada Payments Advisory Committee (FinPay) to advise the government on public policy issues affecting Canada's payment system, and which continues to meet regularly. FinPay is currently engaged in discussions on a number of important payment files. This includes helping guide Canada's payment system operator, Payments Canada, on achieving its vision for the modernization and renewal of the core clearing and settlement infrastructure to support the changing needs of merchants, consumers and other end-users. It also includes working with government officials to pursue the development of a regulatory framework that would ensure appropriate oversight of Canada's retail payment system, which would respond to the growth of new technologies and service providers that have entered the payments market. These two issues have significant importance to the banks and will require a long-term focus and dedication to help shape the direction that is taken.

**Basel III in Canada**

Basel III adoption in Canada is progressing well with Canada ranked category 4 (i.e. final rules in force) on many Basel standards (e.g. definition of capital, capital conservation buffer, liquidity coverage ratio, leverage ratio disclosure requirements, G-SIB and D-SIB requirements) in the BCBS's *Tenth progress report on adoption of the Basel regulatory framework* (April 2016). OSFI is also developing domestic guidance in 2016 for the remaining Basel III standards highlighted in the report (please see further details below).

**Summary of Financial Crisis Regulatory Actions**
***Imposition of Enhanced Capital and Other Requirements***

As part of sound capital management and in response to the continuing uncertainty caused by regulatory reform, Canadian banks must be able to demonstrate to OSFI (both continually and prior to any transaction that may negatively impact their capital levels) that they have prudent internal capital targets and that they would have sufficient capital to meet their internal capital targets at all times. Canadian banks implemented the Basel III regulatory capital requirements on an "all-in" basis as of January 1, 2013, forgoing the Basel Committee's six year transition period.

As of January 1, 2016, the six Canadian domestic systemically important banks (D-SIBs) (i.e. Royal Bank of Canada, TD Bank Financial Group, The Bank of Nova Scotia, Bank of Montreal, CIBC, and National Bank of Canada) have been subject to enhanced capital requirements of 1% common equity tier 1 (a "D-SIB capital surcharge"). These banks are also subject to more intensive supervision and are required by OSFI to comply with the Basel Committee's risk data aggregation and risk reporting principles, as well as the Enhanced Disclosure Task Force's (EDTF) disclosure recommendations.

In 2016, OSFI is expected to publish an updated version of its *Capital Adequacy Requirements (CAR) Guideline* to reflect the Basel Committee's international standards and national discretion items, including:

- Capital requirements for equity investment in funds,
- Capital requirements for central counterparties (CCPs),
- Replacement of the current exposure method for calculating counterparty exposures for derivative contracts with the Standardized Approach to Counterparty Credit Risk (SA-CRR), and
- Countercyclical buffer.

OSFI is also expected to provide new domestic guidance on:

- Downturn Loss Given Default (LGD) floor for residential mortgages,
- Treatment of insured residential mortgages, and
- Treatment of purchased receivables.

***Bail-in Debt Framework***

In June 2016, legislation to implement a bail-in regime in Canada was passed. Corresponding bail-in regulations and a bail-in guideline, which would contain more detail on the bail-in framework, are expected to follow in late 2016, with implementation of the framework expected sometime in 2017.

***Recovery and Resolution Plans (RRPs)***

For several years, the Canadian D-SIBs have been developing RRPs in conjunction with OSFI and the CDIC; D-SIBs work with OSFI on recovery plans and with CDIC on resolution plans. The 2015 Budget made clear that D-SIBs themselves would be responsible for preparing resolution plans, rather than CDIC.

***International Financial Reporting Standard (IFRS) 9 Financial Instruments***

The banks continue to execute on project plans to adopt and implement IFRS 9 for the annual reporting period beginning on November 1, 2017 (Q1/2018 for banks with October 31 year-ends). The most significant area of change is implementation of the International Accounting Standards Board's (IASB's) expected credit loss (ECL) model for impairment. There has been much discussion on IFRS 9 implementation issues, including the incorporation of forward looking information, the modelling of multiple scenarios, and assessing a significant increase in credit risk. OSFI has also issued their final guideline, *IFRS 9 Financial Instruments and Disclosures*, which aims to provide Federally Regulated Entities (FREs) guidance on applying IFRS 9.

### *Risk Data Aggregation*

The Canadian D-SIBs are in the process of implementing data quality measures to ensure compliance with the BCBS's Risk Data Aggregation and Risk Reporting Principles. Canadian D-SIBs have been working closely with OSFI to ensure that compliance can be achieved by December 31, 2016, which is the implementation date set by OSFI.

### *Leverage Ratio*

In 2014, OSFI issued their guidelines on leverage requirements and leverage ratio disclosures. Beginning in Q1 2015, institutions were required to maintain a leverage ratio that meets or exceeds 3% at all times. The BCBS consulted on revisions to the leverage ratio in 2016; we expect these revisions to be finalized in the second half of 2016 and ultimately reflected in OSFI's corresponding leverage requirements guideline.

### *Liquidity Risk Framework*

The D-SIBs began to disclose their Liquidity Coverage Ratio (LCR) in May 2015, which was set at 100% (i.e. no phase-in period was permitted). In addition, banks continue to provide data to OSFI to support other liquidity monitoring tools, such as the domestic Net Cumulative Cash Flow (NCCF) measure. The NCCF captures the maturity spectrum between the 30-day LCR and 1-year NSFR and assumes a business-as-usual, non-stressed scenario.

In 2016, OSFI is expected to update its *Liquidity Adequacy Requirements (LAR) Guideline* for the anticipated implementation of the intraday liquidity monitoring tools and the Net Stable Funding Ratio (NSFR), which will follow the Basel implementation timelines (i.e. 2017 and 2018 respectively). We also expect guidance on the NSFR disclosure requirements.

### *Regulation of Over-the-Counter Derivatives*

In the fall of 2015, OSFI issued a draft guideline on margin requirements for non-centrally cleared derivatives, which closely adhered to the BCBS/IOSCO margin requirements issued in March 2015. The final version of the OSFI guideline was issued in February 2016, with an effective date of September 1st, 2016. The guideline allows for a substituted compliance approach for Canadian banks operating in foreign derivatives markets.

In February 2016, the Canadian securities commissions issued revised proposed rules regarding mandatory central counterparty clearing of derivatives. The mandatory clearing rules are expected to come into effect by the end of 2016.

## CHINA

### Significant Developments in the Banking Industry

- China Construction Bank London Branch (CCBL) joined the London Stock Exchange (LSE) as a member firm, according to LSE's statement issued in September 2015. It is said that LSE is fully committed to working to develop the off-shore RMB market in London as well as facilitating ever closer bonds between British and Chinese capital markets. CCBL is an official RMB clearing bank in Britain.

- On September 30, 2015, the People's Bank of China (PBOC) announced that China had opened its interbank foreign exchange (FX) market to foreign central banks and similar institutions. Foreign central banks and other monetary authorities, international financial institutions, and sovereign wealth funds are now allowed to trade all FX products directly – including spots, forwards, swaps and options – in China's interbank market without any quota restrictions. They can enter the market through three channels: entrusting the PBOC as their agent, using interbank FX market members as their agent(s), or becoming a foreign member. Foreign central banks and similar institutions are asked to register with the PBOC before participating.

- Starting from October 1, 2015, China places a cap on overseas cash withdrawals annually for China UnionPay users, aiming to clamp down on potential money laundering. Users will be limited to withdrawing a total of 50,000 *yuan* ($7,857) outside China's mainland from October to December 2015, and they will be subject to an annual cap of 100,000 *yuan* equivalent from 2016. Cash withdrawal overseas is not currently included in the $50,000 cap on individual purchase of foreign exchange in China.

- On October 8, 2015, China's Cross-Border Interbank Payment System (CIPS), which is designed as an "expressway" to facilitate RMB use in international trade and investment, began operations in Shanghai. The CIPS provides the services of cross-border clearing and payment for domestic and foreign financial institutions. The establishment of CIPS is a milestone as China is accelerating infrastructure construction of the financial system. For the first phase of the CIPS, 11 domestic banks and 8 foreign banks have been approved by the central bank to directly participate in the transactions under the new system.

- On December 25, 2015, the PBOC released a circular on its website, saying that commercial banks in China must verify the identity of clients when they open personal bank accounts to make sure they are using their real names. The PBOC said in a statement that despite real name requirements being in place since 2000, implementation was lax, and anonymous or fake bank accounts appeared from time to time.

- On December 28, 2015, Chinese authorities released a draft of new rules that tighten regulation of peer-to-peer (P2P) lending. The rules were drafted by several government departments including the China Banking Regulatory Commission (CBRC). The new rules will impose 12 restrictions on P2P platforms, prohibiting them from taking in public deposits, pooling investors' money to fund their own projects, or providing any kind of guarantee for lender.

- On December 28, 2015, the PBOC released detailed regulations of online payment services by non-bank institutions. The new rules require real-name registration for all non-bank payment accounts and classify them into three categories depending on the security levels. In addition to limiting the size of transactions, the new regulation also bans payment institutions from opening accounts for firms engaged in financial businesses.

- On June 3, 2016, the PBOC announced that it will change the rules for assessing bank's reserve requirement ratios (RRR) to help banks better manage liquidity. As of July 15, the RRR calculation will be based on the average of daily outstanding deposits, rather than the deposit level at the date of assessment. Calculating the RRR on offshore RMB deposits held onshore will also be based on the average of such deposit holdings in the previous quarter, not just the holdings at the quarter-end.

- On June 7, 2016, the PBOC issued regulations on bank card clearing, opening the process to foreign firms in a bid to boost fairness and improve services. Chinese and foreign firms can apply to become bank card clearing institutions and they will enjoy the same treatment in regards to qualification, procedure and operation management, according to the PBOC. Currently, only China UnionPay, the national bank card association founded in 2002, is approved by the PBOC to provide clearing services for bank card transactions.

**Significant Developments in the Securities Industry**

- On September 29, 2015, the China Securities Regulatory Commission (CSRC) announced that it had issued fines totaling 28.42 million *yuan* ($4.4 million) for illegal stock trading in eight cases.

- On September 14, 2015, China's National Development and Reform Commission (NDRC) announced the adoption of a pre-registration system that requires onshore companies to pre-register with the NDRC or selected local NDRC branches before issuing any kind of offshore debt with maturity of more than one year. This is required whether the debt is issued by the company or through its offshore subsidiaries or branches; or whether it is in Chinese *yuan* or a foreign currency. Companies are also required to file their completed debt issuance within 10 working days.

- In February 2016, China eased curbs on investment quotas and fund withdrawal for foreign investors in the securities markets as it seeks to open wider its capital market and lure overseas funds for Chinese equities, according to the State Administration of Foreign Exchange (SAFE)'s new rules. Participants in the Qualified Foreign Institutional Investor (QFII) program will be allowed to invest a base amount which is decided by a formula linked to their assets under management. SAFE also eased rules restricting QFIIs from moving funds in and out of China. Under the new rules, the capital lock-up period for QFII redemptions was cut to three months, down from one year formerly. QFII mutual funds are allowed to make subscriptions and redemptions daily, instead of a weekly basis, under the rules.

**Significant Developments in the Insurance Industry**

- In March 2016, China's insurance regulator ordered a halt on short-term insurance and financing products sold by insurers. The halt aims to improve the country's insurance industry, according to the China Insurance Regulatory Commission (CIRC). The halt includes insurance products with a maturity duration of less than one year. The authority has also said those with a maturity duration between one and three years will be reduced to half of the total quota over three years.

- China and Russia inked a memorandum to further cooperation on insurance regulation, according to a statement released by the CIRC on November 16, 2015. The statement said that the CIRC and Russia's central bank will facilitate information exchange and coordination on insurance regulation.

- On June 12, 2016, Shanghai officially launched the long-awaited insurance exchange, as part of efforts to build the city into an international insurance center. The exchange will help local businesses align with global insurance practices and channel risks outside the insurance market. It's an important step to promote the upgrading of China's insurance industry.

## EUROPEAN UNION

**Banking Supervision and Regulation**

*Finalisation of Basel 3*

The Basel Committee has launched a program to finalise the Basel 3 standards by the end of 2016. However the industry realises that the components of this finalisation program go far beyond the original scope of Basel 3 as agreed by the Group of Governors and Heads of Supervision (GHOS) in 2010. It embraces new policy proposals that could significantly increase the capital requirements for banks like the revision to the standardised approach for credit risk, the review of internal risk models and the new approach to operational risk.

The agreement should be reached in successive BCBS meetings throughout the second half of 2016. Thereafter, jurisdictions across the world shall start the transposition processes into local law. In the EU, the current amendments to the Capital Requirements Regulation (CRR) and Directive (CRD 4) could potentially overlap with the implementation of the new standards agreed by the BCBS. The finalisation of Basel 3 will be a long process.

*Single Supervisory Mechanism (SSM)*

The Single Supervisory Mechanism (SSM) has completed its first full supervisory yearly exercise over the 129 significant institutions under direct SSM supervision. The implementation of the new supervisory practices is a daunting task that is progressing thanks to the determination of the ECB management and staff and the commitment of banks. The leading supervisor of every bank has changed and also the SSM governance structure is new. The fact that the regulatory landscape is more complex and still in a state of flux compounds the difficulties associated with the transition to the new supervisory regime.

In the second year of SSM supervision, the ECB is consolidating the procedures put in place after the handover of responsibility from National Competent Authorities (NCA). The

decision and approval process has speeded up but it is still too slow in some areas. The Supervisory Review and Evaluation Process (SREP) is underway and will produce the second round of scores towards the end of the year. The options and national discretions embedded in the legislative texts are being scrutinised by the ECB after a second public consultation and are expected to be narrowed down significantly. The reporting burden has become an issue for banks and they claim that a streamlining process is needed.

*Single Resolution Mechanism (SRM)*

The Single Resolution Mechanism (SRM) became fully operational on 1 January 2016. It implements the EU-wide Bank Recovery and Resolution Directive (BRRD) in the euro area. The full resolution powers of the Single Resolution Board (SRB) also started to apply in January 2016.

*European Deposit Insurance Scheme (EDIS)*

On 24 November 2015, the Commission has proposed a euro-area wide deposit insurance scheme (EDIS) for bank deposits and has set out further measures to reduce remaining risks in the banking sector in parallel. The Committee of Permanent Representatives agreed to establish within the Council the Ad Hoc Working Party on the Strengthening of the Banking Union. The preparation of a draft report on the EDIS is currently ongoing in the European Parliament and it should be presented by the end of September.

**Financial Markets and Securities**

*Credit Rating Agencies (CRAs)*

On 23 October 2015, the European Commission adopted a report addressed to the European Parliament and the Council on the feasibility of an EU creditworthiness assessment for sovereign debt. Relating to the Credit Rating Agencies Regulation, the Commission also published a study on the Feasibility of Alternatives to Credit Ratings in December 2015 and a study on the State of the Credit Rating Market in January 2016.

*Markets in Financial Instruments Review (MiFID II/MiFIR)*

On 28 September 2015, the European Securities and Markets Authority (ESMA) submitted the final Regulatory Technical Standards on MiFID II/MiFIR to the Commission for endorsement. In April 2016, the European Commission informed ESMA about its decision to endorse the draft RTS on non-equity transparency, the ancillary test and commodity position limits only under the condition that certain changes are made.

On 24 May 2016, the Commission published the MiFID II Delegated Directive and the MiFID II Delegated Regulation was published by the Commission in April 2016, and the MiFIR Delegated Regulation was published on 24 May 2016.

In February 2016, the Commission proposed a one year extension for the application of MiFID II, in order to give ESMA, national competent authorities and market participants more time to build the necessary systems to comply with the new rules. On 4 May 2016, texts on the MiFID II and MiFIR ‘Quick Fix’ to delay implementation by one year were agreed in trilogue.

*Packaged Retail Investment Products (PRIIPS)*

On 11 November 2015, the Joint Committee of the ESAs published a consultation paper on PRIIPS Key Information Documents to gather stakeholder views on proposed rules on the

content and presentation of the Key Information Documents. The Joint Committee of the ESAs subsequently published the final draft RTS on 7 April 2016, which were then finalised and published by the Commission on 30 June 2016.

Due to the short timeline for implementation in the PRIIPs Regulation, in May 2016, 12 Member States sent a letter to the Commission, requesting the postponement of the application date of the articles of the PRIIPs Regulation which deal with the Key Information Document for nine months after the entry into force of the Regulatory Technical Standards. The Commission has so far refused to amend the deadline.

*Indices and Benchmarks*

On 15 February 2016, ESMA published a first discussion paper regarding the technical implementation of the Benchmarks Regulation seeking input from stakeholders on draft Regulatory Technical Standards (RTS) and Technical Advice (TA) to be sent to the European Commission. ESMA also held an open hearing on 29 February on the discussion paper. ESMA published a consultation paper on the draft implementing measures under the Benchmarks Regulation on 27 May 2016. The Regulation was published in the Official Journal on 29 June 2016.

*Central Securities Depositories Regulation (CSDR)*

CSDR requires ESMA to elaborate draft regulatory technical standards (RTS) and implementing technical standards (ITS) covering:

- the authorisation, recognition, supervision of CSDs, organisational and prudential requirements for CSDs, access requirements (between a CSD and its participants, by issuers to CSDs, between CSDs, and between CSDs and other market infrastructures),
- internalised settlement reporting requirements (covering securities transactions settled outside a securities settlement system), and
- settlement discipline measures.

ESMA delivered draft RTS on all the above mentioned issues. Those are currently under review by the EC.

ESMA also received a mandate from the European Commission to provide technical advice under CSDR on the level of penalties for settlement fails, and on the substantial importance of a CSD for the functioning of the securities markets and the protection of the investors in a host Member State. On 4 August 2015 ESMA delivered the technical advice and related impact assessment, to the European Commission that is currently still reviewing it.
On 16 December 2015, EBA delivered to the European Commission the final report on the draft RTS on CSD prudential requirements with the related impact assessment. Those are currently under review by the EC.

Additionally in order to contribute to the objective of ensuring supervisory convergence, and a level playing field with regard to the implementation of the CSDR and of the related Level 2 measures, ESMA might issue Guidelines, recommendations, opinions and Q&As.

*European Market Infrastructure Regulation*

On October 2015, ESMA submitted to the Commission a draft RTS for the central clearing of index CDS that was then adopted by the Commission in March 2016. The draft RTS for the central clearing of Interest Rate Swaps was then submitted to the Commission on 10 November.

The ESMA also published a consultation paper on indirect clearing arrangements under EMIR and MiFID on 5 November 2015.

The Commission announced in June 2016 that it intends to delay the timeline for the application of the margin requirements for non-centrally cleared OTC derivatives. The rules were originally scheduled to apply in September 2016, however as the rules will not be ready in time they will now be applied as of mid-2017.

*Capital Markets Union*

As widely announced, the CMU is a medium-to-long term project. However some important initiatives were immediately launched by the Commission. In fact, together with the CMU Action Plan, the Commission unveiled a first set of measures to relaunch high-quality securitisation and new rules amending the Solvency II regime to promote long-term investment in infrastructure. The Commission also proposed changes to the Prospectus Directive, with a view to making it easier and less expensive for small and medium-sized companies to raise capital.

In addition, the Commission launched two consultations on Venture Capital Funds and on Covered Bonds while others are expected to be launched soon.

Moreover in keeping with the principles of Better Regulation, the Commission also launched a call for evidence on the cumulative impact of financial legislation with the aim to identify possible inconsistencies, incoherence and gaps in financial rules agreed over the last five years, as well as unnecessary regulatory burdens and factors negatively affecting long-term investment and growth.

In the context of the CMU the Commission services are reviewing progress in removing barriers in the post-trade environment as efficient and safe post-trade infrastructures are essential to good functioning of capital markets. This follows the implementation of recent legislation and market infrastructure developments. This review is assisted by the European Post-Trade Forum, a Commission expert group which started work in March 2016. The Commission Services also aim to publish a study on conflict of laws in 2016 as regards securities ownership and debt assignment.

The Commission also launched a consultation on business restructuring and insolvency on 23 March 2016. The first stakeholder forum on insolvency took place on 7 April 2016 and further meetings are planned. The consultation feedback and impact assessment work will help the Commission to prepare a principles-based legislative initiative by the end of this year, building on national regimes that work well.

Finally it is also important to mention that the Commission is working with banking and business associations and Member States to develop solutions to better connect small and medium-sized enterprises (SMEs) with different sources of finance. The Commission asked leading European banking associations to look at ways to strengthen banks' feedback to SMEs

applying for credit by promoting best practices recently developed in some Member States across the EU. The Commission will also support the development of information systems to help small businesses to navigate new funding opportunities more effectively. The intention is to promote best practices in delivering relevant information to firms which could benefit from alternative funding sources and seek to build pathways between the most successful national or regional support platforms.

*Call for Evidence*

The Call for evidence on the cumulative impact of the financial reform closed at the end of January 2016. Overall, respondents have raised three principal sets of concern in respect of the legislation: (i) insufficient proportionality in legislation; (ii) a negative impact on the amount of financing available to the wider economy; and (iii) excessive regulatory burden due to unexpected interactions, duplications and inconsistencies. The Commission Services held a public hearing in May 2016. The analysis of responses will be completed this summer and the Commission Services will report on how they intend to follow up on the results of this analysis. This input will also feed into the scheduled reviews of individual pieces of legislation like the CRR/CRD IV review scheduled for December.

*Prospectus Directive*

In November 2015 the Commission issued a proposal to review the Prospectus Directive. The aim of the proposal is to reduce the costs for companies accessing capital markets and to simplify corporate capital-raising by reducing the cost of issuance and streamlining the approval process, whilst maintaining investor protection. The European Parliament's Committee on Economic and Monetary Affairs (ECON) draft report was published on 16 March 2016, although their work has been delayed by the departure of ALDE group rapporteur Philippe De Backer. The Council reached a General Approach under the Dutch Presidency on 03 June 2016.

**Financial Reporting and Taxation**

*Automatic Exchange of Information*

On 14 April 2016, Finance Ministers of the 5 largest EU Member States suggested in a common letter the immediate creation of transparency registers of beneficial owners and the launch of a pilot initiative for automatic exchange of information on beneficial owners.

The Parliament decided to set up an Inquiry Committee which will investigate breaches to AML and other EU law (AEOI, tax legislation) and the role played by financial institutions such as assets managers, insurers, ad-hoc vehicles; and the links between the EU legal framework and third countries tax systems.

*Tax Transparency Package and Action Plan on Fairer Corporate Taxation*

In accordance with its Work Programme of December 2014 and with its Tax Transparency Package communicated in March 2015, the Commission presented on 17 June 2015 an Action Plan on Fairer Corporate Taxation in the EU. This plan focuses on re-launching the Common Consolidated Corporate Tax Base (CCCTB) and capitalising on the OECD Action Plan on Base Erosion and Profit Shifting (BEPS) with a view to improve Transfer Pricing rules. These initiatives should bring taxation closer to where profits are generated and improve the tax environment for business. The Action Plan also seeks to enhance tax transparency notably through the automatic exchange of information on tax rulings and the reform of a number of EU coordination tools (e.g.

the coordination on tax audits between Member States, the Code of Conduct Group on Business Taxation and the Platform on Tax Good Governance).

*Anti-Tax Avoidance Directive*

On 28 January 2016, the European Commission published the proposal for a so-called Anti-Tax Avoidance Directive. It would apply to all taxpayers which are subject to corporate tax in an EU Member State, including corporate taxpayers without cross-border activities. The Directive includes measures such as a general interest limitation rule; a provision on exit taxation; a general anti-abuse rule and a framework against hybrid mismatches which addresses both hybrid entities and hybrid instruments.

*Financial Transaction Tax*

The EU 10 Member States postponed any decision until June 2016 in order to clarify their positions. It was noted that while for some countries reservations were due to new governments, others continue to fear effects on the real economy. The European Commission should reassess the revenue that the proposed Financial Transaction Tax could raise.

Actually, some countries still have concerns over the financial viability of the proposed tax. Notably, Estonia left the enhanced cooperation in December 2015 and the Belgian, Slovakian and Italian governments are still considering their participation in the cooperation. A minimum of 9 Member States are needed for enhanced cooperation to be allowed under the Treaties.

**Retail Financial Services and Payments**

*Green Paper on Retail Financial Services*

On 10 December 2015, the European Commission published a Green paper on Retail Financial services and Insurance with a deadline to respond on 18 March 2016. This Green Paper seeks the views on how to improve choice, transparency and competition in retail financial services to the benefit of European consumers and how to facilitate true cross-border supply of these services. Preliminary results of the consultation were published on 24 March 2016. A feedback statement on the Consultation should be published in July 2016 and an action plan in October/November 2016.

The European Parliament is currently preparing an own-initiative report to present its views and to give some orientations on the next steps the European Commission should take. Digitalisation, improving consumer trust and removing barriers to cross border supply should be the key priorities of the Green Paper.

*Payment Services Directive (PSD2) -*

After the adoption of the revised Directive on Payment Services (PSD2) in November 2015, the European Banking Authority (EBA) has published a consultation document on Secure Customer Authentication and secure communication with Third Party Providers (TPPs), as part of the forthcoming PSD2 level 2 measures. An ad hoc meeting was subsequently organised by the EBA to further investigate EBF proposal to make full use of the eIDAS Regulation to certify TPPs. Draft requirements for Regulatory Technical Standards will be published during the summer (presumably mid-August) for a 2 months consultation, for final approval by the end of 2016. The Euro Retail Payments Board (ERPB) is considering working on the effective deliverables that must be inter-operable, open and harmonised.

*Interchange Fees Regulation -*

Many provisions of the Regulation on interchange fees for card-based transaction adopted on 29 April 2015 are already applicable (interchange fee caps, choice of application and brands at the Point of Sale, separation of scheme and processing,…). The European Commission (DG Competition) is currently coordinating a study, so called "zero study" to gain intelligence on the way banks charge their clients, retailers and consumers, the costs for managing cards, in view of revisiting the interchange fee rates in 2019. A further drastic drop in interchange fee rates for both debit and credit is expected in the range of 0€for debit and 0.15% for credit.

*Payment Accounts*

On 12 April 2016, The European Banking Authority published an Opinion on the application of customer due diligence measures to customers who are asylum seekers from higher-risk third countries or territories.

Initially, the European Banking Authority was supposed to prepare draft regulatory technical standards on Union standardised terminology for those services that are common to at least a majority of Member States, by 18 September 2016. In addition, after consulting national authorities and after consumer testing, it was supposed to develop draft Implementing Technical Standards regarding a standardised presentation format of the fee information document/statement of fees and their common symbol. A consultation paper with draft technical standards will only be published during the summer 2016 with a 3 months period consultation in order to final them for the first part of 2017 (6 months later than the initial date).

*Digital Banking*

The European Commission aims at creating a Digital Single Market (DSM). This DSM strategy is made up of three policy areas: a) Better online access to digital goods and services, to help to make the EU's digital world a seamless and level marketplace to buy and sell; b) An environment where digital networks and services can prosper, to design rules which match the pace of technology and support infrastructure development; and c) Digital as a driver for growth, to ensure that Europe's economy, industry and employment take full advantage of what digitalisation offers.

Following several consultations in 2016 a package of initiatives was published which notably target the platforms, cloud, e-commerce and the prohibition of geo-blocking.

In addition, in June 2016, the Commission adopted a Communication "A New Skills Agenda for Europe" which includes targeted actions on Digital Skills to support co-operation among education, employment and industry stakeholders. It also published a consultation on the safety of apps and other non-embedded software.

On 1 July 2016, the new rules on trust services under the eIDAS Regulation came into effect in the Member States. This Regulation lays down a new legal framework for trust services and grants a safe access to services and transactions online and across borders to the EU citizen, administrations and businesses.

The Commission should publish by the end of 2016 an initiative on the free flow of data within the EU in order to provide clear rules to prevent unjustified localisation requirements and to address the issues of data ownership.

**Corporate Governance and Financial Crime**

*4th Anti-Money Laundering Directive -*

On 5 June 2015, the AML package (Regulation (EU) 2015/847 on information accompanying transfers of funds and the Directive "AMLD4" (EU) 2015/849 was published in the Official Journal of the European Union. The deadline of implementation is the 26 June 2017.

The 4th AML Directive aims at updating the EU legislative framework to incorporate the necessary changes following the FATF recommendations published on 16th February 2012.The Scope of the Directive is extended to cover online gambling. It should be noted that Money Laundering definition now covers tax crime. The ultimate objective is to strengthen money laundering prevention systems by the use of the "risk based" approach.

Following the terrorist attacks last year in France, the Commission proposed on 2nd February 2016 a Joint Action Plan to on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing. The aim of this Action Plan is to build on existing EU rules and complementing them where necessary. Through concrete measures, it will adapt or propose additional rules to deal with new threats. The Action Plan lists a number of measures that will be put into practice by the Commission immediately. Others measures will follow in the months to come. All the actions presented in the Action plan should be carried out by the end of 2017.

One of the immediate actions, was to amend the AMLD 4. The Commission legislative proposal was published on 5th July (2016/0208 (COD)) including targeting amendments on tax transparency and tax avoidance which is a direct consequence of the release of the Panama papers.

*Corporate Governance*

Revision of the Shareholders' Rights Directive: On 9 April 2014, the Commission released its proposal for revision of the shareholder rights Directive. The proposal lists the following preferred policy options: Creating a framework to allow listed companies to identify their shareholders and requiring intermediaries to rapidly transmit information to shareholders to facilitate the exercise of shareholder rights (Articles 3a to 3e); Mandatory transparency of institutional investors and asset managers on their voting and engagement and certain aspects of asset management arrangements (Articles 3f to 3h); Binding disclosure requirements on the methodology and conflicts of interest of proxy advisors (Article 3i); Disclosure of the remuneration policy and individual remunerations, combined with a shareholder vote (Articles 9a and 9b); Additional transparency and an independent opinion on more important related-party transactions and submission of the most substantial related-party transactions to shareholder approval (Article 9c); In the EC, the file is under the responsibility of the unit in charge of corporate governance and company law within DG JUSTICE.

The Council's compromised proposal was approved on Wednesday 25 March 2015. The European Parliament approved its version of the text on 08 July 2015. First political trilogue meeting took place on 27 October 2015. Five technical meetings were held under the auspices of

the Luxembourg Presidency (13, 16, 30 November and 7 December 2015 and 15 January 2016). Other technical meetings, under the Dutch Presidency, were held on 19th and 26th February 2016. The second trilogue meeting has been scheduled for the end of June 2016, however, it is likely that it will be conducted only in the second part of the year under the Slovak Presidency. It is not yet clear when the conclusion of the trilogue should be expected due to protracted discussions concerning provisions related to the Country-By-Country Reporting which were included in the final proposal by the European Parliament and which are not acceptable by the Council.

Remuneration: The CRD IV and CRR have introduced the toughest remuneration rules for banks in the world. These rules have been applicable from 1 January 2014. Under Article 161.2 of the CRD IV the Commission is required to submit to the European Parliament and the Council by 30 June 2016 a report on the implementation of the remuneration provisions of the CRD IV.

It is expected that the Commission's report will endorse the EBA's opinion on the application of the principle of proportionality to the remuneration provisions in Directive 2013/36/EU. According to the EBA's opinion, there exist wide divergences among the EU member states in applying the remuneration provisions of the CRD IV. In order to have a uniform application of these rules, EBA suggested that the Commission amends the remuneration provisions to explicitly allow use of waivers of some of the provisions under certain conditions. Therefore, it is expected that the Commission will suggest that the remuneration provisions are amended.

*Data protection*

On 14th April 2016, the European Parliament adopted the data protection reform package. The data protection reform package includes the General Data Protection Regulation (GDPR) and the Directive for data protection in the police and justice sectors. On 4th May 2016, both the GDPR and the Directive were published in the Official Journal of the European Union. The reform should provide clarity as regards the rules to be applied for data processing, and improve the control of EU citizens over their data.

In May 2016, a plenary debate on the proposed EU-U.S. Privacy Shield took place in the European Parliament. Following the debate, the European Parliament adopted a non-binding resolution, in which it indicates the need for introducing further improvements to the proposed EU-U.S. Privacy Shield. In particular, the resolution calls on the European Commission to fully implement the recommendations set out by the Article 29 Working Party in its Opinion 01/2016 on the EU-U.S. Privacy Shield draft adequacy decision. On 30 May 2016, the European Data Protection Supervisor (EDPS) also published its Opinion 4/2016 on the EU-U.S. Privacy Shield draft adequacy decision, and asked for necessary improvements of the draft adequacy decision.

*Cybersecurity –*

On 17 May 2016, the Council formally adopted the Network and Information Security (NIS) Directive, which introduces new rules toward the implementation of a security of network and information system across the EU. The NIS Directive requires operators of essential services, including in the banking sector, and providers of key digital services, to take appropriate security measures and report incidents to the national authorities.

The Council position at first reading is in line with the agreement reached with the European Parliament on 8 December 2015. The Netherlands Presidency together with the EU Agency for Network and Information Security (ENISA) has already started preparing the implementation of the Directive through informal meetings.

**Economy, Business and Trade**

*Investment Plan for Europe*

The European Commission's Investment Plan for Europe, also known as the 'Juncker Plan', is a 3-year infrastructure investment project launched in November 2014. The Investment Plan focuses on removing obstacles to investment, providing visibility and technical assistance to investment projects and making smarter use of new and existing financial resources. To achieve these goals, the plan is active is three areas: mobilising investments of at least €315 billion in three years; supporting investment in the real economy; and creating an investment friendly environment.

On 28 May 2015, EU legislators successfully concluded negotiations on the Regulation for a European Fund for Strategic Investments (EFSI), the core of the Investment Plan for Europe which should be operational by September 2015.

On 30 October 2015, the European Commission published a one-year review report since the launch of the Investment Plan. Progress will be reviewed, including at the level of Heads of State and Government. Further options may be considered ahead of the mid-term review of the Multi-annual Financial Framework.

## FRANCE

**Law Sapin II: bill on transparency, the fight against corruption and the modernisation of the economy**

*Investment banking and market activities: the derivatives activity (EMIR) and the lending capacity of certain funds*

- The Law Sapin II (not adopted yet) will amend the French banking secrecy rules and adjust them to the EMIR's constraint imposed on counterparties to report to a "*trade repository*" the derivative contracts they have entered into (or modified or terminated).

  The banking secrecy exemptions provided for by EMIR cover only the reporting made to a trade repository located in the European Union (EU). In order to exempt French banks from any criminal risk in case of a reporting made outside the EU, the *Code monétaire et financier* (French Monetary and Financial Code) will expressly state that any reporting made to a trade repository, wherever it is located (i.e. in the EU or outside the EU), shall not be considered as a breach of the French banking secrecy rules.

- The Law Sapin II will also extend (within limits to be still determined) the lending capacity of certain funds (i.e. the long term investment funds which are dedicated to professional investors) in favor of the industrial and commercial companies.

*Article 51 of the Law Sapin II: introduction of a new category in the ranking of creditors of credit institutions under French insolvency law, in order to facilitate the implementation of resolution procedures*

The purpose of the article 51 of the proposed law is to introduce a new category in the ranking of creditors of credit institutions under French insolvency law, in order to facilitate the implementation of resolution procedures, as provided for in Directive 2014/59/EU of the European Parliament and of the Council, by creating legal certainty about the loss absorbing capacity of a newly created class of senior unsecured debt securities or instruments (hereinafter referred to as 'senior non-preferred debt instruments').

In particular, the proposed legislation introduces in the existing insolvency hierarchy of creditors of a credit institution the new category of senior non-preferred debt instruments. These senior non-preferred debt instruments consist of debt securities or instruments with characteristics similar to debt securities other than structured debt securities. The original maturity date of senior non-preferred debt instruments will be not less than one year. Finally, the contract of issuance for senior non-preferred debt instruments is required to provide that the owner or holder is unsecured within the meaning of this specific provision creating this new category of senior non-preferred debt instruments.

In the hierarchy of creditors, owners of senior non-preferred debt instruments will rank before creditors holding subordinated debt and after the following categories of creditors, respectively: (1) certain specified preferential or secured creditors; (2) creditors in respect of the portion of their deposits covered by the Deposit Guarantee Scheme (DGS); (3) certain other specified depositors, comprising natural persons and micro, small and medium-sized enterprises either (a) for the portion of their deposits that are eligible for coverage under the DGS and which exceed the coverage level of EUR 100,000 or (b) for the deposits which would be eligible for coverage under the DGS if they had not been made with branches of a credit institution located in a country which is not a Member State of the European Union or the European Economic Area; and (4) creditors other than owners of senior non-preferred debt instruments.

The draft provisions also specify that the new provisions do not have retroactive effect and will apply only to insolvency proceedings that commenced following the entry into force of the law that will contain the draft provisions.

*The fight against corruption*

The Law called « Sapin II » sets out a French Anti-corruption Agency which operates under the authority of the Minister of justice and the budget Minister and whose mission is to reduce corruption, trading in influence, unlawful taking of interest, misappropriation of public funds and favoritism.

This bill requires companies to have an anti-corruption plan encompassing:

- A code of conduct;
- An internal warning system;
- A risk mapping;

- Assessment procedures of clients and suppliers's position;
- Procedures of internal and external accounting control;
- Implementation of training systems;
- Disciplinary measures.

Sapin II creates a general regime applying to all whistleblowers and laying down a common definition, warning channels and protective measures.

**French Banking Sector Facts and Figures**

The banking sector is one of France's main economic assets, according to the OECD. In January 2016, the French banking industry numbered 378 banks. Financial corporations account for 4.5% of total value added in France, of which approximately 60% for the banking industry. There are five French banks among the 35 largest banks in the world in terms of Tier 1 capital. The banking industry employed more than 370,000 people at the end of 2015, representing 2.3% of the private workforce in mainland France.

The results of the combined asset quality assessment and stress testing, conducted by the European Banking Authority and the European Central Bank, demonstrate the high level of capitalization of French banks. French banks are far more resilient than in 2007, with a solvency ratio that has doubled, from 6% to 12%.

The six largest French banking groups, which mostly operate according to the 'universal banking' model, reported a strong financial performance in 2015, with total net banking income of 146.3 billion euros (+7.3% compared to last year), of which retail banking activities account for 67.1%, a total cost of risk of 12.9 billion euros (up 2.2%) and group net income of 23.7 billion euros (up 65.9%).

French banks are contending with a growing number of international and European regulatory requirements and heavier tax burdens.

*French banks at the core of financing the economy*

Regulatory changes and advances in technology are prompting banks to transform and adjust their models for financing the economy. Despite these hurdles, French banks continue to finance businesses and households. At the end of 2015, outstanding loans to the economy stood at 2,092 billion euros, up 4.0% year-on-year.

Outstanding loans to businesses stood at 874 billion euros at the end of December 2015, up 4.2% year-on-year. Investment outstanding loans were the fastest-growing segment, at 605 billion euros (+3.1%). Short-term loans rose by 6.6%.

SMEs are the primary beneficiaries of bank lending. Loans to SMEs accounted for 43% of total loans granted to businesses in December 2015. Total outstanding loans to these businesses rose by 3.1% year-on-year. Applications for loans by SMEs were very broadly approved, with nine out of 10 SMEs obtaining the investment loans they requested and eight out of 10 SMEs receiving

the short-term loans requested in the last quarter of 2015. However, demand for loans remained low in 2015: only 24% of SMEs sought an investment loan and 8% requested short-term loans.

French banks also actively finance the projects of French retail customers. Outstanding household loans stood at 1,055 billion euros at the end of December 2015, up 4.0% year-on-year. Most household loans were home loans, representing 866 billion euros (+3.9% year-on-year).

*The financing model is evolving*

Businesses are increasingly using the financial markets and banks are actively helping them find new sources of financing. Out of total corporate financing of 1,431 billion as of the end of December 2015, the proportion of bank lending to market financing was 61%/39%, compared to 70%/30% at the end of 2009.

**Cybersecurity**

*Background*

In 2013, the Wall Street Journal estimated that the cost of cybercrime in the U.S. was approximately $100 billion. The estimate disputed other reports which pegged the numbers by as much as ten times higher.

In 2015, the British insurance company Lloyd's estimated that cyber-attacks cost businesses as much as $400 billion a year, which includes direct damage plus post-attack disruption to the normal course of business.

From 2013 to 2015 the cybercrime costs quadrupled, and it looks like there will be another quadrupling from 2015 to 2019. Juniper research recently predicted that the rapid digitization of consumers' lives and enterprise records will increase the cost of data breaches to $2.1 trillion globally by 2019, increasing to almost four times the estimated cost of breaches in 2015.

The World Economic Forum (WEF) says a significant portion of cybercrime goes undetected, particularly industrial espionage where access to confidential documents and data is difficult to spot. Those crimes would arguably move the needle on the cybercrime numbers much higher.

Large banks, retailers, and federal agencies make the headlines when they are hacked - but all businesses are at risk. According to Microsoft, 20% of small to mid-sized businesses have been cybercrime targets.

Cybercrime is fuelling the market for cybersecurity products and services, which is expected to grow from $75 billion in 2015 to $175 billion by 2020. The cyber insurance market is also getting a boost from cybercrime – and projected to grow from $2.5 billion in 2015 to $7.5 billion by 2020.

**Actors**

Cyber criminals

Besides “ethic attackers” or “nation state attackers” with their own “motivation”, the cyber criminality is now well organised in the “dark web”, with specialists dedicated in a various range of products and services. Attackers are becoming more sophisticated, more resourceful, and better organized than some years ago.

The European Parliament published the main cyber threats in 2014, confirming the diversity of attacks.

LEA – Law enforcement authorities

EUROPOL:

In Europe, in 2013, EUROPOL has created EC3 (European Cyber Crime Centre) to strengthen the law enforcement response to cybercrime in the European Union (EU) and to help protect European citizens, businesses and governments.

SDLC :

In France, the Sous Direction de lutte contre la cybercriminalité (Central Cybercrime Prevention Office) was created in 2014 under the Ministery of Interior (Police Judiciaire).

ANSSI (Agence Nationale de la sécurité de systèmes d’information):

This French Network and Information Security Agency is the national authority in the area of cyberdefence and network and information security (NIS). As a national authority, ANSSI reports to the Secretary General for Defence and National Security (secrétaire général de la défense et de la sécurité nationale - SGDSN). The SGDSN assists the Prime Minister in fulfilling his responsibilities in matters of national defence and security.

To fulfil its missions, ANSSI deploys a broad range of regulatory and operational activities, from issuing regulations and verifying their application, to monitoring, alert and rapid response – particularly on government networks.

Others organisations

FS-ISAC :

Launched in 1999, FS-ISAC, or the Financial Services Information Sharing and Analysis Center, is the global financial industry's go to resource for cyber and physical threat intelligence analysis and sharing.

FS-ISAC is able to disseminate to its more than 6,000 members (financial services firms worldwide), physical and cyber threat alerts and other critical information issued by financial services providers, commercial security firms, federal/national, state and local government agencies, law enforcement and other trusted resources.

Global Cyber Alliance:

Global Cyber Alliance ("GCA") is an international, cross-sector effort designed to confront, address, and prevent malicious cyber activity, founded by the New York and London Police departments. This organization has now an international “recognition”.

Cybersecurity companies

The business of these companies is focused on detecting malwares/cyber attacks and on providing their customers with high value technical solutions of cybersecurity. The main are Symantec, Trend Micro, Kaspersky,IBM, FireEye, … (not exhaustive list).

Financial institutions

Financial institutions are a prime target for cyber criminals and are subject to daily attacks generating more and more significant damages, including personal data theft or embezzlement, online-bank websites suddenly unavailable or employees' computers infected, denial of service attack, espionage, and sabotage.

For years, huge investments have been made by the banking sector to hedge such risks and will be maintained in the future as to keep the highest degree of safety to comply with new European and French regulations.

Because threats and attacks are multiple and internationally originated, cooperation is the key action to response to this criminality.

Other "targets"

Besides financial institutions, everybody, individuals or small and medium sized companies, big companies, in all business sectors, being of public or private sector, mainly in developed countries, are targets for cyber criminals.

**Cooperation**

At a European level, the European Banking Federation has created a cybersecurity working group with participants of around 25 countries. With quarterly meetings, the WG allows participants to have the benefits from different kinds of expertise.

Moreover, in September 2014, the European Banking Federation and Europol's EC3, signed a Memorandum of Understanding which paves the way for intensifying cooperation between law enforcement authorities and the financial sector in the EU.

In 2016, one major initiative has been launched with the European extension of the "Online Fraud Cyber Center and Expert Network (OF2CEN)" created in 2015 by Italian Police and Banks.

The EU OF2CEN information sharing initiative is a European project with a primary focus on European Member States aiming at fighting the financial crime by a stronger cooperation between public and private entities among European countries. France is part of this initiative.

In France, FBF has initiated a cooperative relationship with the French Police and the main projects are (i) to improve the fight against the false CEO wire transfer schemes and (ii) to build a framework to better combat all kind of malwares (in cooperation with EC3/Europol). Actions against fraud are also part of the action plans among the banking industry.

**Regulation**
2016 saw 2 new main European regulations related to cyber:
EU General Data Protection Regulation (GDPR)

The EU General Data Protection Regulation (GDPR) was finally approved by the European Parliament in April 2016. All organisations that process personally identifiable information (PII) must comply with the Regulation by 25 May 2018 or face penalties of up to €20 million or 4% of annual global turnover – whichever is the greatest.

The objective of this new set of rules is to give citizens back control over of their personal data, and to simplify the regulatory environment for business. The data protection reform is a key enabler of the Digital Single Market which the Commission has prioritized. The reform will allow European citizens and businesses to fully benefit from the digital economy.

NIS Directive

The Network and Information Security (NIS[12]) Directive was adopted on 6 July 2016. The Directive will enter into force in August 2016. Member States will have 21 months to transpose the Directive into their national laws and 6 months more to identify operators of essential services.

This regulation aims to increase the level of protection against network and information security incidents, risks and threats across the EU and, in terms of its impact on businesses, will affect "operators of essential services" in critical sectors (such as energy, transport, banking…) and "digital service providers" (such as cloud computing service providers).

In France, this European regulation will be closely linked with the current provisions of the Military Planning Act 2014-2019[13] already covering the critical infrastructures essential for the maintenance of vital economic activities as defined by ANSSI.

Some French banks are regulated by this law and must comply with some specific rules and obligations. The French banking sector and the FBF fully approve this evolution of security/safety measures and maintain a close cooperation with ANSSI to facilitate the application of the new regulation.

**Fédération Bancaire Française**

Since 2014, FBF has strengthened its actions to improve cyber security and to better answer the needs of the French banking community and develop cooperation in France and at the European level.

Internally, the FBF's Committee dedicated to Major Risks and Security is now closely working with the main bank's Chief Information Security Officers (CISO / RSSI en français): the objective is to centralise main points of attention on cybersecurity and to determine the global actions to share with French or European regulators.

[12] Directive (EU) 2016/1148 of the European Parliament and of the Council of 6 July 2016 concerning measures for a high common level of security of network and information systems across the Union
[13] Loi de programmation militaire – le décret d'application sectorielle (Finances) sera publié d'ici fin 2016.

Moreover, in the near future, the main French banks' global fraud managers will join this Committee to broaden its coverage to all cyber issues. Besides FBF, CISOs maintain a very close contact to cover technical and operational matters, through the CERTs[14] network and within an association of French banks and insurance companies' CISOs.

At FBF, the main objective is to maintain customer trust vis-à-vis the banking sector that is essential to preserve. The banking relationship is based on trust and security. In an environment of rising cybercrime, banks are continuing their efforts to combat fraud and ensure their clients' data is protected. The banks' ability to protect the integrity of the financial system, both in terms of payments and protection of cyberdata, is an advantage given the increasing sophistication of cybercrime. As a result, the banks are constantly investing in system security and fraud prevention. French banks also benefit from high levels of trust on the part of their clients. It is why the FBF pursues initiatives to alert all stakeholders on the issues of security and supervision involved by the PSD2 which was definitively adopted this year.

## GERMANY

**German legislation has issued its draft Administrative Principles for Profit Attribution to Permanent Establishments to provide clarification concerning the application of the Authorised OECD Approach (AOA). The final administrative principles are expected to be published in the second half of 2016. In order to facilitate the restructuring of companies an evaluation of the insolvency law reform is scheduled for 2016. Other reforms are taking place in the field of company law, risk management and insolvency regulation. In addition, paydirect, a new scheme for online payment, has been introduced at the end of 2015 offering consumers and merchants a joint payment scheme with which it is possible to pay directly from one's own bank account.**

### New Developments in Company Law

The law amending the Stock Corporation Act (*Aktienrechtsnovelle 2016*, formerly *Aktienrechtsnovelle 2014*) entered into force on 31 December 2015. The new law is designed to further develop current stock corporation law. One main change is that banks operating in the legal form of a stock corporation (*Aktiengesellschaft*) will be allowed for the first time to generate Tier 1 capital by issuing non-voting preference shares that do not give entitlement to deferred dividend payments. In addition, reversible convertible bonds providing for a conversion right of the issuer, i.e. the company, are to be introduced.

### New Developments in Insolvency Law

Currently, there are two major proposals for reform:

- A draft bill for a law facilitating the management of corporate group insolvencies was published in 2014. This is intended to prevent corporate groups from falling apart

[14] CERT (Computer Emergency Response Team). Each main financial institution (worldwide) has its own CERT, being a structure in charge of handling information security incidents and cybercrime issues targeting the firm. National or Transnational CERTs are also live in some country or area. For example, see https://cert.societegenerale.com/en/

uncontrollably in insolvency and to preserve the chances of restructuring. The draft bill creates a new group venue for corporate group insolvencies and generally relies on coordination and cooperation. There will be no consolidation of the group companies' assets. The draft bill gives each group-affiliated debtor the right to apply for a uniform group venue. A distinction must be made between the application for a uniform group venue and the insolvency petition. The group venue will lie with the court in which the application for a uniform group venue was first filed, as soon as that court has confirmed jurisdiction. If the insolvency court grants a group venue, the group venue will also apply to group companies which would otherwise have had another venue.

- Further, a draft bill for a reform of the regulations concerning actions to set aside willful disadvantages was published in 2015 and is currently being discussed in parliament.

In addition, an evaluation of the insolvency law reform, implemented in 2012 by the German Act on Further Facilitating the Restructuring of Companies (*Gesetz zur weiteren Erleichterung der Sanierung von Unternehmen*), will start in 2016. This may conflict with the European Commission's legislative proposal, expected by the end of 2016, for early debt restructuring and second chance provisions and for minimum harmonization in the field of insolvency law in the context of capital markets union (CMU).

**Tax Developments: Draft Administrative Principles for Profit Attribution to Permanent Establishments (PEs)**

On 18 March 2016, the German Federal Ministry of Finance issued for public discussion its draft Administrative Principles for Profit Attribution to Permanent Establishments. The draft comprises 152 pages of detail and clarification concerning the application of the Authorised OECD Approach ("AOA"), which has already been implemented under Section 1 (5) of the German Foreign Tax Act (Außensteuergesetz [AStG]) and the Regulation for Profit Attribution to Permanent Establishments (Betriebsstättengewinnaufteilungsverordnung [BsGaV]).

The final administrative principles are expected to be published by the Federal Ministry of Finance in the second half of 2016.

The draft principles constitute the typical third element in the German tax legislative process alongside the legal provisions in the act and the regulation – namely an application guide for the German tax authorities with an indirect and indicative impact on the taxpayer.

For all financial years starting after 31 December 2012, Germany has treated a PE with a head office in another state as a (nearly) separate and independent enterprise for income tax purposes. This reflects the basic principles of the AOA as set out in the OECD reports of 17 July 2008 and 22 July 2010 on the attribution of profits to permanent establishments. The profit attributable to the PE is determined in a two-step approach:

- Step one: Attribution of functions performed, assets owned or used, opportunities and risks assumed and external transactions based on identified significant people functions. Recognition of dealings between the different parts of the enterprise.

- Step two: Pricing of these dealings in accordance with the arm's length principle and the transfer pricing methods discussed in the OECD Transfer Pricing Guidelines.

The draft principles provide guidance on the attribution of functions, assets, opportunities and risks, as well as on the determination of the capital attributable to a PE, the attribution of interest expenses and the recognition of dealings.

For all financial years beginning after 31 December 2014, the taxpayer has had to prepare an "auxiliary calculation" with respect to the assets, capital, remaining revenues and expenses resulting from internal dealings. The draft principles do not provide an explicit template for the auxiliary calculation, however.

The draft principles also provide additional guidance on the specific requirements for profit allocation to PEs of banks.

The draft does not comment on the OECD's BEPS project ("Base Erosion and Profit Shifting") on Action 7 ("Preventing the artificial avoidance of PE status").

**Amendment to the German Minimum Requirements for Risk Management**

In March 2016, the German Federal Financial Supervisory Authority BaFin initiated a revision of Germany's Minimum Requirements for Risk Management (MaRisk). MaRisk flesh out the requirements of Pillar 2 of the Basel Framework in a principles-based manner and in line with the principle of proportionality. The amendment essentially focuses on implementation of BCBS 239 (risk data aggregation and risk reporting), risk culture and outsourcing.

**"paydirekt" – new online payment scheme operated by German banks**

At the end of 2015, Germany's private, cooperative, and savings banks launched a new online payment scheme called "paydirekt". Through this industry-wide cooperation, the banks offer consumers and merchants a joint payment scheme enabling those who shop online to pay easily, securely and directly from their own bank account. The scheme provides both protection for buyers and a payment guarantee for merchants and is potentially available to over 50 million bank account holders. Technical processing is handled by paydirekt GmbH, a joint enterprise set up by the participating banks and institutions. These comprise Commerzbank and comdirect bank, Deutsche Bank, and Deutsche Postbank, paydirekt Beteiligungsgesellschaft privater Banken, coordinated by HypoVereinsbank, the cooperative central banks DZ BANK and WGZ BANK, on behalf of the Cooperative Financial Network, as well as GIZS, for the Savings Banks Finance Group.

The following other private banks also participate in the scheme through paydirekt Beteiligungsgesellschaft privater Banken: ING-DiBa, TARGOBANK, Santander Consumer Bank, Bankhaus Max Flessa, Consorsbank, Degussa Bank, MLP Finanzdienstleistungen, NATIONAL-BANK, Oldenburgische Landesbank, SÜDWESTBANK, and Volkswagen Bank. Shareholdings are spread equally between the private banks, the Cooperative Financial Network, and the Savings Banks Finance Group.

## HONG KONG

### Banking Industry Overview

During the period between July 2015 and June 2016, the capitalisation of the banking sector remained well above the minimum international standards. The consolidated total capital ratio of locally incorporated Authorized Institutions (AIs) increased from 16.8% at the end of 2014 to 18.3% at the end of 2015, well above the minimum of 8% required by the Basel capital standard. The tier-one capital ratio increased to 15.3% at the end of 2015 from 13.9% a year earlier.

### Belt and Road Initiative

The Hong Kong Monetary Authority (HKMA) has established Infrastructure Financing Facilitation Office (IFFO) to facilitate the financing of infrastructure projects and provide a platform for pooling the efforts of investors, banks and the financial sector to offer comprehensive financial services for various infrastructure projects. The new establishment aims to assist market players in capturing opportunities arising from the Belt and Road Initiative where Hong Kong is particularly well-equipped to serve as a platform for financing and fund management for the markets along the route.

### Renminbi (RMB) Banking Business

The development of offshore RMB business in 2015 is highlighted below:

| **Offshore RMB banking statistics** | **As of end-2015 (RMB billion)** | **Growth against end-2014** |
|---|---|---|
| RMB deposits and certificates of deposit | 1,010 | -13% |
| RMB trade settlement transactions | 6,833 | +9% |
| Outstanding RMB loans | 297 | +58% |
| Outstanding dim sum bonds | 368 | -3% |

The decrease of RMB deposit pool in 2015 was largely due to the change in market expectation in RMB exchange rates and interest rates in the second half of 2015. Notwithstanding the reduction in RMB liquidity pool, the Hong Kong RMB market has been operating orderly. There was also a continuous growth in cross-border trade settlement and lending in renminbi. From 1 July 2015, eligible funds such as general equity funds, bond funds and mixed funds established in Mainland China and in Hong Kong can be distributed in each other’s market, providing a wider selection of fund products to investors in both markets under the Mutual Recognition of Funds Scheme.

From 18 August 2015, banks in Hong Kong may trade CNY Spot/Forward/Swap for customer transactions in cross-border goods trades, service trades and foreign direct investment with one leg in Hong Kong and the other in the Mainland.

**Payment Systems and Stored Value Facilities Ordinance**

The Ordinance commenced operation in November 2015 and empowers the HKMA to designate and oversee certain retail payment systems and to regulate the issue of certain stored value facilities (SVFs) with commensurate powers for performing relevant supervision and enforcement functions. A one-year period is allowed for existing issuers of SVFs or new market operators to apply for a licence from the HKMA.

**Launch of e-Cheque**

The e-Cheque service was launched on 7 December 2015. In contrast to paper cheques, the entire payment process of an e-Cheque, including issuance, delivery and deposit, is effected online.

**Cybersecurity and Technology Risks**

The HKMA revised its Supervisory Policy Manual (SPM) module on the risk management of electronic banking (e-banking) in September 2015. The revised module sets out sound risk management principles and practices applicable to AIs' e-banking services, including areas involving strengthened controls. In light of technological advancement and industry development, AIs are given more flexibility in offering e-banking services which are secure and provide adequate protection for customers.

In September 2015, the HKMA issued a circular on cyber security emphasising the importance of boards and senior management of AIs playing a proactive role in ensuring effective cyber security risk management as well as collaborating with other institutions in gathering and sharing cyber threat intelligence in a timely manner.

The HKMA announced on 18 May 2016 the launch of a "Cybersecurity Fortification Initiative" which aims to further enhance the cyber resilience of the banking sector in Hong Kong. It consists of a Cyber Resilience Assessment Framework, a Professional Development Programme and a Cyber Intelligence Sharing Platform.

**Implementation of Basel III in Hong Kong**

The HKMA continues to implement the Basel III reform package in Hong Kong in accordance with the timetable set by the Basel Committee on Banking Supervision:

- In August 2015, the HKMA issued a revised SPM module "Guideline on the Application of the Banking (Disclosure) Rules" to align with the amendments made to the Banking (Disclosure) Rules from 2013 for the purposes of implementing the Basel III standards. The revisions also reflected changes in prudential reporting requirements relating to AIs' Mainland activities and international claims.

- In September 2015, the HKMA issued a new SPM module on the operation of the countercyclical capital buffer: "Countercyclical Capital Buffer (CCyB) — Geographic Allocation of Private

Sector Credit Exposures". This provides guidance to AIs on how to determine the jurisdiction to which their credit exposures should be ascribed for the purposes of calculating their individual specific CCyB requirements.

- A jurisdictional CCyB for Hong Kong at a rate of 0.625% became effective on 1 January 2016. The HKMA also announced in January 2016 that this will be increased to 1.25% with effect from 1 January 2017. These rates are consistent with the Basel III phase-in levels.

- On 31 December 2015, the HKMA announced an updated list of Domestic Systemically Important Banks (D-SIBs). These D-SIBs are required to meet their corresponding higher loss absorbency (HLA) capital requirements from 1 January 2017. Again, these HLA capital requirements are being phased-in in line with the Basel Committee timetable.

**OTC Derivatives Market Regulation**

In December 2015, the HKMA released a consultation document and a draft SPM module outlining its proposed approach to implementing global margining and risk mitigation standards for AIs involved in non-centrally cleared OTC derivatives transactions. These standards are designed to reduce counterparty credit risk and limit contagion by ensuring that collateral is available to offset losses caused by the default of a derivatives counterparty, to promote legal certainty over the terms of derivatives contracts and to facilitate timely resolution of disputes.

**Financial Institutions (Resolution) Ordinance**

The Ordinance was gazetted on 30 June 2016. In line with international standards in the Financial Stability Board's Key Attributes of Effective Resolution Regimes for Financial Institutions, the Ordinance seeks to establish a legal framework for the orderly resolution of financial institutions in Hong Kong, conferring various powers on the Monetary Authority, the Insurance Authority and the Securities and Futures Commission as the sectoral Resolution Authorities for the banking, insurance and securities industries respectively.

**Inland Revenue (Amendment) (No. 3) Ordinance 2016**

The Ordinance was gazetted on 30 June 2016 to put in place a legal framework for Hong Kong to implement the new international standard for automatic exchange of financial account information in tax matters (AEOI) as promulgated by the Organisation for Economic Co-operation and Development. Under the new standard, a financial institution is required to identify financial accounts held by tax residents of reportable jurisdictions, collect the reportable information in respect of these financial accounts, and furnish such information to the Inland Revenue Department for exchange with the tax authorities of AEOI partner jurisdictions on an annual basis.

**Prevention of Money Laundering and Terrorist Financing**

Effectiveness and risk-based continue to be the main focuses in Hong Kong's anti-money laundering and counter terrorist financing (AML/CFT) regime and had driven developments throughout 2015 and 2016, including Hong Kong's first jurisdiction-wide money laundering and terrorist financing risk assessment which will be published by end 2016. The Hong Kong

Association of Banks also published a Guidance Paper on Combating Trade-based Money Laundering in February 2016, a project which involved close collaboration with the HKMA.

**Securities and Futures (Amendment) Ordinance 2016**

The Ordinance was gazetted on 10 June 2016 to provide for a new open-ended fund company structure in Hong Kong as an alternative legal structure for open-ended investment funds in addition to the unit trust structure. This will provide a more flexible choice of investment fund vehicle for fund managers and increase Hong Kong's attractiveness as an international asset management centre.

**Inland Revenue (Amendment) (No. 2) Ordinance 2016**

The Ordinance was gazetted on 3 June 2016 to give profits tax concession to qualifying corporate treasury centres; to make provisions for profits tax purposes regarding interest on money borrowed from, or lent to, associated corporations; to treat regulatory capital securities (Additional Tier 1 and Tier 2 instruments) as debt securities for profits tax purposes and to provide stamp duty relief for transactions and transfers relating to such regulatory capital securities.

**Deposit Protection Scheme (Amendment) Ordinance 2016**

The Ordinance was gazetted on 24 March 2016 to simplify the payout process by moving from a net payout approach to a gross payout approach to enable depositors to have swifter access to compensation payments in relation to the protected deposits upon the trigger of the Deposit Protection Scheme.

**Competition Ordinance**

The Ordinance, enacted in June 2012, came into full effect on 14 December 2015 and applies to all commercial sectors. The full implementation of the Ordinance ensures Hong Kong remains a competitive, dynamic and free market by curbing harmful anti-competitive conduct, bringing the benefits of a level-playing field to Hong Kong consumers, businesses and the wider economy.

**Insurance Companies (Amendment) Ordinance 2015**

The Ordinance was enacted in July 2015 to facilitate the establishment of an independent Insurance Authority and a statutory licensing regime for insurance intermediaries. In addition, it provides more flexibility and a better equipped toolbox for supervision of the insurance industry.

# INDIA

## General Economic Review

India's economic growth could be considered as impressive for the financial year 2015-16. India's Real GDP at market prices stood at 7.6 per cent for the year 2015-16. It is far better than 3.1 per cent of the world economic growth. Economic development was characterised by macro-economic stability, narrowing fiscal and current account deficits and receding inflation. Private consumption remained the key driver of the acceleration in real GDP growth of India. In the external front, steep contraction in imports as compared to exports led to trade gains and narrowed the current account deficit to 1.1 per cent of GDP, which was comfortably financed along with sizable addition to reserves. In terms of financing, a noteworthy feature of 2015-16 was the highest ever inflows of foreign direct investment, despite the challenging external developments. By the end of the year, the level of reserves was equivalent of 11 months of imports. Other indicators of external sustainability also recorded improvement. The effects of Brexit on the Indian economy have been relatively muted, including the immediate impact on equity and foreign exchange markets. Yet, in view of the linkages to the UK and the euro area, spill overs through trade, finance and expectations channels cannot be ruled out at this point in time. Though the external developments continue to be challenging, internal developments are turning positive for the year 2016-17. For India, domestic consumption would be the main driver for the growth for the year 2016-17. However, the major concern at this point is tardy growth in the private investment.

Some of the flagship programmes initiated by the Government for sustainable economic growth are the following:

**Pradhan Mantri Jan Dhan Yojana (PMJDY)** is a nationwide, bank led financial inclusion scheme launched by Indian government in August 2014. This scheme envisaged to provide banking access to each and every household in India. It was a grand success. As of March 2016, 215 million bank accounts are opened with a deposit amount of ₹ 366 billion. The scheme provides accident and life insurance also. Banks played a key role in the effective implementation of the schemes.

Along with PMJDY, financial literacy is also given importance by the Government and RBI. Financial literacy is crucial for imparting efficacy to financial inclusion initiatives. In the context of a changing financial landscape, especially with the introduction of PMJDY, the emphasis is on keeping new bank accounts operationally active. Banks were, accordingly, advised in January 2016 to focus on enhancing the efficacy of financial literacy programmes through: (i) Board-level policies for a stronger financial literacy architecture; (ii) a tailor-made approach to financial literacy and organising camps for different target groups; and (iii) following a concerted approach among various stakeholders at the district/panchayat/village level (local officials of NABARD and the Reserve Bank, district and local administration, block level officials, NGOs, SHGs, BCs, farmers' clubs, panchayats, primary agricultural credit society (PACS), and village level functionaries).

As at end-March 2016, 1,384 financial literacy centres (FLCs) were operational in the country, up from 1,181 FLCs at end-March 2015. During the year ended March 2016, 87,710

financial literacy activities were conducted by FLCs as against 84,089 activities during the preceding year.

**Roll out of Insurance & Pension Schemes:** The Government has also rolled out insurance schemes namely Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) which is a life policy and Pradhan Mantri Jeevan Suraksha Yojana (PMJSY) which is an accident policy. As of date 94 million accident Policies and 29 million life policies were sold through banks under these schemes. Atal Pension Yojana (APY) was also launched as a pension policy for the unorganized sector. The objective of the scheme is to increase the pension penetration in the unorganized sector so that financial security is available to these self-employed/employed people in the unorganized sector with no pension benefits.

**Pradhan Mantri Mudra Yojana :** Micro Units Development and Refinance Agency (MUDRA) is launched with a purpose to support micro entrepreneurs. Under this scheme commercial banks provide loans in three different brackets such as 1) For starters loans upto ₹ 50,000 2) for mid-stage finance seekers ₹ 50,000 to ₹ 5 lakh and 3) for next level growth seekers from ₹ 5 lacs to ₹ 1 million. It also aims to encourage the micro and small enterprises to contribute to the objective of "Make in India" and provide sufficient self-employment opportunities to the young skilled generation. So far, loans disbursed under this scheme has crossed over ₹ 1329 billion with 34.8 million beneficiaries.

**Start up India :** Startup India campaign was launched by the Government in January, 2016 and is based on an action plan aimed at promoting bank financing for start-up ventures to boost entrepreneurship and encourage start ups with jobs creation. It adopts three fold strategy such as 1) incentivising the startups by the simplification of procedures 2) provision of tax incentives and 3) easy access to bank credit to these initiatives. Already quite a few banks have opened dedicated branches only to meet the needs of the Start ups.

**Stand up India :**There is also another scheme launched by the government that is Stand up India which aims to provide loans to entrepreneurs belonging to backward classes and women. 2,50,000 entrepreneurs from these segments of society are expected to be nurtured and financed over a three year period. Loans from ₹ 1 million to ₹ 10 million would be considered under Standup India scheme.

**Digital India:** The Digital India programme is a flagship programme of the Government of India with a vision to transform India into a digitally empowered society and knowledge economy. The Digital India programme is centred on three key vision areas such as 1) Digital infrastructure as a core utility to every citizen, 2) Governance and services on demand and 3) Digital empowerment of citizens.

**Make in India:** The Make in India program was launched in September 2014 as part of a wider set of nation-building initiatives. It is devised to transform India into a global design and manufacturing hub. Make in India represents a comprehensive and unprecedented overhaul of out-dated processes and policies. Under Make in India, 25 key industrial sectors are identified and necessary steps are initiated to attract investment and encourage collaboration. The major objective behind the initiative is to focus on job creation and skill enhancement in 25 sectors of the economy.

**Skill India** : The Skill India programme was launched in July, 2015 with the aim to train over 400 million people in India in different skills by 2022. The initiatives include creation of National Skill Development Mission, National Policy for Skill Development and Entrepreneurship 2015, Pradhan Mantri Kaushal Vikas Yojana (PMKVY) scheme (ie, Skill Development) and the Skill Loan scheme to defray the cost of acquiring skills.

**Pradhan Mantri Crop Insurance Scheme:** Since agriculture is quite important for the Indian economy and considering the fact it is largely affected by the vagaries of monsoon, farmers are quite often susceptible to financial distress. To encourage farmers to buy crop insurance to cover their risks, the government has launched a new crop insurance scheme by simplifying and reducing the premium to be paid by the farmers to avail crop insurance.This is one of the landmark decision taken by the Government of India in recent years.

Over and above all these measures, Government is focusing on improving the ranking of the country in **"Ease of Doing Business"** in India. India improved its position from 134 to 130 in the **World Bank Doing Business 2015** ranking, although various reforms are underway to further improve the business environment. The effects of all these schemes will positively impact the country and is expected to have multiplier effect generating adequate employment and overall growth of the country.

**Developments in the Monetary Front**

A Monetary Policy Framework Agreement (MPFA) was signed between the Government of India and the Reserve Bank on February 20, 2015. The repo rate which is the policy rate was reduced by 75 bps during 2015-16 and 25 bps during 2016-17 so far, in support of an accommodative policy stance. The target for CPI inflation below 6.0 per cent by January 2016 was met and the focus has shifted to attaining the inflation target of 5 per cent by the end of FY 2016-17. Effective liquidity management kept the weighted average call rate (WACR) tightly around the policy repo rate during 2015-16. In April 2016, the liquidity management framework was revised to progressively move to a position closer to neutrality. The policy rate corridor around the repo rate was narrowed to +/- 50 bps. The Reserve Bank introduced the Marginal Cost of Funds based Lending Rate (MCLR) system effective April 1, 2016. The Union Budget 2016-17 announced the constitution of a Monetary Policy Committee (MPC) by amending the RBI Act, 1934. The amendment to the Act came into force on June 27, 2016.

**Performance of the Banking Sector in India during 2015-16**

India's financial system remained stable although banks had a challenging period in the year 2015-16. Due to challenging economic scenario, the credit growth was subdued. Business growth of the banks was just around 10.0 per cent during 2015-16. Banks also faced the problem of stressed assets owing to stress in the corporate sector, particularly on sectors such as steel, infrastructure, power distribution, road sector etc. In the year 2015-16 while all banks could declare operating profit, due to increased provisioning for stressed assets, a few banks were in red.

## Other Developments in the Banking System

### Priority Sector Lending (mandated lending to sectors like agriculture, MSME, education, weaker sections etc)

During 2015-16, Priority Sector Lending Certificate (PSLCs) were introduced as a mechanism for incentivising banks having surplus in lending to different categories of the priority sector thereby enhancing lending to these sectors. Like carbon credit trading, PSLCs will allow the market mechanism to drive priority sector lending by leveraging the comparative strengths of different banks. For trading purposes, a dedicated portal was launched in April 2016.

### Initiatives for MSME Sector

In August 2015, the banks were advised to review their existing lending policies to the micro and small enterprises (MSEs) sector and fine-tune them by allowing for standby credit facilities in case of term loans, additional working capital limits, mid-term review of regular working capital limits and timelines for credit decisions. Subsequent to the notification of a 'Framework for Revival and Rehabilitation of Micro, Small and Medium Enterprises' by the Government to provide a simpler and faster mechanism for addressing the stress in MSME accounts, the Reserve Bank issued related guidelines along with operating instructions on March 17, 2016. Under this framework, the revival and rehabilitation of MSME units having loan limits up to ₹ 250 million will be undertaken. Banks were also required to put in place Board approved policies to operationalise the framework not later than June 30, 2016.

### Differentiated Banks

RBI has initiated the process of giving differentiated license to small banks and payment banks. The aim is to further improve the financial inclusion activities of the small banks and payment banks. These local area banks, payment banks and Small Banks are expected to meet credit and remittance needs of small businesses, unorganized sector, low income households, farmers and migrant work force. RBI has given license to 10 small banks and 11 payment banks in 2015.

### On- Tap Licensing Guidelines

The RBI has issued final guidelines on "on tap licensing" in August, 2016. Important highlights of the guidelines are as follows:

**Large Corporates :** The RBI has excluded large industrial houses as eligible entities from the purview, though they can invest in banks up to 10 percent.

**Minimum Paid-up Capital :** The initial minimum paid-up voting equity capital for a bank should be Rs 500 crore and thereafter, the bank should have a minimum net worth of Rs 500 crore at all times.

**Promoter Holdings:** The promoter's or the promoter group / non-operative financial holding company (NOFHC) shall hold a minimum of 40 percent of the paid-up voting equity capital of the bank. It will have a lock-in of five years from the day the bank kicked off business. The promoter group's shareholding should be brought down to 15 percent within 15 years of the

start of the bank. 'Residing' Promoters Individuals/professionals who are 'residents' in India and have 10 years of experience in banking and finance and existing non-banking financial companies (NBFCs) that are 'controlled by residents' and have a successful track record for at least the same period can apply for the licence.

**Unbanked Rural Centres:** The applicant should have opened at least 25 per cent of its branches in unbanked rural centres.

**FDI Eligibility**: The foreign shareholding in the bank would be as per the existing foreign direct investment rules. At present, the aggregate foreign investment limit is 74 per cent.

**Recapitalisation of State Owned Banks**

In the Union Budget, the Centre had allocated a total of ₹.25,000 crore for the capitalisation of public sector banks in the current financial year 2016-17, in line with the infusion plans announced under the umbrella scheme "Indradhanush" introduced last year. The plan proposes infusions adding up to ₹.25,000 crore in 2015-16 as well as in 2016-17, followed by Rs.10,000 crore each in 2017-18 and 2018-19. The purpose of capital infusion is to strengthen the public sector banks and also to help them to meet the Basel III capital requirements. In July, the government infused capital to the tune of ₹ 22,915 crores to 13 public sector banks.

**Developments in Capital Markets**

**Merger of FMC with SEBI**

With a view to strengthen the regulation of commodity forward markets and to reduce wild speculation, Finance Minister has proposed to merge the commodity market regulator Forwards Markets Commission (FMC) with the capital market regulator Securities and Exchange Board of India (SEBI). FMC, a statutory body set up in 1953 under the Forward Contracts (Regulation) Act, 1952 (FCRA) is a regulatory authority overseen by the Ministry of Finance, Government of India. The Commission is a chief regulator of commodity futures markets in India and allows commodity trading in 22 exchanges in India. Established in the year 1988, SEBI is a regulator for the securities market in India and had been given statutory powers through the SEBI Act, 1992. However, with the said merger taking into place, there will be a single integrated financial sector regulator SEBI, which will regulate the commodity futures trading apart from the regulating the capital market. The merger became effective in September, 2015.

**Revamping of Insider Trading Norms**

To further tighten gaps in the insider trading norms, the Securities and Exchange Board of India (Sebi) has revamped the more-than-two-decades old insider regulations, replacing it with the SEBI (Prohibition of Insider Trading) Regulations, 2015. Penal actions for prohibited transactions, enlarged scope of definitions and new concepts are some features.
While trading in securities, those with access to unpublished price-sensitive information have an unfair advantage over innocent investors. This can be any information in the market with the potential to materially affect the price of securities. Some examples are financial results, dividends, change in capital structure, merger, de-merger and acquisitions. The new regulations could be

more effective in curbing the malpractices in the securities market and creating a level environment for investors. The code of conduct is applicable not only on listed entities and intermediaries but on every other person required to handle unpublished price-sensitive information in the course of business operations.

**New norms for risk management in commodity markets**

To strengthen risk management framework of the commodities market, the Securities and Exchange Board of India (Sebi) issued norms for early delivery as well as pay-in facility and penalty on sellers in case of delivery default. It has also put in place measures such as staggered delivery system, fixation of final settlement price (FSP) and change in expiry date. The norms would come into effect immediately. Under the staggered delivery, in all futures contracts tender period would start with onset of the applicable staggered delivery period. In case the day happens to be a holiday, the tender period would start from next working day. Open position on expiry of the contract would result in compulsory delivery and would be settled at FSP of the respective contracts and pay-in and pay-out would happen latest by the second working day after expiry. The process of pay in and pay-out will be completed on T+2 basis, where 'T' stands for the day on which matching has been done. Exchanges will provide early pay-in facility to market participants permitting market participants to deposit certified goods to the bourse accredited warehouse against relevant futures contracts sold.
Penalty on seller will be imposed in case of delivery default (default in delivery against open position at expiry in case of compulsory delivery contracts and default in delivery after giving intention for delivery). The exchange can advance expiry date of running contract in case physical market is closed in the notified basis centre on the expiry day of the contract due to festivals, strikes and erratic weather conditions. Such decision will be intimated to participants at least 10 days before the revised expiry date.

**Insurance Sector**

India’s insurable population is anticipated to touch 750 million in 2020, with life expectancy reaching 74 years. Furthermore, life insurance is projected to comprise 35 per cent of total savings by the end of this decade, as against 26 per cent in 2009-10. The future looks promising for the life insurance industry with several changes in regulatory framework which will lead to further change in the way the industry conducts its business and engages with its customers. Demographic factors such as growing middle class, young insurable population and growing awareness of the need for protection and retirement planning will support the growth of Indian life insurance.

The Government of India has taken a number of initiatives to boost the insurance industry. Some of them are as follows:
The Union Budget of 2016-17 has made the following provisions for the Insurance Sector:

- Foreign investment will be allowed through automatic route for up to 49 per cent subject to the guidelines on Indian management and control, to be verified by the regulators.
- Service tax on single premium annuity policies has been reduced from 3.5 per cent to 1.4 per cent of the premium paid in certain cases.
- Government insurance companies to be listed on the exchanges

- Service tax on service of life insurance business provided by way of annuity under the National Pension System regulated by Pension Fund Regulatory and Development Authority (PFRDA) being exempted, with effect from April 01, 2016.
- The Insurance Regulatory and Development Authority (IRDA) of India has formed two committees to explore and suggest ways to promote e-commerce in the sector in order to increase insurance penetration and bring financial inclusion.
- IRDA has formulated a draft regulation, IRDAI (Obligations of Insures to Rural and Social Sectors) Regulations, 2015, in pursuance of the amendments brought about under section 32 B of the Insurance Laws (Amendment) Act, 2015. These regulations impose obligations on insurers towards providing insurance cover to the rural and economically weaker sections of the population.
- Certain state governments has launched a first of its kind banking and insurance services helpline for farmers where individuals can lodge their complaints on a toll free number.
- Government of India has launched an insurance pool to the tune of Rs 1,500 crore (US$ 220.08 million) which is mandatory under the Civil Liability for Nuclear Damage Act (CLND) in a bid to offset financial burden of foreign nuclear suppliers.
- Foreign Investment Promotion Board (FIPB) has cleared 15 Foreign Direct Investment (FDI) proposals including large investments in the insurance sector by Nippon Life Insurance, AIA International, Sun Life and Aviva Life leading to a cumulative investment of Rs 7,262 crore (US$ 1.09 billion).

## ITALY

### Significant Market Developments

In 2015, the Italian economy returned to growth for the first time since the onset of the sovereign debt crisis, although at a moderate pace (0.8%). The improvement in the short-term economic outlook was reflected in the activity of Italian banks.

Lending has continued to recover gradually, thanks in part to the ultra-accommodative monetary policy stance. Bank lending stabilized at the end of 2015 and, for the first time in four years, rose slightly in the early months of 2016. Lending to the nonfinancial private sector is growing at a modest pace, though with more strength in the sectors where the economic recovery has taken firmer root. Signs of improvement in loan dynamics have appeared as indicated by the strong increase in the flows of new loans to households.

In recent years Italian banks' earnings have been squeezed by the need to adjust the value of non-performing loans (NPLs) that are largely the legacy of the long and deep recession.
The economic recovery is now being reflected in a significant reduction in the flow of NPLs, which in 2015 fell to 3.7% of total loans compared with 4.9% in 2014.

Even the stock of NPLs has fallen slightly for the first time since 2008. At the end of 2015, net of provisions the stock of NPLs amounted to 10.8% of total loans (4.8% for bad debts alone). All in all, the issue of impaired loans for Italian banks seems somewhat overstated by the market. Looking at bad debts alone, namely the most delinquent component of total NPLs, the net value is less than €85 billion as at May 2016 (€89 billion as at December 2015), the coverage of gross bad

debts is in line with the European average, the amount and the quality of guarantees are sound and the majority of bad debts are held by banks with strong capital ratios levels. It seems therefore incorrect to considered the NPLs as an emergency for the Italian banking sector as a whole.

In 2015, €9 billion worth of bad debts were sold and deleted from banks' balance sheets, twice as much as in 2014.
Over the last three years, the write-downs made by banks increased by about 8 percentage points in the NPL coverage ratio (the amount of loan loss provisions in relation to corresponding gross exposures), which was 45.4% at the end of 2015 (46.5% for the five banking largest groups), a value in line with the average for the main European banks. Italian bank loans secured by collateral amount to €160 billion, about 50% of gross non-performing exposures (67% including personal guarantees). With respect to bad debts, the value of the collateral exceeds the book value of the loans.

One factor that until now has played a role in the increase of the stock of NPLs has been the slowness of insolvency and recovery procedures. Legislative reforms introduced in summer 2015 and in May 2016 serve to speed them up.

The reduction of problematic loans is expected to benefit from a number of initiatives recently introduced in Italy: 1) a guarantee scheme for securitized bad debts (GACS) which enable Italian banks to securitise and offload bad debts with a State guarantee in a way not considered State aid and 2) an alternative investment fund of a private nature, called *Atlante*, to support banks' capital increases and to ease the deconsolidation of NPLs from Italian banks' balance sheets.

In 2015, profitability of the five largest groups, while still below the levels recorded before the global financial crisis, improved: ROE jumped to 4.6% (compared with -1.8% in 2014). The improvement stemmed mainly from the growth in fee income, mostly in connection with asset management, and from the decrease in loan loss provisions consequent to the decline in loan impairment rates.

With the start of the recovery, the gap of profitability at Italian banks vis-à-vis European peers is narrowing. The difference is largely due to the magnitude of the contraction of output suffered during the crisis and by the business model. Banks that get a substantial share of their revenues from lending to households and SMEs were hit harder by the recession owing both to the decrease in net interest income and to the increase in loan loss provisions. In 2015 the cost-to-income ratio of Italian banks (65%) was 2 percentage points higher than that of other EU banks. The difference in the ROE was 1.6 percentage points, down from 7.1 points in 2014.

In 2015 Italian banks' operating costs, net of the contributions to the National Resolution Fund, remained stable. The cost-income ratio is 64%, slightly above the average for European banking groups.

Over the past years, Italian banks have started to restructure their networks by shutting down low-profit branches after the significant expansion since the nineties. Italian banks have been stringent in enforcing a significant curbing of costs, an increase in efficiency and a diversification of income sources as it is evident from the bank business plans (workforce cut,

requalification of personnel, outsourcing of back-office functions, M&A, development of digitization, reduction in branch network).

After revenues plunged because of the recession, the Italian banking system started to take remedial actions by cutting the number of staff (298.575 at the end of 2015 versus 306.607 in 2013) and of branches, which in 2015 declined to around 30,000, 11% less than in 2008. The relevant capital strengthening of Italian banks is continuing: from 2007 to 2016 they raised about €55 billion of capital; in 2015 about €4 billion of additional capital were injected.

At the end of 2015 Italian banks' common equity tier 1 capital (CET1) was equal on average to 12.3% of risk-weighted assets, from 7% at the end of 2007. For significant banks the CET1 ratio was 11.5%, about 2 percentage points lower than the average found by the EBA for a sample of large European banks.

**Regulation and Supervision of Banks**

**Regulatory/supervisory structures, including changes in the organization and/or responsibilities and powers of regulatory, central bank and other governmental authorities in the financial sector**

Legislative Decree n. 72/2015, transposing CRD IV, modified the Consolidated Acts in Banking and Finance (TUB and TUF) to provide the relevant authorities with new powers. Among the most relevant, the Decree enables the authorities to:

- require natural or legal persons to provide all information necessary in order to carry out the tasks of the competent authorities, including third parties to whom entities have outsourced operational functions or activities
- remove members of the management board when their activity may cause prejudice to the sound and prudent management of the credit institution
- remove the board in case of serious breaches of EU, national and statutory provisions
- directly convene general meetings
- impose non pecuniary penalties, including:
  - temporary bans against a member of the institution's management body or any other natural person, who is held responsible, from exercising functions in institutions
  - orders to cease the conduct and to desist from a repetition of that conduct

**Imposition of enhanced capital and liquidity requirements, including stress testing and contingent capital/debt "bail-in" requirements**

Legislative Decree n. 180/2015 and Legislative Decree n. 181/2015 transposed in Italy the "Bank Recovery and Resolution Directive" (BRRD). The BRRD requires resolution authorities to draft resolution plans for institutions. Resolution plans should include an institution-specific Minimum Requirement for own funds and Eligible Liabilities (MREL) and a deadline to achieve it.

The BRRD Decrees identified in the Bank of Italy the resolution authority. The Bank of Italy, prior approval of the MEF, adopts a resolution program that, among other things, identifies

the specific instruments applicable to resolution, defining also the terms of any recourse to the resolution fund.

The Bank of Italy will have a resolution tool kit that includes (a) the sale of assets and legal relations to a third party; (B) the sale of assets and legal relations to a bridge institution; (C) the sale of assets and legal relations to a special purpose entity for the management of assets; (D) the bail-in, defined as "the reduction or conversion to equity of rights of shareholders and creditors".

The bail-in assigns a resolution authority the power to order the devaluation and conversion of certain liabilities of the institution subjected to resolution, depending on the absorption of losses and recovery of capitalization levels appropriate to the maintenance of market confidence. **The BRRD Decree excludes from bail-in a set of liabilities, including, for example, the guaranteed deposits (i.e. deposits up to 100,000 euros), interbank liabilities (excluding intercompany transactions) with an original maturity of less than 7 days and the secured liabilities, including covered bonds. All liabilities not expressly excluded may be subject to bail-in.**

## Other Regulatory Developments

### Compounding of Interest

A new law (Law of April 8, 2016, n. 49) was approved and modified once again Art. 120 (2) of the Consolidated Law on Banking) providing that the Interministerial Committee on Credit and Savings (CICR) establishes the methods and criteria for the generation of interest in transactions undertaken in the context of banking business, providing, in any event that:

In current accounts or payment account is assured to clients, the same frequency in the count of the borrowing and creditor interests; the count of interests cannot be less than one year; the interest is calculated on December 31 of each year and, in any case, at the end of the contract for which they are due. Compared to the previous law it remains valid the principle that debtor interests cannot generate additional interest (with the exception of arrear interest), and they are figured solely on the principal amount. Specific provisions were introduced for overdraft and overrunning: 1) the borrowing rates are calculated at 31 December and become payable on March 1 of the year following that in which they are earned; in the case of permanent closure of the relationship, the interest is payable immediately; 2) the customer may authorize, even preventively, charging interest to the account at the time when they become due; in this case the charged amount is considered the principal due; the authorization is revocable at any time, provided that before the charge has taken place. The CICR resolution has yet to be passed.

### Anti -Money Laundering

Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC has been published in the official Journal of the European

Union on June 5th, 2015. The Directive is currently under transposition in national legislation and the relevant Legislative Decree is currently being discussed at Parliament level.

**Data Protection**

Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) has been published in the EU Official Journal in all the official languages. While the Regulation has entered into force on 24 May 2016, it shall apply from 25 May 2018. The regulation will be directly applicable in all Member States without the need for implementing national legislation. It will not come into force immediately (this is likely to be in 2018).

**Digitalisation of Banking Business - Regulatory Changes**

Following the enactment of the new technical rules (on the electronic document and document management, the storage system and electronic signatures), the legal framework of reference in the area of digitalisation has gradually been implemented. In 2015 *Agenzia per l'Italia Digitale* (Agency for Digital Italy) issued the Guidelines on the storage system of electronic document and the implementing regulations of the Decree of the President of the Council of Ministers of 24 October 2014, which defines the characteristics of the public system for managing the digital identities of citizens and companies (SPID).

In March 2016 Bank of Italy, according to ministerial decree no. 205 of 3 October 2014, issued the new rules of the presentation for payment in electronic form of cheques and bank drafts.

**Cybersecurity and the Protection of Bank IT Systems**

On May 2016, the Bank of Italy updated the national regulation on internal controls, information systems and business continuity, including the EBA Guidelines on the security of internet payments, that will be effective from 30th September 2016.

**Regulation of over-the-counter (OTC) derivatives, including registration of derivatives dealers, the imposition of execution, clearing, margin and reporting requirements on OTC derivatives transactions, and the applicability of "equivalence" or "substituted compliance" determinations to cross-border derivatives transactions**

In December 2015, the European Commission published on the Official Journal of the European Union the Delegated Regulation (EU) 2015/2205 of 6 August 2015 supplementing Regulation (EU) No 648/2012 with regard to regulatory technical standards on the clearing obligation for interest rate derivatives (IRS) providing for the obligation to come into force (i) on the 21st of June 2016 for counterparties falling in Category 1[15] of such Regulation, (ii) on the 21st

[15] Category 1 should include both financial and non-financial counterparties which, on the date of entry into force of this Regulation, are clearing members of at least one of the relevant CCPs and for at least one of the classes of interest rate OTC derivatives subject to the clearing obligation, as those counterparties already have experience with voluntary clearing and have already established the connections with those CCPs to clear at least one of those classes. Non-financial counterparties that are clearing members should also be included in this first category as their experience and preparation towards central clearing is comparable with that of financial counterparties included in it.

of December 2016 for counterparties in Category 2 [16] and further dates for other counterparties' categories [2]. Annex to said Delegated Regulation provides the relevant details for each of the four classes of IRS subject to the obligation (Basis Swaps, Fixed-to-float interest rate swaps, Forward rate agreements, Overnight index swaps, in EUR, GBP, JPY and USD currencies).

In April 2016, a further Delegated Regulation (EU) 2016/592 was published, providing for the clearing obligation of some classes of credit derivatives, i.e. European untranched Index CDS (iTraxx Europe Main and iTraxx Europe Crossover, Tenor 5 years, EUR currency). Such obligation will take effect on (i) 9 February 2017 for counterparties in Category 1; (ii) 9 August 2017 for counterparties in Category 2 and further dates in 2018 and 2019 for Categories 3 and 4.

The Delegated Regulation was adopted on the 10th of June 2016 by the European Commission (and it is subject to a 3-month non-objection period of the European Parliament and the Council at the time of writing this report), extending the clearing obligation to two classes of IRS (Fixed-to-float interest rate swaps, Forward rate agreements) on three further currencies, i.e. Norwegian NOK, Polish PLN, Swedish SEK.

As it regards the developments in the Italian local regulation in the scope of over-the-counter derivatives, no major developments were recorded in the national legislation during the period under review. Indeed, the majority of additions made to the Italian Consolidated Law on Finance, (Legislative Decree n. 58 of 24 February 1998) in order to comply with Regulation EU n. 648/2012 were introduced in 2013 and 2014.

## JAPAN

### Market Developments

#### *Introduction of Negative Interest Rates by the Bank of Japan*

The Bank of Japan (BOJ) decided to introduce "Quantitative and Qualitative Monetary Easing (QQE) with a Negative Interest Rate" at the Monetary Policy Meeting of its Policy Board held on January 29, 2016. Application of the negative interest rate started on February 16.

In addition to the previous QQE, the BOJ has implemented the new "Quantitative and Qualitative Monetary Easing (QQE) with a Negative Interest Rate" which includes application of a negative interest rate to the current-account deposits that financial institutions hold at the BOJ. Specifically, the BOJ has divided the current-account deposits into three tiers and has respectively applied a positive interest rate, a zero interest rate and a negative interest rate (minus 0.1% initially upon introduction).

[16] Category 2 and Category 3 should comprise financial counterparties not included in the first category, grouped according to their levels of legal and operational capacity regarding OTC derivatives.

## Regulatory Developments

### *Prudential Regulations*

"Basel III: A global regulatory framework for more resilient banks and banking systems" published by the Basel Committee on Banking Supervision (BCBS) in December 2010 and other regulations required banks to establish (1) the capital conservation buffer, (2) the countercyclical buffer, (3) the buffer for global systemically important banks (G-SIBs) and (4) the buffer for domestic systemically important banks (D-SIBs).

Based on this, the Financial Services Agency (FSA) revised Cabinet Office ordinances, etc. in November 2015 regarding the introduction of (1) the capital conservation buffer for internationally active banks, (2) the countercyclical buffer for internationally active banks, (3) the G-SIB buffer for banks etc. designated as G-SIBs, and (4) the D-SIB buffer for banks etc. designated as D-SIBs. The FSA also prepared its "Comprehensive Guidelines for Supervision of Major Banks" and "Inspection Manuals" with regard to these buffers.

The capital buffer rules have been phased in from March 31, 2016 through 2019 based on international agreements.

# LATVIA

## Regulatory Developments

### *Banking Sector*

Since July 2015, the Financial and Capital Market Commission (the FCMC) has been continuing enhancement of the regulatory framework governing the activities of financial and capital markets.

Taking into account the entry into force of EU Single Supervisory Mechanism a number of adjustments in legislation were necessary. Amendments to the Credit Institution Law were drawn up to specify the supervisory authority regarding decision-taking on issuing of a licence (permission) to a credit institution and authorizing or forbidding the acquisition of a qualifying holding within the Single Supervisory Mechanism, bearing in mind the division of competence between national authorities and the European Central Bank.

Since transposition of CRD IV/CRR the FCMC has been **designated authority for implementation of macro-prudential instruments.** The financial crisis demonstrated the presence of systemically important financial institutions that in the event of facing problems may have an impact also on other financial market participants and the real economy. In view of activity of systemically important financial institutions and their material role in the financial sector, there is a need to introduce additional requirements, for example, increased capital buffer rates in accordance with the importance of institution. Application of macro-prudential tools enables the most significant financial market participants to become more resistant to unforeseen circumstances. In accordance with the Credit Institution Law, the FCMC shall identify credit institutions that are O-SIIs (other systemically important institutions) once a year, as well as it may

set the capital buffer rate of other systemically important institution of up to 2 per cent of risk weighted assets. In 2015, the FCMC identified six systemically important credit institutions in the local financial sector, placing the list of them on the FCMC website, as well as determined that no advantages shall be applicable to them in ensuring compliance with certain corporate governance requirements. The decision on setting the O-SII capital buffer is to be taken in 2016.

The FCMC adopted the **regulations on the calculation of credit institution specific countercyclical capital buffer rate**, specifying credit exposures to which countercyclical capital buffer rate is applicable, procedure for determining countercyclical capital buffer rate applicable to exposures to the Latvian, EU Member State or other foreign residents, as well as date of the application of the relevant countercyclical capital buffer rate and algorithm according to which the relevant countercyclical capital buffer rate shall be calculated. The FCMC shall set and publish quarterly the countercyclical capital buffer rate for the exposures to the Latvian residents that is to be used for the calculation of institution specific countercyclical capital buffer rate for 12 months after its setting. Based on April 2016 estimates, the countercyclical capital buffer rate for exposures to the Latvian residents was set at 0 per cent until the year 2018.

The results of lessons learned in the area of credit institutions during the financial crisis were the Basel III standards, implementation of which was intensively continued also in 2015. **Regulations for the Disclosure of Encumbered and Unencumbered Assets** define conditions according to which credit institutions and investment firms shall disclose information on encumbered and unencumbered assets. Regulations also determine characteristics of the assets that are deemed to be encumbered, specify minimum requirements for provision of additional narrative information and unified templates for public disclosure of information about the recognized encumbered and unencumbered assets. The templates for information disclosure (within Pillar III) are consistent with reports for supervisory purposes. Frequency of disclosure, means and publication site are specified in accordance with the EU Regulation No 648/2012.

**Regulations on the Reporting of Funding Plans of Credit Institutions** were developed to introduce the European Banking Authority's (EBA) Guidelines on harmonised definitions and templates for funding plans of credit institutions that credit institutions should use to report to their competent authorities under the Recommendation of the European Systemic Risk Board of 20 December 2012 (ESRB/2012/2). Reports on funding plans of credit institutions provide for information on the funding plans for coming 3 years and enable the competent authorities to assess the planned sources of the funding for credit institutions broken down by various areas (type, terms, price) and a potential impact of the measures specified in the funding plans, including on the supply of credits to the real national economy.

The FCMC continued to implement changes arising from directly applicable EU regulation, particularly in relation to CRDIV/CRR, BRRD and DGSD. This included the ongoing implementation of a number of technical standards developed by EBA and introduction of single reporting framework (COREP, FINREP). Many of these changes to the EU regulatory framework have been implemented through consultations, supervisory statements, and incorporated into internal procedures. Harmonised liquidity coverage ratio has been introduced as from 1 October 2015 with phasing in of the minimum requirement until 2018, while preserving parallel application of liquidity requirements set by the FCMC (30% minimum liquidity ratio and Pillar 2

individual liquidity ratio). Also annual public disclosure of leverage ratio by banks has been set to begin with 2015 Pillar 3 disclosures.

Important steps have been taken in order to **strengthen AML/CTF supervision**. The money laundering prevention framework in Latvia is based on the Law on the Prevention of Money Laundering and Terrorist Financing (the AML/CTF Law) which in its turn forms the basis for regulations promulgated by the Cabinet of Ministers, regulations for enhanced customer due diligence approved by the FCMC. The AML/CTF Law was adopted in July 2008 and the latest amendments to it came into force on 2 March 2016 when the definition of politically exposed person was broadened in line with EU IV AML Directive and taking into account additional risk factors.

The FCMC has approved **Regulations on the Customer Due Diligence for Credit Institutions and Licensed Payment and Electronic Money Institutions** (came into force on 31 December 2015). The Regulations specify certain segments and factors increasing the money laundering risk as well as require the institutions alongside with risk-based approach to apply clearly defined risk-scoring models for all customer base.

The FCMC has approved **Regulations on the Management of Money Laundering and Terrorist Financing Risk** exposure of credit institutions (came into force on 03.02.2016). The regulation specifies requirements for management of the credit institution's overall money laundering and terrorist financing risk, including its assessment, reporting and stress testing.

**Amendments to the Credit Institution Law** were adopted on 2 June 2016 increasing fines for AML/CTF violations and setting personal fines for the management of deficiencies in the AML/CTF internal controls. Powers of the FCMC were strengthened by amending the Law on the Financial and Capital Market Commission. Amendments of the 19 May 2016 enable the FCMC to issue additional specific regulations, assign external audit investigation as well as authorize the FCMC to access banks' databases online.

To increase AML/CFT supervision capacity and efficiency the FCMC has restructured its Financial Integrity Division into a Compliance Control Department with 5 divisions. The FCMC has increased the staff in the Compliance Control Department from 5 tol 15 and during 2017 will increase and fill 5 additional vacancies.

*Financial Instruments Market*

In the financial instruments market a number of EU legal acts were transposed. **Amendments to the Law on the Financial Instruments Market** were adopted in order to transpose the EU Transparency Directive (Directive 2013/50/EU)**.** In order to take account of financial innovation and ensure that issuers and investors have full knowledge of the structure of corporate ownership, the definition of financial instrument subject to notification is broadened to cover all instruments of similar economic effect to holdings of shares and entitlements to acquire shares, whether giving right to a physical settlement or not. The operation of a central access point for the search of regulated information at the Union level is provided.

Amendments address share buyout offers. The amendments decreased the threshold at which a person or persons acting in concert must offer to buy out the shares belonging to other shareholders from 50% to 30%. In cases where shareholders are suspected of acting in concert, the onus would be on the shareholder to prove they do not exercise dominant influence in the company. The amendments also raised the ceiling for sanctions for the breaches of the Law on the Financial Instruments Market. The amendments raised applicable fines against legal persons either to EUR 10 million, up to 5% of the company's total annual turnover, or up to twice of the amount of the profits gained or losses avoided because of the breach (applying whichever is higher). Natural persons are subject to fines of up to EUR 2 million or up to twice the amount of the profits gained or losses avoided because of the breach. Amendments would further strengthen applicable sanctions or administrative measures for market manipulation and insider trading, in response to the EU market abuse regulation, which must be implemented by national governments by 3 July 2016.[17] These proposed changes include sanctions against natural persons of up to EUR 5 million and sanctions against legal persons of up to EUR 15 million or 15% of the company's total annual turnover, whichever is higher.

**Amendments to the Criminal Law** were adopted in order to set higher criminal penalties for market manipulation and insider trading. The law raised the ceiling for the maximum term of imprisonment (maximum term of imprisonment of at least four years will be set for insider dealing, recommending or inducing another person to engage in insider dealing and for market manipulation; a maximum term of imprisonment of at least two years will be set for unlawful disclosure of inside information.)

On the basis of commitments taken during accession to the OECD, Latvia broadened the scope of countries where UCITS investment funds, funded pensions schemes and private pension schemes are entitled to hold accounts with banking institutions. Following the **amendments to the Law on Investment Management Companies, the Law on Private Pensions and the Law on Sate Funded Pension Scheme adopted** on 4 February 2016 Latvia has extended the scope of countries where UCITS investment funds, funded pensions schemes and private pensions schemes may hold accounts to those OECD countries that are considered according to the Regulation No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms as countries applying supervisory and regulatory arrangements to credit institutions equivalent to those applied in the European Union. Thereby Latvia's requirements for banking institutions in which UCITS investment funds, funded pensions schemes and private pension schemes may hold accounts abroad ensure equal treatment of all OECD countries.

*Insurance Sector*

The new risk-based European supervisory framework for insurance – Solvency II – has become applicable as of 1 January 2016. Solvency II framework introduces new regulatory requirements in the areas of quantitative capital requirements, governance and risk management, supervisory reporting and disclosure. The basic principles of Solvency II are introduced by the Insurance and Reinsurance Law as well as secondary legislative acts adopted during 2015

17 . Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC

(transposing the Directive 2009/138/EC). EU secondary legislative acts (Delegated Acts and Implementing Technical Standards - regulations that are directly applicable by the EU Member States) set further more detailed Solvency II implementation requirements. National regulations regarding technical provision calculation, reporting and valuation of assets and liabilities have been adopted at the beginning of 2016 to implement European Insurance and Occupational Pensions Authority's guidelines in these areas. In addition, Solvency II regulatory requirements on supervisory review process are being incorporated into internal proceedings.

## Luxembourg

### Legislative Developments

- Law of 27 May 2016 reforming the legal publication regime relating to companies and associations.

- Law of 10 May 2016 transposing Directive 2013/50/EU; transposing Article 1 of Directive 2014/51/EU; 3. amending the law of 11 January 2008 on transparency requirements for issuers of securities, as amended; 4. amending the law of 10 July 2005 on prospectuses for securities, as amended.

- Grand-ducal Regulation of 10 May 2016 transposing Article 3 of Directive 2013/50/EU of the European Parliament and of the Council of 22 October 2013 amending Directive 2004/109/EC of the European Parliament and of the Council on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market, Directive 2003/71/EC of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading and Commission Directive 2007/14/EC laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC; amending Grand-ducal Regulation of 11 January 2008 relating to the transparency requirements for issuers of securities, transposing Directive 2007/14/EC of the European Commission of 8 March 2007 laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market.

- Law of 10 May 2016 implementing Directive 2014/91/EU amending Directive 2009/65/EC on UCITS as regards depositary functions, remuneration policies and sanctions amending the Law of 17 December 2010 on undertakings for collective investment.

- Law of 15 March 2016 on OTC derivatives, central counterparties and trade repositories.

- Law of 18 December 2015 implementing Directive 2013/34/EU on annual and consolidated financial statements and related reports amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC.

- Law of 18 December 2015 implementing Directive 2014/86/EU of 8 July 2014 modifying Directive 2011/96/EU on the common system of taxation applicable in the case of parent

companies and subsidiaries of different Member States Directive 2015/121/EU of 27 January 2015 modifying Directive 2011/96/EU.

- Law of 18 December 2015 implementing the agreement on the transfer and mutualisation of contributions to the Single Resolution Fund signed in Brussels on 21 May 2015.

- Law of 18 December 2015 implementing Directive 2014/59/EU on bank recovery and resolution and Directive 2014/49/EU on deposit guarantee schemes.

- Law of 18 December 2015 on the automatic exchange of financial account information in the field of taxation and implementing Directive 2014/1077EU of 9 December 2014 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation and amending Law of 29 March 2013 on administrative cooperation in the field of taxation.

- Law of 7 December 2015 implementing tax treaties with Andorra, Croatia, Estonia and Singapore and protocols to existing tax treaties with United Arab Emirates, France, Ireland, Lithuania, Mauritius and Tunisia.

- Grand Ducal Regulation of 5 August 2015 amending the Grand Ducal Regulation of 1 February 2010 providing details on certain provisions of the amended Law of 12 November 2004 on the fight against money laundering and terrorist financing.

- Law of 25 July 2015 on electronic archiving and amending Article 1334 of the Civil Code, Article 16 of the Commercial code and the amended Law of April 5, 1993 in relation to the financial sector.

- Law of 24 July 2015 approving the Agreement between the Government of the Grand-Duchy of Luxembourg and the Government of the United States of America (USA) on improving compliance with tax obligations on an international level, and relating to the provisions of the USA on the exchange of information – the so-called Foreign Account Tax Compliance Act (FATCA) – including its two annexes and the memorandum of Understanding in relation thereto.

- Law of 23 July 2015 implementing Directive 2013/36/EU (CRDIV) of 26 June 2013 and articles 2 and 3 of Directive 2011/89/EU on as regards the supplementary supervision of financial entities in a financial conglomerate. Regulations of the Commission de Surveillance du Secteur Financier (CSSF).

- CSSF Regulation No 16-03 on the setting of the countercyclical buffer rate for the third quarter of 2016.

- CSSF Regulation No 16-02 on the setting of the countercyclical buffer rate for the second quarter of 2016.

- CSSF Regulation N° 16-01 on the automatic recognition of countercyclical capital buffer rates during the transitional period.

- CSSF Regulation N° 15-06 concerning systemically important institutions authorised in Luxembourg.
- CSSF Regulation N° 15-05 on the exemption of investment firms qualifying as small and medium-sized enterprises from the requirements to maintain a countercyclical capital buffer and capital conservation buffer.
- CSSF Regulation N° 15-04 on the setting of a countercyclical buffer rate.
- CSSF Regulation N° 15-02 relating to the supervisory evaluation process that applies to CRR institutions.
- CSSF Regulation N° 15-01 on the calculation of institution-specific countercyclical capital buffer rates, transposing Article 140 of Directive 2013/36/EU.

## THE NETHERLANDS

The Dutch Banking Association (Nederlandse Vereniging van Banken, NVB) is the representative voice of the Dutch banking community with 79 members, including large and small, domestic and international banks, conducting business in the Dutch, European and international markets. The NVB strives towards a strong, healthy and internationally competitive banking sector. Representing the common interests of the banking sector, the NVB works towards the effective operation of market forces whilst taking into account the interests of its interlocutors.

### Dutch Banking Sector[18]

The Dutch banking sector is characterised by its relatively large size, high level of concentration and its international orientation. The Dutch banking sector has shrunk considerably in the past years. The size of the assets relative to the GDP of the Netherlands has decreased from 600% in 2008 to 400% in 2014.

The Dutch banking sector is increasingly regulated on a European Union level, in particular with regard to prudential and financial markets legislation. Most of this legislation requires the national implementation of EU laws, in which national authorities and policy makers have some scope to adjust the EU standards to the national context and to complement it with specific national legislative measures.

The Netherlands being a member of the Eurozone is subject to additional European banking legislation compared to those EU-countries that use other currencies than the euro. The Banking Union project established a Eurozone-wide banking supervision and resolution

[18] See here all facts and figures on the Dutch Banking sector: https://www.nvb.nl/en/association/272/dutch-banking-association.html

mechanism. Seven banks in the Netherlands are under the direct supervision of the Single Supervisory Mechanism, which is part of the European Central Bank (ECB).

The Dutch banking sector rapidly adjusts to the new challenges, one of the major challenges is the innovation in financial services. In 2015, 93% of the population used online banking and 86% a mobile banking app. Because of the strong digital infrastructure in the Netherlands standards are high and new start-ups (Fintech) and traditional banks seeking cooperation are at the same time competing to deliver excellent financial services.

**Culture and Conduct Map.**

Together with several partners the Dutch Banking Association (NVB) has developed a Culture and Conduct map for the Financial Industry. This Culture and Conduct Map is the result of eight meetings held between January 2014 and February 2015, in which various groups of young people shared ideas and discussed the culture and conduct in the financial industry. The Culture and Conduct Map contains the values and the accompanying working attitudes of the required culture and the appropriate conduct.

**Oath and Discipline Law**

Along with the introduction of a social charter and updating the Banking Code, the Dutch banking industry has also taken the initiative to implement an ethics statement. The Dutch banks intend this to show that everyone working in the industry is bound by the codes of conduct for the ethical and careful practice of this profession. Employees have a personal responsibility for complying with those codes of conduct and can be held accountable for non-compliance.

The bankers' oath is a so-called "ethics statement" subscribed to by all employees working at bank offices in the Netherlands. It has the aim for banking employees to be fully aware of and keep into mind their special role in society, ensuring that they always carefully weigh the interests of all stakeholders with the interests of the customer taking a central place. The most important parts of the bankers' oath concern:

- Integrity and diligence;
- Careful weighing of interests with the customers' interests taking a central place;
- Compliance with laws, rules and code of conduct;
- Confidentiality and no abuse of knowledge;
- Transparency and responsibility;
- Preservation of trust in the financial industry.

If there is a violation of the code of conduct, a report regarding the relevant employee is submitted to an independent Bank Disciplinary Law Foundation (Stichting Tuchtrecht Banken) especially set up for this purpose. The Bank Disciplinary Law Foundation carefully reviews whether there was a violation and if it was serious enough to bring to the Disciplinary Commission. This Commission can impose penalties.

Since April 1 2015 the oath and the Disciplinary Law are effective and implemented in the Dutch Financial Supervision Act ("Wft"). As of April 1 2016 all 80.000 employees in the Dutch Banking Sector have taken the oath and are subject to the disciplinary law.

## Sustainability

A joint policy of the banks in the field of sustainability has started in 2014, this entails:

- Participation in the Dutch Energy Agreement and Green Deal in 2014, leading to the creation of centre of expertise for financing sustainable projects such as for example ground heat;
- The Dutch Banking Association has drawn up a protocol that offers banks a tool to report in detail on all outstanding loans on the balance sheet. The aim is to show customers and other stakeholders what economic activities are financed by banks.
- Publication of the climate statement in November 2015, in anticipation of the international Climate Summit in November in Paris;
- Working on the International Corporate Social Responsibility (ICSR) covenant to substantially address risks of human rights abuses and environmental damage; and
- Dialogue with NGOs and banks on improving reporting on sustainability.

## Prudential Requirements

On 1 January 2014 various amendments to the Dutch Bank Act and the Dutch Financial Supervision Act came into effect. With the European Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD IV) having entered into force, DNB in 2014 imposed additional capital requirements, the so-called systemic risk buffer of 3% of risk- weighted assets on ING Bank, Rabobank and ABN AMRO Bank and 1% on SNS Bank.

## Bank Structure Reform

The Dutch banks have written in their social charter that investment banking and proprietary trading activities are always related to the service to customers or careful management of risks and are not an object in themselves. In 2014 the Commission adopted a proposal on Bank Structure Reform, which includes a ban on proprietary trading, the separation of trading activities (e.g. market making) from the deposit taking function and others measures to prevent a shift of such activities to other legal entities. To date the proposal is still being discussed by the EU Member States and the European Parliament.

## Resolution Planning

On 1 January 2016 the Single Resolution Mechanism has become fully operational, and is regarded as an important step towards the European Banking Union, indispensable in developing the European Economic and Monetary Union and to prevent bank bail-outs. Resolving failing banks can be expensive for the society as a whole. Based on the Bank Recovery and Resolution Directive, the Single Resolution Mechanism will ensure that any resolution costs must first be borne by a bank's shareholders and creditors.

In the Netherlands, pursuant to the EU's Single Resolution Mechanism (SRM) Regulation the Dutch Central Bank (DNB) has been the designated National Resolution Authority (NRA). The European Single Resolution Board (SRB), in charge of deciding when to place a bank in resolution, is fully operational since 1 January 2016. The SRB consists of representatives from the relevant national authorities (those where the bank has its headquarters as well as branches and/or

subsidiaries). It has the powers to decide whether and when to place a bank into resolution and sets out, in the resolution scheme, a framework for the use of resolution tools and the Single Resolution Fund (SRF). Under the supervision of the SRB, the NRA is in charge of the execution of the resolution scheme.

Furthermore, together with the DNB they are preparing recovery plans for events of default. In the Netherlands the final implementation of the Banking Recovery and Resolution Directive (BRRD) has been finalised November 2015. The Dutch banks will contribute approximately EUR 550 million in 2016 and in total EUR 4.5 bln (in 9 years).

**MIFID II/MIFIR (financial instruments)**

The EU is updating its Markets in Financial Instruments legislation (MIFID/R II), which governs the provision of investment services in financial instruments by banks and investment firms and the operation of traditional stock exchanges and alternative trading venues. MiFID II contain more stringent rules in order to encourage efficient, competitive and transparent European financial markets. The new rules also aim to increase the protection of investors. The laws are entering into force in 2018. The European regulators are currently working on the technical specifications and many of these will directly applicable to banks and other financial institutions in the Netherlands.

**EMIR**

The European Commission has adopted technical specifications to complement the obligations defined under the Regulation on OTC derivatives, central counterparties (CCPs) and trade repositories (EMIR) which was adopted on 4 July 2012 and entered into force on 16 August 2012. The European institutions are currently in the stage of finalizing the technical specifications, which are expected to be finalized in the coming half a year. The Netherlands Authority for the Financial Markets (AFM) and the Dutch central bank (DNB) are carrying out the supervision of the obligations under EMIR.

**Central Clearing**

In 2016, two central counterparties (CCP’s) established in the Netherlands are authorised under the European Markets Infrastructure Regulation (EMIR): ICE Clear Netherlands and European Central Counterpart. According to the draft technical standards on the clearing obligation it will only start applying as of the 9$^{th}$ October 2016 and only for a limited number of counterparties.

Since 2014 the European Commission has adopted several 'equivalence' decisions for the regulatory regimes of central counterparties (CCPs) including Australia, Hong Kong, Japan, Singapore, Canada, Mexico, South Africa, Switzerland, the Republic of Korea and in March 2016 the United States.. The CCPs in these third country jurisdictions will be able to obtain recognition in the EU, and can therefore be used by market participants to clear standardised OTC derivatives as required by EU legislation, whilst remaining subject solely to the regulation and supervision of their home jurisdiction. Although rules may differ in the detail, international regulators are pursuing the same objectives to promote financial stability by promoting the use of CCPs that are

subject to robust prudential requirements. Through the use of deference, as agreed by the G20, regulatory gaps, duplication, conflicts and inconsistencies which can lead to regulatory arbitrage and market fragmentation are limited.

**Remuneration**

The Dutch Act on the Remuneration Policies Financial Undertakings has come into effect on 7 February 2015. The Act is part of the Dutch government's endeavours aimed at a sound and sustainable Dutch financial sector. Remuneration rules are included in the Capital Requirement Directive (CRD4) in which a 1:1 ratio is set between fixed and variable remuneration. The Dutch Act is more restrictive with a bonus cap of 20%. The Act also introduces all-encompassing legislation that requires financial undertakings to maintain sound remuneration policies and sets out rules with respect to the type of remuneration, as well as malus and claw-back provisions.

**Cybersecurity**

The EU has agreed on the Directive on security of network and information systems (NIS Directive), which is the first piece of EU-wide legislation on cybersecurity expected to enter into force on August 2016. The Directive sets minimum security standards for digital networks, services and services and is compulsory for certain sectors that provide essential services. Each Member State will determine what these sectors are and the deadline set for national implementation is May 2018. For the Netherlands this is expected to include financial services.

The Dutch government in its overview of cybersecurity risk published in October 2015 (Cyber Security Beeld Nederland), concluded that cybercrime and digital espionage are the biggest threats to digital security. The government is currently reviewing its Cybersecurity strategy, which could lead to further measures and public-private partnership initiatives.

## NORWAY

Norway is not a direct member of the EU which has led to a need for clarification when it comes to EU's structure for supervision for financial markets. Norwegian authorities do not accept that EBA, ESMA and EIOPA are the decision-making authorities for Norwegian private entities, since transferring powers to international organizations where Norway is not a member, violates the Norwegian constitution. On the other hand, EU does not want involvement from the domestic supervision authorities in relevant situations.

However, the Norwegian government, EU countries and other EEA-countries were able to find a solution to the problem during the fall of 2014. Under the agreed model, EFTA Surveillance Authority (ESA) will be responsible for decisions that are binding on Norway or Norwegian companies. The goal is that the EFTA and EU supervisory bodies will cooperate and be able to participate in each other's introductory work and decision-making processes. The suggested solution was approved by the Norwegian Parliament on 13 June 2016.

The new European capital adequacy regime was introduced in Norway in 2013, with a gradual introduction of new buffer requirements along with a requirement for banks to hold capital

against risks not covered by the minimum and buffer requirements. On 1 July 2016 the capital requirement build-up will reach its end, implying that Norwegian institutions have to have a CET1 ratio of minimum 11.5 percent. This includes a countercyclical capital buffer at 1.5 percent. The countercyclical capital buffer is set by the Ministry of Finance based on a recommendation from the Norwegian Central Bank (Norges Bank) and may be up to 2.5 percent. The central bank delivers its comments on the level of the buffer 4 times a year, when it publishes its Monetary Policy Report. The advice is confidential until the Ministry of Finance has reached a decision.

In addition to the 11.5 percent, financial institutions regarded as systemically important (SIFI) have to hold an additional CET1 of 2 percentage points (from 1 July). DNB, Nordea and Kommunalbanken are currently considered as systemically important banks. To become a SIFI, at least one of the following criteria must be met:

- By the end of the previous year, total assets must have been equivalent to over 10 percent of GDP for Mainland – Norway.
- By the end of the previous year, market share for domestic lending to the general public needs to have been higher than 5 percent.

The Ministry of Finance concluded 25 November 2015 on regulations regarding the Liquidity Coverage Ratio (LCR) for banks etc. The new regulation corresponds to the equivalent requirements in the EU. The LCR requirement implies that one shall have liquid reserves which is equal to net liquidity outflow in a given stress period of 30 days. The LCR requirement is set to 70 percent as of 31 December 2015, 80 percent as of 31 December 2016 and 100 percent as of 31 December 2017. Systemically important financial institutions had to fulfill an LCR requirement of 100 percent already from 31 December 2015. The institutions are also obliged to report LCR for "significant currencies" (debt in one currency that exceeds 5 percent of total debt). The Ministry of Finance has asked the Norwegian FSA to assess whether institutions also should face a LCR requirement for each significant currency. The FSA's assessment is due in August 2016.

A new law regarding financial institutions ("Finansforetaksloven") was approved in the spring of 2015 and came into effect from 1 January 2016. The new law implies that several new EU/EEA regulations as well as different, previous laws regarding financial institutions are combined into one law. The corresponding, more detailed regulation will be finalized during the summer.

**Cybersecurity**

On 17 December 2015, The Norwegian FSA changed the regulation concerning information and communication technology. The change implies that the board of directors in a financial company has to address matters related to the outsourcing of IT-activities. As a part of this, plans regarding the outsourcing process as well as a risk assessment shall be presented to the board.

On 1 January 2016, new regulation on systems for payment services became effective. The regulation is in line with the development in the EU and implies mandatory risk and vulnerability assessments when implementing new payment services. The regulation also includes several safety measures to ensure confidentiality etc.

## Housing Market

The Norwegian government announced a new strategy for the housing market in 2015. The objective of the strategy was to simplify regulations and bureaucracy to increase housing supply in relevant areas, as well as tighten credit regulations to dampen the growth in house prices and household debt. The latter led to a change in regulation, and lenders now face the following requirements:

- Maximum LTV of 85 percent (it is possible with higher LTV if one has additional security in the form of a mortgage on other property or others provide a personal guarantee).
- Mandatory installments for loans with LTV over 70 percent (set to 2.5 percent annually or the equivalent to installments on an annuity loan with 30-year duration).
- Credit lines up to maximum 70 percent of market value.
- Lenders must be able to withstand an increase in the mortgage interest rate of 5 percentage points.

To ensure flexibility, banks are able to deviate from the above requirements in certain cases. The limit is however set to 10 percent of granted loans each quarter. The new regulations will only affect new loans, i.e. refinancing or transferring a loan to another bank is not affected. This applies as long as the nominal amount is the same, collateral is in the same object and the maturity is the same or lower. The regulation became effective from 1 July 2015 and is set to last until 31 December 2016, but the Ministry of Finance is currently contemplating if the regulation shall be extended further.

## Solvency II

Solvency II entered into force for Norwegian insurance companies on 1 January 2016. The main elements of the Solvency II-framework are implemented in Norwegian legislation through a new law for financial institutions (in force on 1 January 2016). The law is complemented by a regulation based on the implementing measures (Level 2) to the Solvency II framework Directive. This regulation was adopted on 25 August 2015 by the Norwegian FSA, and includes several of the permanent and transitional measures for long-term guaranteed products under Solvency II that were introduced by the Omnibus II-Directive in 2013. For life insurers, one of the transitional measures are of particular importance, giving the companies an optional 16-year period to phase in their full Solvency II technical provisions. However, this measure is made subject to a national limitation, capping much of the effect.

Due to the Solvency II implementing measures (Level 2) not yet being included in the EEA agreement, the Norwegian FSA adopted on 22 December 2015 a more detailed regulation based on said measures. This regulation will be replaced by the actual implementing measures as soon as these are made part of the EEA agreement.

Solvency II is mandatory for both life and non-life insurers, but not pension funds. New solvency requirements for pension funds are being discussed in the EU, but not likely to be implemented in the foreseeable future. As a consequence, the Norwegian Ministry of Finance has asked the Norwegian FSA to assess the need for new solvency requirements also for pension funds.

The FSA gave its advice on this matter in January 2016, suggesting a simplified version of Solvency II for pension funds to be applicable from 1 January 2018.

The Norwegian Supervisory Authority is expected to publish guidance to the complete Solvency II regulation by the end of Q3 2016.

The implementation of Solvency II and CRR/CRD IV connotes the introduction of significantly different capital requirements regimes for the different sectors of financial institutions, and the largest financial institutions in Norway are part of groups with activities within different sectors. On 18 December 2015 the Norwegian Ministry of Finance adopted a regulation for consolidated capital requirements for financial groups. The regulation defines the different cross-sectoral groups, and which groups are to be subject to CRR/CRD IV or Solvency II. The regulation entered into force on 31 January 2016.

**Life Insurance and Pensions**

For several years there has been a trend in Norway of transmission from defined benefit pension schemes (DBs) to defined contribution schemes (DCs) in the private sector, regarding old-age pensions. Lower interest rates, higher longevity risk and the introduction of Solvency II supports this development even further. These trend is an increasing challenge for life insurance companies, due to the increasing amount of paid-up policies. Paid-up policies are up-earned pension rights for employees who quit a company with a DB scheme or works in a company that changes the pension scheme from a DB to DC. The capital linked to paid-up policies are around 260 billion of NOK, and has an annual interest rate guarantee.

Almost all of the new pension schemes drawn in the Norwegian market are DC plans, and almost none of the new private plans established the past couple of years were DB plans.

The hybrid pension product (“target benefit pensions”) was a new competitive old-age pension scheme introduced by new legislations from 2014. However, the first hybrid pension schemes occurred the first time in 2015, and has still a small market share (around 3.000 employees) in the Norwegian market, which is dominated by defined contribution pension schemes (around 1.2 billion employees has DC). Around 250.000 employees have DB plans.

Due to high capital requirements for DB schemes and paid-up policies under Solvency II, insurance companies are no longer willing to receive a DB product or paid-up policies from other life insurance companies.

From 1 September 2014 the legislator introduced a new product called “paid-up policies with investment choice”. The new product makes it possible for existing holders of paid-up policies with guarantees, to convert paid-up policies into unit-linked policies (if they relinquish the guarantees). As of yet, only one company is offering this product in a larger scale.

From 1 January 2016 there was introduced new rules of disability pensions in private sector, with a transitional period of one year to stablish new disability pension schemes. Within one year the employers therefore will have to change all of the disability pension schemes.

The market for public sector pensions has changed significantly, due to fewer providers of municipal pensions and new legislation for public-sector disability pensions introduced from 1 January 2015.

## PORTUGAL

### Regulatory and Legal Framework

During the period under review, as in previous years, the evolution of the financial sector legislative and regulatory framework in Portugal continued to be largely influenced by the European regulatory and legislative context.

On 6 July 2015, Law 66/2015 introduced changes to the basic bank account regime converting it from a voluntary to a mandatory regime applicable to all credit institutions authorised to accept deposits in Portugal. It also introduced the requirement for credit institutions to provide clients with an annual fee statement recapping all fees charged on products and services linked to a current account. Additionally, it also established legal principles regarding fees charged by credit institutions and introduced the prohibition on levying fees on cheques returned to their beneficiary.

In September 2015, Law 147/2015 implemented Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009, on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), establishing new capital and governance requirements. It also granted several new supervisory powers to the Portuguese Insurance and Pension Funds Regulator (ASF).

Law 148/2015 was also issued in September, implementing Directive 2014/56/EU of the European Parliament and of the Council of 16 April 2014, regarding statutory audits of annual accounts and consolidated accounts, at national level. Pursuant to this law, the Portuguese Securities and Exchange Commission (CMVM) became the supervisor of the Auditing sector, being responsible for supervising audit reports, certifying new auditors and maintaining a registry of all certified auditors.

The Portuguese legal framework of cooperative banks was also amended with the approval of Decree-law 190/2015 of 15$^{th}$ September. Cooperative banks can now be separated into two types, with specific legal provisions. On the one side commercial cooperative banks, which are subjected to the regular legal framework of any other bank, and, on the other, non-commercial cooperative banks which can only be created for purposes of mutualism.

On 10 November 2015, Banco de Portugal issued Notice 3/2015 which defines the procedures for the submission, maintenance and review of recovery plans, as well as other additional rules concerning the procedures for determining simplified obligations in the preparation and reporting of the recovery plans. At the same time, EBA Guidelines on the range of scenarios to be used in recovery plans and on the minimum list of qualitative and quantitative recovery plan indicators were integrated into the Legal Framework of Credit Institutions and Financial Companies.

On 7 December 2015, Banco de Portugal issued Notice 5/2015 that requires all entities subject to Banco de Portugal supervision to prepare their financial statements on an individual and consolidated basis, where applicable, in conformity with the international accounting standards, and establishes transitional provisions to be in force up to 31 December 2016 for certain entities.

In relation to macro prudential measures, on 7 September 2015, Banco de Portugal issued Notice 1/2015 which regulates the implementation of the capital conservation buffer of 2.5%, with effect from January 2016. According to Banco de Portugal, the decision to frontload the full implementation of this buffer to January 2016, instead of gradually implementing it between January 2016 and 2019, aimed at making financial institutions more resilient, by increasing their capacity to absorb unexpected losses, and therefore contributing to financial stability.

On 29 December, Banco de Portugal published a press release informing on its decision to set the countercyclical buffer at 0%, with effect from 1 January 2016 and to prevail in the first quarter of the year. This buffer applies to all credit exposures to the domestic private non-financial sector of credit institutions and investments firms in Portugal subject to the supervision of Banco de Portugal or the European Central Bank (Single Supervisory Mechanism), and is meant to contain the risks of system-wide stress generated by excessive credit growth. The buffer is reviewed on a quarterly basis. On 30 March 2016, Banco de Portugal kept the countercyclical buffer rate at 0%.

On that same day, Banco de Portugal issued a press release with the names of the banking groups identified as O-SIIs (Other Systemically Important Institutions) in 2015 and the respective capital buffers which have to be complied with from 2017 onwards. The 6 banking groups classified as O-SIIs had the buffer established at levels ranging from 0.25% to 1%. The aim of this buffer is to compensate for the higher risk that these institutions present to the financial system due to their size or business complexity, importance for the economy and the degree of interconnection with other institutions in the financial sector and, in the event of insolvency, the potential contagion effects to the rest of the financial system.

**Solvency and Liquidity**

With regards to solvency, the Portuguese banking system continued to present a solid situation. The banking sector's Common Equity Tier 1 (CET 1) Ratio stood at 12.4%, at the end of 2015 (11.3% in 2014). On the other hand, the Overall Solvency Ratio was 13.3% in December 2015 (12.3% in 2014).

In November 2015, the ECB (the Single Supervisory Mechanism) published the results of the Comprehensive Assessment conducted to nine financial institutions of the euro area that had not been included in the same exercise held in 2014, which included, the Portuguese bank, Novo Banco.

In the baseline scenario of the stress test, Novo Banco surpassed the minimum threshold of 8% for the CET 1 ratio in every year of the test, even considering the applicable phased-in criteria, reaching a ratio of 8.23% at the end of 2017. Under the adverse scenario, the bank surpassed the 5.5% threshold for the CET 1 ratio in the first two years of the test, even considering the applicable phased-in criteria. However, Novo Banco registered a decrease of the ratio to 2.43% at the end of

2017, which corresponds to a projected capital shortfall of EUR 1.398 billion. This shortfall has been covered at the end of 2015 through the transfer of five senior bonds valued at EUR 1.9 billion from Novo Banco back to the "bad bank" Banco Espírito Santo (BES)[19]. This action boosted Novo Banco's CET1 ratio to approximately 13%.

In terms of liquidity, Portuguese banks kept a comfortable position, confirmed by the 102% Loan-to-Deposit Ratio at the end of 2015 (107.2% in 2014), which clearly stood below the threshold of 120% recommended by Banco de Portugal. The positive trend followed by deposits highly contributed to this situation and provided Portuguese banks with a stable funding structure. This source of financing accounted for over 61% of the sector's aggregated balance sheet (on a consolidated level) at the end of 2015. Furthermore, Portuguese banks have managed to reduce their dependency on the ECB funding, with the amounts borrowed from the Eurosystem decreasing by 11.4% between June 2015 and March 2016.

**Other Relevant Developments**

On 20 December 2015, the Portuguese authorities announced the resolution of Banif - Banco Internacional do Funchal, S.A. (Banif) and the sale of the majority of its assets and liabilities to Banco Santander Totta for EUR 150 million. The measure also involved the transfer of assets with a book value (before the application of an haircut around 66%) of €2.2 billion from Banif to an asset management vehicle owned by the National Resolution Fund and required the injection of a total of EUR 2.255 billion into the bank, of which 1.766 billion by the Portuguese Treasury and EUR 489 million by the National Resolution Fund.

On 29 December 2015, Banco de Portugal, the National Resolution Authority, approved a number of decisions that completed the resolution of Banco Espírito Santo (BES), which occurred in August 2014. In particular, five senior bonds valued at EUR 1.9 billion (4 percent of total liabilities) were transferred from Novo Banco back to its predecessor BES.

Although the Portuguese banking sector remains overall stable, the resolution of Banif and the transfer of Novo Banco senior bonds back to BES had a negative impact on international investors' confidence in the national banking system.

## ROMANIA

During the period under review, the following developments were recorded in the field of prudential regulation:

**Legislation**

The *Directive 2014/49/EU on deposit guarantee schemes* was transposed in the national legislation by the *Law no.311/2015 on deposit guarantee schemes and the Bank Deposit Guarantee Fund*. The Bank Deposit Guarantee Fund is regulated as a scheme administered by a

[19] Following the resolution measure applied to Banco Espírito Santo (BES), in August 2014, its general activity, healthy assets and deposits were transferred to a bridge bank, Novo Banco. Troubled assets, subordinated liabilities and own funds remained in BES, which is due to be liquidated.

public body and, according to the law is entrusted with competences for administrating also the resolution fund.

The *Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012* was transposed in the national legislation by the *Law no.312/4.12.2015 on the recovery and resolution of credit institutions and investment firms, as well as on amending and supplementing of certain normative acts in the financial field transposing Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms.* The legal framework is based on three pillars, respectively prevention, early intervention and bank resolution, for each pillar being established, the conditions for application, the authorities involved and their powers, the tools that may be applied and the implementation method thereof.
The resolution tools are the following:

- sale of business of an institution under resolution;
- setting up a bridge institution, for receiving and holding shares or other ownership instruments or same or all of the assets and liabilities of the institution under resolution;
- separation of toxic assets of an institution under resolution;
- bail-in.

In this respect, the National Bank of Romania is entrusted with both current statutory duties (as a central bank and as a supervisory authority), as well as with the resolution powers, which are structurally separated by specific provisions of the Law. The management of the contributions raised for funding the resolution fund is entrusted to the Bank Deposit Guarantee Fund, while the financing of resolution measures is determined and ordered by the National Bank of Romania, as a resolution authority. According to the provisions of the Law, the Ministry of Public Finance shall become a decision-making factor within the recovery and resolution process of credit institutions, especially where such measures would have a direct fiscal impact or a systemic impact.

In 2015, the Romanian Parliament adopted the *Law no.304/2015 on the issuances of covered bonds*. The new legislation was developed according to the best practices mentioned within *EBA Report on EU Covered Bonds Frameworks and Capital Treatment (2013).*

At the beginning of 2016, NBR issued *Regulation no.1/2016 on the activity of issuance of covered bonds*, which was necessary for the implementation of the new law on covered bonds. The main areas addressed by the secondary legislation are:

- the procedure for the NBR approval of the issuance of covered bonds and the authorization of the cover pool monitor;
- conditions for structuring of the cover pool assigned to guarantee covered bonds;
- requirements for the management of asset and liabilities risks in covered bonds (including the calculation of overcollateralization requirements, the liquidity risk management, conditions for using derivative financial instruments for hedging the interest rate and foreign exchange risk, stress tests factors);
- supervisory reporting obligations for the issuer to be transmitted to NBR; and

- transparency and disclosure obligations for the issuer.

According to the *NBR Order No.12/2015 regarding the capital conservation buffer and the countercyclical capital buffer*, issued on the basis of *Recommendation of the National Committee for Financial Stability No.1/2015 regarding the implementation of capital buffers in Romania*, starting from January 2016, the credit institutions have to maintain a capital conservation buffer of Common Equity Tier 1 capital equal to 0.625 percent of their total risk exposure amount, which will rise gradually over the next three years. The countercyclical capital buffer is set at 0 percent.

According to the *NBR Order No.11/2015*, issued on the basis of Recommendation of the National Committee for Financial Stability, the credit institutions authorized in Romania and identified as O-SII by the National Bank of Romania on the basis of the data collected in 2015 have to maintain an O-SII buffer of 1 per cent. of their total risk exposure amount.

**Ongoing Financial Regulatory Reform Efforts**

NBR was actively involved (along with the National Authority for Consumer Protection) in the drafting of the text proposal for the transposition of the provisions of the *Directive 2014/17/EU on credit agreements for consumers relating to residential immovable property* (Mortgage Credit Directive). Currently, the proposal of the NBR regulation transposing in the national law the articles related only to creditworthiness assessment and remuneration policies for creditors that are already supervised by NBR is in the approval process, according to the agreement with the National Authority for Consumer Protection.

Another objective in the regulation field is to update the national regulatory framework in the area of *money laundering and terrorism financing* by transposing into the national legislation the provisions of the *Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing* (in collaboration with National Office for Prevention and Control of Money Laundering, Ministry of Justice and other national authorities).

As regards the transposition of *Directive (EU) 2015/2366 on payment services in the internal market* (that amends the existing EU directive in this field), NBR is actively participating in the inter-institutional transposition group (lead by the National Authority for Consumer Protection) in order to update the existing legislative framework. The relevant legislation - *Government Emergency Ordinance No. 113/2009 on payment services*, needs to be updated until January 2018.

**Developments in the Accounting Regulation Field**

Taking into consideration the Ministry of Public Finance reporting requirements, in order to ensure the comparability of the information covered by the semi-annually accounting reports at the national level, the Semi-annually accounting reporting system, applicable to the entities under the National Bank of Romania accounting regulation scope, was updated by the National Bank of Romania in August 2015 by issuance of the following order:

- Order no.8/2015 amending Order no.10/2012[20], modifying the template of one of the semi-annually accounting reporting forms - code 30 – "informative data", for all the categories of entities under the scope of the NBR Order no.10/2012, according to the reporting requirements set out in the *Ministry of Public Finance Order no.773/2015 approving the Accounting reporting system on the 30th of June 2015 for the economic entities and amending and supplementing some accounting regulations*, as well as updating the semi-annual accounting reporting forms templates, applicable to the credit institutions, according to amendments brought to the FINREP reporting framework during 2014.

In order to ensure the optimal conditions for the unitary application of the FINREP individual reporting framework by the Romanian credit institutions, as well as the correlation thereof with the amendments brought to the FINREP consolidated reporting framework, approved by the EBA in March 2015, Order no.6/2014[21] was amended by the National Bank of Romania by issuance of the following orders:

- Order no.5/2015[22] (applicable starting with the reference date for reporting 30.06.2015), the main aspects envisaged thereby being: the clarification of the reporting instructions related to non-performing/ forborne exposures and the update of the correlations within/ between individual FINREP forms, based on the latest version of the validation rules related to FINREP consolidated reporting framework, published on the EBA website in March 2015;

- Order no.10/2015 (applicable starting with the reference date for reporting 31.01.2016), mainly amending the threshold for reporting the individual FINREP forms on geographical breakdown and clarifying the presentation within individual FINREP reports of the negative interest income on financial assets.

With a view of ensuring the comparability of the financial and accounting statistical information related to Romanian branches of credit institutions having their headquarters in other Member States, needed for performing analyses and studies at the National Bank of Romania level, with the similar information reported by the credit institutions in the FINREP reports, Order no.5/2014[23] was also amended by the above-mentioned National Bank of Romania Order no.5/2015 and Order no.10/2015.

In order to ensure the transposition of the applicable provisions of the ***Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council***

[20] National Bank of Romania Order no.10/2012 for the approval of the Semi-annually accounting reporting system, applicable to the entities under the National Bank of Romania accounting regulation scope

[21] Order no.6/2014 for the approval of the Methodological rules regarding the preparation of FINREP individual financial statements, according to International Financial Reporting Standards, applicable to the credit institutions for prudential supervision purposes

[22] This order was published on 30.06.2015 and it was not included in the previous Global Survey.

[23] Order no.5/2014 for the approval of the Methodological rules regarding the preparation of the periodic reports containing financial and accounting statistical information applicable to Romanian branches of credit institutions having their headquarters in other Member States

***and repealing Council Directives 78/660/EEC and 83/349/EEC*****,** the National Bank of Romania **has issued two orders as follows:**

- Order no.6/2015 (applicable to entities, other than credit institutions, covered by NBR accounting regulation scope, starting with 01.01.2016), the main aspects envisaged by the order compared to the previous regulation[24] being: the transposition of the novelty elements of the new accounting directive; the inclusion of some IFRS provisions/accounting treatments for those situations in which the new accounting directive does not provide accounting treatments for certain transactions; the completion of the accounting regulations with provisions of the legislation applicable to the economic operators, in order to ensure a unified treatment at the national economy level;

- Order no.7/2015 (applicable to credit institutions starting with 01.01.2016) amending Order no.27/2010[25], which introduced/ updated some provisions related to the management report, corporate governance, financial statements audit and publication, as well as some disclosure requirements in the notes.

For ensuring a unified treatment with that provided for the economic operators in the regulation issued by the Ministry of Public Finance[26] and to meet the information needs for that authority, Order no.1/2013[27] was updated in May 2016 by issuance of the following order:

- Order no.3/2016, amending the template of the annual accounting reporting form code 30 – "Informative data", according to the Ministry of Public Finance requirements, as well as updating the correlations within the form and repealing the provisions related to stamping.

## SINGAPORE

### Significant Developments in Banking

Resolution Regime for Financial Institutions in Singapore – In April 2016, MAS consulted on legislative amendments to enhance the resolution regime for financial institutions in Singapore. This follows MAS' June 2015 policy consultation on proposals to enhance the resolution regime to promote the orderly and efficient resolution of distressed financial institutions, which was guided by the Financial Stability Board's Key Attributes of Effective Resolution Regimes for Financial Institutions[28]. In particular –

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[24] National Bank of Romania Order no.27/2011 for the approval of Accounting regulations according to the European directives, as subsequently amended and supplemented (repealed by Order no.6/2015)

[25] National Bank of Romania Order no.27/2010 for the approval of Accounting regulations according to International Financial Reporting Standards, applicable to the credit institutions, as subsequently amended and supplemented

[26] Order no.123/2016 of the minister of public finance regarding the main aspects related to the preparation and submission of the annual financial statements and accounting reports of the economic operators to the territorial units of the Ministry of Public Finance

[27] National Bank of Romania Order no.1/2013 for the approval of the Methodological rules regarding the preparation of the annual reporting for Ministry of Public Finance information needs, applicable to the credit institutions

[28] MAS had in April 2013 strengthened its resolution regime for financial institutions and expanded its powers under the Monetary Authority of Singapore Act ("MAS Act") for the resolution of financial institutions. MAS extended its resolution powers to cover a wider range of financial institutions and enhanced our resolution toolkit. For example, MAS has

- MAS proposed recovery and resolution planning requirements for financial institutions that are systemically important or that perform critical functions. These financial institutions are also required to adopt measures to address deficiencies in their recovery plans, and remove impediments to resolvability.
- To facilitate orderly resolution, MAS proposed to have powers to impose temporary stays on early termination rights of financial contracts. Temporary stays can also be applied to contracts that are non-financial in nature, but that are necessary to ensure continuity of essential services and functions of a financial institution.
- MAS also proposed to have powers to recapitalise a financial institution by writing down its unsecured subordinated creditor claims or by converting them into equity stakes in the financial institution.
- MAS also consulted on a creditor compensation framework, and proposed to fund costs relating to resolution expenses through ex-post funding arrangements.

*The Banking (Amendment) Bill 2016 ("the Bill")* – The Bill was passed in Parliament on 29 February 2016. The Bill sets out the legislative amendments proposed by the Monetary Authority of Singapore ("MAS") to enhance prudential safeguards, corporate governance and risk management controls in the banking industry. These amendments serve to strengthen MAS' regulatory and supervisory framework, and align them with international best practice. Certain amendments have also been made to formalise MAS' existing regulatory requirements and to clarify MAS' policy intent on certain matters. The Bill proposes amendments to the Banking Act (Cap. 19) in respect of the following areas:

- Prudential safeguards;
- Corporate governance;
- Risk management controls; and
- Duty to inform MAS of material adverse developments.

*Liquidity Coverage Ratio Disclosure Requirements* - In November 2014, MAS issued Notice 649 to update liquidity regulations for banks. In particular, the Liquidity Coverage Ratio ("LCR") requirement was introduced for domestic systemically important banks in Singapore ("D-SIBs").

On 14 December 2015, MAS issued Notice 651 pursuant to section 55 of the Banking Act (Cap. 19) (the "Act") and applies to every bank incorporated in Singapore which has been notified by the Authority that it is a domestic systemically important bank ("D-SIB"). This Notice sets out requirements for a D-SIB to disclose quantitative and qualitative information about its Liquidity Coverage Ratio ("LCR"). It also sets out guidance on disclosure of non-mandatory quantitative and qualitative information that a D-SIB is encouraged to make. Together, these disclosures are intended to facilitate market participants' understanding of the D-SIB's liquidity risk profile and management, and thereby promote market discipline.

powers to assume control of a financial institution, effect a compulsory transfer of business or shares of a financial institution in resolution, effect a compulsory restructuring of share capital of a financial institution in resolution, and set up a bridge financial institution.

*Proposed Amendments to Implement Revised Basel Capital and Disclosure Requirements* – On 9 October 2015, MAS consulted on the proposed amendments to MAS Notice 637 to implement the revised Basel capital and disclosure requirements for Singapore-incorporated banks. The proposed amendments will enhance the risk capture of banks' equity exposures and counterparty credit risk exposures (including exposures to central counterparties), and improve comparability of banks' capital disclosures.

*Anti-Money Laundering and Countering the Financing of Terrorism Controls in Trade Finance and Correspondent Banking* – MAS issued an information paper to provide guidance to banks, merchant banks and finance companies on the anti-money laundering and countering the financing of terrorism controls relating to trade finance and correspondent banking activities. Besides setting out MAS' supervisory expectations and highlighting areas for attention and improvement, it also serves to assist banks in their benchmarking against industry norms and identification of control gaps.

*Notice and Guidelines on the Prevention of Money Laundering and Countering the Financing of Terrorism* - The MAS Notice 626 was amended in Nov 2015 to clarify the application of Simplified Due Diligence to Singapore and foreign government entities, and to require additional information to be obtained for beneficiaries of direct life insurance plans that are sold through banks.

*The Association of Banks in Singapore Guidelines to Banks on AML/CFT (ABS Guidelines)* - The Association of Banks in Singapore embarked upon a major revision of their AML/CFT Guidelines to Banks. The first round of revision was made in Nov 2015 and then a further round of revision was undertaken in Apr 2016. The objective was to align the ABS Guidelines to the new MAS AML/CFT Notices and Guidelines to give greater clarity to Banks in applying them. The Guidelines are principles based and have various sections that are specific to business lines such as retail banking, investment banking, private banking, trade finance etc.

*Cancellation of Notice on Prohibition on Transactions with the Iranian Government and with Iranian Financial Institutions* - On 28 January 2016, MAS Notice MA-N-EXT 1/2012 on "Prohibition on Transactions with the Iranian Government and with Iranian Financial Institutions" was cancelled in line with the lifting of nuclear-related sanctions on Iran pursuant to the Joint Comprehensive Plan of Action. There is no longer a general prohibition on financial institutions being involved in a transaction or business relationship with the Government of Iran, the Central Bank of Iran and financial institutions in Iran. Nonetheless, the MAS (Sanctions and Freezing of Assets of Persons – Iran) Regulations 2007, which implements UN targeted financial sanctions on Iran, continues to apply.

**Significant Developments in Financial Advisory**

*Legislation and legislative amendments to effect some of the policy proposals under FAIR under the Financial Advisers Act (FAA)* - On 1 Jan 2016, MAS issued the legislation and legislative amendments to effect some of the policy proposals under FAIR under the FAA. The initiatives that were implemented included the following:

- **Balanced Scorecard Remuneration Framework for representatives and supervisors**
  This framework seeks to promote a culture of fair dealing by subjecting a significant proportion of a representative's remuneration to non-sales key performance indicators. Under the Balanced Scorecard (BSC) framework, the representative is assessed based on whether he has understood the customer's needs, recommended suitable products, made adequate disclosures and conducted himself professionally and ethically.

- **Restrictions on Non-Financial Advisory Activities Representatives**
  MAS implemented legislation restricting the types of non-Financial Advisory (non-FA) activities which representatives may conduct to maintain a high level of professionalism and competence in the FA industry. Any non-FA activities conducted by these persons should not be in conflict with their FA roles, result in a neglect of their FA duties or bring disrepute to the FA industry. Representatives are also prohibited from conducting moneylending businesses, promoting junkets for casinos, acting as real estate agents and marketing products that are not regulated under the Financial Advisers Act as investments.

- **Banning of Short-Term Incentives**
  MAS banned the payment and receipt of short-term incentives in the FA industry. This will better align the interests of FA firms and their representatives with those of their customers and ensure that FA firms and their representatives are not influenced by such incentives when recommending investment products to their customers.

- **Continuing Professional Development**
  MAS prescribed Continuing Professional Development (CPD) training requirements for FA representatives to ensure that they remain current and up-to-date in their knowledge of market and regulatory developments. FA representatives are required to fulfil a minimum of 30 CPD training hours annually, of which 12 hours are to be in Ethics, and Rules and Regulations.

**Significant Developments in Securities**

*Good Drafting Practices for Prospectuses* - The Guidelines aim to provide guidance to issuers and their professional advisers on good drafting practices for prospectuses. The SFA requires a prospectus to contain all the information that investors and their advisers would reasonably require to make an informed investment decision. To improve the readability of prospectuses and facilitate investors' understanding of the key information disclosed in prospectuses, issuers and their professional advisers should follow the general principles and drafting practices set out in these Guidelines when drafting prospectuses.

*Proposed Amendments To The SFA (Part XII And Section 324) -* The MAS released a consultation paper on 24 Aug 2015 on proposed legislative amendments under Part XII of the SFA to strengthen the effectiveness of MAS' enforcement regime in deterring market misconduct. This consultation follows the feedback MAS received for the proposals set out in section 4.2 of a consultation paper issued on 11 February 2015, explaining MAS' policy position regarding the intended draft amendments.

The proposed legislative amendments are as follows:

- Revision of section 199 of the SFA to clarify that there is no requirement of material price impact to establish a case of false or misleading disclosure;
- Introduction of a statutory definition in section 214 of the SFA of the phrase "persons who commonly invest" which is found in sections 215 and 216 of the SFA;
- Amendments to section 232 of the SFA, in order that the civil penalty imposed may be commensurate with the gravity of misconduct, even in cases where the profit gained or loss avoided happens to be low;
- Priority for MAS' civil penalty claims over debts by other unsecured creditors that accrue subsequently after contravention; and
- Amendments to section 324 of the SFA to make clear that MAS' officers, who may exercise investigation powers under the CPC in the course of their investigation, would be able to apply for an order under section 324 of the SFA regardless of whether the investigations were being carried out under the SFA or the CPC.

*Proposed Amendments To The Securities And Futures Act, Financial Advisers Act And Trust Companies Act* - The MAS released a consultation paper on 18 Sept 2015 on proposed legislative amendments to the Securities and Futures Act ("SFA"), Financial Advisers Act ("FAA") and Trust Companies Act ("TA") to identify areas where MAS' supervisory powers should be further enhanced, as well as to strengthen business conduct requirements applicable to entities regulated under these Acts. In line with the ongoing review of the Banking Act ("BA"), the proposed enhancements will also harmonise similar requirements across the various Acts where appropriate. The proposed policy amendments set out in this consultation are as follows –

- Enhancements to Supervisory Powers
- Strengthening of Business Conduct Requirements
- Pledging securities held in CDP direct accounts for collateralised trading

*Proposals to Enhance Regulatory Safeguards for Investors in the Capital Markets –* Following a July 2014 public consultation, MAS has announced it will proceed with its proposals to enhance safeguards for investors in the capital markets.

The proposals will be implemented via amendments to the Securities and Futures Act ("SFA"), expected to be tabled in Parliament in 2016:

- Extension of the current capital markets regulatory safeguards to investors in certain non-conventional investment products that are in substance capital markets products; and
- Introduction of an opt-in regime for accredited investors ("AIs"), where investors who meet the prescribed income or wealth thresholds ("AI-eligible investors") will have the option to benefit from the full range of capital markets regulatory safeguards applicable for retail investors.

In its 2014 Consultation Paper, the MAS had also proposed to introduce a complexity-risk ratings framework by which investment products can be rated for their relative complexity and risk of loss, and to disclose such ratings in product offering documents for new and ongoing offers to

retail investors. The MAS will separately release its Response to feedback received on this proposal.

**Note**: click here for a table of significant legislative/regulatory developments between July 1, 2015 and June 30, 2016

## SOUTH AFRICA

### South African Government Approach to Cybersecurity

The South African Government has in recent times launched several initiatives to improve the South African resilience against cyber threats. Related activities are mainly driven by the NCPF National Cyber Security Framework for South Africa (NCPF) adopted by Government. Implementation of the framework is led mainly by the State Security Agency with other departments within government taking responsibility for implementation of specific sections thereof that are aligned to their mandates. The JCPS Cybersecurity Response Committee is the decision making body established to implement the policy and also to advise Cabinet on cybersecurity threats amongst other things.

The Department of Justice published a draft cybercrime and cyber security bill late last year that aims to address some gaps in current South African legislation relating to cyber related crime and to legislate the cybercrime combating structures and cybersecurity requirements specified in the NCPF. We expect that the bill will go to Parliament in the near future.

The Department of Telecommunications and Postal Services was mandated to implement a national CSIRT called the Cyber Security Hub (CSH) which was launched in October 2015 and is operational in limited capacity at the moment. The CSH should facilitate information sharing and co-ordination within the private sector and between the private sector and Government, going forward.

The banking industry is recognized by Government as a key stakeholder in the fight against cybercrime in South Africa and was also the first industry to be on boarded as a stakeholder by the CSH. The banking industry, through the South African Banking Risk Information Centre (SABRIC) and the CSH, are collaborating to ensure that the industry's needs are catered for in the operational model adopted by the latter. In theory, all cybersecurity threats that come to the knowledge of Government via any of its departments, will be shared with the banking industry CSIRT hosted at SABRIC via the CSH.

The establishment of private public partnerships has been central to the South African banking industry's fight against organised criminal syndicates targeting banking clients, platforms and/or infrastructure. Over the years SABRIC on behalf of the banks, established well defined and operationally effective private public partnerships with law enforcement and other governments in South Africa and relevant cybercrime information - be it tactical, operational or strategic- is also shared by our law enforcement partners with the banking industry through SABRIC in order to aid in the detection and prevention of cybercrime.

Organised cybercrime is indeed well organised since skill and expertise of participants are contracted to ensure success. It is evident from this that partnerships and collaboration are also key elements within crime fighting organisations when organised crime is to be challenged. The banking industry acknowledges that bank related crime is a collective responsibility and the support of all stakeholders in the prevention and investigation thereof is vital in inhibiting such criminal activity.

This approach has yielded positive results in South Africa and particularly in the contact crime environment where shared skill and expertise within the police service, banking industry and prosecuting authority, working together, have been responsible for a significant reduction of such crimes.

The South African Government has on several occasions place on record that cybersecurity and the combating of cybercrime has to be a collaborative effort and that Government is not able to address or mitigate the threat without entering into public private partnerships. Whilst the willingness to partner is confirmed continuously, and several public private partnerships aimed at addressing cybersecurity resilience have proven to be effective, we are still experiencing capacity and skill shortages within Government that impact on the effectiveness of the model overall.

## Significant Developments in the Financial Sector

### *Protection of Investment Act, 22 of 2015*

In terms of this Act, international investors will now enjoy equitable treatment of their investments and protection aligned to local legislative frameworks, irrespective of bi-lateral investment/trade agreements which may have been concluded under different terms. Furthermore, before a dispute can be referred for international arbitration, all local mediation efforts have to be exhausted. We currently await gazetting of this Act for it to become effective.

### *Financial Intelligence Centre Amendment Bill*

The Financial Intelligence Centre Act of 2001 creates a regulatory framework with the intention to combat money laundering activities, the financing of terrorism and related activities.

During 2015, amendments to the current Financial Intelligence Centre Act were introduced in Parliament. The proposed amendments were in response to recommendations by the Financial Action Task Force to introduce the adoption of a risk based approach to customer due diligence for anti-money laundering, recognising scarce resources should be targeted at higher risks, with reduced compliance burdens for lower risks.

Additional amendments include the obligations for the identification of beneficial ownership; additional record keeping requirements for transactions; providing for the implementation of the United Nations Security Council Resolutions relating to the freezing of asset; enhancing the customer due diligence requirements for accountable institutions; and the management of prominent influential persons as clients.

The bill is still before parliament and is expected to be finalised in 2016.

### *Financial Sector Regulation Bill*

The financial sector regulation bill creates and gives effect to two regulatory authorities the Prudential Authority (a prudential regulator) and the Financial Sector Conduct Authority (a market conduct regulator) and seeks to achieve a financial system that works in the interests of the financial customers and supports balanced and sustainable economic growth in South Africa by establishing a regulatory and supervisory framework that promotes:

- financial stability;
- the safety and soundness of financial institutions;
- the fair treatment and protection of financial customers;
- the efficiency and integrity of the financial system;
- the prevention of financial crime;
- financial inclusion; and
- confidence in the financial system.

The objectives of the bill will be achieved by:

- granting the South African Reserve Bank the mandate to protect and enhance financial stability, and if a systemic event has adversely affected financial stability, to restore and maintain financial stability;
- establishing the Prudential Authority and the Financial Sector Conduct Authority to supervise and regulate the provision of financial products and financial services;
- ensuring co-operation, collaboration, co-ordination and consistency between the Prudential Authority, the Financial Sector Conduct Authority, the National Credit Regulator, the South African Reserve Bank and other organs of the state;
- protecting the interests of customers acquiring or using financial products and financial services by ensuring that financial institutions treat customers fairly and provide customers with financial education programs;
- providing for the regulation of significant owners of financial institutions and creating a framework for the supervision of financial conglomerates;
- ensuring a consistent and standardised approach to financial regulation, by establishing harmonised systems of licensing, supervision, complaints resolution, enforcement and review mechanisms;
- providing for procedural matters such as information sharing arrangements, information gathering and for supervisory on-site inspections and investigations into the affairs of a financial institution;
- providing financial sector regulators with enforcement powers, by establishing the Financial Services Tribunal to hear reviews of decisions made in terms of the financial sector laws, and for the imposition of administrative penalties and related orders; and
- establishing the Financial Sector Ombud Schemes Regulatory Council to provide for the regulation of Ombud Schemes.

**Amended Bank Regulations**

The amended Regulations relating to Banks incorporates the Basel Committee on Banking Supervisions revised requirements for Basel III and were published in *Government Gazette* No. 40002, on the 20th May 2016, becoming effective on the 1st of July 2016.

**Resolution Framework**

The National Treasury, in collaboration with the South African Reserve Bank and the Financial Services Board, published a discussion document titled "Strengthening South Africa's Resolution Framework for Financial Institutions" on 13 August 2015 for public comment. As part of enhancing SA's resolution framework, the SARB has commissioned a comprehensive research project on resolution and deposit guarantee schemes. The results of the research project on establishing a deposit guarantee scheme in SA are expected to be published for further comment during June 2016 before final decisions on the design features of the deposit guarantee scheme are taken.

**Insurance Bill**

The draft insurance bill was submitted to Parliament during 2015. The purpose of the Bill is to provide for a legal framework for the prudential supervision of insurance business in the Republic that is consistent, where relevant, with international standards for insurance regulation and supervision and to introduce a legal framework for microinsurance in South Africa to promote financial inclusion. It is anticipated that Parliament will request further public comments or hold further public deliberations on the insurance bill towards the latter part of 2016.

**Financial Markets Act**

National Treasury published the second draft of the Regulations under the Financial Markets Act during 2015. The draft Regulations, amongst other matters, deals with the central clearing of OTC derivative transactions; authorisation requirements for OTC derivatives; and the licensing and supervision provisions for central counterparties and trade repositories. In addition, the Financial Services Board published draft board notices establishing a framework for the reporting of OTC transactions to trade repositories; setting out and margin requirements for non-centrally cleared OTC derivative transactions; and the code of conduct which will be binding on all OTC derivatives providers, their employees and clients, to provide requirements aimed at protecting investors, such as enhanced disclosure requirements and appropriateness tests. It is anticipated that National Treasury and the Financial Services Board will release the draft Regulations, together with relevant supporting notices, for a third round of public consultation before the end of June 2016.

**New Exchange and CSD**

On 8 March 2016 the Registrar of Securities Services (Registrar) granted ZARX's application to be licensed as an exchange. The conditional approval was granted subject to compliance by ZAR X, to the satisfaction of the Registrar and by no later than 31 August 2016,

with certain suspensive conditions. ZAR X Stock Exchange is the first new stock exchange in over 100 years.

The licensing of Granite Central Securities Depository will introduce the first new CSD in 27 years. The focus of the CSD will be bonds and money market instruments. Granite is not yet operational.

**Developments Relating to Payment Systems**

The regional real time gross settlement system known as SIRESS, (SADC Integrated Regional Electronic Settlement System) reached a further milestone at the end of April 2016 with ZAR 2 trillion in value being processed through the system. Volumes remain steady at around 20,000 per month. Banks in a further 5 countries will be joining the SIRESS settlement system this year. Work continues on the next phase of development, being the low value payment stream and securities settlement, whilst the introduction of other SADC currencies for settlement is progressing.

The review of the collections landscape by the SARB has resulted in the payments industry looking at improved ways to facilitate collections, by way of electronic authentication. The abuse of early debit orders has been a source of concern for the industry for some time now and although this project is still in progress, it is anticipated to deliver an enhanced collections framework for all early debit orders.

The industry has collaborated, through PASA with Visa and MasterCard, to design and develop a fully interoperable biometric CVM acceptance specification. The specification will allow for interoperable fingerprint verification to be facilitated through the country's point of sale acceptance infrastructure.

This industry project, facilitated through the various PASA structures, aims to design, develop and implement enhanced electronic payment systems for both debit and credit payments respectively, that will accommodate improved flexibility and efficiency of messaging in future.

The SARB is conducting a formal review of the role and functioning of the Payments Association of South Africa (PASA) as the Payment System Management Body. A number of regulatory enhancements and changes are anticipated as a result of the move to a twin peaks regulatory architecture.

**Market Infrastructure**

In a significant milestone for South Africa's financial markets, ESMA, the European Union's Securities and Markets Authority recognised JSE Clear, the JSE-owned derivative central counterparty (CCP), as a third country CCP under Title III of Chapter 4 of EMIR. ESMA's recognition of JSE Clear as "equivalent" to CCPs in the EU followed the EU Commission's determination, in Q4 2015, that South Africa has an equivalent regulatory regime, for central counterparties, to the European Union.

The JSE equities market will move from its current of T+5 cycle to a T+3 settlement cycle on 11 July 2016. The move to T+3 is a regulatory imperative and will align the South African market to global standards improving both the credibility and operational efficiency of the local market.

In collaboration with National Treasury, Primary Dealers and Strate (CSD), the JSE has initiated a project to establish an electronic trading facility for government bonds in the primary market. This market is expected to go live in H2 2017, initially only for Primary Dealer participants; and in a second phase, the trading facility will be extended to other market participants.

## SPAIN

During the last year, the Spanish Parliament has been disolved twice and legislative elections have been held for the second time on 26 June 2016.

In general terms, due to such parliamentary situation and to an existing transitional government since 21 December 2015, small legislative activity has taken place in Spain during the period under review, mainly in the form of lower ranking regulations.

However, the need to continue transposing into Spanish law applicable European Directives has resulted in the following provision:

- Royal Decree 1012/2015 that develops Law 11/2015 of 18 June and concludes the transposition of Directive 2014/59/UE, stating the legal regime of recovery and resolution for Banks and investment services companies.
- Royal Decree 1021/2015 establishing the obligation to identify the tax residence of persons holding or controlling certain financial accounts and to report them within the context of mutual assistance. It transposes into domestic legislation Council Directive 2011/16/EU, amended by Council Directive 2014/107/EU, as regards mandatory automatic exchange of information in the field of taxation.

In addition to the foregoing provision, laws have also been enacted to respond to the current economic and legal situation. The most significant of these measures are the following:

- Law 25/2015, of July 28, 2015, on the second chance mechanism, reducing the financial burden and other measures of a social nature (originating from Royal Decree-Law 1/2015, of February 27, 2015): this new legislation consolidates in the Insolvency Law (Ley Concursal or "LC"), following some amendments, the new legislation ushered in by Royal Decree-Law 1/2015, of February 27, 2015 ("RDL 1/2015") concerning out-of-court payment agreements and the new rules on debt relief for individual debtors, known as the "second chance" mechanism.
- Law 5/2015, on promoting corporate financing. Among other matters, it establishes a number of changes to encourage bank financing to small and medium-sized enterprises, sets out the new legal framework on financial credit establishments and regulates

crowdfunding. It has also introduced amendments on other matters, including securitisations and debt issuance.

- Organic Law No. 1/2015, amending the Criminal Code (Organic Law No. 10/1995 of November 23, 1995). It makes a clarification about the Criminal Responsibility of Legal Entities. Companies have the obligation to institute new measures directed to detect and prevent crimes, and, in the event that those crimes have already taken place, mitigate the criminal responsibility, inasmuch as the installation of this kind of measures would work as a mitigating circumstance of the criminal responsibility.
- Order ECC/2314/2015 regulating the start of operation of the "Financial Holding File", as provided for by section 24 of Law 10/2010 on the Prevention of Money Laundering and the Financing of Terrorism. In compliance with the provisions set out in section 53.1 of Royal Decree 304/2014 which passed the Regulations of Law 10/2010, financial entities are under the obligation to provide the "Executive Service for the Prevention of Money Laundering of the Bank of Spain" (Sepblac) with information regarding the opening and cancellation of certain types of accounts (mainly current and savings accounts, securities and fixed-term deposits) as well as its holders and their representatives.
- Royal Decree-Act 9/2015, on urgent measures to reduce the tax burden on personal income tax payer and other economics measures. It covers certain tax modifications, mainly in order to bring forward to 2015 the second phase in the reduction in personal income tax rates initially scheduled for 2016.
- Law 34/2015 partially amending General Taxation Law 58/2003. It introduces relevant amendments with the purpose of strengthening the powers and rights of the tax authorities such as the possibility to impose penalties under the application of a specific general anti-avoidance rule (the so-called "conflict in the application of tax law").
- Law 48/2015 on the General State Budgets for 2016. It introduces new items of tax legislation such as the modification of the regime for conversion of certain deferred tax assets into a loan payable by the tax authorities.

## SWEDEN

### The Banks' Results and Key Figures

The four major commercial banks in Sweden jointly represent about 70 per cent of the market. These major banks have considerable activities in markets outside Sweden. The following is mainly based on the Swedish Central Bank, The Riksbank, Financial Stability Report, National Institute of Economic Research (NIER) and Finansinspektionen (the Swedish FSA).

### Market Developments

The Swedish economy has been growing strongly for more than a year and GDP increased by 1.3 per cent from the third to the fourth quarter of 2015. This was due to a sharp rise in domestic demand, while exports also grew surprisingly strongly given the weak growth in world trade according to the National Institute of Economic Research (NIER) latest report. The strong growth in exports in the fourth quarter was due partly to non-recurring effects, however, and investment in home improvements also surged temporarily. Together with the statistics available for the first quarter this year and indicators for households and firms, this suggests that growth in

GDP will slow in the first half of 2016. Growth will nevertheless be strong enough for the Swedish economy to enter a boom period this year, according to the NIER.

Recent years' strong growth in Sweden is partly a result of the global economy recovering from the financial crisis, according to NIER. The low interest rate policy has stimulated domestic demand while also keeping down the value of the krona, which has boosted exports. The stronger investment climate in the OECD countries means that Swedish exports – which include a high proportion of investment goods – will continue to grow this year and next, albeit not as rapidly as last year. Both fiscal and monetary policy will stimulate domestic demand in 2016 and 2017. Government consumption is forecast to grow by around 4 per cent this year, which is very high by historical standards. The increase is due largely to higher refugee-related costs, but a growing share of young and elderly people in the population is also increasing the need for government-funded welfare services. The Swedish Migration Agency's latest forecast indicates that inflows of asylum seekers will remain high in 2016 and 2017.

After rising rapidly over the past two years, housing investment is now at its highest level relative to GDP for more than 20 years. A shortage of labour and development land will, however, rein in this growth. There is already an unmet need for housing, and the strong population growth means that demand for housing will continue to rise rapidly. Housing investment will still therefore be insufficient to address the housing shortage. To do this, action will be needed both to further increase supply and to ensure more efficient use of the existing housing stock.

All in all, this means that GDP will continue to grow relatively quickly this year and next according to NIER. Expressed per capita, however, growth will not be especially strong: there will be only a modest increase of 0.9 per cent next year, and GDP growth per capita will be even weaker in the years after that. One reason is that the population is set to expand rapidly as the refugees now arriving in Sweden receive residence permits and begin to count as part of the population. It will, however, take a long time for many of them to gain employment and so contribute to output, which will put a damper on GDP growth per capita. If the refugees are integrated successfully into the labour market, GDP per capita may instead increase more quickly further ahead as more find work.

Employment has grown relatively swiftly in recent years, and the number of employed increased by 0.5 per cent in the fourth quarter of 2015. Firms' recruitment plans as reported in the NIER's Economic Tendency Survey, together with other indicators, suggest that employment will continue to rise at around the same rate in the coming quarters. Slightly further ahead, however, the increase will slow as demand growth in the economy eases. The growing need for welfare services means that the government sector will make an unusually large contribution to the rise in employment.

Inflation has been well below the Riksbank's target for the past five years. The protracted global downturn has led to weak growth in prices for internationally traded goods. At the same time, the domestic downturn put a damper on wage growth and made it harder for firms to transfer cost increases to consumers. Inflation as measured by the consumer price index with a fixed interest rate (CPIF) increased last year, however, due primarily to the depreciation of the krona since 2013, but was still only 0.9 per cent.

Fiscal policy was expansionary in the period 2009−2014, resulting in a decline in structural net lending in the government sector. Last year, fiscal policy became more contractionary, as all increases in expenditure were funded with equivalent tax increases. This helped strengthen structural net lending. In 2016 and 2017, however, structural net lending will deteriorate as a result of heavy refugee-related expenditure.

**Household and Corporate Borrowing**

Household debts consist primarily of mortgages. How quickly house prices increase therefore greatly affects the rate at which household debts increase. In recent years, Swedish house prices have increased sharply, according to Finansinspektionen (FI), the Swedish supervisory authority. Since the end of 2015, the rate of increase has slowed slightly, but this positive trend has continued over a number of years. Developments reflect the high demand for housing, primarily in metropolitan areas where there is high population growth and a large shortage of housing. The supply of rental housing is also limited. Low interest rates and the design of the tax system are also reducing costs for loan-financed housing purchases, which increases households' willingness to pay.

In order to decrease the risks associated with household indebtedness, FI has taken a number of measures. For example, FI implemented a mortgage cap in 2010 to decrease the risk that households would find themselves in situations of negative equity if house prices were to fall. FI is also introducing an amortisation requirement on 1 June of this year. The amortisation requirement means that the size of the loans of households will decrease over time, which reduces their sensitivity to shocks and thus reduces macroeconomic risks. FI's measures to manage the risks of household indebtedness are structural in nature. This means creating buffers and ensuring that households are resilient to different types of shocks. Firms' loans generally increase at a more irregular rate than those of households, according to FI. At present, corporate loans from Swedish banks are increasing by around 2.5 per cent a year.

**Continued Good Profitability in the Swedish Banking Sector**

Earnings in the Swedish banking sector continue to be strong, according to FI. One factor behind this is that growth in Sweden has been strong. Strong growth combined with low interest rates has contributed to households and firms opting to borrow. Strong economic growth also improves the payment capacity of borrowers, which in turn decreases the risks for credit losses.

Higher income in relation to expenses has resulted in higher aggregate profits for the major banks. Compared to European banks, the Swedish banks have a high return on equity. The credit losses of the major banks continue to be low and have held steady at the same level for the past five years. Low credit losses and high profitability mean that Swedish banks continue to be very resilient.

## Bank Capital

Most Swedish banks have satisfactory resilience to losses and are judged to have sufficient capital to maintain critical services even under more turbulent conditions, according to FI. The major banks currently have solid access to cheap funding in both SEK and the global reserve currencies, EUR and USD. The funding the banks receive from the general public is covered by the deposit insurance scheme and is stable.

The four major banks meet capital requirements. The marked increase in the banks' capital in relation to risk-weighted assets in recent years is primarily due to tighter capital requirements implemented by FI during this period. The banks have strengthened their capital somewhat compared to last quarter.

The major banks' total capital requirements amount to on average approximately 22 per cent of their risk-weighted assets. These requirements are distributed relatively evenly between the minimum requirements, the requirements set out in Pillar 1 and Pillar 2 and buffers.

The combined buffer requirements include the countercyclical capital buffer that is set by FI. Starting in June this buffer is set at 1.5 per cent and FI has decided to raise it to 2 per cent as of 19 March 2017.

In addition to the total capital requirement, the banks normally also hold a voluntary buffer. This allows banks to distance themselves even more from a situation where their own funds might fall below the total capital requirements. These buffers further enhance the banks' resilience.

# SWITZERLAND

The banks in Switzerland are an important sector for the Swiss economy, one that accounts for approximately 6 percent of the country's total economic performance. However, structural change in the banking sector continued in the past year. A further decline in interest rate margins and the emerging digitalisation of the financial sector will drive structural realignment in the banking sector in the coming years. The high density of regulation and the ensuing compliance costs are leading foreign banks in particular to re-evaluate their business activities in Switzerland. Two measures taken by the Swiss National Bank in January 2015 to weaken the Swiss Franc had a remarkable influence on the banking business: the lifting of the minimum exchange rate CHF of 1.20 per Euro and the introduction of negative interest rates on sight deposit account balances that exceed a given exemption threshold.

## Capital and Liquidity Requirements

Regarding the ongoing refinements of Basel III, a National Working Group led by the Swiss Financial Market Supervisory Authority (FINMA) is currently preparing the Swiss implementation of the additional standards by the Basel Committee on Banking Supervision. For example, public consultations on revised requirements in the fields of credit risk as well as risk diversification are planned to take place in the course of 2016.

As far as the leverage ratio is concerned, the details of its calculation have entered into force at the beginning of 2015 (FINMA circular 2015/3), whereas the final calibration will be determined subject to the time-table of the Basel Committee on Banking Supervision. In February 2013, and with effect from end of September 2013, a counter-cyclical capital buffer for mortgage loans has been activated at the level of 1%. In January 2014, this buffer has been increased to 2%, with effect from end of June 2014. The buffer targets loans financing residential property located in Switzerland and refers to the associated risk-weighted positions.

On the liquidity side, the revised Liquidity Ordinance by the Federal Council and a new FINMA circular (FINMA circular 2015/2) have entered into force at the beginning of 2015. They address liquidity risk management as well as the requirements with regard to the Liquidity Coverage Ratio (LCR). The implementation of the Net Stable Funding Ratio (NSFR) is intended to come into force in 2018, in line with the Basel Committee's time-table.

With specific reference to systemically relevant banks, a regulatory package on "Too Big to Fail" has been put in place in 2012/2013. On the level of the Banking Law as well as a couple of Ordinances by the Federal Council, these additional requirements refer to capital, liquidity, risk diversification and contingency planning. Currently, the Swiss regulation on "Too Big to Fail" is being revised by the Federal Council, with a view, for example, to the new recommendations by the Financial Stability Board (FSB) on Total Loss-Absorbing Capacity (TLAC). A corresponding consultation has taken place until February 2016. The position of the Swiss Bankers Association (SBA) is available online at www.swissbanking.org.

**Fight Against Money Laundering**

Following the review of the 40 FATF recommendations, Switzerland has adapted its respective legislation. In order to comply with the revised FATF recommendations Switzerland has revised its Criminal Code (aggravated tax misdemeanour, in force as of January 2016), the Swiss Financial Market Supervisory Authority FINMA has revised its Anti Money Laundering Ordinance - FINMA, of June 3, 2015 (in force as of January 2016) and the Federal Act on Combating Money Laundering and Terrorist Financing in the Financial Sector (AMLA) has added a new definition of a politically exposed person (PEP). Additionally, the Swiss Bankers Association has revised its binding Agreement on the Swiss banks' code of conduct with regard to the exercise of due diligence (CDB) in order to address, in particular, the beneficial ownership of legal entities (controlling person) or the beneficial ownership of assets. Swiss banks are now obligated to identify the controlling persons of companies and vehicles. Other changes are made due to the heightened transparency requirements for legal persons, also stated in the reviewed FATF recommendations. In this context, new rules regarding the identification of beneficial owners as well as transparency rules for non-listed companies issuing bearer shares have been introduced. Further changes concern the identification of national politically exposed persons and the introduction of new rules with regard to real estate and cash transactions.

**Financial Market Legislation**

Switzerland is currently overhauling its financial market legislation. The government has launched a large-scale legislative project to this end that revises the existing legislation to varying

degrees. The aim is to update investor protection and, where required, align legislation with the European and international regulatory framework. The new financial services architecture will be based on six "floors", which include the existing Financial Market Supervision Act (FINMASA), the new Financial Services Act (FinSA) now considered in Parliament, the new Financial Market Infrastructure Act (FMIA) already in force, and the new Financial Institutions Act (FinIA). A number of fundamental decisions have already been made: the FMIA has already been adopted by Parliament and came into force at the beginning of 2016. FinIA foresees that independent wealth managers will come under the remit of a single supervisory body. FinSA will introduce standardized rules of conduct and distribution rules for all financial services providers, and set minimum requirements for the basic and advanced training of client advisors. FinSA and FinIA are currently under parliamentary consideration. If they get a final trim and no burdening by over-regulation they will contribute significantly to investor protection and the competitiveness of Switzerland as a financial center. Further important amendments will follow.

## Tax Issues

*Automatic exchange of information*

The automatic exchange of Information (AEOI) is becoming an international standard. The Swiss authorities have adopted the legal frameset to implement the AEOI so that data can be collected from 2017 and exchanged from 2018. Before exchanging information, fair and feasible solutions to regularise untaxed assets have to be found. The standard should be applied by all important financial centres in the world and should provide for transparency of all financial instruments, including structures like trusts. The AEOI should be based on reciprocity, the principle that exchanged data are exclusively used for tax purposes and appropriate data protection measures. The AEOI should create a level playing field, it is therefore not acceptable that exceptions are granted to single jurisdictions such as the US.

*Switzerland/US: Switching to FATCA Model 1*

FATCA is currently implemented by Swiss financial institutions under Model 2 Intergovernmental Agreement (IGA), which means among others that Swiss financial institutions disclose account details directly to the US tax authority. The Federal Council has approved a mandate for negotiating with the United States in order to switch to FATCA Model 1 IGA; negotiations are currently underway.

## PEP regulation

Until 31.12.2015 politically exposed persons (PEP) have been defined in the Anti Money Laundering Ordinance – FINMA. This definition has been transferred into the revised Federal Act on Combating Money Laundering and Terrorist Financing in the Financial Sector (AMLA), broadening the definition of a PEP by two new categories including domestic PEP as well as PEP of intergovernmental agencies and people in a close relationship of a PEP. The new regulation came into effect on January 1st, 2016.

### Corporate Governance

The Swiss Financial Market Supervisory Authority (FINMA) is currently consolidating its requirements for the banking sector in the fields of corporate governance, internal control systems and risk management. This consolidation is meant to result in a single FINMA circular called "Corporate Governance". More concretely, FINMA has submitted its draft of the new circular for consultation until April 13, 2016, together with amendments to the existing circulars on "Operational Risks" and "Remuneration Schemes". The corresponding position of the Swiss Bankers Association (SBA) is available online at www.swissbanking.org. The new circular on corporate governance is intended to reflect findings from the financial market crisis as well as revised international standards. Amongst other topics, it addresses the principles and required structures for supreme governing bodies and executive boards of banks.

## TURKEY

### Basel Harmonization Efforts

Within the frame of the said Regulatory Consistency Assessment Programme (RCAP) being conducted by Basel Committee on Banking Supervision (BCBS) since 2012, the compliance of our national laws and regulations with Basel III Accord is also reviewed, and a detailed project is carried out for amending the relevant laws and regulations as required.

The RCAP process, initiated in the last quarter of 2015, has been completed by an assessment report published about our country. As a result of a review conducted by a team comprised of representatives of BCBS member states, our national banking legislation is found to be fully compliant with the international Basel standards.

In this context, all of the laws and regulations pertaining thereto have been reviewed in 2015. The new regulations drafted accordingly have been published in the Official Gazette edition 29511 on 23/10/2015 with effect from 31/03/2016. Said regulations have been shared with RCAP Assessment Team created and appointed by BCBS for completion of the preliminary assessment process. The regulations published in the Official Gazette edition 29511 on 23/10/2015 in the course of RCAP preparations process are as listed below:

- Regulation Revising the Regulation on Shareholders' Equity of Banks
- Regulation Revising the Regulation on Internal Systems and Internal Capital Adequacy Assessment Process of Banks
- Regulation Revising the Regulation on Financial Holding Companies
- Regulation Revising the Regulation on Principles and Procedures Regarding Accounting Practices and Keeping of Documents of Banks
- Regulation Revising the Regulation on Principles and Procedures Regarding Preparation and Publishing of Yearly Activity Report by Banks
- Regulation on Measurement and Assessment of Capital Adequacy of Banks
- Regulation Revising the Regulation on Principles and Procedures Regarding Audits Conducted by Banking Regulation and Supervision Agency

- Communiqué Revising the Communiqué on Financial Statements and Their Explanations and Footnotes to be Publicized by Banks
- Communiqué Revising the Communiqué on Calculation of Capital Requirements For Market Risk Arising Out of Options According to Standard Method
- Communiqué on Public Statements of Banks Regarding Risk Management
- Communiqué on Calculation of Risk Weighted Amounts Regarding Securitization
- Communiqué on Calculation of Amount Subject to Credit Risk by Internal Ratings Based Approaches (as drafted with participation of member states of the Committee)
- Communiqué on Calculation of Market Risk by Risk Measurement Models and on Assessment of Risk Measurement Models
- Communiqué Revising the Communiqué on Preparation of Consolidated Financial Statements of Banks
- Communiqué Revising the Communiqué on Credit Risk Mitigation Techniques
- Communiqué Revising the Communiqué on Calculation of Amount Subject to Operational Risk by Advanced Measurement Approach

Furthermore, for the sake of making sure that our country rating is at the best level as far as possible, it has become necessary to make some additional amendments in some issues detected in the course of RCAP process, and accordingly, a second set of revised regulations has been prepared by considering the points agreed upon with RCAP Team, and this set of regulations has been published in the Official Gazette edition 29599 on 20/01/2016 with effect from 31/03/2016.

Regulations published as a part of the second set of revised regulations are as listed below:

- Regulating Revising the Regulation on Calculation of Liquidity Coverage Ratio by Banks
- Regulating Revising the Regulation on Measurement and Assessment of Capital Adequacy of Banks
- Regulation Revising the Regulation on Internal Systems and Internal Capital Adequacy Assessment Process of Banks
- Regulation Revising the Regulation on Shareholders' Equity of Banks
- Regulation Revising the Regulation on Principles Regarding Authorization and Activities of Rating Agencies
- Communiqué Revising the Communiqué on Credit Risk Mitigation Techniques
- Communiqué Revising the Communiqué on Public Statements of Banks Regarding Risk Management
- Communiqué Revising the Communiqué on Financial Statements and Their Explanations and Footnotes to be Publicized by Banks
- Communiqué Revising the Communiqué on Calculation of Amount Subject to Credit Risk by Internal Ratings Based Approaches
- Communiqué Revising the Communiqué on Calculation of Market Risk by Risk Measurement Models and on Assessment of Risk Measurement Models

What's more, as a part of the initiatives carried out for the sake of full compliance with Basel III Accord, amendments have been made in the Regulation on Internal Systems and Internal Capital Adequacy Assessment Process of Banks and in Guidelines on ISEDES Report and some other codes of good practices taken as a reference in issuance of ISEDES Reports. In 2015, 4 new

Codes of Good Practices have been published and put into force by a Decision of the Board. There are 14 Codes of Good Practices currently in force.

Said codes and guidelines put forth not only the principles guiding the banks in effective management of risks, but also the criteria that may be used in onsite audits for assessments as to whether banks are effectively and efficiently managed or not.

**Other Banking Legislative Instruments**

*Regulation Revising the Regulation on Principles of Foundation and Operations of Financial Leasing, Factoring and Financing Companies (Official Gazette edition 29398 dated 26/06/2015):*

This amendment makes sure that general reserves and provisions are also taken into consideration in calculation of shareholders' equity of financing companies in order to eliminate the legislation-based differences preventing free market competition, with a view to resolving the problem of unfair competition between banks and financing companies and contributing to development of different crediting channels.

*Regulation Revising the Regulation on Accounting Practices and Financial Statements of Financial Leasing, Factoring and Financing Companies (Official Gazette edition 29398 dated 26/06/2015):*

This amendment eliminates the unfair competition between banks and financing companies, by bringing the ratios regarding the general reserves and provisions obligations of financing companies to the same level with those of banks.

*Regulation Revising the Regulation on Calculation of Liquidity Coverage Ratio of Banks (Official Gazette edition 29451 dated 20/08/2015):*

Upon demand of banks with regard to implementation of the Regulation on Calculation of Liquidity Coverage Ratio of Banks and of the frequently asked questions document prepared, adopted and published by BCBS with a view to clarifying the points of hesitation regarding implementation of "Basel III: The Liquidity Coverage Ratio and Liquidity Risk Monitoring Tools" document again adopted and published by BCBS, the schedules attached to the said Regulation have been revised and amended.

*Regulation Revising the Regulation on Financial Holding Companies (Official Gazette edition 29511 dated 23/10/2015):*

This Regulation aims to ensure that the principles applied by banks in shareholders' equity, capital adequacy, leverage ratio and liquidity adequacy calculations of financial holding companies are taken into account, as a result of review of the Agency's regulations before 2015 assessment of our country as a part of RCAP process.

*Regulation Revising the Regulation on Shareholders' Equity of Banks (Official Gazette edition 29511 dated 23/10/2015):*

Before 2015 assessment of our country as a part of RCAP process, the Agency's regulations have been revised, and accordingly, the Regulation has been revised and amended for the sake of full compliance with Basel standards.

*Regulation Revising the Regulation on Principles and Procedures Regarding Accounting Practices and Keeping of Documents of Banks (Official Gazette edition 29511 dated 23/10/2015):*

As a result of review of our Agency's regulations before 2015 assessment of our country as a part of RCAP process, the Regulation has been revised and amended so as to include the risk management statements in financial reports of banks.

*Regulation Revising the Regulation on Principles and Procedures Regarding Preparation and Publishing of Yearly Activity Reports by Banks (Official Gazette edition 29511 dated 23/10/2015):*

As a result of review of our Agency's regulations before 2015 assessment of our country as a part of RCAP process, the Regulation has been revised and amended so as to include the risk management statements in yearly and interim activity reports of banks.

*Regulation on Measurement and Assessment of Capital Adequacy of Banks (Official Gazette edition 29511 dated 23/10/2015):*

Definitions given in third article of the Regulation have been updated for compliance with Basel standards. Parallel to Basel standards, credit conversion ratios of non-cash credits and commitments have been rearranged over the features of products, not in product details, and the Banking Regulation and Supervision Board has been authorized to issue a more detailed regulation in connection therewith. The Regulation has greatly maintained its provisions as to calculation of operational risk, but has made amendments and changes in gross income definition covered by standard approach and in its provisions pertaining to management of operational risk. How the capital requirements taken as zero for risks arising out of central counterparties will be calculated has been regulated in exhibit 4 of the Regulation by taking into consideration the relevant provisions of Basel III as a requirement of compliance with RCAP. Section of the Regulation pertaining to calculation of Amount Subject to Market Risk has been rearranged within the frame of Basel standards by also aiming to ensure its comparability as a part of RCAP process, and this section has been revised and amended as needed for the sake of conformity with standards.

*Regulation Revising the Regulation on Internal Systems and Internal Capital Adequacy Assessment Process of Banks (Official Gazette edition 29511 dated 23/10/2015):*

As per the revised text, third paragraph of article 5 of the Regulation provides that the board of directors is under obligation to ensure that ISEDES is established and implemented, and that an adequate capital is held for the risk exposures.

*Regulation Revising the Regulation on Principles and Procedures Regarding Audits Conducted by Banking Regulation and Supervision Agency (Official Gazette edition 29511 dated 23/10/2015):*

This Regulation makes amendments and changes in the onsite audit and supervision activities included in the Agency's audit system.

*Regulation Revising the Regulation on Bank Cards and Credit Cards (Official Gazette edition 29543 dated 25/11/2015):*

As per the revised text, seventh paragraph of article 26 of the Regulation pertaining to payment of credit card debts in installments has made it possible to pay the expenditures for white goods and furniture and for education and training fees in installments of twelve months, and the same provision has been adopted also for the corporate credit cards referred to in eighth paragraph of the same article.

*Regulation Revising the Regulation on Crediting Operations of Banks (Official Gazette edition 29543 dated 25/11/2015):*

As per the revised text, the credits to be made available for house renovation works, and credits to be made available for financing of education and training fees have been kept outside the scope of maturity limitation set forth in third paragraph of article 12/A of the Regulation.

*Regulation Revising the Regulation on Principles of Foundation and Operations of Financial Leasing, Factoring and Financing Companies (Official Gazette edition 29543 dated 25/11/2015):*

As per the revised text, the credits to be made available for house renovation works, and credits to be made available for financing of education and training fees have been kept outside the scope of maturity limitation set forth in second paragraph of article 11/A of the Regulation.

*Regulation on Principles Regarding Repo and Reverse Repo Transactions of Banks (Official Gazette edition 29554 dated 06/12/2015):*

This Regulation is issued on the basis of the draft text prepared by the Capital Markets Board for intermediary institutions with a view to closing the gap in regulations pertaining to repo and reverse repo transactions of banks.

*Regulation Revising the Regulation on Payment Services and Electronic Money Issue and Payment Institutions and Electronic Money Institutions (Official Gazette edition 29574 dated 26/12/2015):*

With a view to contributing to the modus operandi of the process relating to payment services, and preventing the probable difficulties in practice, the required revisions and amendments have been made in the articles of the Regulation pertaining to operating license, board of directors, shareholders’ equity, privileges for low-value payment means and electronic money, frame agreement, one-time payment transaction, invoice definition and payment services.

**Market Developments**

The number of banks operating in the banking sector was 53 as of June 2016. 34 of them were deposit banks, and 13 were development and investment banks. Of the deposit banks, 3 were state-owned banks, and 9 are private banks. In addition, there were 6 participation banks.

Due to change of shareholders, T. Garanti Bankası A.Ş. and Tekstil Bank A.Ş.–the latter being renamed as ICBC Turkey Bank A.Ş. in November 2015 –shifted from private bank status to foreign bank status.

Ziraat Participation Bank A.Ş. and Vakif Participation Bank A.Ş. commenced operations. The number of foreign banks, where residents abroad hold 51 percent or a higher share in capital, was 21.

In the stated period the number of bank branches was around 12.300. Population per branch was around 6,500 and population per bank employee was around 360. The number of bank employees increased to 220 thousand.

## UNITED KINGDOM

### Key Regulatory and Market Developments

#### *Bank of England Act*

The Bank of England and Financial Services Act received Royal Assent in May 2016. It strengthened the governance and accountability of the Bank of England, by ending the subsidiary status of the Prudential Regulation Authority and allowing the National Audit Office to undertake value for money reviews of the Bank for the first time. The Act also updated resolution planning and crisis management arrangements between the Bank and Treasury and provided statutory underpinning for the Senior Managers and Certification regime being extended to all authorised persons.

#### *Stress Testing*

The PRA and its predecessor had largely implemented the requirements of Basel III but in December 2015 confirmed the expectation, as result of the 2015 stress testing exercise, that the 7 largest banks in the UK should hold a minimum of 7% CET1 capital at a consolidated level. In addition, it finalised the leverage ratio regime which:

- requires all PRA-regulated banks and building societies with retail deposits equal to or greater than £50 billion, to meet a 3% minimum leverage ratio requirement;
- applies a counter cyclical leverage ratio buffer to UK G-SIIs and major UK banks calibrated at 35% of a relevant firm's countercyclical capital buffer (CCB) rate; and
- expects UK G-SIIs to voluntarily hold a counter cyclical leverage ratio buffer calibrated at 35% of a G-SII's combined systemic risk buffers.

#### *Resolution*

The PRA is working to promote the effectiveness of resolution by mandating banks to include contractual terms in certain of their contracts binding the counterparty to respect specific resolution actions taken by the UK authorities. Article 55 of the Bank Recovery & Resolution Directive (BRRD) requires banks to include contractual terms recognising the possibility of UK

bail-in in a wide range of liabilities entered into under non-EEA law. The PRA's rules on contractual stays require banks to include contractual recognition provisions in any non-EEA contracts which give the counterparty termination rights to close out in the event of the bank's failure. The contractual stay provision requires the counterparty to abide by any temporary stay on close-out (subject to the bank under resolution continuing to perform the requirements of the contract) imposed by the Bank to facilitate resolution. The Article 55 rules apply from 1 January 2016 (although there has been a partial PRA & FCA waiver in place due to the administrative burden of implementing the requirement which expires on 31 July 2016) and the contractual stay rules are being implemented in two phases: phase 1 from 1 June 2016 applies to contracts with credit institutions and investment firms and phase 2 applies to all other relevant contracts from 1 January 2017.

The Bank of England has consulted on the UK approach to implementing Total Loss Absorbing Capacity and the conceptually similar BRRD requirement for banks to maintain a Minimum Requirement of Eligible Liabilities (MREL). The proposed approach will require UK GSIBs and the subsidiaries of non-UK GSIBs to maintain an MREL requirement aligned with TLAC. Other firms are likely to be subject to MREL requirements tailored to support the implementation of their resolution strategies. The smallest institutions, unlikely to be subject to resolution action, will have MREL set at the level of their going-concern capital requirements. A policy statement can be expected before the end of 2016.

***Ring Fencing***

Rather than going down the US 'Volcker Rule" route, the UK has decided that banks with retail and SME deposits in excess of £25bn should 'ring-fence' their retail and SME operations from investment banking activity. This follows the recommendations of the Independent Commission on Banking chaired by Sir John Vickers being enacted under the Financial Services (Banking Reform) Act 2013. If 2014 saw work on the definition of the 'location' of the ring-fence through the drafting of the secondary legislation, 2015/16 has seen work on the 'height' of the ring-fence through the development of the regulatory framework. With this due to be completed this year, and preparations on the part of the banks involved progressing, we should be left with a good lead time to ensure a smooth transition to the new regime by the time of the 1 January 19 start date.

***MiFIR & EMIR***

In May 2016, ESMA issued two final draft regulatory technical standards (RTS) on indirect clearing under the Markets in Financial Instruments Regulation (MiFIR) and EMIR respectively. EMIR introduced a clearing obligation for certain OTC derivative contracts and MiFIR extended the scope of the clearing obligation to all derivative transactions concluded on a regulated market which means that the vast majority of derivative transactions will be cleared. The European Commission now has a three month period to accept or reject them. This follows activity in April, which saw the ESMA publish a report on the review of Article 26 of Delegated Regulation 153/2013 which contains regulatory technical standards (RTS) supplementing EMIR with regard to central counterparties' (CCPs) client accounts.

### *Individual Accountability*

During 2015 the senior managers' and certification regime was finalised and implemented in March 2016. It requires the allocation of responsibilities for key areas of the bank to senior managers who will take personal responsibility for failure in areas of the bank for which they are accountable. Individuals must sign statements of responsibility and the banks provide a responsibilities map, to ensure no key areas are overlooked. Senior managers will be subject to prior approval by the PRA and FCA.

At the next level down the Certification Regime will apply to all employees who perform a role relating to a bank's regulated activities but who are not in a senior manager function and have, for instance the ability to take material risks on behalf of their bank or clients or affect the risk profile of their bank. Such individuals must be annually certified as 'fit and proper by the bank.

The Rules of Conduct are the final level of requirements that will apply to virtually all individuals within the bank from March 2017, although senior managers and certified persons are already subject to them.

### *Limitations on Incentive Compensation Arrangements*

The UK's remuneration code, which closely follows EU requirements and applied to senior managers and material risk takers requires:

- deferral of at least 40% of a bonus over a period of at least three years for all staff covered by the code. At least 60% must be deferred for the most senior management or when an individual's bonus is more than £500,000;
- payment of at least 50% of any bonus in shares, share-linked instruments or other equivalent non-cash instruments of the bank. They should be subject to an appropriate retention period; and
- banks not to offer guaranteed bonuses of more than one year. Guarantees may only be given in exceptional circumstances to new hires for the first year of service.

The senior managers' regime introduced additional requirements requiring senior mangers' bonuses to be deferred for seven years with no vesting earlier than year three and no faster than on a pro rata basis and a five year deferral for all other material risk takers, with vesting permitted from year one and no faster than on a pro rata basis.

## Other Regulatory Developments

### *Anti-money Laundering Developments*

The UK Government's consultation on the Anti-Money Laundering (AML) Action plan, which closed on the 2 June, provides a welcome opportunity to help reshape the AML landscape to become a more strategic, intelligence led approach which supports the financial sector to manage and mitigate risks and threats. Overall, there is much to welcome in the general content of the consultation, not least the commitment for more powers on intelligence sharing and fundamental reform of the Suspicious Activity Regime (SARs) and the intention to place the Joint Money

Laundering Intelligence Taskforce (JMLIT) onto a permanent footing. If these are delivered successfully, it will allow a rebalancing of approach from a mainly reactive process of submitting over 300k SARs, mostly unused, to a more strategic approach based on intelligence sharing and collaboration between public and private sector.

Alongside this, there is a clear and growing need for a more holistic approach to all types of financial crime and compliance. Current and future requirements on fraud, bribery and corruption AML and tax evasion, have, and will require, different compliance and reporting systems. The landscape is further complicated through initiatives such as the Payment Accounts Directive (PAD), which could prevent banks closing accounts based on suspicion; and the General Data Protection Regulation (GDPR), which could fetter information sharing.

***UK Countercyclical Capital Buffer***

In December 2015, the Financial Policy Committee (FPC) signalled its intention to set the UK countercyclical capital buffer (CCyB) rate in the region of 1%.

The CCyB ensures the banking system is resilient to stress without restricting essential services, such as the supply of credit to the real economy. It can be varied, up or down by the FPC in line with its expectation that the banking system will incur losses.

The FPC intends to set the level of the CCyB above zero before the level of risk becomes elevated but vary it gradually.

It will be based on annual stress testing and a range of indicators, including:

- measures of borrower balance sheet stretch;
- measures of gaps between asset and property prices and their equilibrium levels;
- growth rate of credit and indicators of its availability; and
- measures of macro-economic risk, such as economic imbalances.

In March the Committee, taking into account market conditions, decided to increase the UK countercyclical capital buffer rate from 0% to 0.5% of risk weighted assets.

This new setting will become binding with effect from 29 March 2017, at which time the overlapping aspects of Pillar 2 supervisory capital buffers will be lifted, to ensure capital neutrality.

This decision was reversed in July 2016 as part of the Bank of England's response to the UK referendum on membership of the European Union. The buffer rate was returned to 0% with immediate effect. The Bank estimated this reduced aggregate UK capital requirements by £5.7bn and raised lending capacity by approximately £150bn.

***FPC Liquidity Study***

The FPC is investigating market liquidity and in particular the impact of automated trading, including high-frequency trading, and increase in passive trading strategies on financial

markets. It is also examining investment funds' stress-testing practices, the information provided to investors about possible use of tools to manage stressed redemptions, and the effects this may have on investors' incentives and behaviour.

***Credit Conditions and the Buy-to-let Market***

The Board of the PRA issued a Supervisory Statement to clarify its expectations for underwriting standards in the buy-to-let market. The FPC will continue to monitor developments, including the impacts of this initiative and forthcoming tax changes, and to assess the implications for financial stability of the buy-to-let mortgage market. HM Treasury has consulted on giving powers of direction to the FPC on buy-to-let mortgage lending, and will respond to that consultation, including with final secondary legislation, in due course. The FPC will prepare a statement of its policy for the use of powers of direction ahead of any such powers being approved by Parliament.

***Retail Banking Market Investigation***

The Competition and Markets Authority (CMA) has extended the timetable for its investigation into the retail banking market to August 12, 2016 and published for consultation revised proposals to remedy the adverse effects on competition identified in its provisional report. The CMA's report was originally scheduled for publication in February 2016.

***Bank Loss Relief Restriction***

The UK is consulting on a change of scope to the bank levy, to restrict the scope to UK assets only. This is primarily likely to affect UK headquartered banks, but the policy change is offset by a bank tax surcharge of 8% which applies to the majority of banks (introduced in 2015). Further restrictions on the use of losses will reduce the amount of a banking company's annual taxable profit that can be offset by pre-April 2015 carried-forward losses from 50% to 25%. The measure will take effect from 1 April 2016, and results in an acceleration of tax payments into the period prior to 2020.

***Fair and Effective Markets Review***

The Bank of England's Fair and Effective Market Review final report was published 10 June 2015, setting out 21 recommendations to:

- raise standards, professionalism and accountability of individuals;
- improve the quality, clarity and market-wide understanding of FICC trading practices;
- strengthen regulation of FICC markets in the United Kingdom;
- launch international action to raise standards in global FICC markets;
- promote fairer FICC market structures while also enhancing effectiveness; and
- promote forward-looking conduct risk identification and mitigation.

The Review called on senior leadership of FICC market participants to create a new FICC Markets Standards Board (FMSB) with participation from a broad cross-section of global and domestic firms and end-users at the most senior level. The FICC Markets Standards Board

(FMSB) has now been established, and its purpose is to define and sustain good practice standards for wholesale FICC markets and raise standards of behaviour, competence and awareness across those markets and among participants, thereby contributing to the fairness and effectiveness of these markets.

## UNITED STATES

On July 1, 2016, nearly six years after enactment, new rules went into effect under the Dodd-Frank Act requiring large foreign banking organizations with nonbranch U.S. assets of $50 billion or more to house their U.S. subsidiaries under a single intermediate holding company (IHC), subject to the same risk-based capital, leverage standards, capital planning and stress-testing requirements applicable to large U.S. bank holding companies. As more than a dozen FBOs were in the process of setting up their IHCs, the Federal Reserve Board on October 30, 2015 proposed "Total Loss-Absorbing Capacity" (TLAC) rules that would apply to both U.S. Global Systemically Important Banking Organizations and the U.S. IHCs of foreign G-SIBs. In the derivatives area, the Commodity Futures Trading Commission on August 4, 2016 issued its sixth extension of the deadline for compliance with its November 2013 cross-border staff advisory. In other significant developments, New York State's Department of Financial Services issued a final rule on June 30, 2016 that requires DFS-regulated institutions to maintain programs to monitor and filter transactions for potential anti-money laundering and Bank Secrecy Act violations and prevent transactions with sanctioned entities, and on September 13th the Department issued proposed cybersecurity regulations.

Following is a review of key developments that are of particular importance to foreign banking organizations operating in the United States.

### Dodd-Frank Act

- **Enhanced Prudential Standards.** As of the July 1st compliance date, about a dozen FBOs restructured their non-branch U.S. subsidiaries under a single U.S. intermediate holding company. This controversial requirement, implemented by the Federal Reserve Board under Section 165 of the Dodd-Frank Act, subjects broker-dealer subsidiaries of these FBOs to an extra layer of bank capital and liquidity requirements at the IHC level, on top of SEC capital requirements, and home-country capital and liquidity requirements. In addition, while IHCs can only rely on their U.S. resources to meet the Federal Reserve's capital, liquidity and stress-testing requirements, U.S. bank holding companies subject to the same requirements can take into account their global consolidated operations.

  **TLAC.** The Federal Reserve Board on October 30, 2015 issued for comment a proposed rule establishing Total Loss-Absorbing Capacity (TLAC) and Buffers, Long-term Debt, and Clean Holding Company Requirements for U.S. G-SIBs and U.S. IHCs of foreign G-SIBs. In general, the Fed's proposal is more restrictive in significant aspects - for example, the calibration of required TLAC, the imposition of "clean" holding company requirements, and separate long-term debt (LTD) and TLAC buffer requirements - compared to the Financial Stability Board's global standard.

The "internal TLAC" regime applied to IHCs is similar in structure to the "external TLAC" regime applicable to U.S. G-SIBs (including the imposition of LTD, TLAC buffer and "clean" holding company requirements), with certain adjustments made to tailor the requirements to the specific circumstances of IHCs. Among other things, the IHC rules prescribe a specific process for determining which IHCs are within scope (rather than simply relying on G-SIB designations by the FSB) and would require qualifying LTD to include debt conversion clauses that would enable the Fed, and not the appropriate home country authority, to control the immediate cancellation of LTD or its immediate conversion/exchange to common equity tier 1 capital. In addition, the IHC regime imposes higher TLAC requirements on IHCs of foreign banks that are expected to be subject to a "multiple point of entry" resolution as compared to those of foreign banks that are expected to be subject to a "single point of entry" resolution. The TLAC requirements would be effective January 1, 2019, with a three-year phase-in period for the risk-weighted assets components of both external and internal TLAC.

Federal Reserve Board Governor Daniel Tarullo said in a November 5th speech that the Fed's proposed TLAC requirement for FBO intermediate holding companies "should enhance the prospects for an orderly firmwide global resolution of an FBO by its home country resolution authority through increasing confidence that the U.S. operations of the FBO will obtain their appropriate share of the loss absorbency capacity of the consolidated foreign bank." He was speaking at a conference sponsored by the Chicago Fed on "The Future of Large and Internationally Active Banks".

The IIB on February 19th submitted a comment letter on the Fed's TLAC proposal that expressed fundamental concerns about how the Fed proposes to implement the FSB standards in the U.S. with respect to covered U.S. IHCs. "In our view, the Proposed Rules would impose excessive costs on Covered IHCs, unduly constrain Covered IHCs' ability to participate in U.S. credit and financial markets, lead to competitive disparities and unfair treatment in international banking without commensurate benefits to resolvability or U.S. financial stability, limit, rather than promote, home-host coordination in a cross border resolution of an FBO and potentially make FBOs less resilient," the IIB letter stated. Instead, the IIB recommended that the Federal Reserve Board more closely align its TLAC rules with those of the FSB by re-calibrating the amount of internal TLAC required of Covered IHCs to facilitate cross-border coordination with home country supervisors and to reflect properly the risk, if any, the Covered IHCs pose to the financial stability of the U.S. In a supplemental comment letter on July 1st, the IIB focused on key aspects of the proposed internal LTD requirement for IHCs that raised serious concerns regarding the characterization of internal LTD as equity and not as debt for federal income tax purposes. The letter explained the severely adverse impact such a characterization would have on FBOs that are subject to the internal LTD requirement and suggested amendments to the rule to address these concerns. The IIB also addressed the U.S. tax treatment of internal LTD in its comments on the IRS's proposed Section 385 regulations (discussed below).

**Single Counterparty Credit Limits.** The Federal Reserve Board on March 4th re-proposed single counterparty credit limits for large U.S. bank holding companies and

foreign banking organizations. A global systemically important bank, or G-SIB, would be restricted to a credit exposure of no more than 15 percent of the bank's tier 1 capital to another systemically important financial firm, and up to 25 percent of the bank's tier 1 capital to another counterparty; a bank holding company with $250 billion or more in total consolidated assets, or $10 billion or more in on-balance-sheet foreign exposure, would be restricted to a credit exposure of no more than 25 percent of the bank's tier 1 capital to a counterparty; a bank holding company with $50 billion or more in total consolidated assets would be restricted to a credit exposure of no more than 25 percent of the bank's total regulatory capital to another counterparty; and bank holding companies with less than $50 billion in total consolidated assets, including community banks, would not be subject to the proposal. Similarly tailored requirements would also be established for foreign banks operating in the United States. The proposed rule implements part of the Dodd-Frank Act and builds on earlier proposals released by the Board in 2011 and 2012, and includes some modifications based on comments received. Additionally, the proposal seeks to promote global consistency by generally following the international large exposures framework released by the Basel Committee on Banking Supervision in 2014, the Fed said. The Fed also released a white paper explaining the analytical and quantitative reasoning for the proposed rule's tighter 15 percent limit for credit exposures between systemically important financial institutions.

The IIB on June 3rd submitted a comment letter on the reproposed SCCL, setting forth a number of fundamental concerns about the ways in which the Fed's proposal would adapt Section 165(e) to the U.S. operations of FBOs. "Generally, the Proposal is inconsistent with the statutory language of Section 165(e), fails to comply with the statutory mandates to take into account comparable home country standards and the principles of national treatment and competitive equality, and does not tailor the requirements of Section 165(e) in a manner commensurate with an FBO's U.S. footprint," the IIB said. Specifically, the IIB stated concerns regarding the way in which the proposal would apply an SCCL as a U.S.-specific requirement to all FBOs with $50 billion or more in global assets, regardless of the size of their U.S. operations or systemic footprint, and its application of various and sometimes inconsistent lending limits to sub-consolidated levels of an FBO's operations, compounding operational, compliance and resource challenges and complications for FBOs - challenges and complications which would not be experienced by U.S. BHCs.

The IIB letter set forth a recommended approach to the application of an SCCL to FBOs under which the SCCL would apply only to an FBO's U.S. IHC, based on IHC capital, in the same manner as the SCCL applies to a U.S. BHC. In addition, the IIB letter said the Fed Board should have flexibility in the final rule to further tailor the applicability of the SCCL to individual IHCs depending on individual circumstances, and to create exceptions where necessary. Similar to the manner in which the Board has recognized home country standards of capital and stress testing and the manner in which the Board has tailored its application of enhanced prudential standards to FBOs already subject to such a regime, an FBO with total consolidated assets of $50 billion or more would be required to confirm to the Board that it meets, on a consolidated basis, the large exposure limits established by its home country supervisor that are consistent with the Basel Committee's final standards setting out a supervisory framework for consolidated large exposure limits, as amended

from time to time. Existing U.S. lending limits would continue to apply to U.S. IDIs and U.S. branches and agencies.

**Net Stable Funding Ratio.** The federal banking agencies on May 3rd proposed a rule to strengthen the resilience of large banking organizations by requiring them to maintain a minimum level of stable funding relative to the liquidity of their assets, derivatives, and commitments, over a one-year period. The rule, the net stable funding ratio, or NSFR, is being proposed by the Federal Deposit Insurance Corporation, the Federal Reserve, and the Office of the Comptroller of the Currency. The proposal is designed to reduce the likelihood that disruptions to a banking organization's sources of funding will compromise its liquidity position. The proposal would require institutions subject to the rule to maintain sufficient levels of stable funding, thereby reducing liquidity risk in the banking system. By requiring firms to have more stable funding profiles, the proposal would also enhance financial stability.

The NSFR proposal would complement the liquidity coverage ratio (LCR) rule, which requires large banking organizations to hold a minimum amount of high-quality liquid assets that can be easily and quickly converted into cash to meet net cash outflows over a 30-day stress period.

The proposed rule would be tailored to the risk of the banking organizations. The most stringent requirements would apply to the largest firms--those with $250 billion or more in total consolidated assets or $10 billion or more in on-balance sheet foreign exposure, as well as those banking organizations' subsidiary depository institutions that have assets of $10 billion or more.

Holding companies with less than $250 billion, but more than $50 billion in total consolidated assets, and less than $10 billion in on-balance sheet foreign exposure would be subject to a less stringent, modified NSFR requirement. The rule would not apply to holding companies with less than $50 billion in total consolidated assets and would not apply to community banks. Holding companies subject to the proposal would be required to publicly disclose information about their NSFR levels each quarter. The NSFR would become effective on January 1, 2018.

The IIB on August 5th submitted a comment letter on the proposed rulemaking, focused specifically on two aspects of the proposal that are uniquely relevant to foreign banking organizations: the potential over-inclusive impact of the $10 billion foreign exposure threshold as applied to covered IHCs; and the impact assessment's understated costs to IHCs. With respect to the former, the IIB letter recommends that the methodology be revised to exclude a covered IHC's exposures to its parent FBO, its other non-U.S. affiliates and the FBO's U.S. branches and agencies from calculation of the $10 billion threshold. Exposures of an IHC to its parent FBO's home country sovereign (including its agencies, instrumentalities and political subdivisions) also should be excluded, the IIB argued. With respect to the latter, the IIB said the assessment of the potential impact of the proposal understates the potential costs to all covered companies, and covered IHCs in particular.

- **Volcker Rule.** The Federal Reserve Board on July 7th announced that it will extend until July 21, 2017 the conformance period for banking entities to divest ownership in certain legacy investment funds and terminate relationships with funds that are prohibited under the rule. The Fed announced in December 2014 that it would make this extension to provide for orderly divestitures and to prevent market disruptions. This is the final of the three one-year extensions that the Fed is authorized to grant under the Volcker Rule (section 619 of the Dodd-Frank Act). The extension gives banking entities additional time to divest or conform only "legacy covered fund" investments, such as prohibited investments in hedge funds and private equity funds that were made prior to December 31, 2013. The extension does not apply to investments in and relationships with a covered fund made after December 31, 2013 or to proprietary trading activities; banking entities were required to conform those activities to the final rule by July 21, 2015. Additionally, the Fed is permitted under section 619 to provide up to an additional five years to conform investments in certain illiquid funds, where the banking entity had a contractual commitment to invest in the fund as of May 1, 2010.

- **Living Wills.** The Federal Reserve Board and FDIC on June 10th announced they are permitting 84 foreign banking organizations with limited U.S. operations to file "reduced content" resolution plans for their next three resolution plans. The decision is intended to increase clarity and reduce burden by creating more certainty around future filing requirements, the agencies said. All of the 84 firms have less than $50 billion in total U.S. assets. The agencies said the reduced content plans should focus on changes the firms have made to their prior resolution plans, actions taken to improve the effectiveness of, or that may alter, those plans, and, where applicable, actions to ensure any subsidiary insured depository institution is adequately protected from the risks arising from the activities of nonbank subsidiaries of the firm. The first of these reduced content plans must be submitted to the agencies by December 31, 2016. To file reduced content plans for the next three years, the firms must maintain less than $50 billion in U.S. assets and not experience any material events, the agencies said. The agencies also gave four large FBOs an extra year to submit their next resolution plans, which are now due on July 1, 2017. The extension was granted in view of the significant restructuring these companies were undertaking to come into compliance with the IHC requirement.

  On August 2nd the agencies further announced they were extending by one year, until December 31, 2017 the deadline for 38 firms to submit their next resolution plans. These firms include 36 domestic bank holding companies and foreign banking organizations, as well as two nonbank financial companies designated by the Financial Stability Oversight Council (click here for a list of the 38 firms). The agencies said they expect to provide feedback and guidance based on the firms' December 2015 plans for use in their December 2017 submissions.

- **OTC Derivatives.** The Commodity Futures Trading Commission on August 4th further extended the deadline for compliance with its November 14, 2013 cross-border staff advisory 13-69 (i.e., swaps arranged, negotiated, or executed in the United States). Commission Chairman Timothy Massad said he intends this fall to ask the Commission to consider a rule to address the "arrange, negotiate, or execute" issues raised by the 13-69 staff advisory.

The Securities and Exchange Commission on February 10th approved cross-border security-based swap rules that incorporate a U.S. activity test into the application of the *de minimis* exception to its security-based swap dealer registration requirements. The rules require a non-U.S. company that uses its personnel who are located in a U.S. branch or office, or personnel of its agent who are located in a U.S. branch or office, to arrange, negotiate, or execute a security-based swap transaction in connection with its dealing activity with other non-U.S. persons to include that transaction in determining whether it is required to register as a security-based swap dealer.

**Margin Requirements for Uncleared Swaps.** The FDIC and OCC on October 22, 2015 approved an inter-agency final rule on margin requirements for uncleared swaps. The Fed followed suit on October 30th and the CFTC did so on December 16th. The rule approved by the prudential regulators includes special rules for a covered swap entity's swaps with its affiliates pursuant to which the covered swap entity is required to collect initial margin from its affiliates but is not required to post initial margin to the affiliate. Instead, the covered swap entity is required to calculate the amount of initial margin that would be required to be posted to an affiliate that is a "financial end user with a material swaps exposure" and provide documentation of such amount to the affiliate on a daily basis. The rule does not apply to swaps of financial institutions with $10 billion or less in total assets that enter into swaps for hedging purposes. This exception tracks similar exceptions that are available to these small institutions from the requirement to clear standardized swaps through a clearinghouse. In addition, the rule does not apply to swaps entered into by commercial end users for purposes of hedging commercial risk. CFTC Chairman Massad said the Commission's rule was "practically identical" to the rules approved by the prudential regulators and "substantially similar" to international rules. The rule requires initial margin on certain inter-affiliate swaps to prevent evasion, but otherwise generally exempts inter-affiliate swaps from initial margin. The rule requires the exchange of variation margin between affiliates. Initial margin requirements are phased-in starting September 1, 2016 and ending September 1, 2020 from the largest participants to smaller ones. Variation margin requirements are effective September 1, 2016 for the largest participants and March 1, 2017 for the rest.

The CFTC on May 24th adopted a final rule implementing a cross-border approach to the CFTC's margin requirements for uncleared swaps applicable to CFTC-registered swap dealers and major swap participants for which there is no prudential regulator. The CFTC's final rule is closely aligned with the cross-border margin requirements included in the final inter-agency rule adopted by the prudential regulators. The rule generally requires covered swap entities to comply with the CFTC's margin requirements for all uncleared swaps in cross-border transactions, with a limited exclusion for certain non-U.S. CSEs. The exclusion is not available to non-U.S. CSEs that are consolidated with a U.S. parent (foreign consolidated subsidiaries). In certain circumstances, the rule would allow CSEs to comply with comparable margin requirements in a foreign jurisdiction as an alternative means of complying with the CFTC's margin rule for uncleared swaps to the extent that the CFTC determines that the foreign jurisdiction's requirements are comparable to the CFTC's.

As provided in the Agencies' final rules, U.S.-prescribed margin requirements for uncleared swaps took effect on September 1st, notwithstanding that implementation of such requirements has been delayed in certain other jurisdictions. In recognition of practical and technical limitations that swap dealers are experiencing with respect to complying with the applicable custodial arrangement requirements, the CFTC Division of Swap Dealer Intermediary Oversight on September 1st issued a no-action letter providing 30-day relief from such requirements, provided that during this transition period a swap dealer makes diligent, good faith implementation efforts. In a statement accompanying the no-action letter, CFTC Chairman Massad highlighted that such relief may be of particular benefit to smaller firms or foreign firms that have not been able to put in place the necessary arrangements by September 1st. On August 31st, CFTC Commissioner Giancarlo issued a statement criticizing the decision by the U.S. authorities not to delay implementation of the margin requirement.

**Substituted Compliance.** The CFTC on March 16th approved a substituted compliance framework for dually-registered central counterparties located in the European Union, together with a comparability determination with respect to certain EU rules. "Our unanimous action today means that European CCPs registered with the CFTC can comply with many of our rules by meeting the corresponding European Market Infrastructure Regulation (EMIR) requirements," CFTC Chairman Massad said in a statement. "The equivalence agreement announced by European Commissioner Jonathan Hill and myself is an important step in achieving cross-border harmonization of derivatives regulation." The action follows the agreement on February 10th between the CFTC and the European Commission regarding dually-registered derivatives clearing organizations. Under the comparability determinations, CCPs that are authorized in the EU under the European Market Infrastructure Regulation (EMIR) and registered with the CFTC may comply with certain CFTC requirements for financial resources, risk management, settlement procedures, and default rules and procedures by complying with corresponding requirements under the EMIR framework.

***De Minimis* Exception.** On August 15th, the CFTC's Division of Swap Dealer and Intermediary Oversight issued its final report on the swap dealer *de minimis* exception, following a preliminary report issued on November 18, 2015. The current *de minimis* threshold for swap dealer registration of $8 billion is scheduled to decrease to $3 billion in December 2017, unless the Commission takes further action. The preliminary report used available swap data to assess the *de minimis* exception level in light of the policy goals for swap dealer registration, and requested public comment on the report. The Final Report summarizes the public comments received in response to the Preliminary Report and provides further data analysis. It also discusses the *de minimis* exception alternatives noted in the Preliminary Report and identifies issues for the Commission's consideration. The final report made no recommendations to the Commission. In a September 15th speech, CFTC Chairman Massad said he will recommend a one-year delay in the scheduled reduction of the threshold in order for the Commission to have more time to consider the issue. In a January 19th comment letter on the CFTC staff's preliminary report, the IIB said a number of smaller foreign banks have either curtailed their participation in, or withdrawn from, the U.S. swaps markets because of their inability to rely on the *de minimis* exception,

and recommended several modifications and clarifications to encourage smaller foreign banks to re-enter the U.S. swaps markets.

- **Executive Compensation.** An interagency proposed rule on incentive-based executive compensation was unveiled on April 21st, pursuant to Section 956 of the Dodd-Frank Act. The new proposal replaces an earlier version issued by the agencies in 2011. The proposed executive compensation rule applies to all financial institutions with total assets of $1 billion or more. The new proposal takes a tiered approach, dividing institutions into 3 categories based on asset size - $250 billion and above; $50 billion to $250 billion; and $1 billion to $50 billion. Most of the rule's requirements apply to the two largest categories of institutions.

  On July 22, the IIB submitted a comment letter on the proposed rule, addressing aspects of particular significance to the U.S. operations of financial institutions that are headquartered outside the United States. The IIB recommended the adoption of a substituted compliance approach whereby the U.S. operations of non-U.S. financial institutions whose home country regulatory or supervisory requirements, guidance and practices are in accordance with the incentive-based compensation Principles and Implementation Standards adopted by the Financial Stability Board would be deemed in compliance with the requirements prescribed under Section 956. The IIB letter also addressed considerations relevant specifically to non-U.S. financial institutions in the absence of substituted compliance, including the scope of "U.S. operations" of foreign banking organizations that would be subject to the proposed rules, the application of the rules to non-U.S. investment advisers, the identification of covered persons, senior executive officers and significant risk-takers, the need for exceptions from the clawback requirements, the adaptation of governance provisions to the corporate and management structure of non-U.S. financial institutions, and the effective date for compliance with the requirements.

- **Legislative Proposals.** In a June 7th speech at the Economic Club of New York, House Financial Services Committee Chairman Jeb Hensarling outlined his proposal to replace the Dodd-Frank Act with what he called a "new legislative paradigm in banking and capital markets." Under the legislation, banks that maintain a leverage ratio of at least 10 percent and have a composite CAMELS rating of 1 or 2, would be able to opt out of the "post-Dodd-Frank supervisory regime, the Basel III capital and liquidity standards, and a number of other regulatory burdens that pre-date Dodd-Frank," he said. Rep. Hensarling's bill would also replace regulators' orderly liquidation authority with a new subchapter of the Bankruptcy Code, repeal the Volcker Rule, remove the powers of FSOC to designate firms as systemically important, and reform the CFPB. It would also impose stiffer penalties for fraud and deception. The House Financial Services Committee subsequently approved the bill on September 13th, but it is not expected to come to a vote on the House floor this year.

**Capital Planning/Stress Testing**

The Federal Reserve Board on November 25, 2015 approved a final rule modifying its capital plan and stress testing requirements. The changes are in effect for the 2016 capital plan and stress testing cycle. Firms subject to the supplementary leverage ratio would begin to incorporate

it into their capital plan and stress testing for the 2017 cycle. For stress-testing exercises, all firms would continue to use the generally applicable risk-based capital framework, but use of the advanced approaches risk-based capital framework--which is generally applicable to firms with at least $250 billion in total consolidated assets or $10 billion in on-balance sheet foreign exposures--would be delayed indefinitely. However, those firms would continue to be subject to the advanced approaches framework for their regulatory capital ratios.

The common equity tier 1 capital requirement in the Board's revised regulatory capital rules--which significantly strengthened the quality and quantity of capital held by banking organizations--will be fully phased in over the nine-quarter planning horizon of the 2016 capital plan and stress testing cycles. Generally, this ratio will require firms to hold more regulatory capital than the tier 1 common ratio, which was used before the introduction of the Board's revised regulatory capital rules. The final rule would remove the requirement for firms to calculate a tier 1 common ratio.

**AML/BSA**

New York's Department of Financial Services on June 30th issued a final rule that requires DFS-regulated institutions to maintain programs to monitor and filter transactions for potential Bank Secrecy Act (BSA) and anti-money laundering (AML) violations and prevent transactions with sanctioned entities. The final regulation requires regulated institutions annually to submit a board resolution or senior officer compliance finding confirming steps taken to ascertain compliance with the regulation.

Under the new rule, which will be effective January 1, 2017, institutions will be required to review their transaction-monitoring and filtering programs and ensure that they are reasonably designed to comply with risk-based safeguards. The institutions also must adopt (at the institution's option) an annual board resolution or senior officer compliance finding to certify compliance with the DFS regulation beginning April 15, 2018. The resolution or finding must state that documents, reports, certifications and opinions of officers and other relevant parties have been reviewed by the board of directors or senior official to certify compliance with the regulation. Institutions must maintain supporting data for the certification, for review by DFS, for five years.

The Treasury Department on May 6th announced measures to combat money laundering and tax evasion, including a final customer due diligence rule and proposed beneficial ownership legislation (click here for Treasury Secretary Lew's letter to House Speaker Paul Ryan). The CDD rule adds a new requirement that financial institutions - including banks, brokers-dealers, mutual funds, futures commission merchants, and introducing brokers in commodities - collect and verify the personal information of the beneficial owners who own, control, and profit from companies when those companies open accounts. The final rule also amends existing Bank Secrecy Act (BSA) regulations to clarify and strengthen obligations of these entities.

The CDD Final Rule harmonizes BSA regulations and makes explicit several components of customer due diligence that have long been expected under existing regulations, as well as incorporating a new requirement for covered financial institutions to collect beneficial ownership information. Specifically, the rule contains three core requirements: (1) identifying and verifying the identity of the beneficial owners of companies opening accounts; (2) understanding

the nature and purpose of customer relationships to develop customer risk profiles; and (3) conducting ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information. With respect to the new requirement to obtain beneficial ownership information, financial institutions will have to identify and verify the identity of any individual who owns 25 percent or more of a legal entity, and an individual who controls the legal entity. Based upon comments received in response to the proposed rule that was published in August 2014, the final rule extends the compliance date until May 2018, expands the list of exemptions, and makes use of a standardized beneficial ownership form optional as long as a financial institution collects the required information.

The Administration's proposed beneficial ownership legislation would require companies to know and report adequate and accurate beneficial ownership information at the time of a company's creation, so that the information can be made available to law enforcement. As part of the legislation, companies formed within the United States would be required to file beneficial ownership information with the Treasury Department, and face penalties for failure to comply. The proposed legislation also contains technical amendments to the current Geographic Targeting Order (GTO) authority which would clarify FinCEN's ability to collect information under GTOs, such as bank wire transfer information. As part of the package of measures, Treasury also announced proposed regulations related to foreign-owned single-member limited liability companies.

**Section 385**

On April 4th, the IRS issued proposed regulations under Section 385 of the Internal Revenue Code regarding the treatment of certain instruments issued by corporations in related-party transactions as debt or equity for federal tax purposes. The action was taken in connection with the additional action taken by the Treasury Department to curb corporate inversions. Addressing the "earnings stripping" aspects of such transactions, the proposal has raised concerns regarding its potential adverse impact on the debt capitalization of U.S. subsidiaries of foreign corporations more broadly.

The IIB on June 30th submitted a comment letter on the Treasury Department's proposed regulations, explaining the commercial and regulatory reasons why FBOs and other financial institutions are different from other business entities in fundamental ways that are relevant for the application of Section 385 and describing in greater detail how the proposed regulations will adversely impact the day-to-day, customer-driven business activities of FBOs and run counter to bank regulatory requirements. The letter sets forth several recommendations for narrowing the scope of these rules in a manner that would mitigate their deleterious consequences for FBOs, including with respect to the characterization of internal LTD issued for TLAC purposes as debt or equity, while preserving their effectiveness in countering the types of transactions identified in the notice of proposed rulemaking.

**QFC Early Termination Rights**

The Federal Reserve Board on May 3rd proposed a rule that would require U.S. global systemically important banking institutions (G-SIBs) and the U.S. operations of foreign G-SIBs to amend contracts for common financial transactions to prevent the immediate cancellation of the

contracts if the firm enters bankruptcy or a resolution process. This change should reduce the risk of a run on the solvent subsidiaries of a failed G-SIB caused by a large number of firms terminating their financial contracts at the same time, the Fed said. The contracts, called qualified financial contracts (QFCs), are used for derivatives, securities lending, and short-term funding transactions such as repurchase agreements. The proposal would apply to bilateral, uncleared QFCs. Because G-SIBs conduct a large volume of transactions through these contracts, the mass termination of QFCs may lead to the disorderly unwind of the G-SIB, spark asset fire sales, and transmit financial risk across the U.S. financial system, the Fed said in announcing the proposed rule.

The IIB on August 5th submitted a comment letter on the proposed restrictions. While supportive of the overall objective of the proposed rule to avoid early termination of QFCs, the IIB expressed concern about the significant costs and limited benefits arising from the interaction of the Fed's proposed rule with overseas jurisdictions' regulatory frameworks if the definition of foreign G-SIBs' "U.S. operations" is not revised. "While we have no objection to the application of the FRB's Proposed Rule to locally incorporated entities which may be subject to the U.S. resolution regime, in our view, the FRB's Proposed Rule would impose duplicative requirements on foreign G-SIBs' U.S. branches, whose Qualified Financial Contracts ("QFCs") are already subject to existing and substantially equivalent resolution powers, without a proportionate incremental benefit to their resolvability or reduction in risks to U.S. financial stability," the IIB stated.

**Cybersecurity**

President Obama on December 18, 2015 signed a $1.1 trillion omnibus spending bill that included the Cybersecurity Information Sharing Act of 2015. The cyber bill is aimed at promoting information sharing between the government and private sector.

The New York State Department of Financial Services on September 13, 2016 proposed regulations that would require banks, insurance companies, and other DFS-regulated financial services institutions to establish a cybersecurity program; adopt a written cybersecurity policy; designate a Chief Information Security Officer responsible for implementing, overseeing and enforcing its new program and policy; and have policies and procedures designed to ensure the security of information systems and nonpublic information accessible to, or held by, third-parties, along with a variety of other requirements to protect the confidentiality, integrity and availability of information systems. The proposed regulation is subject to a 45-day notice and public comment period before its final issuance. The proposed regulation includes certain regulatory minimum standards while maintaining flexibility so that the final rule does not limit industry innovation and instead encourages firms to keep pace with technological advances, DFS said. Prior to proposing this new regulation, the Department said it surveyed nearly 200 regulated banking institutions and insurance companies to obtain insight into the industry's efforts to prevent cybercrime.