EUFederation
Factoring & Commercial Finance

# Monthly Monitoring Report

**AUGUST 2019**

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29th August 2019: The Bank for International Settlement publishes a summary on Basel III

On the 29th of August, the Bank for International Settlement (BIS) published an executive summary explaining the scope of application of the Basel III standards.

The document first reminds the 3 pillars structure of the Basel III standards:

- Pillar I: minimum risk-based, liquidity and large exposure standards and buffer requirement;
- Pillar II: supervisory review process
- Pillar III: public disclosure.

Regarding the scope of application, the summary reminds that all banking and other relevant financial services part of a group that contains an internationally active banks are subject to the requirements set by the revised standards of Basel III.

This list contains:

- Majority-owned or controlled banking entities;
- Securities entities
- Other financial entities

The paper reminds that insurance entities are not subject to the Basel III standards. In that regards, it means that when calculating regulatory capital, banks must remove from their balance sheet assets and liabilities and third-party capital investments in an insurance subsidiary.

The paper also details the specific treatment of banks' investment in banking, financial and insurance entities that are outside the scope of regulatory consolidation that are subject to specific rules.

14th August 2019: Updated Questions and Answers on Basel III standards

On the 14th August, the Bank for International Settlement (BIS) published its Questions and Answers (Q&A) regarding the standardized approach for operational risk in the final Basel III standards.

The document focuses on the following elements:

- Treatment of **non-performing loans** in the business indicators
- The timeline for **the exclusion or inclusion of losses and business indicators** after divestiture/ deconsolidation and acquisition/merger
- Conversion of losses from foreign subsidiaries into local currency
- Treatment of refunds due to overbilling
- Treatment of losses from outsourced activities

5th august 2019: Basel III: EBA publishes its impact study and recommendations to the European Commission

On the 5th of August, the European Banking Authority (EBA) published the results of its impact study and key recommendations to the European Commission regarding the transposition of Basel III provision, agreed between the international regulators in December 2017.
This report follows the public hearing held on the 2nd of July 2019.
The report comes with specific policy advice on operational risk, on the output floor, on credit risk and on Securities financing Transactions (SFTs).

Basel III standards are to be phased in from 2022 to 2027 together with the revised Basel Framework for market risk (FRTB – *Fundamental review of the trading book*) as amended in 2019.

The EBA stresses that the "***credibility benefit the EU banking sector will derive from strictly complying with the framework far outweighs (…) the overall limited regulatory capital gains assessed in this report in relation to keeping certain EU deviations in the implementation of the final Basel framework***".

***Main findings and recommendations in the EBA report***

- ***Global cost, assessed under "conservative assumptions", should reach €135,1bn for the whole EU banking sector.***

- ***Distrust vis-à-vis internal models.***
  - ***Basel III finalization as a prerequisite "to restore credibility of the international regulatory framework based on internal models".***
  - ***The output floor should be applied at all levels of consolidation, unless waivers are granted to individual level requirements.***

- ***Implementation without deviation from Basel III. A "[strict compliance] with the framework far outweighs, in the view of the EBA, the overall limited regulatory capital gains assessed". By consequences :***
  - ***the output floor should be applied at all levels of consolidation, unless waivers are granted to individual level requirements***
  - ***Suppression of the SME supporting factor***

- ***Approach toward factoring activity***
  - ***Assimilation of factoring and leasing business models***
  - ***EBA's definition of factoring doesn't take into account CRR II***
  - ***For eligible purchased receivables, the EBA foresees a 18% increase of the RWA. This estimate should however be taken with caution due to data quality.***

## I. Implementation of Basel III in the EU

### a) Impacts of Basel III on the EU banking sectors

**According to the EBA, the Basel III standards will have the following consequences:**

- **Estimated shortfall for the EU banking sector:** € 135.1 billion of which € 91.1 billion for the common equity tier (CET1)
- **Minimum Required Capital (MRC):** the reform will increase the tier 1 MRC by 24.4%

- **Output Floor:** the output floor will be increased by 9.1% (average of all banks). The new output floor set at 72.5% of the total risk-weighted assets is expected to constrain 40 out of 79 internal model banks, which account for around 70% of internally-modelled RWA in the sample (189 banks)

**The impacts differ between banks depending of their size, business model and risk:** The EBA underlines that the impacts of the reforms should be mainly borne by large and systemically important institutions. In terms of business model, they are expected to have a *"negative impact mostly on banks' business model/organisation/client relationship (in particular for cross border universal banks, domestic universal banks, mortgage banks, automotive and consumer credit banks, savings and loan associations and a cooperative banks), revenues, lending rates and decision to use internal models (…)".*

**As shown in the table below, the output floor will be one of the main driver of the increase of the Minimum required capital (MRC)**.

**Table 1** Percentage change in T1 MRC (relative to current T1 MRC), by bank size

| Bank size | Δ SA | Δ IRB | Δ CCP | Δ SEC | Δ MKT | Δ OP | Δ CVA | Δ LR | Δ OF | Δ Total |
|---|---|---|---|---|---|---|---|---|---|---|
| **All banks** | **2.7** | **2.7** | **0.1** | **0.6** | **2.5** | **3.3** | **3.9** | **-0.5** | **9.1** | **24.4** |
| Large | 2.3 | 2.8 | 0.1 | 0.7 | 2.6 | 3.4 | 4.1 | -0.5 | 9.5 | 25.0 |
| of which: G-SIIs | 1.7 | 3.5 | -0.1 | 1.2 | 4.2 | 5.5 | 5.1 | 0.0 | 7.6 | 28.6 |
| of which: O-SIIs | 2.3 | 1.7 | 0.2 | 0.3 | 1.6 | 2.1 | 3.7 | -0.5 | 12.1 | 23.6 |
| Medium | 9.7 | 0.1 | 0.0 | 0.0 | 0.9 | 0.3 | 0.5 | -1.1 | 0.9 | 11.3 |
| Small | 10.7 | 0.0 | 0.2 | -1.9 | 0.0 | -3.7 | 0.3 | -0.1 | 0.0 | 5.5 |

Sources: EBA 2018-Q2 quantitative impact study (QIS) data and EBA calculations.
Notes: Based on a sample of 189 banks: Large (104), of which G-SII (8), of which O-SII (67); Medium (61); Small (24). SA, standardised approach to credit risk; IRB, internal rating-based approach to credit risk; CCP, central counterparty; SEC, securitisation; MKT, market risk; OP, operational risk; CVA, credit valuation adjustment; LR, leverage ratio; OF, output floor.

In the report, the EBA clearly shows its ambition to apply the Basel III standards on internal models. In its preliminary presentation of its report, the EBA had underlined that "***new Basel III framework introduces a more risk-sensitive framework for the standardised approaches, while limiting the elements of internal approaches, which in the past have given rise to some degree of variability in capital requirements***".

For the internal ratings-based (IRB) approach to credit risk, the requirement will increase for exposures currently treated under the advanced IRB approach (A-IRB) and will "*slightly*" decrease for those currently treated under the foundation IRB approach (F-IRB).

### b) <u>Main recommendations of the EBA</u>

The main recommendations of the EBA are the followings:

- **EU-specific supporting factors to SMEs:** The Capital Requirement Regulation (CRR) provides a supporting factor to eligible exposures to SMEs under both the SA and IRB framework.

  Even though the banking package adopted last spring by co-legislators has reinforced the supporting factors to SMEs, the EBA recommends that the EU legislator should not adopt any EU specific supporting factors to SMEs and infrastructure lending.

The EBA justifies this recommendation based on the fact that the supporting factor is not part of Basel III standards and that the benefits of a *"[strict compliance] with the framework far outweighs […] the overall limited regulatory capital gains assessed*".

- **Prudential ratio:** the EBA recommends to use floored RWA to compute the full stack of capital requirements applicable in the EU, including pillar 2 requirements and EU-specific systemic buffers.

- **A tough stance toward Internal models**

  In July, 2nd the EBA stated that "*the credibility of internal models [was] low at the BCBS table and among global regulators."* And that *"Output floor was the compromise to continue to maintain the use of internal models".*

  **The EBA is of the view that the output floor should be applied at all levels of consolidation**, "*unless waivers are granted to individual level requirements*".

  For the European Authority**, a consolidated approach would be contrary to the current capital requirements**: the existing capital requirements are applied at individual level (including the output floor and leverage ratio).

- **Recommendations regarding the Standardised approach (SA)**
  - To adopt the newly designed standardised approach, replacing all currently existing regulatory approaches to operational risk capital.
  - To keep the external ratings-based approach across exposure class. This should results in a more risk-sensitive regulatory treatment, particularly in light of the increase risk sensitivity of the new SA framework as well as the broader EU regulatory efforts to improve the reliability and governance of external ratings.

## II. TREATMENT OF FACTORING

### a) Factoring and leasing

In the report, the EBA treats the factoring and the leasing the same way (see pages 18 and 34 of the report). The "***Business model code***" for leasing and factoring banks is "*Leasing*", with very small samples.

The definition of factoring **used by the EBA does not reflect the definition** included in CRR II in Article 411:

- **EBA defines factoring activities** as "financing *method in which the bank pays a company the value of the invoices less a discount for commissions and fees*".
- **Article 411 of CRR II** provides that " *'factoring' means a contractual agreement between a business (the 'assignor') and a financial entity (the 'factor') in which the assignor assigns or sells its receivables to the factor in exchange for the factor providing the assignor with one or more of the following services with regard to the receivables assigned:*
  *(a) an advance of a percentage of the amount of the assigned receivables, generally short term, uncommitted and without automatic roll-over;*

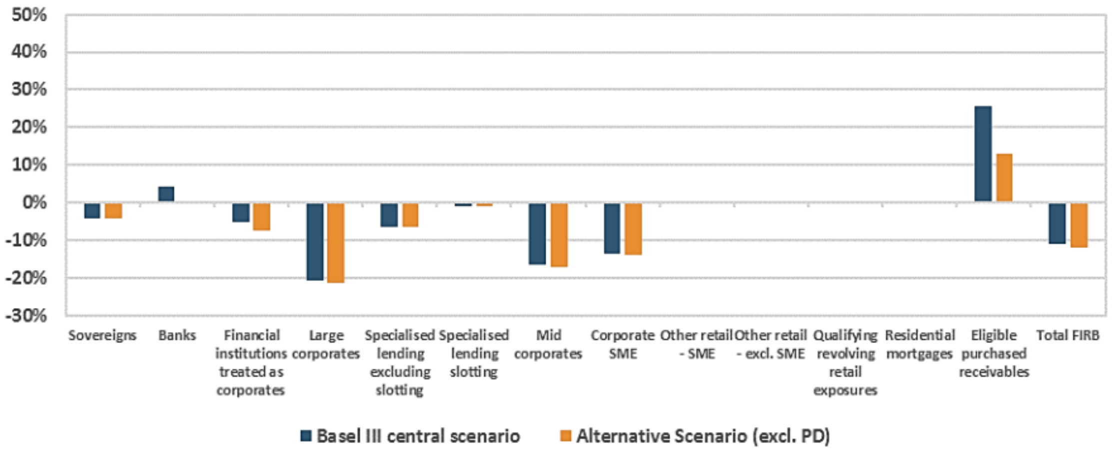
*(b) receivables management, collection and credit protection, whereby, in general, the factor administers the assignor's sales ledger and collects the receivables in the factor's own name"*

### b) A tougher risk weight treatment for eligible purchased receivables

The EBA foresees **an 18% increase of the risk-weighted asset (RWA) for the eligible purchase receivable**. The EBA underlines that this figure should be considered with caution due to the poor data quality.

The EBA also found that eligible purchased receivables which are currently subject to F-IRB (Foundation - Internal Rating Based) will be affected by the new probabilities of default (PD) input floors as shown in the table below.

**Figure 50** Percentage change in FIRB RWA per exposure class excluding PD input floor (relative to exposure class current FIRB RWA)




**The Breakdown of the Internal Rating Based (IRB) with the exposure at default (EAD) is also representative of the impact of Basel III.**

**Table 132** Breakdown of IRB EAD, by exposure (sub-)class, bank size and IRB approach (%)

| Exposure class | Large | | Medium | | G-SIIs | | O-SIIs | |
|---|---|---|---|---|---|---|---|---|
| | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB |
| Banks | 67 | 33 | 15 | 85 | 94 | 6 | 46 | 54 |
| Corporate SME | 80 | 20 | 69 | 31 | 77 | 23 | 81 | 19 |
| Eligible purchased receivables | 61 | 39 | 0 | 0 | 62 | 38 | 60 | 40 |
| Financial institutions treated as corporates | 90 | 10 | 0 | 100 | 99 | 1 | 60 | 40 |
| Large corporates | 86 | 14 | 100 | 0 | 96 | 4 | 74 | 26 |
| Medium-sized corporates | 78 | 22 | 90 | 10 | 83 | 17 | 73 | 27 |
| Other retail | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 |
| Qualifying revolving retail exposures | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 |
| Residential mortgages | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 |
| Sovereigns | 63 | 37 | 0 | 100 | 80 | 20 | 35 | 65 |
| Specialised lending excluding slotting | 65 | 35 | 82 | 18 | 92 | 8 | 33 | 67 |

Sources: EBA 2018-Q2 QIS data and EBA calculations.
Note: Based on a sample of 78 banks.

**Table 133** Breakdown of IRB EAD, by exposure (sub-)class, country and IRB approach (%)

| Exposure class | AT | | BE | | DE | | DK | | ES | | FR | | GR | | IE | | IT | | NL | | NO | | PT | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F-IRB | A-IRB | F- |
| Banks | 0 | 100 | 91 | 9 | 35 | 65 | 98 | 2 | 94 | 6 | 93 | 7 | 0 | 0 | 3 | 97 | 98 | 2 | 95 | 5 | 0 | 0 | 0 | [illegible] |
| Corporate SME | 0 | 100 | 93 | 7 | 31 | 69 | 94 | 6 | 94 | 6 | 67 | 33 | 6 | 94 | 9 | 91 | 98 | 2 | 99 | 1 | 100 | 0 | 100 | [illegible] |
| Eligible purchased receivables | 0 | 100 | 0 | 0 | 30 | 70 | 86 | 14 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 100 | 0 | 100 | 0 | 0 | 0 | 0 | [illegible] |
| Financial institutions treated as corporates | 0 | 100 | 100 | 0 | 76 | 24 | 93 | 7 | 96 | 4 | 100 | 0 | 0 | 0 | 100 | 0 | 98 | 2 | 100 | 0 | 100 | 0 | 0 | [illegible] |
| Large corporates | 0 | 100 | 86 | 14 | 62 | 38 | 95 | 5 | 89 | 11 | 97 | 3 | 0 | 100 | 8 | 92 | 97 | 3 | 100 | 0 | 100 | 0 | 100 | [illegible] |
| Medium-sized corporates | 0 | 100 | 94 | 6 | 66 | 34 | 92 | 8 | 94 | 6 | 64 | 36 | 0 | 100 | 21 | 79 | 98 | 2 | 99 | 1 | 100 | 0 | 100 | [illegible] |
| Other retail | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | [illegible] |
| Qualifying revolving retail exposures | 100 | 0 | 100 | 0 | 100 | 0 | 0 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 0 | 0 | 100 | [illegible] |
| Residential mortgages | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | 0 | 100 | [illegible] |
| Sovereigns | 0 | 100 | 70 | 30 | 44 | 56 | 0 | 0 | 97 | 3 | 74 | 26 | 0 | 0 | 37 | 63 | 99 | 1 | 100 | 0 | 0 | 0 | 0 | [illegible] |
| Specialised lending excluding slotting | 0 | 100 | 89 | 11 | 42 | 58 | 98 | 2 | 0 | 100 | 92 | 8 | 0 | 100 | 0 | 100 | 85 | 15 | 100 | 0 | 100 | 0 | 0 | 1 |

Sources: EBA 2018-Q2 QIS data and EBA calculations.
Note: Based on a sample of 87 banks.

2nd August 2019: The ECB publishes two decisions on TLTROs

On the 2nd of August 2019, two decisions of the European Central Bank regarding the third and second series of targeted longer-term refinancing operations were published in the Official journal:

- DECISION (EU) 2019/1311 OF THE EUROPEAN CENTRAL BANK of 22 July 2019 on a third series of targeted longer-term refinancing operations (ECB/2019/21)
- DECISION (EU) 2019/1312 OF THE EUROPEAN CENTRAL BANK of 22 July 2019 amending Decision (EU) 2016/810 (ECB/2016/10) on a second series of targeted longer-term refinancing operations (ECB/2019/22)

2nd August 2019: Publication of the updated Single Rule Book Q&A with new CRR II and CRD V

On the 2nd of August, the European Banking Authority (EBA) published its updated version of its Single Rulebook Questions and Answers in order to align them with the amended version of CRR and CRD IV (CRR II and CRD V)

23rd July 2019 – the ECB publishes its July 2019 lending survey

The European Central Bank published its July 2019 bank lending survey.

***Credit standards***

The ECB concludes that in the second quarter of 2019, credit standards for loans to firms tightened for small and medium-sized enterprises but remained unchanged for loans to large enterprises.

The reasons behind this change are:

- **the risk perception and risk tolerance of banks**: banks have noted a deterioration in the general economic and firm-specific situation;
- the **cost of funds** and the **balance sheet constraints**.

The survey notes that the tightening of credit standard is visible mainly in France, in Italy and to a lesser extent in Germany. Credit standards remained unchanged in Spain and in the Netherlands.
In other countries however, competitive pressure contributed to an easing of credit standards in all large countries.

***Terms and conditions***

During this second quarter 2019, overall terms and conditions that banks apply when granting new loans or credit lines also tightened in France and Germany but have eased in Spain. This tightening also affected margins on average NFC loans (defined as the spread over relevant market reference rates). Banks are also stricter on the collaterals. This tightening is explained by the change in risk perceptions, the cost of funds for banks and the balance sheet constraints.

***Rejection rate***

The survey reveals that the rejection rate of loans to enterprises have continued to increase in the euro area with 7% of the loan requests rejected (2% in the first quarter 2019).

***Net demand for loans***

The demand for loans have increased in Germany, France and Italy for small and medium-sized enterprises but not for large firms. The demand has decreased in the Netherlands and in Spain.
This increase was supported by the low general level of interest rates and fixed investments

12th July 2019: EBA publishes its report on the monitoring of the LCR implementation

On the 12Th of July 2019, the European Banking Authority (EBA) published its first report regarding the implementation of liquidity coverage ratio (LCR). With this monitoring exercise, the EBA aims at fostering a higher degree of harmonization in the implementation of the LCR.
The liquidity coverage ratio has been applicable in the European Union since October 2015. In 2018, the LCR reached its full implementation with a 100% coverage ratio.

The EBA's report focuses on LCR items for which the EBA and national authorities have observed differences in the implementation between the Member States.
Differences have been pointed out in:

- The identification and quantification of wholesale deposits received that can benefit from the outflow preferential treatment of operational deposits;
- The definition of material penalty in the context of retail deposits maturing beyond 30 days that can be excluded from outflows;
- The recognition of inflows from maturing high-quality liquid assets (HQLA);
- Optional and contingent flows;
- Interbank swaps of retained covered bond or asset-backed securities (ABS);
- The time dimension of the LCR;
- The item subject to the notification process.

The report outlines the following elements for which further guidance would be useful for banks and national supervisory authorities:

- **Operational wholesale deposits**: the report points out that there is a difference in the LCR whether the wholesale deposits received are treated as operational or non-operational and the LCR delegated regulation does not provide enough information on that;
- **Excluded retail deposits from outflows**: this measure allows credit institutions to exclude from the calculation of outflows retail deposits maturing after 30 days when the depositor is not legally allowed to withdraw the deposit before 30 days are up or when the depositor can do so only by paying a material penalty. The exclusion of retail deposits has a significant impact on the banks' LCR. The lack of a concrete definition of material penalty in the LCR delegated regulation may lead the banks to use different approaches.
- **The recognition of inflows stemming from maturing HQLA**
- **Optionality and contingent inflows**
- **Interbank swaps of retained covered bonds or ABS**
- **The time dimension of the LCR**

**Next step**
**The EBA will regularly monitor the implementation of the LCR by EU banks and will further assess how this guidance will be used by banks and supervisors.**

9th of July 2019 – EBA publishes its report on the its progress to repair IRB models

On the 9th of July, the European Banking Authority (EBA) published a progress report on the road map to repair internal models (IRB).
Published in 2016, this road map aimed at enhancing the robustness and the comparability of the internal risk estimates by:

- Addressing the concerns about **undue variability of own funds requirements**;
- Restoring trust in IRB models by **ensuring comparability of the estimates of risk parameters**, while retaining their risk sensitivity.

Among others, the report addresses the following point:

- **Implementation deadline**: the deadline is extended for introducing changes in the rating systems by one year (end 2021);

- **Loss given default (LGD)** and conversion factors models: the implementation is extended to 2023.

The EBA will **not amend its guidance on internal models** but will focus on the monitoring and exploring whether there is evidence of reduced variability of risk-weighted exposure amounts.

4th of July – the EBA publishes its 2019 risk board

On the 4th of July, the European Banking Authority published its 2019 risk board. The board summarises the risks and vulnerabilities in the European Union for the banking sector.

The 2019 risk board includes the following conclusions/elements:

- **CET 1:** CET 1 ratio remained at the same level ( from 14.5% to 14.7% at the first quarter 2019);
- **Risk exposure amounts:** rose slightly which reflect an increase in total loan volumes;
- **Non-performing loans (NPLs):** the ratio of NPLs continued to decline in 2019 ( from 3.8% in Q1 2018 to 3.1% in Q1 2019);
- **Risk Assessment Questionnaire (RAQ):** the RAQ includes banks' and market analysts' expectations for future trends and development. According to the responses to the questionnaire, banks plan to further expand their corporate lending especially for SMEs and households (mortgage and consumer lending). Half of the banks responding to the questionnaire declared that they will fund their growth by increasing MREL liabilities and retails deposits. However, respondents raised the risk of a possible deterioration of corporate and commercial real estate exposure.
- **Banks profitability:** profitability has not improved in the EU with a 6.8% return on equity (RoE);
- **IFRS 9** related data on asset quality and banks' fair valued positions;

Information about their **sovereign exposures**

2nd of July 2019 – The FSB reviews the implementation of the TLAC Standard

On the 2nd of July, the Financial Stability Board (FSB) has published a technical review of the implementation of the Total Loss-Absorbing Capacity (TLAC) Standard.

As a reminder, TLAC is an international standard established by the Financial Stability Board (FSB) in 2015. Those standards are intended to ensure that global systemically important banks (G-SIBs) have enough equity and bail-in debt to pass losses to investors and minimize the risk of a government bailout. Since 1st of January 2019, G-SIBs must held a TLAC amount of 16% in terms of risk-weighted assets (RWAs) or 6% of the leverage exposure. From January 2022, these ratios will increase (18% of RWAs and 6.75% of the leverage exposure).

Those requirements are really important to:

- Enhance the **resolvability of G-SIBS**;
- Strengthen the **cooperation between home and host authorities**;
- Boost market confidence in authorities' capabilities to **address "too-big-to-fail"** risks.

The TLAC Standards should help promote financial stability by providing home and host authorities and markets with confidence that G-SIBs have appropriate capacity to absorb losses, both before and during a resolution, to implement the preferred resolution strategy and to maintain the continuity of the essential functions of the institution.

The report concludes that the implementation of those requirements has been steady and significant in both the setting of external TLAC requirements by authorities and the issuance of external TLAC by G-SIBs. Those standards are respected in the EU (through the EU Banking Union), Canada, Hong-Kong, Switzerland, the United Kingdom and the United States.

The FSB points out that there is no need to modify the TLAC but further efforts are needed to **address home/host challenges and the risks of market fragmentation**. To that end, the FSB reminds that it is important to determine the appropriate group-internal distribution of TLAC resources across home and host jurisdictions in order to reduce the risks of fragmentation of capital resources.
Further work is also needed to implement the TLAC Holdings Standards of the Basel Committee on Banking Supervision (BCBS).

The report also notes that:

- some jurisdictions have **restricted the distribution of TLAC to retail investors** even though the TLAC standards do not provide for specific restrictions of the sale of TLAC to retails investors;
- more work is needed **to ensure the appropriate group-internal distribution of TLAC across home and host jurisdictions** and to ensure balance between TLAC resources that are prepositioned at material subsidiaries or subgroups (MSGs) as internal TLAC and those that would be readily available to deploy flexibility where needed in times of stress.

The FSB sets a series of recommendations, among them:

- to continue monitoring the implementation of the TLAC standards and the issuance of TLAC instruments with an annual report;
- to review the Resolvability Assessment Process (RAP) template to ensure that Crisis Management Groups (CMGs) consider the quantity, quality and group-wide distribution of TLAC resources;
- to strengthen the resolution-related disclosures;
- to keep working on bail-in execution.

**28th June 2019 – ECB studies the impacts of higher capital buffers on banks' lending and risk taking**

On the 28Th of June, the European Central Bank (ECB) has published a **working paper** on the impact of higher capital buffers on banks' lending and risk-taking.

Other Systemically Important Institutions (O-SIIs) buffer is defined as a macro-prudential policy aiming to increase banks' resilience. **CRR** and **CRD IV** provides that national authorities must identify banks who can be

qualified as O-SIIs and who have to apply a buffer of up to 2 percent of the total risk exposure amount. The level of these capital buffers is designed based on the capital to risk-weighted assets ratio.
O-SIIs can comply with the capital buffer requirement in two ways:

- By decreasing their risk-weighted assets by either shifting investments to assets with lower risk-weights or decreasing lending together;
- By issuing new equity.

This requirement aims at increasing banks' resilience to adverse shocks but the report also concludes that higher capital requirements can constrain lending which could pose costs for economic activity (at least in the short term).

The report also adds that by changing the relative attractiveness of different asset classes, a higher capital requirement could also lead to risk-shifting and therefore promote the build-up (or deleverage) of banks' risk-taking.

The study shows that banks identified as O-SIIs reduce their credit supply to households and financial sectors and shifted their lending to less risky counterparts within the financial and households sectors within the non-financial corporations. However, it seems that this policy has reduced impacts in the medium-term.

To sum up, the report concludes that the implementation of the O-SII's framework could have a positive disciplining effect by reducing banks' risk-taking while having only reduced adverse impact on the real economy through a temporary decrease in credit supply.

**15th June 2019** – The Future of the euro area Banking

In a speech on the future of the European and Global Banking at the 25th Dubrovnik Economic Conference on the 15th of June 2019, Pentti Hakkarainen, member of the Supervisory Board of the European Central Bank addressed the developments of the European banking and its future.

Since the launch of the Banking Union in 2014, improvements were noted:

- The average Common Equity Tier 1 (CET1) ratio rose from 11.3% in 2014 to 14.3% in 2018;
- The average leverage ratio rose from 4.0% in 2014 to 5.3% in 2018;
- The level of non-performing loans (NPLs) decreased from €1 trillion in 2015 to €580 billion in 2019.

However, the banking sector profitability remains low: in 2018, the return on equity (RoE) of euro area banks remained at 6% which is below the level required for profits to outweigh the cost of equity. But this is not the case for all banks. Indeed, a number of banks are very profitable. Pentti Hakkarainen explains this difference due to two factors: their high cost-efficiency and the intensive use of modern technology.

To explain the low profitability of the majority of the banking industry, Pentti Hakkarainen points out **the excess capacity of the euro area banking industry and underlines its poor cost-efficiency performance** (excessive number of branches in relation to their customer base, excessive staff costs, etc…).

He also points out the fact that the injection of public money in order to keep the banking system functioning has allowed some of the market players to remain in the market. Without this public intervention, they would have had to exit the market. Some of the public intervention also aimed at keeping the national and historical champions in the market. He believed that this excess capacity should be dealt with through the exit of less favorable banks from the market.

Pentti Hakkarainen also discussed the influence of the public sector in bank consolidation. States must make sure that critical financial services are available whatever the economic and financial circumstances are. States are able to set conditions and requirements to be met by the market players and those conditions must be fair and unbiased as it is not the role of the State to save non-viable banks. According to him, those banks should be allowed to exit the market to leave room for more competitive institutions. The bail out of banks by member states leads to wrong incentives according to him, since it wastes taxpayers' money and delay the consolidation of the market.

To help member states in this task, the Banking Union (i.e. the Single Supervisory Mechanism and the Single Resolution Mechanism) provides the tools to help foster a healthy banking sector. The European deposit guarantee system, once adopted by the co-legislators, should also help to complete the Banking Union.

Along with the public sector and the Banking Union, the future of the banking area will also rely on the use of financial technologies. An intensive use of modern technology can allow banks to operate more efficiently. Physical access to retail bank facilities will keep decreasing in the coming years and consumers will rely more and more on online banking services. **Pentti Hakkarainen points out that financial technology will also ensure financial stability since it will allow the cross-border distribution of banking services when national players cannot answer to the financing needs.**

**12th June 2019** – The European Commission publishes the fourth progress report on NPLs

On the 12th June, the European Commission released its fourth report on the reduction of non-performing loans (NPLs) and the reduction of risks in the Banking Union.

The report reminds that the EU and the member States have taken several steps to reduce the ratio of non-performing exposure in the EU.
Among them, the report mentions:
- The strengthening of banks' solvency, leverage and liquidity positions;
- The improvement of the governance in the banking sector and in the supervision scheme;
- The enhancement of the banks' resolvability.

These steps have allowed the following improvements:
- The average Tier 1 capital ratios of euro area banks directly supervised by the Single Supervisory Mechanism have remained stable: 15.54% in Q4-2018 compared to 15.63% in Q4-2018;
- Higher average leverage ratio: 5.28% in Q4-2018 and 5.41% in Q4-2017( above the 3% requirement);
- Resilience to liquidity stocks remains strong with a liquidity coverage ratio at 145.61% in Q4-2018 against 143.56% in Q4-2017 (well above the 100% requirement)

Along with those steps, the European institutions have taken complementary measures:
- Review of the banking package to put in place a more robust framework to regulate the banks' activity;
- Adoption of the insolvency directive.

The EU institutions and Member States efforts led to a decline of NPL ratios from 4.4% in Q3-2017 and 3.3%. In Q3-2018 at the EU level. In Europe, the NPLs ratios vary from 0.9% in Luxembourg and 43.5% in Greece.

**These results should be reinforced thanks to the following complementary measures:**
- The **NPL regulation** which amends the CRR (Capital Requirement Regulation) with the introduction of a "*statutory prudential backstop*" which aims at preventing the under-provisioning of future NPLs. This prudential backstop will reduce the risks for financial stability arising from highs level of insufficiently covered non-performing loans. The regulation was adopted by the co-legislators in April 2019.

- The **NPL Directive** ("Credit servicers, credit purchasers and the recovery of collateral") was submitted along with the NPL regulation to enable banks to deal in a more efficient way with loans by improving the selling of the non-performing exposure to third parties. The directive is still under discussions.
- The Commission is undertaking **a benchmark of national loan enforcement regimes** in order to obtain a full picture of the delays and value recovery rates that banks face in case of borrowers' defaults.
- The European Commission also provided a technical blue print for national **Asset Management Companies (AMC)** but no member states have initiated the set-up of an AMC at national level.
- The **European Central Bank**, the **European Banking Authority** and the **European Commission** are working on the set up of a **European NPL transaction platform.**

**6th June 2019 –** The ECB launches a new series of TLTROs

On the 6th of June 2019, the European Central Bank has announced a new series of TLTROs (Targeted Long-Term Refinancing Operations).

TLTROs can be defined as Eurosystem operations that provide financing to credit institutions for periods of up to four years. They offer long-term funding at attractive conditions to banks in order to further ease private sector credit conditions and stimulate banks lending to the real economy. TLTROs' aim is to reinforce the European Central Bank's current accommodative monetary policy stance and strengthen the transmission of monetary policy by further incentivizing bank lending to the real economy.

TLTROs I and TLTROs II were respectively launched in June 2014 and March 2016. The ECB (the Governing Council) has decided to launch a third series of TLTROs in June 2019. The interest for each operation will be set at a level of 10 basis point (i.e 0.1%) above the average rate applied to the Eurosystem's main refinancing operations (MROs – the interest rate banks pay when they borrow money from the ECB for one week).

**This new series will start in September 2019 and will end in March 2021.**

**23rd May 2019** – The future of EU's capital market

The 23rd of May, Luis de Guindos, Vice-president of the European Central Bank gave a speech at the conference of the Association for Financial Markets in Europe (AFME) on the future of the Capital Markets Union.
The action plan on Capital Markets Union (CMU) launched in September 2015 aimed at fostering deep and diversified capital markets that provide a wide source of financing options to European companies and citizens to encourage investment, innovation and growth. The CMU also aims at completing the banking union by providing channels to mobilize the savings to finance the economy.

Luis de Guindos made three comments regarding the future of the Capital Markets Union:

- Financial markets are playing an increasingly important role in funding the economy but efforts should be made to **foster sustainable cross-border financial integration and risk-sharing**. Most of the regulatory framework that emerged from the Capital Markets Union Plan must now be completed (delegated acts, national transposition…). Therefore, their effects remain to be seen. Luis de Guindos does regret the slowness of the harmonization to remove the barriers. He adds that for some of the initiatives, the texts will not deliver their full potential such as the Pan-european personal pension plan (PEPP). The regulation adopted set up a rather complex product for which keys elements are left at the discretion of the Member States.

- A revamped CMU agenda should be geared towards addressing the challenges facing Europe. In the Brexit context, Luis de Guindos believes that **the CMU should aim to develop and integrate the EU's capital markets Union**. The Brexit should lead to the emergence of financial centers in Europe. In that context, the CMU should facilitate this transition by creating a framework that supports the emergence of an integrated financial market and avoids a return to a fragmentation of activities.

  For that purpose, he believes that the continued expansion of the non-bank sector should be accompanied with a revision of the prudential and supervisory framework.

- Finally, he pointed out that the synergies between the CMU and the banking Union should be strengthened. According to him, more efficient markets could complement banking Union by offering ways to mobilize EU savings that could be used to finance enterprises. For instance, he mentioned that fostering equity investment by addressing the debt-equity bias would support the development of an equity culture and increase household's return on their savings. He also pushes for the creation of a European safe asset.

**14th May 2019** – The Council of the EU adopts the banking package

The 14th of May 2019, the Council of the European Union officially adopted the directive and regulation amending CRD IV and CRR. The European Parliament had adopted the review on the 16th April 2019 by a large majority.

The directive will have to be transposed in national law 18 months after its entry into force (20 days after its publication in the Official Journal of the European Union).

The regulation will be applicable 2 years after its entry into force (20 days after its publication in the Official Journal of the European Union).
As a reminder, the main elements of the revision are the following:

- The proportionality threshold for small and non-complex institutions is set at a €5 billion total value of assets : these entities will benefit from a simplified net Stable Funding Ratio and from simplified disclosure requirements
- Factoring is defined for the first time and will benefit from a more lenient treatment in the implementation of the Net Stable Funding Ratio (NSFR) in the EU
- The leverage ratio remains at 3% with a 50% buffer for Global Systemically Important Institutions (G-SIBs)
- Institutions will have to report to the national authorities their 10 largest exposures to shadow banking entities carrying out banking activities outside the CRR framework
- SMEs will benefit from an extension of the supporting factor for their loans (€ 2.5 million against €1.5 million).

**The texts must now be signed and published in the Official Journal of the European Union.**

**8th May 2019** – Speech of Fernando Restoy on proportionality in financial regulation and supervision

On the 8th of May, Fernando Restoy, Chairman of the Financial Stability Institute for the Bank for International Settlement gave a speech on proportionality in financial regulation and supervision on the Financial Stability Institute/ International Monetary Union (FSI/IMF) global meeting on proportionality.

He started off his speech by reminding the concept of proportionality which stems from the need to limit public intervention (in the form of rules, sanctions and oversight) to what is actually needed to achieve the policy objectives. Public authorities aim at preserving financial stability, market integrity and consumer protection: proportionality protect the market from measures that could distort the financial services market.

He pointed out the different meanings of proportionality. In regulation, a proportionate approach means tailoring regulatory requirements to a firm's size, systemic importance, complexity and risk profile. The aim is to avoid excessive compliance costs or regulatory burden for smaller and non-complex banks. In supervision however, proportionality aims at facilitating the efficient allocation of supervisory resources and activities on firms that are systemically important or are considered high risks. In resolution policies, proportionality aims at adjusting the requirements for recovery and resolution planning and resolvability to the likelihood that regulated firms will cause systemic stress if they fail.

He continued his speech with examples of cases where proportionality has been implemented:

- **In prudential regulation**

The use of proportionality to tailor regulatory requirements differs between jurisdictions based on the criteria used to differentiate institutions, the scope of application and the methods used to apply proportionality. Fernando Restoy points out here the lack of international guidance on how to apply proportionality. In banking, beside the Basel standards for internationally active banks, jurisdictions do not have to apply these standards to other banks and internationally active banks is still not defined in the Basel standards.

According to him, the concept of proportionality is mostly used to the market risk framework, the quantitative liquidity standards and the large exposure regime and jurisdictions apply different tailoring methods for different iterations of the Basel standards.

- **In supervision**

It seems that all authorities apply proportionality in their supervisory schemes. Again jurisdictions have different approaches: some use a principle based approach based on an assessment of the firm when others use other methodologies based on what is called "guided discretion".

The studies undertaken by the FSI conclude that authorities rely more on guided discretion approaches when they decided on the amount of capital add-ons under pillar 2 and use the principles based approach when the authority assesses the quality of a firm's corporate governance.

He concludes with a key takeaway: **the use of proportionality in supervision is not a choice but an intrinsic part of supervision that allows supervisory resources to be better allocated to firms that pose the greatest risks.**

- **In resolution**

The proportionality principle is also used for the tailoring of resolution planning. Here again, approaches differ between jurisdictions: some require resolution plans for all banks when others impose requirement only for G-SIBs or D-SIBs.

In terms of **policy implication**, Fernando Restoy raised the attention on the differences between the United States and the European Union. For instance, in the United States, only a few banks with total assets of $250 billion or more are subject to the Basel III standards on risk-based capital and leverage requirements. In the European Union, nearly all banks are subject to Basel III (with some exceptions for smaller banks).

**7th May 2019** - Basel Committee for banking Supervision releases its progress report on adoption of the Basel regulatory framework

The 7th of May 2019, the Basel Committee for Banking Supervision (BCBS) published its progress report which sets out the adoption status of Basel III standards for each member jurisdiction.

Out of the 28 member jurisdictions, the BCBS reports that:

- 27 member jurisdictions have risk-based capital rules, liquidity ratio (LCR) regulations and capital conservation buffers in force;
- 26 member jurisdictions also have final rules in force for the countercyclical capital buffer and the domestic systemically important bank (D-SIB) requirement;
- All members that are home jurisdictions to G-SIBs have final rules in force;
- The leverage ratio based on the existing exposure definition has been partly or fully implemented in 26 member jurisdictions;
- 26 member jurisdictions have issued final rules for the revised securitisation framework;
- 26 member jurisdictions have issued draft or final rules for the standardised approach for measuring counterparty credit risk exposures (SA-CCR);
- 24 member jurisdictions have issued draft or final rules for the capital requirements for bank exposures to central counterparties.

This report aims at monitoring the adoption progress of all Basel standards agreed but it does not include Basel II and 2.5 standards nor the Basel III standards that have been implemented by all BCBS members. This report includes the following standards:

- **Counter cyclical buffer** which is fully effective since 1st January 2019;
- **Margin requirements for non-centrally cleared derivatives** which are being phased in between September 2016 and August 2020;
- **Capital requirements for bank exposures to central counterparties** which are in effect since January 2017;
- **Capital requirements for equity investment in funds** which are in effect since January 2017;
- The **standardised approach for measuring counterparty credit risk exposure** which are in effect in January;
- **Securitisation framework;**
- **TLAC holdings** requirements which took effect in January 2019;
- **Risk-based capital framework** which will take effect from January 2022. The **output floor** will be phased in between January 2022 and January 2027;
- **Leverage ratio** was revised in 2017 will come into effect in January 2022;
- **Liquidity requirements** with the Net Stable Funding Ratio (NSFR) that became a minimum standard on 1 January 2018;
- **Requirements for systemically important banks (SIBs):**
  - The G-SIB framework will be implemented by 2021
  - The D-SIB framework which applies since January 2016
  - Leverage ratio buffer: reviewed in December 2017 and completed with a leverage ratio buffer for G-SIBs
- **Interest rate risk in the banking book (IRRB)** which will came into effect from end-2018;
- **Supervisory framework for measuring and controlling large exposures** took effect in January 2019;
- **Pillar 3 disclosure requirements** will take effect between 2020 and 2022.

The report summaries the measures that have been taken/ adopted by the European institutions to apply these standards:

- **Countercyclical capital buffer (CCyB):** CRD IV requires national authorities to issue regulations implementing a countercyclical buffer and is applicable since 1st January 2016.
- **Margin requirements for non-centrally cleared derivatives**: the technical standard are applicable from 1st March 2017;
- **Capital requirements for CCPs**: a proposal for implementing the standard on capital requirements was adopted in November 2016 by the European Commission and is under consideration by the co-legislators. The deadline was January 2017.
- **Capital requirements for equity investments in funds**: a proposal for implementing the standard on capital requirements was adopted in November 2016 by the European Commission and is under consideration by the co-legislators. The deadline was January 2017.
- **Standardised approach for measuring counterparty credit risk** (SA-CCR): the proposal for implementing the SA-CCR was adopted by the European Commission in November 2016 and is under consideration by the co-legislators. The deadline was January 2017.
- **Securitisation framework:** the regulations were adopted in 2017 and are applicable since 1st January 2019.
- **TLAC Holdings:** the proposal for implementing TLAC holdings standards was adopted in November 2016 and is under consideration by the co-legislators. The deadline was January 2019.
- **Revised standardised approach for credit risk:** the deadline is January 2022
- **Revised IRB approach for credit risk:** the deadline is January 2022
- **Revised CVA framework:** the deadline is January 2022
- **Revised minimum requirements for market risk:** the proposal for implementing this framework was adopted by the European Commission in November 2016 and is under consideration by the co-legislators.
- **Revised operational risk framework**: the deadline is January 2022
- **Output Floor**: the deadline is January 2022
- **Leverage ratio**:
    - The existing exposure definition: the delegated act was adopted in October 2014 but the proposal for introducing a capital requirement base on the leverage ratio was adopted by the European Commission in November 2016 and is still under consideration by the co-legislators. The deadline was January 2018.
    - The revised exposure definition: a proposal for introducing a capital requirement based on the leverage ratio was adopted in November 2016 by the European Commission and is under consideration by the co-legislators. The deadline is January 2022.
- **G-SIB requirements**: the disclosure requirements for G-SIBs and the identification methodology are applicable since January 2015. The mandatory G-SIB buffer requirements are implemented trough CRD IV and applicable since January 2016.
- **D-SIB requirements:** the optional D-SIB buffer are implemented trough CRD since January 2016.
- **Leverage ratio buffer for SIB:** the European Commission adopted a proposal on the framework for a leverage ratio buffer and is under consideration by the co-legislator. The deadline is January 2022.
- **Interest Rate Risk in the Banking Book (IRRBB):** the European Commission adopted a proposal in November 2016 which is still under consideration by the co-legislators. The EBA published its revised guidelines on July 2018 on the management of interest risks arising from non-trading activities which will be applicable as of 30th June 2019.
- **Liquidity:** CRD sets out that institutions shall have robust strategies, policies, processes and systems for the identification, measurement, management and monitoring of intraday liquidity risk. The Commission proposal on Net Stable Funding ratio (NSFR) is under consideration by the co-legislator.

**Revised Pillar 3 requirements as published in 2015:** the EBA had adopted in December 2016 its guidelines to implement the revised pillar 3 framework released by the Basel Committee in 2015.

**26th April 2019: Publication of the NPL Regulation in the Official Journal of the European Union**

Following its adoption by the European Parliament and the Council of the European Union, the NPL regulation has been published in the Official Journal of the European Union.
As a reminder, the main elements of the agreement are the following:
**The scaling of the minimum coverage level**
The co-legislators had no difficulties in finding an agreement regarding the scaling of the minimum coverage level as the final report of the ECON committee and the position of the Council were close.

- ✓ **Unsecured loans**:

  **Banks will have to provide for a 100% coverage 3 years after the loan has been declared as non-performing**. As a reminder, the Commission had proposed a 100% coverage after 2 years.
  **Banks will provide for at least 35% of their exposure to unsecured loans two years after they go non-performing and then full coverage after 3 years.**

- ✓ **Secured loans:** the calendar agreed between the co-legislators will be the following:

  - **Secured by immovable collateral:** 25% after 3 years, 35% after 4 years, 55% after 5 years,70% after 6 years, 80% after 7 years, 85% after 8 years, 100% after 9 years

  - **Secured by movable collateral:** 25 % after 3 years, 35% after 4 years, 55% after 5 years, 80% after 6 years, 100% after 7 years

However, it should be noted that the wording of the article 47c(3) regarding the scaling up of the minimum coverage level for loans secured by movable collateral has been amended. Whereas the European Parliament suggested "*secured by movable property or other eligible collateral*" , the agreement provides "*secured by other funded or unfunded credit protection".* This change does not change the sense of the article but specifies it.

Please find below a summary table of the calendar agreed between the Council and the European Parliament:

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Council and European Parliament agreement | Unsecured | | 0% | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 70% | 80% | 85% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 80% | 100% | 100% | 100% | 100% |

**Derogations for non-performing exposure guaranteed or insured by an official export credit agency and is case of forbearance measure**

The agreement between the Parliament and the Council confirmed the introduction of two derogations as suggested by the ECON rapporteurs.

- **A derogation for non-performing exposure guaranteed or insured by an official export credit agency (article 47c (3)(a)):**

In this situation, the scaling up of minimum coverage level will be the following:

- **0** for the secured part of the non-performing exposure to be applied during the period between **one year and seven years following its classification as non-performing**
- **1** for the secured part of the non-preforming exposure to be applied as the **first day of the eighth year following its classification as non-performing**

- **Derogation in the case of forbearance measure (article 47c(5)(a))**

When an exposure has been granted a forbearance measure, the scaling of the minimum coverage is modified :

- **For unsecured loans**: Between **one year and two years** following its classification as non-performing, the factor applicable( according to the scaling reproduced above) at the moment the forbearance measure is granted shall be applicable for **an additional period of one year**
- **For secured loans**: Between **two and six years** following its classification as non-performing, the factor applicable (according to the scaling reproduced above) at the moment the forbearance is granted shall be applicable for **an additional period of one year.**

**18th April 2019: the NPL Directive is still pending**

***No adoption before the end of the mandate***

Notwithstanding the accelerated pace of work in the Council of the EU and the Parliament, the European Commission directive proposal on "***Credit servicers, credit purchasers and the recovery of collateral***" will not be adopted before the end this legislative mandate (18th of April).

The colegislators were however quite close to find an inter-institutional agreement as the Council of the European Union reached a compromise on the 27th March and the European parliament presented its draft report on the 11th of March. While the Council was ready for the trilogues, the Committee on economic and monetary affairs (ECON) did not manage to adopt a final report and negotiation mandate.

***Entering into force of the NPL regulation***

The postponing of the adoption of the directive raises questions on the implementations of the regulation which was part of the same regulatory package. The regulation was officially adopted by the European Parliament and the Council and should enter into force the day following its publication in the Official Journal of the European Union.

This regulation amending the regulation on minimum capital requirements (CRR) establishes a common minimum levels of money banks need to set aside to cover losses caused by future loans that will turn non-performing. The coverage level depends of whether the loan is secured ( by an immovable or movable collateral) or not.

This postponing means that **financial institutions would have to apply these new coverage requirements without benefiting from the development of the secondary market for non-performing loans as provided by the directive proposal.**

***What will happen in September?***

Article 229 of the rules of procedures provides that at the end of the legislative mandate "*all Parliament's unfinished business shall be deemed to have lapsed*".

However, at the beginning of each parliamentary term, the Conference of Presidents (composed of the European Parliament president and of the presidents of each political party) "*shall take a decision on reasoned requests from parliamentary committees and other institutions to resume or continue the consideration of such matters*".

Esther de Lange (EPP, NL) ,rapporteur on the proposal, will stand for the next European elections and under the pressure of the European commission, the discussion on the directive will probably be reopened.

**16th April 2019 – Review of the European Supervisory Authorities : The European Parliament adopts the revision of the ESAs**

The European Parliament adopted on the 16th of April 2019 the reform of the European Supervisory Authorities (ESAs : EBA, EIOPA and ESMA) which includes the review of EBA's powers to fight money laundering.
The regulation was adopted by a large majority : 521 in favour, 70 against, 65 abstentions.

As a reminder, the agreement reached between the co-legislators includes the following elements:

- **Strengthening and reinforcing the existing system for more supervisory convergence:** The agreement supports the Commission's objective of harmonising and increasing the efficiency, the transparency and the coherence of the supervisory procedures between the ESAs.

- **Governance of the ESAs :** The agreement does not include the creation of an Independent Executive Board as proposed by the Commission. Instead, the text provides for a reinforcement of the Board of Supervisors and more powers for the Chairperson. The Chairperson will have the power to submit decisions to the Board on the infringement of EU law by market players and decisions to open investigations on financial products.

- **Strengthening of ESAs' powers :** The ambitions of the European Commission have been clearly reduced. ESMA ( *European Securities and Markets Authority*) will only have direct supervision powers over EU and third country critical benchmarks and data reporting service providers.
  **EBA (*European Banking Authority*) will be given more powers to fight against money laundering.** EBA will collect information from EU national competent authorities, will enhance the cooperation between the authorities and will develop common standards.
- **ESAs' funding scheme**
  Whereas the European Commission proposed to ask the industry to contribute to the financing of the ESAs, the co-legislators have decided to preserve the current system ( funded with the EU budget and the contributions of national competent authorities).

**The Council must now officially adopt the text before its publication in the Official Journal of the European Union. The regulation will enter into force on the twentieth day following its publication.**

**16th April 2019 – Banking package: the European Parliament adopts CRR II and CRD V**

The European parliament has adopted the regulation (CRR II) and directive (CRD V) reforming the Capital Requirement Regulation (CRR) and the Capital Requirement Directive (CRD IV).

The legislative package was adopted by a large majority ( 490 in favour, 52 against). The number of abstentions was however quite high (111).
Commissioner Dombrovskis congratulated the European Parliament in passing this important package which represents a big step in the reduction of risks to EU banks and will better protect taxpayers.
As a reminder, the main elements of the revision are the following:

- The **proportionality threshold** for small and non-complex institutions is set at a **€5 billion total value of assets** : these entities will benefit from a simplified net Stable Funding Ratio and from simplified disclosure requirements
- **Factoring** is defined for the first time and will benefit of a more lenient treatment in the implementation of the Net Stable Funding Ratio (NSFR) in the EU
- The **leverage ratio remains at 3%** with a **50% buffer** for Global Systemically Important Institutions (G-SIBs)
- Institutions will have to report to the national authorities their **10 largest exposures to shadow banking entities** carrying out banking activities outside the CRR framework
- SMEs will benefit from an **extension of the supporting factor** for their loans (€ 2.5 million against €1.5 million).

**The Council of the European Union must now officially approve the texts. They will come into force 20 days after their publication in the Official Journal of the European Union.**

**9th April 2019 : Basel Committee launches a new presentation of the Basel standards on its website**

On the 9th of April, the Bank for International Settlement (who is hosting the Basel Committee) has launched a new section dedicated to the Basel Framework on its website. With this new section, the Basel Committee is also issuing a consolidated version of the Basel framework presented in chapter or in full version.
This new section aims at improving the accessibility of the Basel standards as well as to promote their consistent global interpretation.

With this new standards, the Basel Committees aims at reorganizing the requirements.
During the preparation of this new framework, some inconsistencies were revealed which will be addressed through minor policy changes.
The Committee welcomes comments on the presentation of this new framework.

Comments can be uploaded here until the **9th of August 2019**.

**8th April 2019 – EBA: Draft standards on KIRB**

On the 8th of April 2019, the European Banking Authority (EBA) published its draft standards on the conditions to allow institutions to calculate requirements of securitised exposures (KIRB).
These draft RTS (*Regulatory Technical Standards*) set out conditions to allow institutions to calculate capital requirements of the securities exposures (KIRB) in accordance with the purchased receivables approach (Capital requirement Regulation- article 255(9) - CRR) and internal modelling of capital requirements (IRB).

These RTS detail the conditions to allow institutions to calculate KIRB for the underlying pools of securitisations regarding:

- Internal credit policy and models for calculating KIRB for securitisations.

- The use of different risk factors regarding the underlying pool and of proxy data to estimate the probability of default (PD) and loss given default (LGD) ( when sufficient data on the underlying pool are not available).
- Due diligence requirements to monitor the actions and policies of sellers receivables or other originators.

These RTS cover the following areas:

- General approach to the relationship between the IRB on purchased receivables and the SEC-IRBA framework
- Eligibility conditions to compute KIRB
- Internal capital requirements
- Eligibility to use the retail risk quantification standards
- Use of proxy data

**These draft RTS are submitted to the European Commission for adoption and will be then subject to scrutiny by the European Parliament and the Council of the European Union before publication in the Official Journal of the EU.**

**27th March 2019** – NPLs : the Council of the Union adopts its compromise

The Council of the European Union reached a compromise on the 27th of March of the directive on the Commission proposal for a directive on "***Credit services, credit purchasers and the recovery of collateral***".

The main elements of the compromise are the following:

- **Scope of the directive (Recital 11 et article 1)**

**The Council seems to restrict the scope of the directive to non-performing loans only, excluding performing loans:**

- Commission's proposal (Recital 11): it should be possible for credit institutions to sell non-performing or even performing credit agreements on a Union-wide scale in efficient, competitive and transparent secondary markets.
- Council's Compromise (Recital 11): it should be possible for credit institutions to sell non-performing ~~or even performing~~ credit agreements on a Union-wide scale in efficient, competitive and transparent secondary markets.

- **Requirements for granting an authorisation (article 5)**

The Council of the European Union reinforces the requirements for the granting of an authorisation for credit purchasers. To be granted the authorisation, credit purchasers should have a registered office or its head office in the Member State in which he is seeking authorisation (Article 5(1) (a)). The applicant must also have an adequate anti-money laundering and counter terrorism procedures in place.

- **Transfer of a credit agreement by a credit purchaser (article 19 )**

The Council adds new information that must be provided by the credit purchasers to a national authority before a transfer: aggregated outstanding balance of the creditor's right under the non-performing credit agreements or of the non-performing credit.

- **Accelerated Extrajudicial Collateral enforcement (Title V):** the Council removes this provision, as did the European Parliament.

**20th March 2019** - Application of Basel III standards: EBA publishes two reports

On March 20th 2019, the European Banking Authority (EBA) published two reports which measure the impact of implementing the final Basel III reforms and monitor the current implementation of liquidity measures in the EU.

- The **EBA Basel III capital** monitoring report assesses the impact of the Basel reform package on EU banks. The report estimates that the Basel III reforms, once fully implemented, would determine an average increase by 19.1% of EU banks' Tier 1 minimum required capital.

- The **liquidity coverage ratio** of EU banks, which was fully implemented in January 2018, stood at around 146% on average in June 2018, materially above the minimum threshold of 100%.

1. **Basel III capital monitoring report**

The Basel III monitoring report assesses the impact on EU banks of the final revisions of credit risk, operational risk and leverage ratio frameworks, as well as the impact of the introduction of the aggregate output floor.

The report also quantifies the impact of the new standards for the market risk and credit valuation adjustment.

The evaluation of the impacts is based on minimum capital requirement (*Tier 1 minimum required capital –T1 MRC*). The minimal required capital would increase by 19.1% at the full implementation date (2027). The leading factors of this increase are the output floor (8.0%) and the operational risk (5.5%). The global systemic banks will be the most affected.

Change in total T1 MRC, as percentage of the overall current Tier 1 MRC, due to the full implementation of Basel III (2027) (weighted averages, in %)

| Bank group | Credit risk | | | | Market risk | CVA | Op risk | Output floor | Total risk-based | Revised LR | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | SA | IRB | Sec. | CCPs | | | | | | | |
| All banks | 2.2 | 2.0 | 0.7 | 0.0 | 2.3 | 4.7 | 5.5 | 8.0 | 25.4 | -6.2 | 19.1 |
| Group 1 | 1.8 | 1.7 | 0.8 | 0.0 | 2.5 | 4.9 | 6.1 | 8.5 | 26.3 | -6.0 | 20.3 |
| Of which: G-SIIs | 2.2 | 2.1 | 1.1 | 0.0 | 3.3 | 5.4 | 7.4 | 7.3 | 28.8 | -0.3 | 28.4 |
| Group 2 | 4.3 | 3.7 | 0.1 | 0.0 | 0.9 | 3.6 | 1.7 | 5.1 | 19.4 | -7.7 | 11.8 |

*Source: EBA QIS data (June 2018)*

The EBA concludes that, to comply with the new Basel III framework, EU banks would need EUR 39.0 billion of additional total capital, of which EUR 24.2 billion of Tier 1 capital.

Following consultations already initiated, a more detailed report will follow.

**2. The report on liquidity measures**

The EBA's report concludes that European banks have continued to improve the management of their liquidity coverage ratio. For instance, at the reporting date of 30 June 2018, the weighted average liquidity coverage ratio across banks is 146%, the required level being 100%.

The EBA remarks that there were only four banks with liquidity coverage ratio levels below 100%, as they monetised their liquidity buffers during times of stress.The EBA adds that the liquidity coverage ratio levels of global systemically important institutions (GSIIs) is 142%.By comparison, the liquidity coverage ratio levels of other banks is 167%.

The report also discusses the differences in liquidity levels considering items denominated exclusively US dollars currencies: in these cases, liquidity coverage ratio levels are, in general, lower.

**19th March 2019-** Proportionality principle on banking regulation and supervision

Following the launch of a survey on proportionality practices in bank regulation and supervision in 2018, the Basel Committee published a report summarising the responses received.

Within the Basel Committee, more than 21 jurisdictions declared applying proportionality in banking regulation and supervision. 13 States which are not members of the Basel Committee also declared applying this principle.

The survey did not cover measures applied to internationaly-active banks that are more conservative than the Basel framework and did not consider measures related to higher loss-absorbency requirements for global and domestic systemically important banks.

The report raises the following points:

- Proportionality measures are applied to credit institutions whose total assets represent a significant share in the State;
- Member States use a number of balance sheet metrics and indicators to determine proportionality measures;
- Most States apply some form of proportionality to capital and liquidity requirements which take the form of a modified or simpler version of existing Basel standards.

The determinants used by jurisdictions to define proportionality thresholds are the followings:

- Balance sheet metrics
- Business model
- Supervisory judgment

According to the Basel Committee proportionality, can be defined as setting standards for banks – encompassing both prudential and the associated administrative requirements- that are commensurate with their risk profiles.
This "tailored" approach aims at reflecting the different nature of banks' business models, systemic importance, cross-border activity and more generally the risks they are exposed to. The aim of proportionality is therefore not to reduce the resilience of banks or the banking system but rather to adapt the relative differences in risks across banks.

Based on this definition, the report gives some examples of proportionality measures:

- Some jurisdictions of the Basel Committee apply the full Basel framework for some banks and another one for other banks
- For non-Basel Committee members, some of them apply a modified or limited set of the Basel framework

The respondents to the survey also pointed some difficulties in applying this principle:

- **Balancing proportionality and comparability**: they pointed out the delicate trade-off between the benefits of tailoring requirements for different types of banks while preserving comparability in banks' regulatory ratios
- Balancing proportionality and competition principles

**14th march 2019** - NPLs : the European Parliament adopts the regulation by a large majority

On the 14th of March 2019, the European Parliament adopted in plenary session the Regulation amending CRR ((EU) No 575/2013) as regards minimum loss coverage for nonperforming exposures.

The representatives of the European Parliament and the Council of the European Union reached a compromise on the 3rd of January on the European Commission's proposal.

The text was approved with 426 votes in favour, 151 votes against and 22 abstentions.

As a reminder, the main elements of the agreement are the following:

**The scaling of the minimum coverage level**

The co-legislators had no difficulties in finding an agreement regarding the scaling of the minimum coverage level as the final report of the ECON committee and the position of the Council were close.

- ✓ **Unsecured loans**:

  **Banks will have to provide for a 100% coverage 3 years after the loan has been declared as non-performing**. As a reminder, the Commission had proposed a 100% coverage after 2 years.
  **Banks will provide for at least 35% of their exposure to unsecured loans two years after they go non-performing and then full coverage after 3 years.**

- ✓ **Secured loans:** the calendar agreed between the co-legislators will be the following:

- **Secured by immovable collateral:** 25% after 3 years, 35% after 4 years, 55% after 5 years,70% after 6 years, 80% after 7 years, 85% after 8 years, 100% after 9 years

- **Secured by movable collateral:** 25 % after 3 years, 35% after 4 years, 55% after 5 years, 80% after 6 years, 100% after 7 years

However, it should be noted that the wording of the article 47c(3) regarding the scaling up of the minimum coverage level for loans secured by movable collateral has been amended. Whereas the European Parliament suggested “*secured by movable property or other eligible collateral” ,* the agreement provides “*secured by other funded or unfunded credit protection”.* This change does not change the sense of the article but specifies it.

Please find below a summary table of the calendar agreed between the Council and the European Parliament:

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Council and European Parliament agreement | Unsecured | | 0% | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 70% | 80% | 85% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 80% | 100% | 100% | 100% | 100% |

**<u>Derogations for non-performing exposure guaranteed or insured by an official export credit agency and is case of forbearance measure</u>**

The agreement between the Parliament and the Council confirmed the introduction of two derogations as suggested by the ECON rapporteurs.

- **<u>A derogation for non-performing exposure guaranteed or insured by an official export credit agency (article 47c (3)(a)):</u>**

In this situation, the scaling up of minimum coverage level will be the following:

- **0** for the secured part of the non-performing exposure to be applied during the period between **one year and seven years following its classification as non-performing**
- **1** for the secured part of the non-preforming exposure to be applied as the **first day of the eighth year following its classification as non-performing**

- **<u>Derogation in the case of forbearance measure (article 47c(5)(a))</u>**

When an exposure has been granted a forbearance measure, the scaling of the minimum coverage is modified :

- **For unsecured loans**: Between **one year and two years** following its classification as non-performing, the factor applicable( according to the scaling reproduced above) at the moment the forbearance measure is granted shall be applicable for **an additional period of one year**
- **For secured loans**: Between **two and six years** following its classification as non-performing, the factor applicable (according to the scaling reproduced above) at the moment the forbearance is granted shall be applicable for **an additional period of one year.**

**Next steps:**

**The regulation will not be backdated from March 2018 as suggested by the European Commission but will be applicable for loans subscribed after the entry into force of the regulation ( i.e the date following that of its publication in the Official Journal of the European Union).**

**12th March 2019 :** Banking regulation – Basel Committee's priorities for 2019 from the ECB 's views

Sabine Lautenschläger, Member of the Executive Board of the ECB (European Central Bank) gave a speech at the Financial Stability Institute 20th anniversary conference where she reviewed the evolution of the banking regulation and exposed what she considers what should be the priorities of the Basel Committee for 2019.

She reminded and stressed that, risk sensitivity as introduced with Basel II is the best way to align capital requirements with the risk level. However, she emphasized the difficulty to assess the exact level of risks of a financial institution which is why backstops have been introduced alongside risk sensitivity. Basel III provides notably the following backstops to risk sensibility:

- **Input and output floors**
- **Leverage ratio**

As vice chair of the Executive Board of the ECB, she believes that the Basel Committee should focus on the following points in 2019:

- The Committee should monitor **how Basel III is implemented at the national level** and their supervisory practices;
- The Committee should **foster the exchange of information** about the risks and vulnerabilities of the market in a changing macroeconomic environment;
- The Basel Committee should be a **hub for exchanging supervisory knowledge**, tools and approaches on cyber risks;
- The Basel Committee could support national supervisors regarding operational, legal and reputational risks in banks which are linked to conduct risks, anti-money-laundering or green finance.

**11Th March 2019:** the ECON Committee publishes its draft report on Credit services, credit purchasers and the recovery of collateral

On the 11th of March, the 2 rapporteurs from the ECON committee, Esther de Lange (EPP, NL) and Roberto Gualitieri ( S&D, IT) published their draft report on the Commission proposal for a directive on "Credit services, credit purchasers and the recovery of collateral"

This directive proposal comes with the regulation on non-performing loans adopted by the European Parliament on the 14th of March.

**European Commission's proposal**

The Commission's proposal had two main goals:

- Strengthening the protection of secured creditors by giving them access to more efficient methods of recovering the amount with an **out-of-court procedure.** The procedure was excluded for consumer's loans.
- Developing a **secondary markets for NPLs**: the Commission wants to create a common set of rules

The main amendments suggested by the ECON rapporteurs are the following:

- **Scope of the directive**: It seems that the directive will only apply to non-performing loans contracted with credit institutions as defined in CRR whereas the Commission wanted to apply it to both non-performing and performing loans.

- **Accelerated Extrajudicial Collateral enforcement** (*Title V*): The rapporteurs suggest to remove this procedure from the directive.

- **Secondary markets** (*Title III: Credit purchasers*): The draft report reinforces the requirements to credit purchasers. National authorities and consumers should be informed of the transfer and should receive information on the credit purchasers (capital requirements, liquidities and measures applied by the credit purchaser to fight against money laundering…). The transfer of a loan must not undermine the consumer protection.

- **Modification of the credit agreement** (article 34): The draft report reinforces the protection of consumer with new requirements when the terms and conditions of a credit agreement are modified. The rapporteur suggests that these changes must be approved by the debtor.

**Next steps:**
**The rapporteurs intend to adopt a final report before the end of the current legislature. The vote in plenary session is scheduled for the last plenary mid-April.**

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**26th February 2019**: Basel Committee's policy and supervisory initiatives

The Basel Committee gathered on the 26th and 27th February to discuss the following points:

- Up-coming publication of high-level supervisory expectations on crypto-assets regarding the risks associated with these exposures
- Discussion of the different implementation of Basel III global minimum prudential standards
- Implementation of the Basel III standards by the jurisdictions

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**14th February 2019**: CRR II/CRD V: Publication of the final compromise between the European Parliament and the Council of the EU

- **Proportionality**

The agreement provides for a definition of "***small and non-complex institutions***" which will be accompanied by reduced reporting and disclosure requirements in order to lower compliance costs for these entities.

The introduction of this definition is necessary for targeted simplifications of requirements with respect to the application of the principle of proportionality (recital 6a-CRR).

Small and non-complex institutions would benefit from a **simplified net Stable Funding Ratio** (Recital 44a-CRR) and from **simplified disclosure requirements** (article 433(b)).

To be qualified as "***small and non-complex institutions***", the entities will have to fill the following conditions (article 2 (144)(a)):

- ✓ The total value of its assets on an individual basis or on a consolidated basis is on **average equal to or less than the threshold of EUR 5 billion over the four-year period** immediately preceding the current annual reporting period;
- ✓ The institution is subject to **no or simplified obligations** in relation to recovery and resolution planning;
- ✓ The institution's trading book business is classified as small;
- ✓ The total value of the institution's derivative positions held with trading intent **does not exceed 2% of its total on- and off-balance sheet assets**, the total value of its overall derivative positions does not exceed 5%, both calculated according to article 273a(3);
- ✓ More than **75% of both the institution's consolidated total assets and liabilities**, excluding in both cases the intragroup exposures, relate to activities with counterparties located in the European Economic Area;
- ✓ The institution **does not use internal models to meet the prudential requirements** that it is subject to in accordance with this Regulation except for subsidiaries using internal models developed at the group level, provided that the group is subject to the disclosure requirements laid down in article 433a or in article 433c at consolidated level;
- ✓ The institution has not communicated to the competent authority an objection to being classified as a small and non-complex institution;
- ✓ The competent authority has not decided that the institution is not to be considered a small and non-complex institution based on an analysis of its size, interconnectedness, complexity or risk profile.

Reporting and disclosure requirements will therefore be improved to ensure that they can be applied in a more proportionate way and do not create an excessive compliance burden especially for smaller and less complex institutions (Recital 6). The **European Banking Authority (EBA) will be in charge of drafting recommendations on how to reduce reporting requirements for small and non-complex institutions** which should result in an expected average cost reduction (article 434a).

- **Preferential treatment for factoring when it comes to the implementation of the Net Stable Funding Ratio (NSFR)**

As a reminder the Commission proposed in 2016 a **preferential treatment for trade finance activities regarding the Net Stable Funding Ratio (NSFR), without specifying factoring**.

**In the compromise between the European Parliament and the Council, factoring is defined in an EU legislative text for the first time and will benefit from the same regime than trade finance.**

**Article 411 (15a)) of CRR 2**

***Factoring*** *"means a contractual agreement between a business (assignor) and a financial entity (factor) in which the assignor assigns or sells its receivables to the factor in exchange of providing the assignor with one or more of the following services with regard to the receivables assigned:*

*(a) Advance of a percentage of the amount of receivables assigned, generally short term, uncommitted and without automatic roll-over;*

*(b) Receivables management, collection and credit protection whereby in general, the factor administers the assignor's sales ledger and collects the receivables in its own name.*

***For the purposes of Title IV, factoring shall be treated as trade finance".***

**The main consequence of these provisions is that factoring will benefit from the same treatment as trade finance regarding the weighted of the required stable funding factor (RSF):**

- **5% stable funding factor for products with a residual maturity of less than six months**

***Article 428s - 5% required stable funding factor***
1. The following assets and off-balance sheet items shall be subject to a 5% required stable funding factor:
**(d) trade finance off-balance sheet related products as referred to in Annex I of this Regulation with a residual maturity of less than six months.**

- **7.5% stable funding factor for products with a residual maturity between 6 months and one year**

**Article 428ta 7,5% required stable funding factor**
Trade finance off-balance sheet related products as referred to in Annex 1 with a residual maturity of at least six months but less than one year shall be subject to a 7,5% required stable funding factor.

- **10% stable funding factor for products with a residual maturity of more than 1 year**

***Article 428u 10% required stable funding factor***
*The following assets and off-balance sheet items shall be subject to a 10% required stable funding factor:*
*(c) trade finance off-balance sheet related products as referred to in Annex 1 with a residual maturity of one year or more*.

- **Simplified Net Stable Funding Ratio (sNSFR) (article 428(ah)(an))**

The agreement follows the European Parliament's position: entities qualified as "*small and non-complex*" will benefit from a **simplified version of the NSFR (sNSFR)** in order to reduce their administrative burden. **Yet, their prudential treatment will be more conservative.**
In practice, this simplification for small and non-complex institutions results in fewer data points to be collected for calculation and reporting purposes. A less granular version of the NSFR will involve:

*"collecting a limited number of data points, which would reduce the complexity of the calculation for those institutions in accordance with the principle of proportionality, while ensuring that those institutions still maintain a sufficient stable funding factor by means of a calibration that should be at least as conservative as the one of the fully-fledged NSFR".*

- **Leverage ratio**

The negotiators agreed to a **binding 3% leverage ratio (article 92)** and an additional **50% buffer for global systemically important institutions** (G-SIIs).

Regarding the 3% leverage ratio, the European Banking Authority (EBA) concluded that a tier 1 capital leverage ratio calibrated at 3% applied for any type of credit institution would constitute a credible backstop function. This leverage ratio level was also agreed by the Basel Committee. The text also provides an exception for public lending by development banks and officially guaranteed export credits: the leverage ratio will be adjusted for these institutions.

The 50% buffer for global systemically important institutions was calibrated by the Basel Committee with the specific purpose of mitigating the comparable larger risks to financial stability posed by global systemically important banks (G-SIBs) but also by G-SIIs. Further work will be undertaken to determine whether it should apply to other systemically important institutions (O-SIIs).

- **Liquidity and prudential capital management at group level**

The agreement follows the Council's approach on all home-host related provision. In its position, **the Council proposed to suppresses the revision of articles 7** ("*Derogation to the application of prudential requirements on an individual basis*") and **8** ("*Derogation to the application of liquidity requirements on an individual basis*") **of the European Commission regarding the consolidated management by parents companies of liquidity and capital requirements waivers granted at the individual level**.

As a reminder, in its proposal, the European Commission suggested a new exemption scheme for the individual liquidity and prudential capital management.
The agreement between the Council and the European Parliament contains two amendments of article 8 of CRR, mainly to take into account the implementation of liquidity ratio (NSFR and LCR):

- **Article 8(1)(b)** which adds a reference to the monitoring by the parent entity of the NSFR of the subsidiary

*(6) In Article 8 paragraph 1, point b is replaced by the following:*
*"(b) the parent institution on a consolidated basis or the subsidiary institution on a sub-consolidated basis monitors and has oversight at all times over the liquidity positions, **and the funding positions where the NSFR set out in title IV of part Six is waived**, of all institutions within the group or sub-group, that are subject to the waiver and ensures a sufficient level of liquidity, and of stable funding where the NSFR set out in title IV of part Six is waived, for all of these institutions;"*

- **Article 8(3)** regarding the exemptions for groups authorised in several Member States. The amendment adds references to the liquidity coverage ratio (LCR) and to the delegated act setting its calculation.

*6a) In Article 8 paragraph 3, points (b) and (c) are replaced by the following:*
*"(b) the distribution of amounts, location and ownership of the required liquid assets **to be held within the single liquidity sub-group where the LCR as defined** in delegated regulation (EU) No 2015/61 is waived and the distribution of amounts and location of available stable funding within the single liquidity sub-group where the NSFR set out in title IV of part Six of this regulation is waived;*
*(c) the determination of minimum amounts of liquid assets to **be held by institutions for which the application of the LCR as defined in delegated regulation (EU) No 2015/61** is waived and the determination of minimum amounts of available stable funding to be held by institutions for which the application of the NSFR set out in title IV of part Six of this regulation is waived;"*

- **Shadow Banking**

Article 394 (CRR II) provides for a new treatment of shadow banking by the institutions.
The agreement provides new elements **on reporting** and in that regards requests that **institutions must report to the national authorities their 10 largest exposures to shadow banking entities** which carry out banking activities outside CRR framework. They will have to report to the competent authorities twice a year.

The European Banking Authority (EBA) **will be in charge of developing the Regulatory Technical Standards (RTS).** The EBA will take into account developed and internationally agreed standards on shadow banking and will also have to consider if:

- The **relation with an individual or a group of entities** may carry risks to the institution's solvency or liquidity position
- The entities that are subject **to solvency or liquidity requirements <u>similar</u>** to those imposed by CRR and CRD should be entirely or partially excluded from the obligation to be reported.

**To be noticed that those RTS will be mandatory at the EU level.**

- **<u>SME supporting factor</u>**

In its proposal, the European Commission had suggested to reduce certain capital requirements to support lending to small and medium sized enterprises and infrastructure projects by extending the scope of the so called "*supporting factors*" for such entities or activities.

The agreement (article 501) provides for an extension of the existing supporting factor for loans to **SMEs in an amount up to euros 2.5 million (which is currently set at 1.5 million).**

In the previous article SME exposure of up to euro 1.5 million were subject to a 23.81% reduction in risk weighted exposure amount. Considering that the threshold of euro 1.5 million for an SME exposure is not indicative of a change in riskiness of an small and medium enterprise, it was decided that the reduction in capital requirements should be extended to SME exposure of up to euro 2.5 million and the part of an SME exposure exceeding euro 2.5 million should be subject to a 15% reduction in capital requirements.

- **<u>Intermediate Parent Company (IPU) set at €40 billion</u>**

The ECB directly supervises the 118 significant banks established in the participating countries and who hold almost 82% of banking assets in the euro area. The decision on whether a bank is deemed significant is based on a number of criteria such as having a total value of assets exceeding euros 30 billion. Banks which do not reach this threshold are under the supervision of national Competent Authorities (NCAs). In order to avoid the supervision of the ECB, some banks create several subsidiaries which stay under the thresholds of euros 30 billion.

The negotiators decided to act against this practice by requesting large non-EU banking groups with two or more subsidiary institutions in the EU to establish an IPU to consolidate all their activities in the Union under that IPU. The objective is to facilitate group supervision and enhance the resolvability of the firms in scope.

***Article 21b CRD Intermediate EU parent undertaking***

*1. Two or more institutions in the Union, which are part of the same third country group, shall have a single intermediate EU parent undertaking that is established in the Union.*

The agreement lists the following conditions:

- The threshold triggering the creation of **an IPU is set at € 40 billion balance sheet assets** in the EU including those held by third country branches (both those of credit institutions and investment firms);
- Global Systemically Important Institutions (G-SIBs) **are not automatically captured by the requirement** if they do not meet the threshold in the EU;
- IPUs may be set up as investment firms;

- A transitional period of 3 years would be provided;
- EBA would issue a report on the treatment of third country branches under Member States' laws.

▪ **Standardised approach for Counter Credit Risk (SA-CCR)**

The European Parliament and the Council of the Union support the Commission's proposal to introduce a Standardised Approach for Counter Credit Risk (SA-CCR) as defined by the Basel Committee. The European parliament and the Council endorsed this proposal.
The SA-CCR is known to be more risk sensitive that the market to market approach (MtM) or the Standardised Method (SM). The SA-CCR will be calibrated for institutions meeting some criteria in order not to be too complex or burdensome.

***Next steps***:
The European Parliament and the Council of the EU have to officially adopt the texts (first reading) before mid-April.

**13th February 2019**: Non-performing loans - ECB publishes its data for September 2017 to September 2018

The European Central Bank (ECB) published its data for September 2017 to September 2018

The total assets of credit institutions established in the European Union increased by 0,5% between September 2017 and September 2018, from €33.0 trillion in September 2017 to €33.2 trillion in September 2018.

The non-performing loans ratio continued to drop by 1%, from 4.4% in September 2017 to 3;4% in September 2018.

**7th February 2019**: International cooperation in banking supervision

On the 7th of February, Joachim Wuermeling, member of the executive Board of the Deutsche Bundesbank highlighted the benefits of international cooperation in banking supervision.

Joachim Wuermeling raised that since its inception in 1974, the Basel Committee on Banking Supervision (BCBS) has been responsible for:
- The separation of work and cooperation between home and host supervisors
- The building up of continuous exchange between supervisors
- The reduction of the opportunity for regulatory arbitrage and of the likelihood of a regulatory race to the bottom.

Basel III represents the main work and achievement of the Committee between 2009 and 2019. However, and as raised by Joachim Wuermeling, the Basel framework has not prevented financial crisis because regulatory loopholes emerged due to financial innovation and insufficient implementation.

He calls for a complete implementation of the Basel III by all international active banks to achieve a harmonized international framework. The speaker regrets however that the U.S or the EU for instance exclude from these measures internationally active mid-size banks. He remembered that the last crisis did not erupted only because of large institutions but also because of the activity of midsized banks. Yet he believes smaller institutions which are not internationally active should be subject to less burdensome obligations: the U.S and the EU have both started to adopt rules to reduce the burden on these banking institutions.

Joachim Wuermeling underlines that in banking regulation, cooperation can contribute to building a safer banking system. The focus will now shift towards evaluation and implementation monitoring.

He also points out new risks and new challenges that will be faced by banking institutions **and by the regulatory bodies such as crypto-assets or BigTechs which also shows that international cooperation is more than needed in those fields as those topics cannot be grasped at the national level.**
Finally, the speaker reminds that international cooperation does not cause national responsibility to vanish, States are responsible for the implementation of those international standard.

However, international cooperation can only work if national politics are able to overcome the tendencies towards less than full implementation. **International cooperation does not cause national responsibility to vanish.**

**6th February 2019**: CRR II/CRD V : the European Central Bank conducts an analysis of sensitivity risk

The European Central Bank launched a sensitivity analysis of liquidity risk to assess the ability of the banks it directly supervises to handle idiosyncratic liquidity shocks. This test will constitute the 2019 stress test.

Banking institutions will be tested on adverse and hypothetical shocks in which banks face increasing liquidity outflows.

The aim of this test is to evaluate the bank's survival period, i.e. the period during which the bank can pursue its activities without using funding markets. The test will not assess the potential causes of these shocks or the impact of wider turbulence. The results of the test will inform the ECB about the relative vulnerability of banks to different liquidity shocks and will identify improvements needed in banks' liquidity risk management.

29th January 2019- the European Systemic Risk Board (ESRB) suggests macro-prudential tools against Non-performing loans

The European Systemic Risk Board (ESBR) has published a report on macro prudential approaches to reduce non-performing loans (NPLs) in the European Union.

This report comes after the Council of the European Union request in its Action plan to analyse the role of macro-prudential tools that could help the European Union to prevent and avoid the augmentation of non-performing loans and to strengthen banks resilience.

The ESRB points out that the emergence and the accumulation of non-performing loans represents a threat to the European financial system. The Board identifies the business cycles and asset price shocks as the main drivers of non-performing loans. The vulnerabilities that built-up before the financial crisis (excessive credit growth, high level of indebtedness, non-transparent banking practices…) have also weakened the legal and judicial system.

***Macroprudential tools***

The ESRB does not suggest fundamental changes but rather some adjustments particularly on capital buffers and national protectives measures for borrowers.

- **Development of early warning systems (EWSs)** in order to monitor the risks of credit portfolio deterioration from a macro-prudential perspective. Progresses were made these past few years but the initiatives did not focus enough on an early warning. The Board therefore suggests the use of micro-datasets, at both bank and borrower level to identify vulnerabilities building up in specific sectors or subsets of borrowers.

- **Borrower-based measures in macroprudential toolkits** to prevent and mitigate the vulnerabilities underlying the first stage of the lifecycle of a potential non-performing exposure.

- **Capital-based instrument** to address vulnerabilities that could result in a non-performing exposure.

- Use of **countercyclical capital buffer (CcyB) by macroprudential authoritie** to prevent the systemic build-up of macro-prudential imbalances and increase banks' resilience when they face non-performing loans.

- Use of **the systemic risk buffer (SyRB) by macroprudential authorities** in the situation where the potential systemic increase in NPL flows is associated with developments in specific market segments or types of debtors as opposed to situations of generalised excessive credit growth.

17th January 2019: the Basel Committee reviews the principles for sound liquidity risk management and supervision

The Basel Committee has reviewed the principles for sound liquidity risk management and supervision first published in 2008. Following this review, the Basel Committee has concluded that the principles remain fit for purpose but asked the competent authorities and banks to apply them carefully in order to avoid liquidity risks on financial markets.

The Basel Committee recalls the importance of applying these principles and their guidelines to ensure a strong liquidity risk management framework. Liquidity requirements, the liquidity coverage ratio and the Net Stable Funding Ratio complete these principles to ensure a robust liquidity risk management.

Considering the evolution on financial markets since 2008 (digitalisation, new payment systems, use of central clearing derivatives, risks of cyber-attacks…), the Basel Committee concludes that the principles must be applied to ensure a good level of liquidity in the market.

14th January 2019: The Basel Committee publishes an update of Minimum capital requirements for market risk

Following the Basel Committee work on the implementation and evolution of the standards, the Bank for International Settlement (BIS) has published on the 14th January an update of the minimal capital requirements for market risk (pillar 1). These final standards include the recommendations made in the public consultation document published in 2018.

The main elements are the following:

- A clear definition between the **trading book** and **the banking book** : the Basel Committee recalls the classification criteria to classify the different instruments, the instruments to be included in the trading book ( subject to market risk capital requirements) and the instrument to be included in the banking book (subject to credit risk capital requirements).

- An **internal model approach that set out separate capital requirements for risk factors that are deemed non-modellable**: The Basel Committee also reminds market players and competent authorities that the use of an internal model for the purposes of determining market risk capital requirements is conditional upon the explicit approval of the bank's supervisory authority.

- A **standardised model approach that would be more sensitive and well calibrated to be used as a credible fall back to the internal models approach:** The Basel Committee also recalls the general provisions and the structure of the standardised approach for calculating risk-weighted assets for market risk.

The 2019 revision of the standards also adds the following elements:

- A simplified standardised approach for banks with small or non-complex trading portfolios;
- A clarification of the instruments under the scope of the market risk capital requirements;
- A new standardised approach for the risk management of foreign exchange risk and index instruments;
- A new standardised approach for risk weights that would be applicable for general interest rate risk, foreign exchange and certain exposures subject to credit spread risk;
- A review of the assessment process which determine whether the internal model of a bank does reflect the risk of individual trading desk;
- A review of the requirements for the identification of risk factors eligible for an internal model.

***Next steps***

These new standards will apply as of 1st January 2022.

4th January- Non-performing loans: the final compromise between the European Parliament and the Council have been published

Following the political agreement reached between the Parliament and the Council in December 2018, the final compromise has been published.

1. **The scaling of the minimum coverage level**

The co-legislators had no difficulties in finding an agreement regarding the scaling of the minimum coverage level as the final report of the ECON committee and the position of the Council were close.

- ✓ **Unsecured loans**:

  **Banks will have to provide for a 100% coverage 3 years after the loan has been declared as non-performing**. As a reminder, the Commission had proposed a 100% coverage after 2 years.

**Banks will provide for at least 35% of their exposure to unsecured loans two years after they go non-performing and then full coverage after 3 years.**

✓ **Secured loans:** the calendar agreed between the co-legislators will be the following:

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However, it should be noted that the wording of the article 47c(3) regarding the scaling up of the minimum coverage level for loans secured by movable collateral has been amended. Whereas the European Parliament suggested "*secured by movable property or other eligible collateral*" , the agreement provides "*secured by other funded or unfunded credit protection".* This change does not change the sense of the article but specifies it.

**Please find below a summary table of the calendar agreed between the Council and the European Parliament:**

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| | Secured | Immovable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 70% | 80% | 85% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 80% | 100% | 100% | 100% | 100% |

2. **Derogations for non-performing exposure guaranteed or insured by an official export credit agency and is case of forbearance measure**

The agreement between the Parliament and the Council confirmed the introduction of two derogations as suggested by the ECON rapporteurs.

- **A derogation for non-performing exposure guaranteed or insured by an official export credit agency (article 47c (3)(a)):**

In this situation, the scaling up of minimum coverage level will be the following:

- **0** for the secured part of the non-performing exposure to be applied during the period between **one year and seven years following its classification as non-performing**
- **1** for the secured part of the non-preforming exposure to be applied as the **first day of the eighth year following its classification as non-performing**

- **Derogation in the case of forbearance measure (article 47c(5)(a))**

When an exposure has been granted a forbearance measure, the scaling of the minimum coverage is modified:

- **For unsecured loans**: Between **one year and two years** following its classification as non-performing, the factor applicable( according to the scaling reproduced above) at the moment the forbearance measure is granted shall be applicable for **an additional period of one year**

- **For secured loans**: Between **two and six years** following its classification as non-performing, the factor applicable (according to the scaling reproduced above) at the moment the forbearance is granted shall be applicable for **an additional period of one year.**

3. **Date of entry into force :**

The regulation will not be backdated from March 2018 as suggested by the European Commission but will be applicable for loans subscribed after the entry into force of the regulation.

18th December 2018- The Parliament and the Council reach an agreement on NPLs

On the 18th of December, the European Parliament and the Council have easily reached an agreement on the NPLs regulation proposal.

1. **The scaling of the minimum coverage level**

The co-legislators had no difficulties in finding an agreement regarding the scaling of the minimum coverage level as the final report of the ECON committee and the position of the Council were close.

✓ **Unsecured loans**:

**Banks will have to provide for a 100% coverage 3 years after the loan has been declared as non-performing**. As a reminder, the Commission had proposed a 100% coverage after 2 years.
**Banks will provide for at least 35% of their exposure to unsecured loans two years after they go non-performing and then full coverage after 3 years.**

✓ **Secured loans:** the calendar agreed between the co-legislators will be the following:

- **Secured by immovable collateral:** 25% after 3 years, 35% after 4 years, 55% after 5 years,70% after 6 years, 80% after 7 years, 85% after 8 years, 100% after 9 years

- **Secured by movable collateral:** 25 % after 3 years, 35% after 4 years, 55% after 5 years, 80% after 6 years, 100% after 7 years

However, it should be noted that the wording of the article 47c(3) regarding the scaling up of the minimum coverage level for loans secured by movable collateral has been amended. Whereas the European Parliament suggested "*secured by movable property or other eligible collateral*" , the agreement provides "*secured by other funded or unfunded credit protection*". This change does not change the sense of the article but specifies it.

**Please find below a summary table of the calendar agreed between the Council and the European Parliament:**

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Council and European Parliament agreement | Unsecured | | 0% | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 70% | 80% | 85% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 25% | 35% | 55% | 80% | 100% | 100% | 100% | 100% |

2. **Derogations for non-performing exposure guaranteed or insured by an official export credit agency and is case of forbearance measure**

The agreement between the Parliament and the Council confirmed the introduction of two derogations as suggested by the ECON rapporteurs.

- **A derogation for non-performing exposure guaranteed or insured by an official export credit agency (article 47c (3)(a)):**

In this situation, the scaling up of minimum coverage level will be the following:

- **0** for the secured part of the non-performing exposure to be applied during the period between **one year and seven years following its classification as non-performing**
- **1** for the secured part of the non-preforming exposure to be applied as the **first day of the eighth year following its classification as non-performing**

- **Derogation in the case of forbearance measure (article 47c(5)(a))**

When an exposure has been granted a forbearance measure, the scaling of the minimum coverage is modified :

- **For unsecured loans**: Between **one year and two years** following its classification as non-performing, the factor applicable( according to the scaling reproduced above) at the moment the forbearance measure is granted shall be applicable for **an additional period of one year**
- **For secured loans**: Between **two and six years** following its classification as non-performing, the factor applicable (according to the scaling reproduced above) at the moment the forbearance is granted shall be applicable for **an additional period of one year.**

3. **Date of entry into force :**

The regulation will not be backdated from March 2018 as suggested by the European Commission but will be applicable for loans subscribed after the entry into force of the regulation.

17th December 2018- The EBA publishes its guidelines on disclosure of non-performing and forborne exposures

On the 17th of December, the European Banking Authority (EBA) has published it guidelines on the disclosure of non-performing exposure and forborne exposure.

The disclosure of information allows market players to have better view of the state and quality of the banks' assets and the main characteristics of non-performing exposures and forbearance measures held by the bank.

With these guidelines, EBA aims at improving the disclosure requirements and uniform disclosure formats applicable to the financial institutions in order to foster transparency and provide relevant and meaningful information to the market players. These guidelines set concrete templates on the content and format of the information disclosed which will remedy the asymmetries of information, allowing an easier comparison between the players on their level of non-performing loans and forbearance measures.

The principles of proportionality will apply with distinct rules for significant credit institutions with a gross NPL ratio above 5%.

For all credit institutions, the following templates will apply:

- Template 1: Credit quality of forborne exposures
- Template 3: Credit quality of performing and non-performing exposures by past due days
- Template 4: Performing and non-performing exposures and related provisions
- Template 9: Collateral obtained by taking possession and execution processes

For credit institutions with a gross NPL ratio above 5%, specific templates will apply:

- Template 2 : Quality of forbearance
- Template 5: Quality of non-performing exposures by geography
- Template 6: Credit quality of loans and advances by industry
- Template 7: Collateral valuation – loans and advances
- Template 8: Changes in the stock of non-performing loans and advances
- Template 10: Collateral obtained by taking possession and execution processes – vintage breakdown

**Next steps**

These guidelines will apply as of 31th December 2019.

<u>11th December 2018 – the Basel committee on Banking Supervision publishes its updated framework on pillar 3 disclosure requirements</u>

On the 11th of December, the Basel Committee has published its updated framework on disclosure requirements.

As a reminder, Pillar 3 on disclosure requirements aims at promoting market discipline through the publication of regulatory information.

The Committee updates the disclosure requirement on the following fields:

- credit risk, operational risk, the leverage ratio and credit valuation adjustment risk
- risk-weighted assets ( calculated with banks' internal model with the standardised approaches)
- risk management and key prudential metrics

The new updated framework also add new disclosure requirements on asset encumbrance and capital distribution.

**Next steps**

These new disclosures requirement will apply as of 1st January 2022 just as the Pillar 1 framework (minimum capital requirements). There is however one exception for the disclosure of asset encumbrance and capital distribution constraints which will benefit from a one year extension and will therefore apply as of end 2022.

<u>6th December 2018- the European parliament adopts its final report on Non-performing loans (NPL)</u>

On the 6th of December 2018, the ECON committee adopted, with a large majority, its report on the Commission's regulation proposal as regards minimum loss coverage for non performing exposures (NPLs).

1. **<u>Main elements</u>**

   a) **<u>The scaling of the minimum coverage level</u>**

As a reminder, in the draft report, the rapporteurs Esther de Lange (EPP, NL) and Roberto Gualtieri (S&D,IT) suggested to modify the calendar of the minimum coverage level. Despite many amendments tabled by Markus Ferber (EPP, DE), Sven Giegold (Greens, DE) et Paul Tang (S&D, NL), the calendar of the coverage remains the same (see the summary table below).

- **For unsecured loans** (article 47l(2)l), the rapporteur suggests to kick-off the full coverage as ***of the first day of the fourth year*** following its classification as non-performing.

- **For secured loans** , the rapporteurs suggest a distinction between ( distinction also made by the Council):

    - **Loans secured by immovable collateral**: **0, 20** ***coverage*** to be applied during the period between ***the first and the last day of the fourth year*** following its classification as non-performing with a full coverage starting as of the eighth year. For the first three years, there is no coverage (as suggested by the rapporteurs).

    - **Loans secured by movable collateral: 0, 23** coverage to be applied during the period ***as of the first day of the fourth year*** following its classification as non-performing (amendment 44) with a full coverage starting as of the eighth year. For the first three years, there is no coverage (as suggested by the rapporteurs). As a reminder, the Council provides for a full coverage building up after 7 years.

**b) Derogation to the part of the non-performing exposure guaranteed or insured by an official export credit agency (article 47c (3a))**

The ECON Committee suggests to include a derogation to the calendar of minimum coverage level to the part of the non-performing exposure guaranteed or insured by an official export credit agency:

- **0** for the secured part of the non-performing exposure to be applied during the period between **one year and seven years** following its classification as non-performing
- **1** for the secured part of the non-performing exposure to be applied **as of the first day of the eighth year** following its classification as non-performing

**c) Derogation where an exposure has been granted a forbearance (article 47c (5a))**

When a loan has been granted a forbearance, the rapporteurs suggest to extend by one year the factor applicable at the moment the forbearance measure is granted:

- **For unsecured loans** : **between one year and two years** following its classification as non-performing, the factor applicable at the moment the forbearance measure is granted shall be applicable **for an additional period of one year**
- **For secured loans**: **between two and six years** following its classification as non-performing, the factor applicable at the moment the forbearance measure is granted shall be applicable **for an additional period of one year.**

**Please find below a summary table of the coverage level as provided by the European Commission, the Council of the EU and the ECON committee:**

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| EC | Unsecured | Past due more 90 days | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | | Not past due more than 90 days | 0% | 28% | 80% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Past due more 90 days | 0% | 5% | 10% | 17.5% | 27.5% | 40% | 55% | 75% | 100% | 100% | 100% |
| | | Not past due more than 90 days | 0% | 4% | 8% | 14% | 22% | 32% | 44% | 60% | 80% | 100% | 100% |
| Council | Unsecured | | 0% | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 25.5% | 41.5% | 69% | 80% | 80% | 85% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 25.5% | 41.5% | 69% | 80% | 100% | 100% | 100% | 100% |
| ECON Committee | Unsecured | | 0% | 0% | 0% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 20% | 30% | 40% | 55% | 75% | 80% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 23% | 35% | 50% | 80% | 100% | 100% | 100% | 100% |

**d) Guidelines on a common methodology for the determination of the secured part of a non-performing exposure**

The European Banking Authority (EBA) will be asked to include a common methodology for the determination of the secured part of a non-performing exposure in the guidelines to be drafted ( article 47c (5)).

**2. Others elements**

In its report, the ECON Committee stresses the fact that *"consumers should not be deemed exclusively responsible for the cause of the severe build-up of NPEs during the years of the financial crisis" (recital 1a).*

4th December 2018 : CRD V / CRR II : an agreement in trilogue

On December, 4th 2018, the Council of the EU and the representatives of the European parliament have finalised the inter-institutional negotiations on the banking package which aims at reducing risks in the EU banking sector. This agreement comes 2 years after the publication by the European Commission of two legislatives proposals reforming the Capital Requirement Directive (CRD IV) and the Capital Requirement Regulation (CRR). These proposals are intended at implementing reforms agreed by the Basel Committee on Banking Supervision and by the Financial Stability Board (FSB).

- Commission's Proposal amending CRD IV
- Commission's Proposal amending CRR

**The final text is not available** yet but you will find below the pre-agreement which includes 90% of the final provisions.

**A. Points of interest for EUF**

- **Proportionality**

The agreement provides a definition for "***small and non-complex institutions***" would be provided for and accompanied by reduced reporting and disclosure requirements in order to lower compliance costs for these entities.

To be qualified as " ***small and non-complex institutions***", the entities will have to fill the following conditions ( article 4):

- ✓ the total value of its assets on an individual basis or on a consolidated basis is on **average equal to or less than the threshold of EUR 5 billion over the four-year period** immediately preceding the current annual reporting period.
- ✓ the institution is subject to **no or simplified obligations** in relation to recovery and resolution planning
- ✓ the institution's trading book business is classified as small
- ✓ the total value of the institution's derivative positions held with trading intent **does not exceed 2% of its total on- and off-balance sheet assets**, the total value of its overall derivative positions does not exceed 5%, both calculated according to article 273a(3);
- ✓ more than **75% of both the institution's consolidated total assets and liabilities**, excluding in both cases the intragroup exposures, relate to activities with counterparties located in the European Economic Area;
- ✓ the institution **does not use internal models to meet the prudential requirements** that it is subject to in accordance with this Regulation except for subsidiaries using internal models developed at the group level, provided that the group is subject to the disclosure requirements laid down in article 433a or in article 433c at consolidated level.
- ✓ the institution has not communicated to the competent authority an objection to being classified as a small and non-complex institution;
- ✓ the competent authority has not decided that the institution is not to be considered a small and non-complex institution based on an analysis of its size, interconnectedness, complexity or risk profile.

The European Banking Authority (EBA) will be in charge of drafting recommendations on how to reduce reporting requirements for small and non-complex institutions which should result in an expected average cost reduction.

- **<u>Preferential treatment for factoring when it comes to the implementation of the the Net Stable Funding Ratio (NSFR)</u>**

Based on the European Parliament's definition, factoring is defined in a EU legislative text for the first time ( article 411) as such factoring means :

"a contractual agreement between a business (assignor) and a financial entity (factor) in which the assignor assigns or sells its receivables to the factor in exchange of providing the assignor with one or more of the following services with regard to the receivables assigned:

(a) advance of a percentage of the amount of receivables assigned, generally short term, uncommitted and without automatic roll-over,

(b) receivables management, collection and credit protection whereby in general, the factor administers the assignor's sales ledger and collects the receivables in its own name.

**Factoring will benefit from be applied the same treatment as trade finance *(5% - 7.5% - 10%)* regarding the calibration of the net stable funding ratio.**

- **<u>Simplified Net Stable Funding Ratio (sNSFR) (article 428 ah)</u>**

The agreement follows the European Parliament's position: entities qualified as "*small and non-complex*" will benefit from a simplified version of the NSFR in order to reduce their administrative burden. In practice, this simplification results in fewer data points to be collected for calculation and reporting purposes.

- **Liquidity and prudential capital management at group level**

The agreement follows the Council's approach on all home-host related provision. **The Council proposed to suppresses the revision of articles 7 and 8 of the European Commission regarding the consolidated management by parents companies of liquidity and capital requirements waivers granted at the individual level**

- **Leverage ratio**

**The negotiators agreed to a binding 3% leverage ratio and an additional 50% buffer for global systemically important institutions (GSIIs).**

- **SME supporting factor**

In its proposal, the European Commission had suggested to reduce certain capital requirements to support lending to small and medium sized enterprises and infrastructure projects by extending the scope of the so called "*supporting factors*" for such entities or activities.

The agreement provides for an extension of the existing supporting factor for loans to **SMEs in an amount up to euros 2.5 million** (which is currently set at 1.5 million).

**B. Others points of interest for EUF**

- **Intermediate Parent Company (IPU)**

The ECB directly supervises the 118 significant banks of the participating countries. These banks hold almost 82% of banking assets in the euro area. The decision on whether a bank is deemed significant is based on a number of criteria such as having a total value of assets exceeding euros 30 billion. Banks which do not reach this threshold are under the supervision of national Competent Authorities (NCAs). In order to avoid the supervision of the ECB, some banks create several subsidiaries which stay under the thresholds of euros 30 billion.

The negotiators decided to act against this practice by requesting large non-EU banking groups with two or more subsidiary institutions in the EU to establish an IPU to consolidate all their activities in the Union under that IPU. The objective is to facilitate group supervision and enhance the resolvability of the firms in scope.
The agreement provides for the following conditions:

- the threshold triggering the creation of **an IPU is set at € 40 billion balance sheet assets** in the EU including those held by third country branches (both those of credit institutions and investment firms).
- Global Systemically Important Institutions (G-SIBs) **are not automatically captured by the requirement** if they do not meet the threshold in the EU
- IPUs may be set up as investment firms
- a transitional period of 3 years would be provided
- EBA would issue a report on the treatment of third country branches under Member States' laws

- **Anti Money laundering**

The agreement follows the European Parliament's position which suggests to enhance the cooperation and exchange of information between prudential supervisors, financial intelligence units (FIUs) and competent authorities for Anti-money laundering and combatting the financing of terrorism (AML/CFT).
The negotiators introduced an authorisation procedure ( article 8 CRD), designed the EBA to draft regulatory technical standards (RTS) and an exchange of information ( article 56).
Additional amendments would be made to strengthen the AML dimension in the relevant prudential tools on authorisation, fit and proper checks and supervisory review and evaluation process (SREP).

- **Insolvability**
  Institutions that are failing or likely to fail, but not subject to resolution, would be wound up in an orderly manner in accordance with the applicable national law.

- **intangible assets (Software)**

The agreement provides for an exemption from deductions of certain intangible software assets (intangible assets) is granted from own funds items provided that its value is prudentially valued and loss absorbing also in a gone concern situation.
This provision follows the European Banking Federation and aligns the EU legislative framework with the US legislation.

- **Environmental, social and governance risks (ESG)**

EBA will prepare a report on the introduction of environmental, social and governance (ESG) risks in the risk management process. If appropriate, EBA might adopt guidelines for the inclusion of ESG risk in the supervisory review and evaluation process. Banks would also be subject to additional disclosures concerning these risks.

**C. Shadow banking**

The representatives of the European Parliament and Council held the last trilogue on Tuesday 4th in order to finalise the inter-institutional agreement **on shadow banking**, remuneration and off-balance sheet guarantees to CIUs (Collective Investment Undertakings).

Regarding the treatment of shadow banking, unlike the Council, the Commission and the EP want the EBA guidelines released in December 2015 on the "*Limits on exposures to shadow banking entities which carry out banking activities outside a regulated framework under Article 395(2) of Regulation (EU) No 575/2013 (CRR)* to become regulatory technical standards (RTSs), which will make them legally binding.

The EP would even like the EBA to "*develop a methodological standard for competent authorities specifying an appropriate aggregate limit on exposures to shadow banking (SB) entities which carry out banking activities outside a regulated framework, as well as individualized exposure limits to such entities".*

Outcomes of the negotiations are not currently know, we will come back with more details once the final agreement is published.

26th November 2018 – Banking supervision: Basel Committee's meeting and of the International Conference of Banking Supervisors (ICBS)

On November, 26th 2018, the Basel Committee on Banking Supervision and the International Conference of Banking Supervisors met to discuss the challenges of the banking supervision.

The Basel Committee decided to revise the market risk framework, which will be submitted to Group of Central Bank Governors and Heads of Supervision (GHOS): the aim of the revision is to enhance the risk sensitivity of the standardised approach, revise the calibration of certain elements of the framework and improve certain aspects of the internal models approach. If approved by the GHOS, the framework would be publish in 2019

The Basel Committee also agreed to launch a public consultation in order to enhance the disclosure in order to reduce bank window-dressing on the leverage ratio and approved the revision to the pillar 3 disclosure

November 2018: the Basel Committee publishes its report on the implementation of the Basel III regulatory reforms

In November 2018, the Basel Committee published its report on the progresses made by the 27 jurisdiction members of the Basel Committee on Banking Supervision (BCBS) in implementing the Basel III regulatory reforms.

This report assesses the members' progresses in adopting the Basel III standards, the consistency of domestic (national or regional) banking regulations with the Basel III standards and the prudential outcomes of those regulations.
The report concludes that the standards for capital, liquidity and global systemically important banks (G-SIBs) have generally been transposed into domestic regulations. The requirements on the risk-based standards and on the Liquidity Coverage Ratio (LCR) are enforced by all the members.

Some members are also working to adopt other standards such as:
- The margin requirements for non-centrally cleared derivatives,
- **The Net Stable Funding Ratio (NSFR),**
- **The leverage ratio,**
- The revised securitisation framework,
- **The standardised approach for measuring counterparty credit risk exposures (SA-CCR),**
- The capital requirements for bank exposures to central counterparties (CCPs)
- **The revised Pillar 3 disclosure requirements.**

13th November 2018 – the state of the Banking Union after 4 years

Sabine Lautenschläger, Member of the European Central Bank Executive Board and Vice-Chair of the Supervisory Board of the Single Supervisory Mechanism, delivered a speech taking stock of 4 years of Banking Union.

According to the ECB, European regulation reinforced the banking sector making it more secure and resilient. For instance, today, banks hold more and better-quality capital than in the past. The minimum capital ratio increased by 2.6% between 2014 and 2018.

Moreover, banks have a lower stock of non-performing loans (NPLs) on their balance sheets: for banks under the supervision of the ECB, the level of NPLs rose from 958 billion when the single supervisory mechanism was set up to 688 billion in the first quarter of 2018.

The Single Supervisory Mechanism is not the only pillar of the Banking Union. Stricter regulation does not mean that there will be no other bank bankruptcy. Sabine Lautenschläger considers indeed that it is not to the ECB to prevent bank failures. Banks can leave the market if they are managed in a risky and dangerous way or if they are unable to maintain their competitiveness based on a suitable economic model.

Despite the progress made over the past four years, European supervisors remain cautious and continue to monitor banks with the support of European legislators. Sabine Lautenschläger estimates banks must seize the opportunity given by the current financial stability to clean up their balance sheets and adapt their business model.

9th November 2018: ECB publishes final guides for banks on their capital and liquidity management (ICAAPs et ILAAPs)

The European Central Bank (ECB) has published its guides for banks regarding their ***internal capital and liquidity adequacy assessment processes*** (ICAAPs) and their ***Internal Liquidity Adequacy Assessment Process*** (ILAAPs) and ILAAPs).
These guides, which are **not legally binding**, aim to assist banks in strengthening their ICAAPs and ILAAPs, and to encourage the adoption of best practices. Indeed, adequate levels of capital and liquidity are essential for the resilience of individual banks.

As a reminder, Internal Capital Adequacy Assessment Processes (ICAAPs) and Internal Liquidity Adequacy Assessment Process (ILAAPs) aim at supporting banks in their assessment processes on their level of capital and liquidity. Financial institutions must assess the risks and ensure that all the risks are identified, effectively managed and covered by an adequate capital and liquidity levels at all times.

In 2019, the ECB will increase its supervision assessment on ICAAPs and ILAAPs to incentivise banks to improve their ICAAPs and ILAAPs. Every year, the ECB reviews the quality of the banks' ICAAPs and ILAAPs as part of the Supervisory Review and Evaluation Process (SREP).

**Application date:**
These guidelines will apply as of **1st of January 2019.**

8th November: NPLs- State of play at the Council and the ECON Committee

On the 8th of November, the ECON Committee of the European Parliament published its draft report on the Commission proposal as regards minimum loss coverage for non-performing exposures. The rapporteurs appointed are Esther de Lange (PPE, NL) and Roberto Gualtieri (S&D, IT).

The Council of the EU adopted its common position on the 31th October.

**I. COMMISSION'S PROPOSAL**

Non-performing loans (NPLs) are one of the main risks that still threaten the European banking system. Following the Council's request, the Commission released a regulation proposal amending the Capital Requirement Regulation providing for a statutory prudential backstop against any excessive future build-up of NPLs without sufficient loss coverage on banks' balance sheet.

The Commission's proposal consists of two elements:

- ✓ A requirement for institutions to cover up to common minimum levels the incurred and expected losses on newly originated loans once such loans become non-performing( minimum coverage requirement)
- ✓ Where the minimum coverage requirement is not met, a deduction of the difference between the level of the actual coverage and the minimum coverage from Common Equity Tier 1 (CET1) items

The Commission's proposal is built on the principle that the longer an exposure has been non-performing, the lower is the probability to recover the amounts due. The Commission is therefore proposing a scaling-up with the minimum coverage requirement increasing gradually depending on how long an exposure has been classified as non-performing, in accordance with a prescribed timetable.

The Commission's proposal also include two others distinctions:

- ✓ Between secured and unsecured non-performing exposure (NPE): due to the high risk of unsecured loans, the timetable is stricter.
- ✓ Between non-performing exposures where the obligator is past due more than 90 days and other NPEs and other NPEs: the timetable proposed by the Commission is different whether the exposure is non performing because the debtor's arrears are greater than 90 days. When the arrears are greater than 90 days, the minimum coverage requirement is higher.

The Commission is proposing the following timetable:

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| EC | Unsecured | Past due more 90 days | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | | Not past due more than 90 days | 0% | 28% | 80% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Past due more 90 days | 0% | 5% | 10% | 17.5% | 27.5% | 40% | 55% | 75% | 100% | 100% | 100% |
| | | Not past due more than 90 days | 0% | 4% | 8% | 14% | 22% | 32% | 44% | 60% | 80% | 100% | 100% |

## II. COUNCIL'S COMPROMISE

The Council of the EU adopted its common position on the 31th October.

The Council introduced a distinction between the loans secured by immovable and movable collaterals.

- ✓ For secured NPLs
  - o With immovable collateral (commercial or residential real estate) the proposal provides a gradual increase of the minimum loss coverage level over a period of 9 years.
  - o With movable collateral secured by movable and other CRR eligible collateral, the full coverage will have to be built up after 7 years.
- ✓ For unsecured NPLs the maximum coverage requirement would apply fully after 3 years, i.e. one year more than in the EU Commission's proposal.

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Council | Unsecured | | 0% | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 25.5% | 41.5% | 69% | 80% | 80% | 85% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 25.5% | 41.5% | 69% | 80% | 100% | 100% | 100% | 100% |

## III. ECON COMMITTEE'S DRAFT REPORT

The ECON rapporteur proposes to modify the scaling-up of the coverage and introduces the same distinction between secured loans with immovable collateral and movable collateral.

- ✓ **Unsecured loans:** the rapporteur suggests to kick-off the full coverage as of the first day of the fourth year following its classification as non-performing (amendment 37).
- ✓ **Secured loans :**
  - 20% coverage to be applied during the period between the first and the last day of the fourth year following its classification as non-performing with a full coverage starting as of the eighth year. For the first three years, there is no coverage (as suggested by the rapporteurs).
  - 23% coverage to be applied during the period as of the first day of the fourth year following its classification as non-performing (amendment 44) with a full coverage starting as of the eighth year. For the first three years, there is no coverage (as suggested by the rapporteurs).

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| ECON Committee | Unsecured | | 0% | 0% | 0% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 20% | 30% | 40% | 55% | 75% | 80% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 23% | 35% | 50% | 80% | 100% | 100% | 100% | 100% |

**Summary table of the coverage level as provided by the European Commission, the Council of the EU and the ECON committee**

| After Years | | | 0 | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| EC | Unsecured | Past due more 90 days | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | | Not past due more than 90 days | 0% | 28% | 80% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Past due more 90 days | 0% | 5% | 10% | 17.5% | 27.5% | 40% | 55% | 75% | 100% | 100% | 100% |
| | | Not past due more than 90 days | 0% | 4% | 8% | 14% | 22% | 32% | 44% | 60% | 80% | 100% | 100% |
| Council | Unsecured | | 0% | 0% | 35% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 25.5% | 41.5% | 69% | 80% | 80% | 85% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 25.5% | 41.5% | 69% | 80% | 100% | 100% | 100% | 100% |
| ECON Committee | Unsecured | | 0% | 0% | 0% | 100% | 100% | 100% | 100% | 100% | 100% | 100% | 100% |
| | Secured | Immovable collateral | 0% | 0% | 0% | 20% | 30% | 40% | 55% | 75% | 80% | 100% | 100% |
| | | Movable collateral | 0% | 0% | 0% | 23% | 35% | 50% | 80% | 100% | 100% | 100% | 100% |

Next steps: **The Members of the ECON Committee had until the 23rd of November to table their amendments on the draft report.**
**The trilogue negotiation will start after the The vote on the ECON Committee's final report which is scheduled for the 6th of December.**

31th October 2018 – EBA publishes its Guidelines on management of non-performing and foreborne exposures

On October, 31th, the EBA published its Guidelines on management of non-performing and foreborne exposures. As part of the Council Action Plan to tackle non-performing loans (NPLs) in Europe , the EBA was asked to contribute to this Action Plan in particular in supervisory actions to works with banks to improve strategies to reduce NPEs.

**Objectives of these guidelines**

The Guidelines require institutions to establish NPE reduction strategies. To that end, an appropriate governance structure and operational set-up should be in place to facilitate this objective. The guidelines outline the key elements of governance and operations in relation to an NPE workout framework, covering key aspects related to steering and decision-making, the NPE operating model, the internal control framework and NPE monitoring processes.

**Definition of non-performing exposures (NPEs) and foreborne exposures(FBEs):**

1. **NPEs:** A non-performing exposure is an exposure that is:
   - **90 days past-due** (material exposure) **or unlikely to be repaid in full** without collateral 52tandardiza (irrespective of any past-due amount or of the number of days past-due), or
   - **Impaired or defaulted** according to the applicable accounting or regulatory frameworks.

The Guidelines tackle another topic related to NPEs which are foreborne exposures. The definitions of foreborne exposures and NPEs were subject to internal work of the EBA since 2013 (see Power point presentation attached).

2. **Forbearance measures** are defined as **concessions** towards a debtor facing or about to face financial difficulties (loans, debt securities, commitments – no trading exposures). These concessions consists of:
   - **Modification of the terms and conditions of the contract** that would not have been granted had the debtor not been in financial difficulties (judgment in identifying of financial difficulties). For example more favorable terms than the previous terms of the contract or than the terms of other debtors with a similar risk profile, use of embedded forbearance clauses
   - **Total or partial refinancing of an exposure** that would not have been granted had the debtor not been in financial difficulties. For example total or partial repayment of a debt contract with the proceeds from another debt contract.

The guidelines stress that any forbearance measures should be granted only **when they aim to restore sustainable repayment by the borrower** and are thus in the borrower's interests. These guidelines set out requirements relating to processes for recognising NPEs and FBEs, as well as a forbearance-granting process with a focus on the viability of forbearance measures. Credit institutions are expected to monitor the efficiency and effectiveness of forbearance measures and have in place policies and processes to assess borrowers' financial difficulties and identify NPEs.

**Summary of the guidelines**

- **Risk management practices for credit institutions for the management of NEPs and FBEs**: requirements on NPE reduction strategies, governance and operations of NPE workout framework, internal control framework and monitoring

- **Requirements to recognise NPEs and FBEs and the granting of forbearance measures**: The guidelines specify that credit institutions should grant forbearance measures only with the view to return the borrower to a sustainable performing repayment status.

- **Introduction of a 5% threshold of gross NPL ratio to trigger the development of NPE strategies**: The EBA explains that these threshold does not indicate an optimal level for NPLs in a credit institution. The 5% thresholds must not be seen as an automatic target but more as a reference to set a prudential framework for stricter supervisory monitoring. The 5% gross NPL ratio aims at ensuring a minimum level of transparency, and to ensure that credit institutions are prepared to prevent NPEs building up and to take action at an early stage to tackle the issue.

The guidelines will apply as of **30th June 2019.**

3rd September 2018: NPLs – the exchange of views in the ECON committee

On 3rd September 2018, an exchange of views took place in the Economic and Monetary Affairs Committee (ECON) of the European Parliament on the **EU Commission proposals aiming to reduce the level of non-preforming loans (NPLs) in the EU** and especially :

- ✓ the proposal of Regulation on minimum loss coverage for non-performing exposures
- ✓ the proposal of Directive on credit servicers, credit purchasers and the recovery of collateral

**Relevant information for the EUF:**

1. **Differentiation between NPLs and dedicated prudential approach on financial institutions**

The EU Commission proposes to apply different minimum loss coverage requirements depending on the types of NPLs (secured/ non secured, more or less than 90 days past due threshold).

**Co-Rapporteur Esther de Lange (EPP, NL)** wants to avoid to have too many categories of NPLs and considers that some further options – independent assessment, types of forbearance – were too complex and not relevant.

Co-rapporteur Roberto Gualteri (S&D, IT) believes that a key part of the proposal is to maintain a two-pillar system – a **minimum** compulsory backstop together with a **bank-specific pillar**, decided by competent authorities. This provision should guarantee a case-by-case adapted mechanism.

2. **90-day past due threshold**

Esther de Lange casts into doubt the relevance of a **time factor, especially the 90-day threshold of non-payment in due time**. As a reminder, the Commission proposed stricter provisions for non-performing exposures (NPEs) for which the obligor is past due more than 90 days. The rapporteur considers that making a distinction based on a time factor rather than “other reasons” is not a clear cut proposal.

**Shadow rapporteur Ramon Tremosa (ALDE, ES)** considers that **the misapplication of the Late-Payment Directive is at the origin of the high level of non-performing loans in some Member States**. According to him, multinationals and public institutions which do not pay SMEs on time are responsible of their financial difficulties.

3. **Scope of the regulation**

Esther de Lange (EPP, NL) and shadow rapporteurs Sander Loones (ECR, BE) and Sven Giegold (Greens, DE) expressed concerns about current stocks of NPLs as the **Commission's proposal covers only loans issued before the 14th March 2018.**

According to them, **loans issued before that date should also be regulated / taken into account, whether by this text or another regulatory initiative.** This could have a huge impact on EUF's members.

**Next steps: ECON agenda**
- **Consideration of draft report 22nd October**
- Deadline for amendment 26th October
- Consideration of amendments 19th and 20th November
- **Vote in ECON 3rd December**

29th August: NPLs: Member States doubtful regarding the accelerated extrajudicial execution mechanism

In a working paper prepared ahead of an attachés meeting, the Austrian Presidency of the Council of the European Union (EU) takes stocks of progress on title V of the proposal for a directive on non-performing loans (NPLs) which the European Commission published on 14th March 2018. As this working paper is not public, please find it attached in the e-mail.

Title V of the proposed directive sets out an accelerated extrajudicial collateral execution (AECE) mechanism, which aims at making collateral more rapidly and efficiently executable.

The Presidency working paper notes that, in general, Member States support the European Commission's objective to ease and to speed up collateral execution. However, several Member States voiced doubts regarding whether or the AECE would be the most appropriate instrument.

The working paper also mentions that some Member States doubt that there is any need to harmonise collateral execution, and thus questions the existence of Title V of the proposed NPLs directive. They consider that national frameworks already exists to address this issue and function properly. In particular, some Member States raised constitutional concerns regarding the application of AECE to immovable assets.

The main elements being scrutinised by the working group at the Council of the EU are:
- The scope of the proposed directive: articulation of the AECE with judicial processes, exclusion of consumer credit, different sorts of collateral being covered by the AECE;
- Impact on third parties (in cases where a third party might own the collateral);
- Conflicts of laws;
- Enforcement: enforcement event, directly enforceable title, notification, different types of parties involved;
- Right to challenge;
- Transfer of secured credit agreements to a third party.

Legislative works on this text are still at an early stage. The European Parliament has not yet published its draft report.

11th July 2018: NPLs – the EESC warns against the "one size fits all" approach

On 11 July 2018, the European Economic and Social Committee (EESC) adopted an opinion on the Commission's proposals for a regulation and a directive presented last March which aim to impose a minimum loss cover on non-performing exposures (NPEs) and to develop secondary non-performing loan markets (NPLs) at European level.

**While the EESC welcomes the Commission's initiative on provisioning, it warns against any "one size fits all" approach** that "*does not take into account the differences that still exist in national civil laws*".

Similarly, the Committee is **concerned about the timing of the provisioning of new non-performing loans**, which "***may force the banks to sell them quickly, rather than waiting for the financially distressed company to return to a more viable situation***". The Committee believes that this "*could reduce the possibility of allowing for a debt restructuring and a giving entrepreneurs a second chance, with a potentially high negative social impact and negative impact on the employment ratio*".

Therefore, the EESC suggests **launching a new impact assessment** to evaluate "*the potential impact of the proposed regulation on banks, on the transmission of credit to households, on SMEs and on GDP growth*."

**The EESC calls on the Commission to adopt specific treatment for "*smaller and specialised firms with a less complex asset structure* ".**

**The Committee also believes that all EU banks should also be subject to IFRS 9.**

**With regard to the development of secondary markets**, the EESC considers that "***regulators should not encourage the sale of the non-performing loans***" because "***managing impaired loans within banks could imply a higher value through their recovery than the prices collected for their sale*** ". The Committee is also concerned about consumer and worker protection issues.

28th June 2018: CRR 2/ CRD 5: publication of the reports adopted by the ECON Committee

The Committee for economic and monetary affairs (ECON) of the European Parliament published the reports on CRR2 and on CRD 5 adopted on 19th June 2018.

As a reminder, the European Commission published in November 2016 its banking package proposal aiming at reducing risks in the banking sector and including the following legislative initiatives:

- **Proposals to review the regulation and directive on capital requirements (CRR2/CRD5) ;**
- Proposals to review the Baking Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism Regulation (SRMR) (BRRD2/SRMR2).

At the European Parliament, reports on CRR2 and CRD 5 were attributed to Peter Simon (S&D, DE) and reports on BRRD2 and SRMR2 to Gunnar Hökmark (EPP, SE).

**AMENDMENTS ADOPTED**

Among the amendments which have been adopted on June 19th, the following are particularly relevant for the EUF:

- **Definition of factoring, and its specific treatment for the purpose of the Net Stable Funding Ratio (NSFR)** (articles 411 and 428 of CRR)

Article 411 in its version adopted by the ECON Committee includes a new paragraph 15a, which reads as follow:

> *"(15a)* ***'Factoring' means a contractual agreement between a business (assignor) and a financial entity (factor) in which the assignor assigns or sells its receivables to the factor in exchange of providing the assignor with one or more of the following services with regard to the receivables assigned:***
> *(a) advance of a percentage of the amount of receivables assigned generally short term, uncommitted and without automatic roll-over,*
> *(b) receivables management, collection and credit protection generally the factor administering the assignor' sales ledger and collecting the receivables in its own name.*
> ***For the purposes of Part VI, factoring shall be treated as trade finance."***

**This new paragraph introduces a definition of factoring, which also serve the purpose of clarifying its treatment under Part VI on liquidity requirements.** It ensures **factoring to explicitly benefit from the same treatment as trade finance.**

- **Proportionality**

As suggested by the rapporteur Peter Simon, the definition of a small and non-complex institutions is set in article 4 of CRR 2, thus taking a more general dimension as compared to the Commission's proposal, in which the definition apply only for reporting requirements, in article 430bis.

The threshold in terms of total value of assets has been **raised to 5 billion euros in the report adopted in ECON**, while Peter Simon proposed a 1.5 billion euros threshold. The use of an internal model remains a blocking element in order to qualify as small and non-complex entity.

The report adopted by the ECON committee **maintains the possibility of a simplified NSFR**, but yet more stringently calibrated, for small and non-complex institutions which chose this option.

- **Minority interests**

While the draft report prepared by Peter Simon did not amend article 81 of CRR, the report adopted in ECON modifies the wording of article 81. It states that "*minority interests shall comprise the sum of Common Equity Tier 1* ***items of a subsidiary***" where three conditions are met. Whereas the European Commission was suggesting that an intermediate financial holding company in a third country shall be subject to the "*same rules as credit institutions of that third country*", the report adopted in ECON replaces "*same rules as*" by "*prudential requirements* ***as stringent as*** *those applied to*".

Other subsidiaries (non-third countries) do not benefit from this regime.

- **Liquidity and capital waivers**

The rapporteur Peter Simon suggested that institutions should be able to manage their liquidity (article 8 of CRR 2) and their capital (article 7 of CRR 2) at the group level, thus supporting the Commission's proposal to introduce waivers for own funds and liquidity requirements for banking groups which operate across borders.

In **article 7 regarding capital waivers**, the report adopted in ECON provides two additional conditions to qualify for a capital waiver, namely (1) the waiver cannot amount for more than 25% of the minimum own funds requirements, and (2) the parent undertaking has full control of the subsidiary. The approach of the rapporteur, based on opinions produced by the EBA, has been maintained (paragraph 2).

On the contrary, all the amendments proposed by the rapporteur on **article 8 regarding liquidity waivers** have been rejected. The initial proposal of the European Commission is maintained, as opposed to the gradual implementation proposed by Peter Simon.

- **SME supporting factor**

The SME supporting factor is maintained (article 501 of CRR 2).

**During the vote in the ECON Committee on 19th June, members of the European Parliament also voted in favour of the opening inter-institutional negotiations (trilogues), ahead of the vote in plenary session scheduled for the fall 2018.**

14th May 2018: Securitisation: IOSCO and BCBS specify criteria for short-term securitisation

The Basel Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO) published a joint report specifying the criteria to identify which short-term securitisation qualify as simple, transparent and comparable (STC). This report complements a previous edition, dated from July 2015.

The report is addressed to the financial sector and aims at clarifying the STC securitisation implementation. It adds precisions to the general STC approach, specifying its implementation to short-term securitisation and in particular to asset-backed commercial papers (ABCP). The BCBS and IOSCO notes that ABCPs are key elements of the securitisation market in some jurisdictions and that it is important to adjust the STC criteria to those products.

The report clarifies the three STC criteria:

- Simplicity, which refers to the homogeneity of underlying assets in each securitisation financed via an ABCP;
- Transparency, which implies sufficient information to investors and sponsors on underlying assets;
- Comparability, which aims at enabling investors to easily assess different products against each other and across jurisdictions.

The BCBS and IOSCO recall that the criteria they proposed are neither legally binding nor exhaustive and that they cannot replace usual due diligences.

On the same day, the BCBS published a report on the prudential regime for short-term STC securitisation. The report explains that, as long as short-term STC criteria are fulfilled, short-term STC securitisation can benefit from the same favourable prudential treatment as other STC securitisation.

| |
|---|
| The short-term STC framework is applicable as of the publication of the two reports above mentioned. |
| 7th May 2018: Basel III: the EBA is ready to work with the European Commission on the implementation<br><br>The European Banking Authority (EBA) published a press release, in response to the European Commission's call for advice, regarding the preparatory works ahead of the implementation of the so-called Basel III standards – agreed on in the framework of the Basel Committee of Banking Supervision (BCBS) – in the European Union.<br><br>In its call for advice, the European Commission mandated the EBA to assess the potential impact of the various elements of Basel III standards on the EU banking sector, and more broadly on the EU economy. It also requested the EBA to identify potential implementation challenges for EU financial institutions.<br><br>In response, the EBA announced that it will launch in July 2018 a data collection exercise, to gather both quantitative and qualitative data. The EBA indicated that it will work on this topic in cooperation with national competent authorities, actors form the financial sector, and the EU co-legislators.<br><br>The EBA has until 30th June 2019 to deliver its advice to the European Commission. |
| 23rd April 2018: Basel Committee calls for full and timely implementation of its standards<br><br>The Basel Committee on Banking Supervision (BCBS) published a press release accompanying its fourteenth progress report on the adoption of Basel standards.<br><br>As the progress report describes the state of play across jurisdictions on the adoption of Basel standards, the BCBS takes the opportunity of the press release to call for the full and timely implementation of the newest Basel standards, so called Basel III. The BCBS underlines that it expects jurisdictions to proceed to implementation of standards in a complete, consistent and timely manner.<br><br>Regarding progress in the adoption of the current Basel standards, the BCBS notes in its report that a large majority of jurisdictions have yet adopted final rules on leverage ration, net stable funding ratio (NSFR) and 58tandardizatio.<br><br>The report concludes that progress remain needed on compliance with adoption deadlines. The BCBS regrets that technical standards on counterparty credit risk measurement and on prudential requirements for banks' exposures to central counterparties have not been fully adopted in 2017 as planned. On this point, the BCBS recalls upcoming deadlines for the coming year include total loss absorbing capacity standards (TLAC) and interest rate risk (IRRB). The Basel III standards are to be progressively implemented by 1st January 2022.<br><br>The progress report examines the application of standards jurisdictions by jurisdictions. Concerning the European Union, all indicators assessed are either green (adoption process completed) or yellow (on-going adoption process) for legislation under revision. |
| 9th April 2018: annual report of the ECB calls for further risk sharing |

Vitor Constâncio, vice-president of the European Central Bank (ECB), presented the 2017annual report at the committee on economic and monetary affairs (ECON) of the European Parliament.

Vitor Constâncio recalled progress made in 2017 on the risk reduction in the financial sector. He particularly mentioned the new European standards on minimum requirement for own funds and eligible liabilities (MREL) in the event of resolution. He also took note of the reduction of private sector debt and leverage and of the satisfying level of prudential ratio in the banking sector.

Taking into account progress already made, Vitor Constâncio called on co-legislators to overcome the current obstacles to the completion of the Banking Union. In particular, he considered the European Deposit Insurance Scheme (EDIS) as a priority. Highlighting the efforts regarding risk reduction are well under way, Vitor Constâncio encouraged European co-legislators to progress on risk sharing. While mentioning that further risk reduction remains possible, mainly via the reduction of non-performing loans (NPLs) and of national options and discretions (ONDs), he called for the unblocking of the EDIS file.

In his speech, Vitor Constâncio also underlined the importance of the financial sector in transmitting the monetary policy of the ECB to the real economy. Thus, it is crucial that the financial sector is stable and resilient. Constâncio indicated that the ECB will continue its efforts in favour of financial stability. On this point, he also mentioned the importance of ensuring the appropriate regulation of banking-like activities, taking into account its growing role in the financing of the real economy. In this regard, Vitor Constâncio welcomed the European Commission's legislative proposal on investment firms, published in December 2017.

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9th April 2018: CRR/ CRD IV: the European Commission reports on effects on the economic cycle

The European Commission published its bi-annual report examining the potential pro-cyclical effects of the Capital Requirements Regulation and Directive (CRR/ CRD IV).

This report has been draft in application of article 502 of CRR, which requires the European Commission to regularly analyse the possible pro-cyclicality of the CRR/ CRD IV framework. As the report recalls, its purpose is to examine the endogenous relations between the financial system and the real economy and to identify potential amplification of the real economy cycle by prudential legislation. It recalls that the pro-cyclicality of CRRD/ CRD IV constitutes a major potential externality, which could impact financial stability.

**CONCLUSIONS OF THE REPORT**

The report notes that:

- ✓ Own fund ratios in the banking sector significantly increased since the introduction of risk sensitive requirements, in particular since 2014;
- ✓ On the contrary, risk weighted assets ratio overall decreased since 2008, with a slight uptrend from 2014 on;
- ✓ The availability of bank lending since 2008 was more affected by the financial crisis than by the new prudential requirements. However, the European Commission acknowledges that CRR/ CRD IV could have trigged a "*structural break in the regulatory regime (…) affecting the interaction between bank capital, credit and the real economy*".

Consequently, the European Commission considers that the implementation of CRR/ CRD IV did not have significant pro-cyclical effects, in a post-crisis context of massive financial losses. However, the Commission mentions that the sample data analysed is limited and covers only a short period of time.

The European Commission concludes that there is no need, for the time being, to amend the prudential framework. It will never the less continue to analyse on a regular basis the pro-cyclicality of the EU legislation regarding capital requirements.

15th March 2018: the ECB standardizes its *addendum* on NPLs provisioning

The European Central Bank (ECB) published the final version of the *addendum* to the ECB guidance on non-performing loans (NPLs). This publication concludes a tumultuous consultation phase, during which many criticisms were voiced regarding the normative value of the *addendum*.

The final addendum specifies the ECB's supervisory expectations in relation to the provision of **new NPLs as of 1st April 2018**. The ECB underlines that it is **not a binding document** and that **deviations from the supervisory expectations will be considered on a case by case basis**. When the public consultation was launched, legal services from the European Parliament and the Council of the European Union standardizes the ECB for stepping out of its supervisory mandate by promulgating rules which would apply to all banks. European Parliament President, Antonio Tajani (S&D, IT), welcomed on Twitter the changes introduced by the ECB to clarify that the *addendum* is not binding.

According the *addendum*, **new unsecured NPLs shall be fully provisioned two years** after they have been classified as non-performing. **New secured NPLs will be expected to be fully covered seven years** after they have been classified as NPLs. The ECB expects banks to progressively provision for secured NPLs, setting for example a 40% coverage target after three years.

The ECB indicates that it was annually assess the spread between banks' practices and supervisory expectations regarding NPLs provisioning.

**ECB and European Commission : differences persist**

The ECB published its final *addendum* one day after the European Commission has published its legislative proposal on a prudential backstop for NPLs.

Even if the objectives of the ECB and the European Commission are identical – reducing and preventing NPLs stocks -, **both institutions are not fully aligned regarding their supervision expectations**. Indeed, the ECB calls for secured NPLs to be fully provisioned after seven years, when the European Commission sets an eight year target. The progressiveness of the provisioning also differs. For example, a secured loan classified as NPL on 1st May 2018 will have to be covered at 40% for the ECB and 17.5% for the Commission on 1st May 2021, three years after its classification as NPL.

In its addendum, the ECB explains that it recommends higher provisioning targets than the European Commission since **it has a mandate to evaluate and mitigate risks which are not already covered** by the minimal requirements set by the European legislation.

**The legislative process on the NPL legislative proposal by the European Commission is due to start in the coming weeks.**
**The ECB addendum applies to new NPLs as of 1st April 2018.**

14th March 2018: the EBA published its advice to the European Commission on NPL prudential backstop

The European Banking Authority (EBA) published a report sent to the European Commission and providing its views on the proposed prudential backstop for non-performing loans (NPLs).

The EBA considers that, in a post-crisis context, setting minimal and prudential requirements can provide an incentive for banks to proactively reduce existing NPL stocks and prevent new NPLs.

In its report, the EBA provides both an impact assessment and a qualitative study of the legislative proposal of the European Commission.

- **Qualitative study**

In the part of its report which provides a qualitative assessment of the Commission's proposal, the EBA reviews interactions between the proposed prudential backstop and the existing legislative, regulatory and supervisory frameworks.

In particular, the EBA assess the **potential impact of combining minimal prudential provisioning requirements with the Capital Requirements Regulation (CRR), as well as pillar 2 measures and IFRS 9.**

From an **accounting perspective**, the EBA considers as positive the fact that the prudential backstop could incentivize banks to change their provisioning policies. It notes that accounting standards do not differ depending on the origination date of the provisioned loans, the proposed prudential backstop could encourage an earlier recognition of provisions. With regard to the interaction with IFRS 9, the EBA considers that it is too early to provide an assessment since there is for the moment no data on the implementation by banks of the this new accounting standard, which became applicable on 1st January 2018.

The EBA also points out to the European Commission that the concept of 'new NPL' can be ambiguous, in particular in cases of credit restructuration or transformation. It advices the Commission to include in the legislative text a mandate for the EBA to draft technical norms on this issue.

Finally, concerning **interactions with the prudential framework set by CRR**, the EBA underlines that minimal provisioning requirements will need to be introduced in pillar 1, amending CRR. This is indeed the solution proposed by the European Commission in its legislative proposal. Considering that provisioning for NPLs will imply a deduction from CET1, pillar 2 supervisory powers will be limited if the minimal requirements are already reached. Additional pillar 2 requirements are however possible in some cases, even though competent authorities will not be able to require more than a full coverage in six years for secured NPLs. The EBA requests from the Commission a mandate to draft technical norms on the sequencing between pillar 1 and pillar 2.

With regards to **NPLs risk weights**, the EBA notes that it will need to be set at zero for fully provisioned NPLs, in order to avoid a duplication of prudential obligations. The EBA also recommends adjusting risk weights in standardized approaches, aiming at a 150% risk weight where specific credit risk adjustments are less than 20% of the unsecured part of the exposure value if these specific credit risk adjustments were not to be applied, and a 100% risk weight where specific credit risk adjustment are over 20%.

- **Quantitative impact assessment**

In its report, the EBA provides the European Commission with an impact assessment of the proposed measures. Its assessment is based on a **projection on twenty years under constant conditions**, using a conservative methodology and without changes to the regulatory standards and provisioning requirements. This analysis conducted by the EBA indicates that the introduction of a prudential backstop will, on average, lead to a decrease by 205 basis point of CET 1. On a seven year timeline, which corresponds to the period proposed by the European Commission for the full coverage of unsecured NPLs, the impact would be of 56 basis points. The EBA estimates that this is a 10% of retained earnings after dividends. The EBA notes that banks which are already applying conservative provisioning policies will not experience any change due to the proposed prudential backstop.

However, the EBA underlines that this is a **conservative estimate**, using data from 2014 to 2017 and under which banks would not have adjusted their policies. Due to the time constraint to draft its report, the EBA indicates that it has to base its work on existing data rather than on ad hoc data collection, which would have allowed for a more detailed assessment. It adds that a well-functioning prudential backstop should enable banks to prevent new stocks of NPLs.

**Next steps: the EBA plans on publishing guidelines on loan organization and on internal governance.**

22nd February: CRR/ CRD: Members of the European Parliament start examining amendments

Over one year after the publication of the Banking Package, the European co-legislators progress in their legislative work regarding the European Commission's proposals, here and here, to review the Capital Requirements Directive and Regulation (CRD IV/ CRR). After the publication by rapporteur Peter Simon of his draft reports on CRR II and CRD V on 22nd November 2017, amendments on CRR II (180 to 414, 415 to 685, 686 to 935 and 936 to 110) and CRD V (48 to 309 and 310 to 127) were published early February 2018.

On 22nd February, Members of the European Parliament (MEPs) met in the committee on economic and monetary affairs (ECON) for a first exchange of views on amendments. Almost 2000 amendments were tabled and the discussion around compromise amendments is likely to last for months.

Introducing the debate on 22nd February, rapporteur Peter Simon thanked his colleagues for their contribution, which – in his view – reflects the vivacity of the debate around the reform of CRD IV and CRR. As rapporteur, he sets the timeline for discussions. He said that he aims for an **adoption of a report in ECON in May 2018**, while acknowledging that this is a very ambitious timeline.

In is introductory remarks, Peter Simon underlined the following points:

- **Fundamental Review of the Trading Book** (FRTB): Peter Simon took the view that his proposal for a five years transition period is reasonable and should be maintained;

- **Net Stable Funding Ratio** (NSFR): many amendments have been tabled on this issue, particularly regarding the asymmetric treatment of repurchase agreements (repo) and the fact that the European Commission's proposal diverges from the recommendations of the Basel Committee on Banking Supervision (BCBS);

- **Total Loss Absorbing Standard** (TLAC): Peter Simon welcomed the broad level of consensus around the draft report on this point;

- **Leverage ratio**: Peter Simon proposed in his draft reports to provide add-ons for global systemically important banks (G-SIBs), which will still need to be discussed to reach a compromise;

- **Intermediate Parent Undertakings** (IPU): Peter Simon said that the debate will focus on determining which third country banks – including those in the United Kingdom – will be impacted the European Commission's proposal. For the record, the European Commission proposed that third country credit institutions with over €30 billion in assets in at least two EU Member States be required to set up an IPU under EU supervision;

- **Proportionality**: a large number of amendments were tabled on this issue. Peter Simon reminded MEPs of his proposal: a simplified but stricter regime for small banks. In his view the threshold of €1.5 billion to be considered a small bank is already high and there is no need to raise it, especially since he proposed in his draft report a mechanism to adjust the threshold to the Member State's PIB. However, Peter Simon **considered as an interesting approach the amendments tabled by the Greens**. They suggest to raise the threshold to €5 billion and to raise prudential ratios, to 15% for the capital ratio and 6% for the leverage ratio. They also suggest adding qualitative criteria to be respected by institutions under the proportionality regime.

Shadow rapporteur for the EPP, **Othmar Karas** (AT) said that his group has no fundamental issues with the propositions of Peter Simon, but that some adjustment would be needed. Commenting specifically of the proportionality threshold, Othmar Karas considered that **a €5 billion threshold would be appropriate**, but that it should not be higher. On a general note, he warned against the risk of gold plating international standards set by the BCBS, which would be detrimental to the competitiveness of the EU financial institutions.

**Ashley Fox** (ECR, UK), shadow rapporteur, expressed his group's **opposition to the IPU proposal**, underlining that no impact assessment had been conducted. On the proportionality issue, he underlined the importance of providing for a simplified regime for small and non-complex institutions.

For the ALDE group, **Caroline Nagtegaal** (NL) insisted that the main objective of CRR II/ CRD V is to align the EU to new international standards, **without gold plating**. Caroline Nagtegall expressed **support for the IPU mechanism**, but also suggested to raise the threshold above which third country groups would be required to set an IPU.

**Sven Giegold** (Greens/EFA, DE) underlined that debates on CRR II/ CRD V should be set in the context of the **completion of the Banking Union**, in which risk reduction is necessary prerequisite to risk sharing via a European Deposit Insurance Scheme (EDIS). He called on MEPs to progress on the Banking Union, warning against the temptation to simply block discussions on risk sharing in the euro zone. In addition, he highlighted that proportionality for small banking institutions should not be considered as a German issue, since many other Member States also have networks of small banks.

Finally, **Anne Sander** (EPP, FR) also insisted that CRR II/ CRD V should not be a **gold plating** exercise. She called for the **Banking Union to be considered as a single jurisdiction**. In her view, this would allow supervisors to exempt from prudential requirements subsidiaries which are backed at least at 50% by their group. This would also allow for intra-group transactions within the Euro zone to be left aside for the calculation of prudential requirements for systemic banks.

On supervisory issues, Anne Sander warned against the introduction of exemptions for categories and took the view that exemption should remain granted on an individual basis (article 2 CRR), to ensure legal certainty.
On the question of proportionality, Anne Sander considered that increasing the proportionality would be a good thing, as long as it does **not lead to the fragmentation of the single rulebook**. She added that banks would can afford **internal models** should not be granted exemptions on the ground of proportionality, as they can comply with reporting requirements.

**The provisional timeline of the ECON committee foresees a vote in committee on 16th or 17th May 2018, ahead of a vote in plenary session in May 2018 and the start of 64tandardi before the summer**.

The core discussion among shadow rapporteurs to design compromise amendments will thus take place in the coming months.

12th February 2018: Amendment on factoring tabled by MEPs on the CRR-CRD Review

On 12th February, MEPs' amendments on Peter Simon's (S&D, DE) draft reports on the Commission's proposals (CRD5 and CRR2), to review the Capital Requirements Directive and Regulation (CRD IV/ CRR) were published.

- Amendments on CRR II are available here : 180 to 414, 415 to 685, 686 to 935 and 936 to 110
- Amendements on CRD V are available here 48 to 309 and 310 to 427.

As a reminder, the CRR2 / CRDV package is based on the following goals:
- **Appling the latest international banking standards of the Basel Committee within the European Union, such as the Net Stable Funding Ratio (NSFR)**
- Strengthening financial stability while taking into account European specificities so as not to hinder the lending capacity of financial institutions

Regarding the implementation of the NSFR, **specific treatment of factoring when it comes to liquidity risk requirements, was tabled by six MEPs from three main political groups : from the EPP (3), the S&D (1) and the ALDE (2) political groups**. (*See Amendments 716 to 719*).

In particular, 2 keys MEPs on this file, **Pervenche Berès (FR), Coordinator of the S&D group** and **Caroline Nagtegaal (NL), Shadow rapporteur on the text for the ALDE group**, proposed:

- ✓ **to ensure** that**, in the context of the implementation the NSFR, factoring will benefit from the specific prudential treatment provided for trade finance**, i.e. a required stable funding (RSF) of 10% (*Article 428.u.1.c of the Commission's proposal for a Regulation*) by stipulating that : "f*or the purposes of this Part, factoring shall be treated as trade finance*"
- ✓ **a definition of factoring**. If a few differences exist between the amendments of the MEPs most of them define it as such: "*Factoring" means an agreement between a business (Assignor) and a financial entity (Factor) in which the Assignor assigns/sells its Receivables to the Factor and the Factor provides the Assignor with a combination of one or more of the following services with regard to the Receivables assigned: Advance of a percentage of the amount of Receivables assigned, that is generally short term, uncommitted and without automatic roll-over, Receivables management, collection and Credit protection. Usually, the Factor administers the Assignor's sales ledger and collects the Receivables in its own name. The Assignment can be disclosed to the Debtor." (Amendment 717*)

**The provisional timeline of the ECON committee foresees a vote in committee on 16th or 17th May 2018, ahead of a vote in plenary session in May 2018 and the start of 65tandardi before the summer**.

8th February: the European Commission published a fact sheet on post-Brexit banking and payment services

In the framework of its 'Brexit preparedness' efforts, the European Commission has been publishing since January 2018 **sector-specific factsheets, addressed to stakeholders and explicating the foreseen consequences of Brexit.**

Even if "*subject to any transitional arrangement*", the European Commission reminds stakeholders that the United-Kingdom (UK) will formally withdraw from the European Union (EU) on 30th March 2019. In its factsheets, the Commission considers the scenario of a so-called **hard Brexit, in which there would be no transitional arrangements**. For each of the sectors it examines, the Commission points the legal consequences of a hard Brexit and encourages stakeholders to anticipate them.

On 8th February, the European Commission published **seven new factsheets, regarding different aspects of the financial services industry.** Namely, it published factsheets on banking and payment services, asset management, creating rating agencies, markets in financial instruments, post-market services, statutory audit as well as insurance and reinsurance.

For all these services, the European Commission underlines that Brexit will translate into the **loss of access to the European Single Market** and into the **shift to a third country treatment**, **especially for prudential purposes**. Continuity of **existing contracts** and **conflict of law rules** will also be affected.

In its factsheet on banking and payment services, the European Commission focuses on the impact Brexit will have on activities governed by the Capital Requirements Directive and Regulation (CRD IV/ CRR) as well as by the Payment Services Directive (PSD 2).

- **Authorisations**

The European Commission clarifies that the withdrawal of the UK from the EU will entail the loss of the European passport from credit institutions and payment services providers established in the UK. **They will no longer be able to provide their services in the EU on the basis of their current authorisations.**

As in its other factsheets, the Commission distinguishes between **subsidiaries** – which are legally independent from their parent entity – and **branches** – which are not legally independent from their parent entity.

- **Branches of UK entities which were operating in the EU** will have to comply with national law to seek authorization in each Member States in which they wish to continue operating, according to the applicable law for entities having their head office in a third country. They will have to comply with the legal framework applicable in each Member State where they wish to operate, including regarding deposit guarantee arrangements;

- **Payment services providers based in the UK** will not be able to provide payment services in the EU either (i) on a cross-border basis, from the UK, or (ii) through a branch in the EU;

- **Branches of EU entities which are established in the UK** will remain subject to the law applicable to the group they belong to. In particular, **branches of EU entities will remain supervised by the competent authority in the EU**.

- **Arrangements and exposures**

The Commission warns stakeholders about the impact that Brexit will have on existing **outsourcing arrangements, supervisory arrangements, exemptions from the application of large exposures and risks mitigation requirements** which involve UK based entities. It indicates that **intra-group arrangements** are also impacted. In particular, exposures to third parties established in the UK will no longer benefit from the intra-EU prudential treatment provided for by CRD IV.

- **Continuation of existing contracts**

The loss of the EU passport implies that UK entities will no longer be able to perform some of their obligations. In addition, the EU framework regarding **conflicts of law will no longer apply to the UK**.

As a consequence, the European Commission encourages stakeholders to anticipate and assess consequences for existing contracts containing of choice of law or jurisdictions, or governed by UK law.

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6th February 2018: Publication of RTS for the materiality threshold in the OJEU

On the 6th February, the regulatory technical standards (RTS) for **the materiality threshold for credit obligations past due** were published in the Official Journal of the European Union (OJEU).

Adopted under the Capital Requirements Regulation (CRR), these RTS set the terms and conditions for setting the threshold for the payment of arrears on retail and other than retails exposures. The setting of the threshold is left to the responsibility of the competent authorities, who must nevertheless follow the indications of the RTS (absolute component and relative component).

**Article 2 "*Materiality threshold for exposures other than retail exposures*" states that obligor is defaulted** *"when both the limit expressed as the absolute component of the materiality threshold and the limit expressed as the relative component of that* ***threshold are exceeded either for 90 consecutive days or for 180 consecutive days, where the exposures included in the calculation of the credit obligation past due are exposures to a public sector entity and the 90 days have been replaced by 180 days*** *in accordance with Article 178(1)(b) the CRR."*

The RTS are applicable from 7th May 2018. Competent authorities will set a date for the application of the materiality threshold which may vary for different categories of institutions, but which **shall be no later than 31 December 2020** for institutions using the standardised approach.

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29th January 2018: European supervisors on Basel III implementation

During a conference organized in Frankfurt, the European Banking Authority (EBA) chair Andrea Enria and the European Central Bank (ECB)'s Single Supervisory Mechanism (SSM) chair Sabine Lautenschläger welcomed the agreement found on 7th December in the framework of the Basel Committee for Banking Supervision (BCBS).

Sabine Lautenschläger highlighted that the so-called Basel III standards will contribute to make banks safer. Regarding the output floor, which crystallized the divides between Europeans and Americans during the negotiations, Sabine Lautenschläger took the view that a 72.5% output floor will not reduce the risks sensitivity of prudential requirements. According to her, this output floor does not "*kill*" risks sensitivity. Sabine Lautenschläger recalled that banks will be able to keep using internal models and to benefit from lower prudential requirements for low risk activities. She also underlines that, depending on the share of assets subject to a standard model within a credit institution which also apply internal models, the output floor could effectively be lower than 72.5%.

According to Sabine Lautenschläger, the Basel III agreement reinforces convergence between internal and standard approaches, while offering the necessary safeguards to ensure that the prudential framework adjusts to the level of risk.

She acknowledged that the Basel III agreement was not neutral and that some activities would be more impacted than others. However, according to her, it remains difficult to predict how business models in the banking sector will evolve as a consequence of the Basel III standards.

Andrea Enria also welcomed the Basel III agreement, taking the view that it constitutes a major achievement. Regarding the output floor, Andrea Enria considered that the 72.5% compromise strikes the right balance.

Andrea Enria underlined that the challenge will now be to implement the Basel III standards in the European framework, ensuring that this implementation is proportionate and transparent. He added that the European Commission can rely on the EBA to provide assistance in the transposition works.

The Basel III standards is to be fully implemented by 2027.

26th January: ECB aligns with the EBA default definition

The European Central Bank (ECB) published a list of decisions taken by the Governing Council of the ECB between mid-December 2017 and January 2018.

Among the decisions related to banking supervision, the Governing Council took a decision regarding the definition of default to be used for the supervision of significant institutions. On 27th December 2017, the Governing Council decided not to object to a proposition by the Supervisory Council to have the ECB applying the guidelines on the definition of default adopted by the European Banking Authority (EBA in application of the capital requirements regulation (CRR).

As a consequence, from 1st January 2021, the ECB will apply for supervisory purposes the EBA guidelines, in order to ensure a consistent approach of the concept of default.

| **European Analytical Credit Dataset** | *Back to summary* |
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No update in August 2019.

| Shadow Banking | *Back to summary* |
|---|---|

No update in August 2019

**31st October : CRR/CRD – Trilogue raise questions on shadow banking**

The trilogue negotiations on the amendment of the Capital Requirements Directive (CRD IV) and the Capital Requirements Regulation (CRR) have opened several fault lines between the European Parliament and the Council of the EU.

In particular, the European Parliament and the Council held opposing views regarding the follow-up after the EBA published in December 2015 its guidelines on *"Limits on exposures to shadow banking entities which carry out banking activities outside a regulated framework under Article 395( Limits to large exposures) of CRR".*

Unlike the Council, the European Commission and the Parliament want to make the guidelines legally binding by transforming them in Regulatory Technical Standards (RTS). The Parliament would even like the European Banking Authority ( EBA) to "*develop a methodological standard for competent authorities specifying an appropriate aggregate limit on exposures to shadow banking (SB) entities which carry out banking activities outside a regulated framework, as well as individualized exposure limits to such entities*".
As a reminder, on December 15th, the European Banking Authority (EBA) published both a report and its final guidelines regarding exposures of credit institutions to shadow banking entities, i.e. entities carrying "*bank-like activities outside of a regulatory framework*". The Guidelines define an approach aiming at allowing EU credit institutions to set "*internal limits*" for their exposures to shadow banking entities.

This guidelines give the following definition of "*shadow banking entities*": "*undertakings that carry out one or more credit intermediation activities and that are not excluded undertakings*" (see p.20). This very broad definitions is completed by a list of undertakings which are excluded from the scope of the guidelines (see pp.20-24).

The EP could agree to keep the form of the guidelines for reporting issues if only the shadow banking limits are defined by RTS.

The EBA specifies in its analysis of the received responses to the consultation that clarifications have been made about the definition of "*financial institution*" so that it is "*interpreted in line with Article 119(5) of the CRR*" ***in order to take into account factoring companies'*** **specificities** (see p. 46 & pp.48-49).

**When a factoring company is subject to a prudential framework comparable to the *'financial institution'* regime, the entity shall not be treated as a '*shadow banking entity*' for the purposes of the guidelines.**

Current work of the Council and the EP could have a legal impact on those guidelines – and on how factoring players in the EU are considered depending on the prudential regime they have to abide by.

5th March 2018 – Shadow Banking: the Financial Stability Board published its general monitoring report 2017

The Financial Stability Board (FSB) published its Global Shadow banking Monitoring Report 2017.

- **Shadow banking classifications and definitions**

The FSB's definition of *shadow banking* is very wide as it covers "*credit intermediation involving entities and activities (fully or partly) outside of the regular banking system*". If these activities are perceived as "*bringing real added value*" to traditional banking for the financing of the economy, the FSB considers that they can also constitute a risk for financial stability.

The Other Financial Intermediaries (OFIs), which are part of the shadow banking, comprise "*all financial institutions that are not central banks, banks, insurance corporations, pension funds, public financial institutions, or financial auxiliaries*." The OFIs gather one third of total global financial assets to $99 trillion in 2016.

Among the OFIs, **the FSB identifies the so-called "*the narrow measure of the shadow banking*", i.e. "*non-bank credit intermediation that may pose financial stability risks*".** If most of this category relates to collective investment vehicles, **factoring activities are also included within it by the Board**.

Factoring is gathered with activities that "*engage in loan provision that is dependent on short-term funding*".

The FSB considers that they often concentrate their loans in specific sectors, **which can be a risk factor if the sectors on which they focus are cyclical**. Moreover, this risk can be exacerbated if these entities are highly dependent on short-term financing or wholesale funding, or if they depend on the parent companies being themselves in the same sectors of a cyclical nature.

In terms of risk these activities present:

- ✓ **A significant credit intermediation**
- ✓ a transformation of limited or negative maturity
- ✓ **a "*moderate*" liquidity transformation**

- **FSB missions**

FSB's main goals are, "*where oversight and regulation needs to be strengthened* ***to mitigate the potential systemic risks associated with shadow banking***". It wants especially:

- ✓ to mitigate **the spill-over effect between the regular banking system and the shadow banking system;**
- ✓ **to dampen pro-cyclicality** and other financial stability risks associated with securities financing transactions; and
- ✓ to assess and mitigate financial stability risks posed by other shadow entities and activities.

**Regarding FinTech**, the FSB considers they are currently not enough developed to be a threat for financial system stability. Yet, the board is closely monitoring their development.

| **Insurance Mediation Directive II** | [Back to summary](#) |
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| No update in August 2019 | |

| **Rome I regulation / Contract law / Insolvency law** | [Back to summary](#) |
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No update in August 2019

No Update in July 2019

**26 June 2019** – Publication of the Insolvency directive

Following its adoption by the European Parliament on the 23rd of March and by the European Council of the EU on the 20th of June, the directive on "*preventing restructuring, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures*" has been published in the Official Journal of the European Union on the **26th of June**.

The directive will enter into force on the twentieth day following its publication in the Official Journal of the EU. Member states will have to adopt and publish the laws, regulations and administrative provisions by the **17th of July 2021**.

**28th March 2019** - Insolvency : the European Parliament adopts the directive

On the 28th of March 2019, the European Parliament adopted the Directive on "***Preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures***"(the so-called Business insolvency directive). The directive was adopted with 327 votes in favor, 34 against and 142 abstentions.

As a reminder, the European Commission's proposal aimed at improving the 2015 Insolvency regulation which does not harmonise the insolvency law between the Member States. The 2015 regulation did not have impacts on facilitating the rescue of business in financial difficulty and second chance to entrepreneurs.

The European Commission suggested the following points:

- **Preventive restructuring procedures** for debtors in case of insolvency. Companies and SMEs will have access to early warning tools in order to detect difficulties and launch restructuring measures. Preventive restructuring framework should simplify court proceedings if any.
- Measures for the discharge of debts for over-indebted companies and entrepreneurs to enable them to benefit for a second chance. Debtors will be discharged after a maximum of 3 years.
- Measures to **increase the efficiency of the procedures** in order to reduce the lengths and costs of procedures which leads to legal uncertainty for creditors and investors.

- **Training and specialisation of practitioners** in order to improve the length of insolvency, restructuring and second chances procedures.

The directive adopted by the European Parliament includes the following main elements:

- **Preventive restructuring measures and viability test**: preventive restructuring frameworks must enable debtors to restructure effectively at an early stage in order to avoid insolvency. The co-legislators have added a viability test (article 4) as a condition for access to the preventive restructuring procedure.

- **Designation of a practitioner** (article 5): the directive provides that Member States will be able to determine that the appointment of a practitioner in the field of restructuring is always necessary in certain circumstances: when the restructuring plan needs to be confirmed by means of a cross-class cram down or when the restructuring plan includes measures affecting the rights of workers. In other cases, the appointment of a practitioner will be decided on a case-by-case basis.

- **Cross-class cram-down :** Member states will be able to decide the conditions in which a restructuring plan can be adopted with a cross-class cram down. The text adds that in case of a cross-class cram down, Member States should ensure that dissenting classes of affected creditors are not unfairly prejudiced under the proposed plan and that Member States should provide sufficient protection for such dissenting classes.

- **Stay of individual enforcement actions (article 6) :** The directive provides that a debtor should be able to benefit from a temporary stay of individual enforcement actions in order to support the negotiations on a restructuring plan. The stay of individual enforcement actions will be granted by a judicial or administrative authority.
  The stay of individual enforcement will apply for a maximum period of up to 4 months with a maximum extension to 12 months. Member States will also be able to provide for an indefinite stay where the debtor becomes insolvent under national law.

- **Class formation (article 9):** In its proposal, the European Commission had included the creation of "class formation". In order to ensure that rights which are substantially similar are treated equitably and that restructuring plans can be adopted without unfairly prejudicing the rights of affected parties, affected parties should be treated in separate classes which correspond to the class formation criteria under national law.
  The directive defines "class formation" as the grouping of affected parties for the purposes of adopting a plan in such a way as to reflect their rights and the seniority of their claims and interests. Secured and unsecured creditors should always be treated in separate classes.
  SMEs can be exempted from the obligation to treat affected parties in separate classes.

**Next steps**
**The directive must now be adopted by the Council of the European Union before being published in the Official Journal of the European Union.**

20th December 2018 – Business Insolvency: the European Parliament and the Council of the European Union reach a political agreement.

On the 20th December 2018, the European Parliament and the Council of the European Union reached an agreement on the European Commission's proposal for a directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures

***European Commission's proposal***

As a reminder, the European Commission's proposal aimed at improving the 2015 Insolvency regulation which does not harmonise the insolvency law between the Member States. The 2015 regulation did not have impacts on facilitating the rescue of business in financial difficulty and second chance to entrepreneurs.

The European Commission suggested the following proposal:

- Preventive restructuring procedures for debtors in case of insolvency. Companies and SMEs will have access to early warning tools in order to detect difficulties and launch restructuring measures. Preventive restructuring framework should simplify court proceedings if any.
- Measures for the discharge of debts for over-indebted companies and entrepreneurs to enable them to benefit for a second chance. Debtors will be discharged after a maximum of 3 years.
- Measures to increase the efficiency of the procedures in order to reduce the lengths and costs of procedures which leads to legal uncertainty for creditors and investors.
- Training and specialisation of practitioners in order to improve the length of insolvency, restructuring and second chances procedures.

***European Parliament's report***

The Committee on Legal Affairs of the European Parliament represented by Angelika Niebler (EPP, DE) suggested the following changes:

- Preventive restructuring measures: the report voted suggests that Member States must ensure that debtors and companies must have an easy access to these early warning tools in order to detect situations of potential insolvency. Member States should for instance set up accounting and control obligations for debtors.
- Preventive restructuring frameworks: these procedures must be limited to enterprises that have not been finally sentenced for serious breaches of accounting and bookkeeping obligations. The members of the committee suggest that representatives of the debtor's workers receive clear and transparent information on the restructuring procedure.
- Individual actions: the suspension of individual enforcement must not exceed 4 months and should only be possible if there is not yet an obligation to apply for commencement of insolvency proceedings. The total duration of the suspension (extension and renewal) must not exceed months.
- Restructuring plans: these plans have to be validated by a judicial or administrative authority, representatives of workers must have a right of information and consultation and they must include information on organisational aspects regarding employment and the consequences for workers. These restructuring plans must not impact workers' rights (occupational pension funds…).
- Second chance for entrepreneurs: the report suggest that entrepreneurs who are over-indebted may be fully discharged of the debts for the first time after 5 years ( instead of 3 as proposed by the European Commission) from the opening date of the procedure or from the date the repayment plan started.

***Compromis du Parlement et du Conseil de l'Union européenne***

The political agreement reached between the European Parliament and the Council of the EU is quite close from the Council's position.

It introduces the following changes to the Commission's proposal:

- New provisions on the duties and obligations of companies directors during the insolvency proceedings: they must take into consideration the interest of creditors, investors and must avoid deliberate or grossly negligent conduct

- Workers' rights are strengthened: workers will enjoy a right of information and consultation and their rights (collective bargain, industrial action…) will not be affected by the procedures.
- Appointment of restructuring practitioner: the Council and the European Parliament agreed on the situations where practitioner must be appointed. For the other cases, the directive provides that the appointment of a practitioner will be decided case by case.

**Next steps**

**On the 23th of January, the Committee for Legal Affairs of the European Parliament approved the compromised reached with the Council of the Union.**

1st October: Insolvency : the Council of the Union adopts its compromise

The Council of the Union published on the 1st of October its compromise on the Commission directive proposal on "*preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures*"

As a reminder, the Commission's proposal aims at setting an insolvency framework to encourage effective preventive restructuring, second chance, including measures to increase the efficiency of restructuring. However, the definition and implementation of the restructuring frameworks will stay within the member states.

The Commission's proposal lays down rules on:

- ✓ **Preventive restructuring procedure** (when debtors have financial difficulties and when there is a likelihood of insolvency)
- ✓ **Procedures leading to a discharge of debts** ( for over-indebted entrepreneurs to allow them to take up a new activity)
- ✓ **Measures to increase the efficiency of the procedures**
- ✓ **Training, 73tandardizatio of practitioners and courts**

Among others, the Council's compromise amends the Commission's proposal on the following point:

- ✓ **Access to preventive restructuring frameworks:** Member States agreed that a debtor in a likelihood of insolvency should have access to a preventive restructuring framework to prevent insolvency. But some of them raised their concerns on the fact that allowing debtors with no prospect of viability to the framework would cause unnecessary delays of the opening. Therefore, the compromise allows Member States to introduce a viability and optional test for Member States who wants to ensure that the procedure has chances to succeed
- ✓ **Mandatory appointment of an insolvency practitioner**: the Commission's proposal provided that the appointment of a practitioner in the field of restructuring should not be mandatory. Some Member States raised that the intervention of a practitioner would increase the efficiency of the procedure but would also make the procedure more costly and burdensome which will reduce the easy access to the procedure.
- ✓ **Stay of individual enforcement actions:** some Member States preferred to introduce a short stay in order to take into accounts the creditors but others preferred to have a longer stay in order to allow the debtor sufficient time to come up with a restructuring plan. The compromise provides for a maximum period of stay of up to 4 months that could be extended up to 12 months. The rapporteur

for the IMCO (Internal market and Consumer Protection) committee suggested 10 months instead of 12 months as proposed by the Commission.

- ✓ **Class formation:** the Commission proposed to classify the creditors for voting purposes based on their commonality of interest. Some Member States raised that this could be burdensome and costly. The compromise suggests that Member States will have the possibility to allow micro, small or medium-sized enterprises to opt to not treat affected parties in separate classes.
- ✓ **Cross-class cram-down:** this mechanism was new for some Member States who raised two issues regarding
    1. The valuation of the debtor to determine which class of creditors would be impacted financially and could not, therefore, carry the plan by their support in a cross-class cram-down vote
    2. A Priority rule according to which a dissenting class of creditors must be satisfied in full if a more junior class could receive any distribution or keep any interest under the plan.

On both issues raised by the Member States, the compromise provides:

1. for an alternative option by which Member States **can avoid the requirement that only classes of creditors 'in the money' can carry the plan**, namely where a majority of classes of creditors votes in favour of the plan of which at least one class is a secured class of creditors or a class senior to the ordinary unsecured creditors.
2. an alternative option for Member States to introduce a different benchmark with a **priority rule to protect dissenting creditor** classes when using a cross-class cram-down mechanism.

**Reaction from the German delegation**

On the 16th of October, the German delegation declared that they were supporting the Commission's proposal but pointed out that within the context of the banking Union, the directive proposal does not make a significant contribution to the measures necessary for the sustainable reduction and future avoidance of non-performing loans.

**Next steps:** As the Parliament adopted its position, the trilogue will start as soon as possible in order to adopt the text before the European elections in May 2019.

10th July 2018: the JURI committee adopted the report on the law applicable to third-party effects of assignments of claims

On 10 July, the European Parliament's Committee on legal affairs (JURI) adopted the report of the MEP Pavel Svoboda (EPP, CZ) regarding the law applicable to the third-party effects of assignments of claims.

As a reminder, the European Commission published on 12 March 2018 a proposal for a regulation of the law applicable to the third-party effects of assignments of claims. This new regulation would complement the Rome I regulation on the law applicable to contractual obligations. It specifies the regime for the assignments of claims and lays out a general approach according to which "***the third-party effects of an assignment of claims shall be governed by the law of the country in which the assignor has its habitual residence at the material time***" (article 4.1 of the proposal).

The Commission's proposal foresees three exceptions to this general approach: claim related to a cash deposit in a credit institution (law applicable to the cash claim), claims arising from a financial instrument (law of the assigned claim) and securitizations (possibility of choosing the applicable law).

In his draft report, the Czech MEP Pavel Svoboda (PPE) welcomes the Commission's general approach and **suggests that it should cover "*the transfer of the contracts (such as derivative contracts), in which both rights (or claims) and obligations are included, or the novation of contracts including such rights and obligations*"** (amendment 9 adopted in the final report).

**Exceptions to the general approach** – the money credited to an account in a credit institution and claims arising from a financial instrument, for which the applicable law would be that of the assigned claim. As regards the assignments of claims for the purpose of securitisation, the rapporteur wants the assignor to "*choose that the law applicable to the largest number of assigned claims shall apply as the law applicable to the third-party effects of all assignments of claims*." (Amendment 13). Finally, he proposes **to exclude the debtor from the scope of the regulation** (amendments 7).

**It should be noted that the European Central Bank** (ECB) also issued an opinion on the Commission's proposal on 18 July 2018. The ECB **wishes to exclude from the scope financial collateral arrangements as defined by the directive 2002/47/EC in order to apply the law of the assigned claim**.

Next steps: the Council has to adopt its position.

2nd July 2018: Insolvability and second chance: the European parliament adopted its report

On 2 July 2018, the European Parliament's Committee on legal affairs (JURI) adopted the report of Angelika Niebler (PPE, DE) on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures.

**PROPOSAL FOR A PROCEDURES HARMONISATION**

As a reminder, the proposal for a directive, published by the European Commission on 23 November 2016, aims to define a set of principles and rules common to insolvency proceedings at European level. The definition and implementation of restructuring procedures remains, however, within the competence of the Member States.

The creation of common European rules should allow greater coherence and convergence between national regulatory frameworks on business insolvency, in particular the encouragement of early restructuring procedures. The challenge is also to enhance legal certainty in cross-border exchanges.

**KEY ELEMENTS OF THE EUROPEAN PARLIAMENT'S REPORT**

- **Stay of individual enforcement actions (article 6)**

The European Commission suggests a period of 4 months, with the possibility of extending it to 12 months. The JURI report agrees on the 4-month period but limits its extension to 10 months. The report also introduces new conditions for stay:

- ✓ the debtor's obligation to declare himself insolvent was not raised
- ✓ it is still possible for the company to avoid the insolvency procedure

The extension up to 10 months must in turn be accepted in advance by secured creditors.

Finally, the European Parliament takes up the Commission's proposal that creditors must not stop **"essential" contracts for the survival of the company, unless it involves severe financial difficulties for them**.

- **<u>Adoption of restructuring plans and cross-class cram-down (articles 9 à 11)</u>**

In addition to the creditors affected by the restructuring plan, the parliamentary report hopes that employees can also be better involved in the process. For example, if the restructuring plan involves a loss of more than 25% of employees, it must be adopted by a judicial or administrative authority to become legally binding.

The possibility of imposing a restructuring plan on a dissenting minority of creditors and shareholders is maintained under strict conditions (cross-class cram-down procedure).

- **<u>Second chance procedures</u>** (title III):

The report hopes that a "second chance" will be possible by releasing from its debts an "honest" entrepreneur who has become insolvent for the first time, after a maximum period of five years. The Council, in its partial general approach from the beginning of June, set a maximum period of three years.

As soon as the Council adopts its final position, the interinstitutional negotiations will start.

<u>4th June 2018: the European Parliament progresses on the law applicable to third-party effects of assignments of claims</u>

The European Parliament's Committee on legal affairs (JURI) published amendments tabled on the draft report by Pavel Svoboda (EPP, CZ) regarding the law applicable to the third-party effects of assignments of claims.

The European Commission published on 12th March 2018 a proposal for a regulation of the law applicable to the third-party effects of assignments of claims. This new regulation would complement the Rome I regulation on the law applicable to contractual obligations. It specifies the regime for the assignments of claims and lays out a general approach according to which "*the third-party effects of an assignment of claims shall be governed by the law of the country in which the assignor has its habitual residence at the material time*" (article 4.1 of the proposal). The proposal foresees three exceptions to this general approach:

1. When the claim related to a cash deposit in a credit institution: law applicable to the cash claim;
2. Assignments of claims arising from a financial instrument: law of the assigned claim;
3. Securitisations: possibility to choose the law applicable.

**In its draft report, the rapporteur Pavel Svoboda (EPP, CZ) supports the general approach proposed by the European Commission. He also suggests to apply it to securitisations and to the assignment of claims arising from a financial instrument, mentioning in particular derivative contracts. Last, Pavel Svoboda supports to exclude the debtor from the scope of the regulation (amendment 1, 5 and 7).**

Amendments tabled reflect the standpoint of various political groups. Maddy Delvaux (S&D, LU) supports the position of the rapport to extend the general approach to securitisations. She also introduces, together with her colleague Evelyne Gebhardt (S&D, DE), two amendments which add a reference to the protection of consumers.

Jean-Marie Cavada (ALDE, FR) and António Marinho e Pinto (ALDE, PT) introduce amendments to clarify that, if two assignments become opposable at the same moment, the law of the assignor's habitual residence applies.

Kostas Chrysogonos (GUE/NGL, EL) and Jiří Maštálka (GUE/NGL, CZ) add a new 76tandardi to article 6(2) to specify that "in a collective redress procedure, jurisdiction for a claim is governed, also when assigned or securitised, by the respective national *lex fori"* until the collective redress framework is further harmonised in the EU.

**Amendments were discussed within the JURI committee on 20th June 2018 and the draft report was adopted with 18 votes against 1 on 10th July 2018. The JURI Committee also voted in favour of opening interinstitutional negotiations.**

17th May 2018: Insolvability and second chance: the Bulgarian Presidency of the Council secures a partial political agreement

The Bulgarian Presidency of the Council of the European Union (EU) published a proposal for a partial general orientation regarding the proposal for a directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring and insolvency procedures, which was initially published on 22nd November 2016 by the European Commission.

The proposal for a partial general orientation only covers parts of the legislative proposal, namely title III (Second chance for entrepreneurs), title IV (Measures to increase the efficiency of restructuring, insolvency and discharge procedures), title V (Monitoring of restructuring, insolvency and second chance) and some definitions in title I (entrepreneurs and discharge).

Title I (General provisions), title II (Preventive restructuring frameworks) and title VI (Final provisions) has been left aside in the partial general approach and should be further discussed in the next working groups.

Regarding the period of time before which a discharge can be granted to an entrepreneur, the Bulgarian Presidency proposed a maximum of three years, with the possibility for this period to be specified in national law. The European Commission had initially proposed a fixed three years period.

With regards to title IV on the efficiency of restructuring, insolvency and discharge procedures, the Bulgarian Presidency indicated that, given the political dimension of the judiciary system for Member states, the compromise proposed is limited to a principle-based approach. Those principles touch mostly upon the designation, selection, supervision and remuneration of practitioners in national judiciary systems.

Among the principles it proposed, the Bulgarian Presidency still requires Member States to conduct some proceedings electronically. However, the implementation period for this provision has been increased from three to five years, and up to seven years for contestations and recourses.

The general partial approach proposed by the Bulgarian Presidency was adopted by Justices Ministers during the Justice Council on 4th June 2018. Discussions continues on parts of the legislative proposals which were not included in the partial general approach.

12th March 2018: the European Commission published a legislative proposal on assignments of claims

The European Commission released a proposal for a regulation "*on the law applicable to the third-party effects of assignments of claims*".

- The **general approach** of the Commission is the one supported by EUF: article 4.1 states that "***the third-party effects of an assignment of claims shall be governed by the law of the country in which the assignor has its habitual residence*** *at the material time.*"

- **EUF is quoted as a source of reference in the proposal of the EU Commission.** The whitepaper released in 2016, EUF Yearbook 2016-2017 and EUF's answers to the public consultation are all quoted in the proposal. **As a result, EUF is mentioned three times in the text of the EU Commission.**

- **Factoring is** presented **with a very positive glance.** EUF's main arguments and messages underlined during our meeting at the Commission with Maggie and Herman's representative, have been taken by the Commission: **"*Factoring is a crucial source of liquidity for many firms*.** *In factoring, a company (the assignor, most often an SME) assigns (sells) its receivables to a factor (the assignee, often a bank) at a discount price as a means for the assignor to obtain immediate cash. The factor will collect the money owed for the invoices and accept the risk of bad debts.* ***The majority of users of factoring are SMEs: Small represent 76%, Medium 11% and Large 13%. Factoring for SMEs is thus regarded by the industry as a basis for economic growth, as SMEs may find sourcing traditional lending more challenging".***

To be noted that the two co-legislators, the European Parliament and the Council have now to work on the Commission's proposal. **The EUF will need to be vigilant with regard to the following steps to come at the EU level.**

### CONTEXT AND OBJECTIVES OF THE PROPOSAL

On March, 12th, the Commission released its proposal for a regulation "*on the law applicable to the third-party effects of assignments of claims*" together with an impact assessment. Stakeholders can provide their feedback on the proposal until May, 23rd 2018.

Prior to this proposal, the European Commission published in 2016 a report *on the effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over the right of another person* and launched in April 2017 a public consultation on *conflict of laws rules for third party effects of transactions in securities and claims.*

The main objective of the proposal is to "*foster cross-border investment in the EU*" that should "*facilitate access to finance for firms, including SMEs, and consumers*".

In that context, the current European legal framework related to the applicable law is then seen as being source of legal an uncertainty, hampering cross-border exchanges. The European Commission considers that current conflict of law rules governing the effectiveness of assignments against third parties, laid down at Member State level, are inconsistent "*as they are based on different connecting factors to determine the applicable law*".

In order to eliminate the current legal risk in cross-border assignments – that does not exist in domestic assignments – and "*potential systemic consequences*", the current proposal aims at establishing an uniform conflict of law rules at the Union level by defining "*which national law should determine the ownership of a claim after it has been assigned on a cross-border basis*".

### THE PROPOSAL

The European Commission decided to adopt the following general approach: "***the third-party effects of an assignment of claims shall be governed by the law of the country in which the assignor has its habitual residence at the material time***" (Article 4.1).

Exceptions of this general rules are provided for some activities such as securitization. There, if expressly stipulated, "*the assignor and the assignee may choose the law applicable to the assigned claim as the law applicable to the third-party effects of an assignment of claims*" (Article 4.2).

To be noted that the assignor is defined as such: "'*a person who transfers his right to claim a debt against a debtor to another person*" (Article 2.a).

**NEXT STEPS**

The European Parliament and the Council have now to work on the Commission's proposal.

12th March 2018: Conflict of laws rules – European Commission published a Communication on the applicable law to the proprietary effects of transactions in securities

On 12th March 2018, the European Commission published a Communication on the applicable law to the proprietary effects of transactions in securities. This communication is accompanied by an impact assessment which also deals with the law applicable to the third-party effects of the assignment of claims.

**THE LEGAL CONTEXT**

The Commission wishes to reduce the legal uncertainty that may arise from different interpretations of the texts relating to cross-border transactions of securities. Depending on the Member State, the Commission points out that in the context of dispute concerning the ownership of a claim or a security, "*the cross-border transaction may be enforceable or not, or might confer the expected legal title on the parties or not*". This may lead to unexpected losses, particularly in case of insolvency.

The Commission recalls that two elements of transactions in securities are governed by conflict of laws rules:

1. **the proprietary element**, which refers to the transfer of property rights and affects third parties;
2. **the contractual element**, which refers to the obligations of the parties towards each other under the transaction and is already regulated by the Rome I Regulation.

The Communication deals with the proprietary element, namely the third-party effectiveness of of cross-border transactions in securities. It concerns in particular three directives: the Settlement Finality Directive, the Winding-up Directive and the Financial Collateral Directive.

**THE COMMISSION'S CLARIFICATIONS**

The Commission discuss the meaning of the terms 'maintained' and 'located', the wording referring to the place of the account or register, which does not imply any difference in substance, according to the institution.

**To determine where the account or register is 'located' or 'maintained'**, the Commission refers to the Recital (8) of the Financial Collateral Directive, the only one stating clearly the common basis for conflict of laws across the EU: "*The lex rei sitae rule, **according to which the applicable law for determining whether a financial collateral arrangement is properly perfected and therefore good against third parties is the law of the country where the financial collateral is located**, is currently recognised by all Member States.*"

Moreover, the transposition into the national law by many Member States can also lead to diverging results. The different ways of interpretation of the conflict of laws provisions which appear to be valid for the purposes of the relevant EU provisions are enumerated by the Commission as follows:

- considering the location where the custody services are provided;
- using the account agreement for information about the place where the account is maintained;
- defining "maintained" in a in a way that it allows the choice of that Member State's law to be valid under the Hague Securities Convention.

The Commission calls on the various authorities to take into account the elements of its communication while asking the Member States to harmonize their interpretation of the EU rules when "*legal discrepancies occur at the level of national interpretations that might cause market disruptions*."

The Commission will continue to monitor developments in this area and does not exclude a possible legislative measures in the future.

| VAT on financial services | Back to summary |
|---|---|
| No update in August 2019 | |

**17th May 2019 - VAT: The VAT simplification for SMEs Directive is not yet ready for adoption by Council of the EU**

The Directive on the simplification of value added tax (VAT) for small and medium-sized enterprises (SMEs) has been removed from the agenda of the ECOFIN Council on 17 May.

Several countries, including Germany, the Netherlands, Ireland and the United Kingdom, reportedly considered that the text was not yet ready for a ministerial discussion due to a lack of consensus, in particular concerning the VAT exemption thresholds and the entry into force of the text.

The Romanian presidency current compromise has not been published.

- **Objectives of the VAT Simplification for SMEs Directive**

The VAT Directive, adopted in 2006, defines a series of administrative requirements related to VAT registration, invoicing, accounting and VAT reporting.

The VAT Directive includes a "**special scheme for small enterprises**", which allows Member States to opt for a set of measures specifically for small businesses.

Introduced in January 2018 by the European Commission, the proposal for a Directive with regard to VAT for small enterprises aims to amend the "Special scheme for small businesses" of the VAT Directive.

The aim of the Commission's proposal is to reduce the negative impacts of the threshold effect of the VAT Directive and broaden the scope of small companies benefitting from exemptions.

For the record, small companies are defined as all enterprises whose Union annual turnover in the single market is no higher than EUR 2 000 000.

- **The VAT exemption thresholds**

The proposed Directive allows Member States to introduce a VAT exemption to SMEs supplying goods and providing services on their national market.

To define the scope of SMEs benefiting from a VAT exemption, the proposal provides for two thresholds:
- A national exemption threshold, determined by the Member State;
- A European exemption threshold which amounts to **EUR 85 000**. Therefore, the national threshold cannot exceed the EUR 85 000 threshold.

The compromise text of the Romanian presidency proposes to maintain the EUR 85 000 European threshold**.** However, some countries view this threshold as too high where others consider it as too low.

The Commission also proposes a VAT exemption for SMEs selling goods or providing services in a Member State where it is not established. Two conditions are provided:

- The enterprise's annual turnover in a Member State should be below the national exemption threshold, determined by the Member State;
- Its overall turnover in the single market (Union annual turnover) should not be higher than **EUR 100 000.**

The Council has not reached a consensus on these two European threshold.

- **Date of entry into force**

The Commission's proposal provides that the text shall apply from the 1st July 2022. However, many Member States request for more time to properly adapt their national law and computing systems to the new rules.

In its compromise text, the Romanian presidency therefore proposes to postpone the deadline for transposition of the Directive to the 31st December 2023 and the date of application of the new provisions to the 1st January 2024.

The proposed date is not consensus. Some countries request for extending the deadline until the 1st January 2025 and one Member State to the 1st January 2026.

**If the list of issues to be settled between the Member States is still long, the Romanian Presidency plans to reach an agreement before the end of June.**

| **Anti-Money Laundering Directive/Tax fraud and tax evasion** | *Back to summary* |
|---|---|

29th August 2019: New tools to fight Money-laundering and terrorism financing

On the 29th of August, the Bank for International Settlements (BIS) published a document on the utilisation of "suptech" for combatting anti-money laundering.

Suptech are defined as the use by financial authorities of advanced data collection and analytics tools.

In this paper, the Bank for International Settlements explores the idea of using those tools to tackle anti-money laundering and the financing of terrorism by 9 authorities that are in charge of the fight against anti-money laundering and terrorism financing. To support them in their tasks, national authorities have set Financial Intelligence Units (FIUs) in charge of gathering and analysing any suspicious transaction.

To that end, the BIS explains that national authorities need advance data analytics tools to analyse the large amount of information received. The authorities in charge of money-laundering and terrorism financing are developing similar tools such as network analysis, natural language processing, text mining and machine learning.

These tools increase their ability to detect networks of related transactions, to identify unusual behaviours and to transform these data in useful information.

However, for some authorities, it is more easy to use information that are already in the market. The paper notes that the optimal solution for a specific authority depends of the authority profile, the characteristics of the financial system and the legal framework in which the authority operates.

The authorities using these tools noted the gains in terms of time savings which is particularly important for jurisdictions that have been heavily impacted with anti-money laundering and terrorism financing cases.

The paper however notes that these innovative technologies gives rise to a number of challenges regarding the computational capacity. There are also issues regarding data privacy and confidentiality. Moreover, it might be difficult to assess the effectiveness of these tools.

The BIS also points out the need for information-sharing among the authorities on the data analytics tools they are developing or using in order to promote peer learning.

23rd August 2019 - The European Commission considers the creation of a supervisory authority

In a confidential document prepared by the European Commission and published by Politico on the23rd of August, the European Commission consider the next steps that could be envisaged to foster the fight against money-laundering and terrorism financing.

In this document, the Commission points out the weakness of the European anti-money laundering architecture. Even though the legal framework has been recently amended (5th Anti Money Laundering Directive and proposal on the ESAs review increasing the EBA's powers), the document notes:

- "*A divergent application of AML rules as different authorities with different tasks, powers, resources and expertise are involved*"
- "*AML supervision is done by national authorities under the current EU legal framework*"
- "*the perception of risks, and actions required to address those risks, may be misaligned the national and european level*"
- *"deficiencies have been observed in the exchange of information and coordination among AML authorities and with prudential authorities, including the European Central Bank (ECB) and the Single Supervisory Mechanism (SSM)*
- *"the absence of a single point of entry for coordination with third countries on AML aspects is problematic when it comes to third party cooperation"*

The effects of these changes in the legal framework are still to be assessed but the Commission is considering the creation of an EU anti-money laundering supervisor. This new authority will be created steps by steps and would take into account the specificity of anti-money laundering supervision and the existing international obligations.

According to the Commission, the creation of an AML is supported by the financial sectors, the European Parliament has encouraged a serious discussion on the topic and the Single Supervisory Mechanism has publicly called for the creation of this authority. However, some Members States seem reluctant in transferring their competences and they have first asked the European Commission to proceed to a thorough assessment of the current legal framework.

The document concludes "*any proposal for EU level AML supervision should therefore be done with proper assessment, consultation and preparation with Member States*".

Following the publication of this document, Mina Andreeva, the Commission's chief spokesperson, declared that this document was an internal document which should not be confused with an official program of the European Commission as it was not approved neither by the current Commission nor by the future team.

24th of July 2019- European Commission and EBA published 4 reports and an opinion on Money Laundering and financing of terrorism

***European Commission: publication of a communication and 4 reports***

On the 24th of July, the European Commission adopted a communication and published 4 reports:

In the communication, the European Commission stresses the need for the full implementation of the anti-money directives (the 4th and 5th directives) and underlines that some issues still need to be addressed to fight anti-money laundering and the financing of terrorism.

- **A report on supranational risk assessment of the money laundering and terrorist financing risks affecting the European Union**

Adopted every 2 years since 2017, this report is a tool to help Member States identifying and addressing money laundering and terrorist financing risks.
The report concludes that the 2017 recommendations were implemented by the Member States but some vulnerabilities remain regarding anonymous products, the identification of beneficial owners and virtual assets.

- **A report assessing the framework for Financial Intelligence Units' (FIUs) cooperation with third countries and obstacles and opportunities**

The FIU's platform has improved the cooperation between FIU but there is a need to reinforce the cooperation between Financial Intelligence Units (FIU).
However, the reports points out the need to improve the tools, the resources, the access to information for FIU and the information sharing between the FIU.

- **A report assessing the conditions and the technical specifications and procedures for ensuring secure and efficient interconnection of central bank account registers and data retrieval system**

The report assess the interconnection of central bank account registries. The Commission suggests the decentralisation of this system and the creation of a common platform at EU level.

- **A report assessing recent alleged money-laundering cases involving EU credit institutions**

The report analyses ten recent publicly cases of money laundering in EU banks. The report concludes that in most of the cases; banks did not respect effectively or did not comply at all with the anti-money laundering directive. Banks lack internal mechanisms to prevent money laundering and they did not align their anti-money laundering policies when they had risky business models.
The report also points out that national competent authorities responded with significant differences in terms of the timeliness and effectiveness of their supervisory actions. The report raises divergences with respect to the supervision of banking groups, resources and expertise.

***European Banking Authority - Opinion***

On the 24th of July, the European Banking Authority (EBA) also published an opinion on money laundering and the financing of terrorism. In its opinion, the EBA underlines that money laundering and terrorist financing can have significant and adverse impacts on the safety of a credit institutions.
In its opinion, the EBA invites prudential supervisors to inform institutions that in the prudential supervisory process they will consider:

- The risks in the applicant's business model, the proposed risk management systems and controls, and the suitability of its shareholders or members and of its management body, senior management;
- The assessment of acquisitions of qualifying holdings

**15th May 2019 - AML: Regulatory technical standards to mitigate AML risks in certain third countries are published in the JOUE**

The 15th May 2019, the delegated regulation with regard to the measures to be adopted by the banking sector to mitigate money laundering and terrorist financing (ML/TF) risks when they have established branches in third countries was published Official Journal of the EU.

The delegated Regulation aims at mitigating risks when a third country law does not permit the implementation of group-wide ML/TF policies and procedures (e.g. data protection or banking secrecy law).

- **General obligations**

For each third country where they have established a branch or they are a majority owner of a subsidiary, credit and financial institutions shall:

1. Assess the ML/TF risk to their group, record that assessment, keep it up to date and retain it in order to be able to share it with their competent authority;
2. Ensure that the risk referred is reflected appropriately in their group-wide ML/TF policies and procedures;
3. Provide targeted training to relevant staff members in the third country;
4. Obtain senior management approval at group-level for the risk assessment.

- **Overcoming third country's law restrictions or prohibitions when necessary**

Where the third country's law **prohibits or restricts the application of policies and procedures that are necessary to identify and assess** adequately the ML/TF risks, namely **customer data sharing and processing**, **disclosure of information policy related to suspicious transactions**, **customer data transfers to Member States** and **record-keeping measures**, credit or financial institutions shall:

- Inform the competent authority of the home Member State **how the implementation of the third country's law prohibits or restricts the application of policies and procedures** that are necessary.
- Ensure that their branches or majority-owned subsidiaries require their customers to **give consent to overcome restrictions or prohibitions** to the extent that this is compatible with the third country's law.

- **Additional measures**

Where the consent to overcome restrictions or prohibitions is not feasible, banks are required to take additional measures to manage the ML/TF risks. These additional measures are defined **article 8**.

- **Last resort solutions**

Where a credit institution or financial institution cannot effectively manage the ML/TF risks by applying the additional measures indicated in article 8, they shall:

- Ensure that the branch or majority-owned subsidiary do **not carry out the occasional transaction**;
- **Close down some or all of the operations provided by their branch** and majority- owned subsidiary;
- Ensure that the branch or majority-owned subsidiary **terminates the business relationship.**

**This Delegated Regulation shall apply from 3rd September 2019.**

**12th March 2019**: AMLV - the Council amends the list of high-risk third countries in money laundering

During the ECOFIN Council that took place on 12th March 2019, the Council approved a new list of countries, reducing it to 15 jurisdictions instead of 23 in the Commission's proposal.

As a reminder, on 12th February 2019, the European Commission published a delegated act to the 4th anti-money laundering directive. This delegated regulation establishes a list of third countries which have strong deficiencies in their national anti-money laundering regimes.

When financial flows come from the listed States, financial institutions will have to carry out additional verifications.

The establishment of this list is a long procedure: the European Commission grants a discussion period to the listed countries to allow them to prove that their anti-money laundering system is not defective.

**Next steps:**
**The delegated act will be debated again at the ECOFIN Council on 14 June 2019. EU Justice Commissioner Věra Jourová declared that a new delegated act will be presented by the Commission in September.**

**13th February 2019**: AMLV - the Commission widens the list of high-risk third countries in money laundering

On 13th February 2019, the European Commission published a delegated act to the 4th anti-money laundering directive. This delegated regulation establishes a list of third countries which have strong deficiencies in their national anti-money laundering regimes.

When financial flows come from the listed States, financial institutions will have to carry out additional verifications.

The delegated act is based on a new methodology including criterion such as the availability of information on beneficial owners of companies.

In February, 23 countries appear in the new list (while only 16 states were in the last list).

During the ECOFIN Council that took place on 28th February 2019, several member States expressed their opposition to the list.

***Next steps***
The Council and the European Parliament have a period of one month, ie until 13th March 2019, to approve or oppose the list.

During the ECOFIN Council that took place on 12th March 2019, the Council approved a new list of countries, reducing it to 15 jurisdictions.

22nd January 2019- ESAs review: the Council is divided on how to conduct interinstitutional negotiations

On the 22nd January 2019, the ECOFIN Council could not reach consensus on the question whether interinstitutional negotiations should start immediately, but only on the anti-money laundering provisions of the review of the European Supervisory Authorities (ESAs), or negotiating later with the European Parliament after finding a political compromise within the council.

As a reminder, in December 2018, the Council decided to review separately the ESAs reform Regulation:

- The first file dealt with the review of the ESAs' competences and supervisory powers (e.g. prohibition and restrictions of products, oversight mandate on environmental, social and governance risks, investigation powers)
- The second file dealt with the EBA's competence on money laundering. This partial political compromise was adopted on the 19th December 2018.

In December 2018 and January 2019, the Council could not reach consensus on the rest of the reform.

In order to accelerate the negotiations, the Romanian presidency of the Council decided to enter into interinstitutional negotiations only on the anti-money laundering file.

As the European Commission and the European Parliament were firmly against discussing separately the proposal, the ECOFIN Council had a discussion over how to conduct negotiations on the ESAs review.

A group of 8 countries (France, Germany, Portugal, Spain, Italy, The Netherlands, Austria and Slovakia) were against the decision not to reach a compromise on the entire proposition for a Regulation.

France and The Netherlands argued the decision whether to negotiation separately the ESA's reform should be voted upon by qualified majority.

However, the responsibility for negotiations with the European Parliament lies with the Romanian Presidency, which simply needs to obtain sufficient support from the Member States. Among the Council, 17 Member states agreed with the Romanian position. Therefore, the Presidency's conclusions were largely supported.

**Against all odds, on the 12th February 2019, the Council adopted political compromise on the entire ESAs review. The interinstitutional negotiations will start within the coming weeks.**

10th January 2019 – ESAs and Anti-money Laundering: the Parliament adopts its report

The Economic and Monetary Committee of the European Parliament has adopted its report on the ESAS review and on the Anti-Money Laundering proposal ( EBA's competences) on the 10th of January.

1. **Money laundering**

Unlike the Council, the ECON Committee has merged both text (competence of the EBA on money laundering and review of the ESAs) in the same report.

The report provides that EBA will have a leading role in facilitating the cooperation between competent authorities to better coordinate action at Union level in material cases of anti-money laundering and terrorist financing.

EBA will have the power to carry out analysis of the information collected and, if necessary, pursue investigations on allegations brought to its attention concerning material breaches or non-application of Union law. Where there are evidence or significant indications of material breaches, EBA will have the power to request competent authorities to investigate any possible breaches, to consider taking decisions and imposing sanctions addressed to financial institutions.

The main competences of EBA in money-laundering are the following (Article 9a : "Special tasks related to combating money-laundering and terrorist financing"):

- ***leading, coordinating and monitoring*** *role in promoting integrity, transparency and security in the financial system by means of adopting measures to prevent and combat money laundering and terrorist financing*
- *collecting* ***and analysing relevant*** *information from competent authorities* ***and other sources*** *relating to weaknesses identified in the processes and procedures, governance arrangements, fit and proper assessments, business models and activities of financial sector operators*
- ***coordinating closely, and, where appropriate, exchanging information, with competent authorities including the European Central Bank,***
- *developing common* ***guidance and*** *standards for* ***preventing and*** *combating money-laundering and terrorist financing in the financial sector and promoting their consistent implementation* ***in particular by developing draft regulatory and implementing technical standards, guidelines, recommendations, and other measures***
- *developing* ***draft regulatory technical standards*** *to specify the practical modalities concerning the collection of relevant information including the type of information that shall be submitted by competent authorities relating to weaknesses identified in the processes and procedures, governance arrangements, fit and proper assessments, business models and activities of financial sector operators to prevent and combat money-laundering and terrorist financing as well as measures taken by competent authorities, without creating any unnecessary duplicates.*

2. <u>**Creation of an executive board within each ESAs**</u>

This committee will strengthen the authorities' competences in their supervisory and sanctioning powers and will replace the Management board.

- **Composition**
  A chairman and full time members: **3 for EBA and EIOPA, 4 for ESMA**
  - The full time members shall be selected on the basis of merit, skills, knowledge and practical experience of financial institution
  - At least one of the full time members should during the one year prior to being appointed not have been employed by a national competent authority.
- **Nomination**
  The Commission shall submit the shortlist to the EP and the composition of the Executive board shall be balanced and proportionate and shall reflect the Union as a whole. Members of the Executive Board shall not hold any office at national, Union, or international level.
- **Duration**
  The term of office of the full time members shall **be 5 years**, renewable once.

3. <u>**New ESAs powers**</u>

   a. <u>**Prohibition and restrictions of products**</u>

**The ESAs will have the power to prohibit or restrict the marketing, distribution and sale of any financial instrument giving rise to serious concerns regarding investor protection (article 9).**

- The authority shall review the decision as soon as possible and at **least every 6 months**

- The prohibition or restriction **may be renewed twice**, after which period it shall become permanent, unless the authority considers otherwise.

b. **Investigation power :**

The authorities will have an investigation power on financial institutions or products giving rise to concerns regarding consumer protection.

c. **New oversight mandate on environmental, social and governance risks ( articles 23):**

This new mandate is aligned with the Commission Action plan on sustainable finance. The ESAs will put in place **monitoring system to assess material environmental, social and governance-related risks**, taking into account the COP 21 Paris agreement.

4. **Reinforcement of the supervisory and regulatory framework of equivalent regimes for third countries ( articles 33)**

The ESAs may develop contacts and enter into administrative arrangements with ***regulatory,*** supervisory ***and, where applicable, resolution*** authorities, international organisations and the administrations of third countries.

**Exception regarding anti-money laundering:** when a third country is on the list of jurisdictions which have strategic deficiencies in their national anti-money laundering and countering the financing of terrorism regimes that pose significant threats to the financial system of the Union, the ESAs shall not conclude cooperation arrangements with the regulatory, supervisory and, where applicable, resolution authorities of that third country.

ESAs shall, on an ongoing basis, monitor regulatory and supervisory developments and enforcement practices and relevant market developments in third countries for which equivalence decisions have been adopted by the Commission.

*5.* **Principle of « *no-action letter* » (article 9c)**

This new provision, time limited, will allow the market players to ignore EU rules that would undermine the market or harm investors.
These "no-action letter" are possible in one of the following reasons. If compliance :

- would place the financial institutions in breach of other legal and regulatory requirements of Union law
- without further level 2 measures or level 3 guidance is deemed not feasible by the Authority
- would seriously detriment or threat any of the following: market confidence, costumer or investor protection, the orderly functioning and integrity of financial markets or commodity markets, the stability of the whole or part of the financial system in the Union.

6. **New competences for ESMA (European Supervisory Market Authority):**
    - the report provides that ESMA will be competent for the authorisation and supervision of prospectuses issued by financial institutions established within the European Union and in third countries
    - ***ESMA CCP Supervisory Committee (article 44a)***: ESMA shall establish a permanent internal committee for the purposes of preparing decisions and carrying out the tasks relating to the supervision of Union and third country CCPs (CCP Supervisory Committee)."

7. **Financing of the European authorities:** the proposal to ask the financial industry to contribute to the financing of the ESAs was not retained. The current financing framework will therefore remain (35% from the Union budget and 65% from national authorities).

**Next Steps:** The Council of the EU will discuss the ESAs review on the 13th of February.

19th December 2018 : AMLV- Council adopts compromise on new anti-money laundering powers conferred on EBA

On December 19th 2018, the COREPER adopted a political agreement on the new anti-money laundering powers conferred on the European Banking Authority (EBA).

As a reminder, following recent scandals involving several European banking groups in Malta, Latvia or Denmark, the European Commission proposed measures to strengthen the anti-money laundering supervision of banking institutions at European level in its communication «Strengthening *the Union framework for prudential and anti-money laundering supervision for financial institutions* ".

The measures proposed in the European Commission's Communication had been incorporated into the proposal for a Regulation to reform the architecture of the three European Financial Supervisory Authorities (ESAs).
To accelerate negotiations, the Council decided to divide the legislative dossier into two parts: a text containing the provisions on strengthening the ESAs' powers to combat money laundering. The second part shall cover other the rest of the reform.

The Council compromise significantly weakens the proposal of the European Commission:

- **The Council compromise text preserves certain transfers of powers**

The political agreement maintains the possibility for the EBA to ask national in charge of anti-money laundering supervision to launch investigation as well as to directly inflict a penalty to a financial market player.
National authority shall have to inform the EBA of the measures taken to comply with its request within 15 working days, whereas the Commission's proposal provided a 10-day-response time.

- **However, the powers transferred to the EBA are considered temporary**

In its compromise, the Council asks the European Commission to make an evaluation implementation, functioning and efficiency of the new competences entrusted to the EBA. This assessment should be presented to the European Parliament and the Council by January 11th 2022.
The text specifies that, until the submission of that assessment, the new anti-money laundering powers conferred on the EBA should be considered as "*a provisional solution* ".

- **Depolarization of the skills of the EBA**

The other objective of the European Commission's proposal was to polarize the anti-money laundering competences and resources within the EBA, which are currently shared by the three ESAs.

The compromise text of the Council weakens this objective by stating that the EBA will take decisions only with the prior consent of the European Insurance and Occupational Pensions Authority (EIOPA) or the European

Securities and Markets Authority (ESMA) where an individual decision concerns financial institutions or competent authorities falling within the competence of these two authorities.

In addition, the Council considers that representatives of EIOPA and ESMA should participate in the meetings of the new ad hoc committee established within the EBA to prepare decisions on anti-money laundering measures, however, without having the right to vote.

Both authorities should also be able to submit written comments on the draft decisions at any time.

Whereas the Council would like to start the negotiations on the money laundering proposal, the co-rapporteur of the ECON committee (Pervenche Berès, S&D, FR) has been clear: the Parliament will refuse to negotiate the files separately as she considers both file linked. The European Commission would like to see both texts negotiated at the same time and will raise the question during the new ECOFIN meeting on the 22th of January.

The main question is to know whether the inter-institutional negotiations will start first with the Commission proposal on money laundering or if both texts (money laundering and review of the ESAs) will be discussed at the same time once the Council reaches a compromise.

The Council of the EU has not reached a compromise yet on the ESAs review.

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4th December: AMLV – The Council adopted the short terms action plan

On December 4th 2018, the Council adopted its conclusions on the action plan on the supervision of financial institutions to combat money laundering.

As a reminder, this action plan aims at enforcing the short-term, non-legislative anti-money laundering measures proposed by the European Commission in its Communication "*Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions* ", published on September 12th 2018.

Eight series of short-term measures to be taken in 2019 are proposed, consisting mainly of:

- Identifying the factors that contributed to the recent cases of money laundering
- Mapping the best supervising practices
- Ensuring effective cooperation between supervisory and anti-money laundering authorities
- Clarifying the criteria for withdrawal of banking license
- Improve the capacities of the European Financial Supervisory Authorities (ESAs) (see the previous note)

Since the measures are not legislative, the European Parliament does not intervene in this decision-making procedure.

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11th October : AMLV – Council adopts Directive on combating money laundering by criminal Law

On October 11th 2018, the Council adopted the Directive on combating money laundering by criminal Law. The Directive was published on October 23 in the Official Journal of the European Union. The European Commission's proposal for a Directive was published on December 21st 2016.

The new rules are:

- Establishing minimum rules on the definition of criminal offences and sanctions relating to money laundering. Money laundering activities will be punishable by a maximum term of imprisonment of at least 4 years.
- The possibility of holding legal entities liable for certain money laundering activities which can face a range of sanctions (e.g. exclusion from public aid, placement under judicial supervision, judicial winding-up, etc.)
- Removing obstacles to cross-border judicial and police cooperation by setting common provisions to improve investigations.

Member States have up to 24 months to transpose it into national Law.

3rd October : AMLV – European Parliament discussed money laundering risks in the EU

This debate took place in a twofold context:

- Several banking scandals highlighting the shortcomings of a system based mainly on the national level
- The publication of a Communication of the European Commission on September 12th 2018 entitled « Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions"

Members of the European Parliament discussed the risks of money laundering in the European banking sector with Juliane Bogner-Strauß, the Austrian Minister for Women, Family and Youth, and Věra Jourová, Commissioner for Justice, equal opportunities and consumer protection of the European Commission.

- **Unanimous view**

All the MEPs who took the floor drew the same conclusion as the Austrian Minister and the European Commissioner: some EU Member States has shown complacency on money laundering in the banking sector and the Dankse Bank scandal has simply underlined the shortcomings of the system. Petr Ježek (ALDE, CZ) added the financial crimes, tax evasion and tax avoidance Committee (TAX3) studies has shown that small Member States cannot exercise adequate control.

All the speakers concluded that it is necessary to reinforce the European supervision.

- **The debate on the creation of a European authority dedicated to the fight against money laundering.**

The proposition to strengthen the powers of the EBA, at least in the initial stages, is backed by the European Parliament.

However, the proposition of creating a European authority working specifically on the fight against money laundering in a second phase divided the European Parliament.

MEP Othmar Karas (EPP, AT) considers it would be desirable to create a European Central Authority which would have the power to exercise controls and impose sanctions.

Several EPP Members rejected this idea: Brian Hayes (EPP, IE) and Seán Kelly (EPP, IE) consider that strengthening the EBA's powers and resources will suffice.

Luděk Niedermayer (EPP, CZ), speaking on behalf of the EPP, said there was no point in transferring more power to the European Institutions or initiate a new piece of legislation. According to the Czech Member of the European Parliament, the solution lies in the effective application of the existing rules.

The Council is expected to propose measures in December.

2nd October : AMLV – the Council discussed the European Commission's communication on strengthening the supervisory powers of EBA

October 2nd 2018, the Economic and Financial Affairs Council discussed short-term anti-money laundering measures proposed by the European Commission in its Communication on "*Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions*", published on September 12th 2018.

The publication of this Communication took place in a specific political context: several banking scandals have shown the shortcomings of a system that mainly relies on the national level. The aim of the communication is therefore to strengthen the powers of the European Supervisory Authorities (ESAs), in particular the competences and resources of the European Bank Authority (EBA) with regard to money laundering.

It should be noted that the measures proposed in the Communication of the European Commission have been incorporated in the proposal for a Regulation to reform the financial supervision architecture.

More specifically, the European Commission proposes short-term legislative and non-legislative measures, as well as the creation of an ad hoc committee established within the EBA composed of national supervisory authorities to prepare decisions on fight against money laundering and financing of terrorism.

- **Which Member States approve the reinforcement of the powers of the EBA?**

All Member States agree on the need to reform the system for combating money-laundering

- ✓ The Member States in favour of transfers of competences

France, the Netherlands, Malta and Estonia expressed their support for the European Commission's proposals.

Spain further suggested to adopt Regulations, which are directly applicable legislative texts, rather than Directives, which would imply a transposition period.

- ✓ The State reluctant to the proposals of the European Commission

Hungary, on the contrary, opposed any loss of national competence.

- ✓ The half-hearted positions

Denmark, Latvia, Estonia, Finland and Luxembourg cautioned against hasty adoption of the European Commission's proposed measures.

The representatives of these Member States called for waiting for the results of the on-going investigations on the several banking scandals to learn from the outcomes.

After drawing lessons, the next step will be to determine whether the European regulatory framework needs to evolve, given the fact that the 5th anti-money laundering Directive has not been transposed yet.

Germany favors the possibility of amending the regulatory framework at the euro area level through the Single Banking Supervision Mechanism before using an approach which embraces all the European Union.

- **The issue of creating an independent entity**

France and Denmark are open to the creation of an ad hoc committee.

However, Cyprus and Spain have expressed reluctance to the creation of a long-term European entity dedicated to the fight against money laundering.

The issue of transfer of powers related to the fight against money laundering will be debated in the Economic and Financial Affairs Council in December.

12th September 2018: AML – the European Commission published a communication on strengthening the EBA's mandate

On 12th September 2018, the European Commission published a Communication entitled: "*Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions*". This communication represents one of the actions aiming at strengthening and improving the powers of the European supervisory authorities (cf. the proposal for a regulation to reform ESAs published on 20th September 2018).

As a reminder, the applicable legal framework is divided into two parts:

1. **Legislation aimed exclusively at regulating the fight against money laundering**

The Union's anti-money laundering framework was strengthened by the adoption of the Fourth AML Directive (2015) and then the Fifth AML Directive (adopted in 2018, transposed by 2020 at the latest).

2. **Aspects of prudential legislation that contribute to anti-money laundering supervision.**

Prudential legislation requires supervisory authorities to take into account money laundering aspects in all their activities, in particular when granting licences. The European Central Bank (ECB) is in charge of authorisation, licence withdrawal and the assessment of qualifying holdings acquisitions vis-à-vis less significant institutions. In the exercise of this competence, the ECB must therefore rely on the information provided by national supervisory authorities and national AML authorities, whose field of action varies fundamentally from one country to another.

I- **State of play**

The Commission draws the following conclusions:

- Compliance with anti-money laundering legislation follows "***a national approach, based on host country supervision, with only minimum harmonisation of supervisory competences, and no harmonisation of the powers of the supervisory authorities***."

- **There is currently neither a mandatory mechanism nor a detailed guideline** setting out obligations for cooperation between the prudential authorities and the anti-money laundering supervisory authorities.

- **No real coordination exists at national level between the prudential authorities and the anti-money laundering authorities**.

- **No coordination exists between European supervisory authorities (ESA) and national authorities** due to the divergent national transpositions within the banking union.

- **Conditions for withdrawal of licence are insufficiently specified.**

- **Cooperation with third countries is insufficient.**

- **ESAs resources are in competition** because anti-money laundering activities fall under the jurisdiction of several authorities.

The European Commission concludes that even the transposition of the 5th AML Directive will not be enough to fill the gaps in the system. The Commission therefore wishes to propose a broader strategy for reshuffling of competences.

II- <u>**Proposed measures**</u>

The purpose of this communication is therefore to set out the measures to be applied to further strengthen the supervision of financial institutions in the Union with a view to combating money laundering. The European Commission wants to propose:

- Legislative measures to put in place the essential amendments
- Non-legislative measures to deal urgently with certain points

**1. Legislative measures that strengthen the role of the EBA**

The two legislative measures that the European Commission wishes to undertake are:

- **Amendment of the Capital Requirements Directive**

The Commission considers that the Capital Requirements Directive may limit the effectiveness of the 5th AML Directive. More specifically, it considers problematic "***its strict confidentiality regime in combination with the absence of a clear obligation for prudential supervisors to cooperate with the relevant anti-money laundering authorities and bodies.***"

- **European Supervisory Authorities' Review**

The European Commission believes that the concentration of anti-money laundering resources and skills within the European Supervisory Authorities (ESA) is necessary. The EBA would be the most empowered authority to receive these resources, since risks of money laundering and terrorist financing would be most likely to have a systemic impact in the banking sector.

The European Commission therefore proposes to transform the current Anti-Money Laundering Committee of the Joint Committee into **a standing committee within the EBA, which would be composed of the heads of all national anti-money laundering authorities**.

Once established, the national supervisory authorities should transfer some competences to the standing committee.

More specifically, the EBA should carry out periodic independent reviews on AML issues. It should be able to collect all the necessary information and data pertaining to anti-money laundering issues, from AML as well as prudential supervisory authorities, which **should include confidential data relating to specific money laundering cases, as well as any money laundering-related findings in individual fit and proper assessments**.

In addition, the EBA should regularly carry out a **risk assessment exercise** to test strategies and resources in the context of the most important emerging money laundering risks. It would have the power to request national supervisors to investigate cases where financial sector operators are alleged to have breached their obligations under the AML Directive.

**2. Non legislative measures**

- **Guidelines on the articulation between the prudential and anti-money laundering rules for financial institutions**

In these common guidance, the EBA should focus on ways to improve cooperation at all stages of the supervision process including addressing issues of the impact of "*different approaches behind the distribution of competences in prudential supervision (i.e. home country control, consolidated supervision) and anti-money laundering supervision (i.e. host country control, information exchange)* ".

- **Agreement between the ECB and the national supervisory authorities**

The European Commission proposes that the European Central Bank concludes with anti-money laundering supervisors a multilateral memorandum of understanding on exchange of information **by 10 January 2019**, as required by the fifth AML Directive.

12th September 2018: AML V – the European Parliament adopted the directive on countering money laundering by criminal law

On 12th September 2018, the European Parliament adopted in plenary a legislative resolution that aims at countering money laundering by criminal law. The adopted text modifies the European Commission's proposal for a directive on countering money laundering by criminal law, published on 21st December 2016.

As a reminder, the purpose of the Commission's proposal for a directive is to tackle money laundering by means of criminal law, allowing the better cross-border cooperation between competent authorities. It aims to harmonize minimum standards in order to criminalise money laundering throughout the EU. The text establishes common definitions for money-laundering offenses and minimum penalties. It also provides the possibility for the national judge to impose additional sanctions beyond imprisonment, such as the prohibition of access to public funding or fines. According to the proposal, legal persons may also be held liable for money laundering activities and may be penalized accordingly.

In addition, the proposed directive aims at removing obstacles to judicial and police cooperation across borders. It aligns the EU legal framework with the international standards set by the Financial Action task Force (FATF) and the Warsaw Convention of the Council of Europe.

During 97tandardi, co-legislators agreed on a maximum imprisonment of at least four years as well as on several alternative penalties to sanction offences defined in the proposed directive.

It is interesting to note that the resolution also mentions the use of virtual currencies which "*presents new risks and challenges from the perspective of combating money laundering. Member States should ensure that those risks are addressed appropriately*." (*Whereas 6*). Virtual currencies are however not further mentioned in the body of the text.

The Council also voted its position on the proposal on 11th October 2018. The final version of the adopted directive will be published in the Official Journal.

10th July 2018: AMLD V – the new directive published in the OJEU

On 10 July 2018, the directive on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (AMLD V) was published in the Official Journal of the EU. It came into force on July 30th.

As a reminder, the Council and the European Parliament reached an agreement on the text on 16 December 2017. The AMLD directive aims to **harmonize minimal standards in order to ensure that money laundering is considered as a criminal offence across the EU**.

The directive sets **common definitions** for offences related to money laundering as well as **minimal penalties**. It also provides the possibility for the national judges to impose additional penalties on top of imprisonment, for example ban access to public funding or fines. The co-legislators also agreed on a maximum term of imprisonment of at least four years as well as on several alternative sentences for the offenses included in the directive.

**Legal persons may also be held liable for money laundering activities** and may be penalized accordingly.

In addition, the directive aims to **remove obstacles to cross-border judicial and police cooperation** by aligning the EU standards with international obligations set by the Financial Action task Force (FATF) and the Warsaw Convention of the Council of Europe.

Finally, the new rules tighten **control over certain means of payment** that can be used for terrorist purposes and broaden **access to information on beneficial ownership and ownership of companies and trusts.**

**Transparency of trusts remains limited to those demonstrating a 'legitimate interest', which includes NGOs and journalists.**

**Member States have until 10th January 2020 to transpose the directive into their national laws.**

30th May 2018: AML: agreement in 98tandardi on the proposed directive on countering money laundering by criminal law

Interinstitutional negotiations (98tandardi) on the proposed directive on countering money laundering by criminal law led to the adoption of a general approach by Justice Ministers at the Council of the European Union (EU).

Published on 21st December 2015, the proposal for a directive aims at 98tandardiza minimal standards in order to ensure that money laundering is considered as a criminal offence across the EU. The text sets common definitions for offences related to money laundering as well as minimal penalties. It also foresees that national judges will be able to impose additional penalties on top of imprisonment, for example ban access to public funding or fines. Legal entities as well as individual will be subject to the provisions of the text.

In addition, the proposed directive aims at removing obstacles to judicial and police cooperation across borders. It aligns the EU legal framework with the international standards set by the Financial Action task Force (FATF) and the Warsaw Convention of the Council of Europe.
During trilogies, co-legislators agreed on a maximum imprisonment of at least four years as well as on several alternative penalties to sanction offences defined in the proposed directive.

Despite uncertainties about the adoption of the text the political level, the proposed directive was validated by the Coreper on 7th June 2018. It now has to be formally adopted by both legislators. Member States will have 24 months to transpose the directive, once published in the Official Journal.

25th May 2018: Agreement at the Council of the EU on transparency requirements for tax intermediaries

The Council of the European Union (EU) adopted a directive which amends directive 2011/16 on administrative cooperation in the field of taxation. The new directive reinforces transparency requirements on financial operations with the objective of preventing money laundering and aggressive cross border tax planning.

The text adopted requires intermediaries to report to competent authorities any service or operation in which at least one of the hallmarks defined in annex IV is present. Intermediaries are responsible for reporting the service or operation within 30 days. National competent authorities are then required to automatically share information reported via a centralized database.

The directive defines the notion of intermediaries very broadly, so as to cover all possible professions. Article 3 of the directive 2011/16 is amended to add the following definition:

> *""intermediary" means any person that designs, markets, 98tandardi or makes available for implementation or manages the implementation of a reportable cross-border arrangement.*
> *It also means any person that, having regard to the relevant facts and circumstances and based on available information and the relevant expertise and understanding required to provide such services, knows or could be reasonably expected to know that they have undertaken to provide, directly or by means of other persons, aid, assistance or advice with respect to designing, marketing, 98tandardiz, making available for implementation or managing the implementation of a reportable cross-border arrangement."*

Finally, the directive required Member States to incorporate in national law penalties for intermediaries who would not fulfill their obligations. Such penalties would need to be effective, proportionate and dissuasive.

As a reminder, the Council of the EU is sole legislator on this text, as it is a tax matter. The European Parliament, which was only consulted, adopted an opinion prepare by Emmanuel Maurel (S&D, FR) on 3rd March 2018.

The directive has been published in the Official Journal of the EU on 5th June 2018. It will be transposed by Member States by 31st December 2019 and will apply as of 1st July 2020.

19th April 2018: AMLD V: the European Parliament adopts the trilogue agreement

The European Parliament adopted in plenary session the text of the fifth anti-money laundering directive (AMLD V). The text adopted was the result of the agreement reached on 15th December 2018 in the framework of interinstitutional negotiations. In a press release, the European Commission welcomed the European Parliament's vote and commitment against money-laundering and in favour of fair taxation.

As a reminder, the main elements of the text agreed on during the trilogues are the following:

**THRESHOLD FOR THE IDENTIFICATION OF BENEFICIAL OWNERS**

The European Commission initially suggested a threshold for the identification of beneficial owners set at 10% of the entity capital for non-financial entities (NFEs). The European Parliament supported this proposal and asked for the extension of this threshold to companies. This demand of the Parliament was rejected and the threshold for companies in the text is set at 25%.

**POLITICALLY EXPOSED PERSONS**

Germany finally agreed on the scrutiny requirements for the politically exposed persons (PEPs). The European Parliament was refusing to lighten these requirements and Germany was initially against maintaining the *status quo*. Germany finally accepted under the condition that a revision clause be added to require the European Commission to revise this provision two years after the transposition date.

**IMPLEMENTATION OF BENEFICIAL OWNERSHIP PROVISIONS**

The European Commission's proposal to modify article 14 of ALMD to apply beneficial ownership provisions both the new and existing clients. However, this proposal was nuanced and scrutiny will only apply to existing clients "*at appropriate times*" and "*on a risk-sensitive basis*". It will apply in cases of legal update of client information.

Transparency provisions regarding trusts remain limited to people demonstrating a legitimate interest. The European Parliament obtained that NGOs and journalists be included in the definition of the legitimate interest set in recital 35. On the contrary, access on beneficial ownership information for companies will be public.

**FOREIGN COMPANIES**

The European Parliament asked for foreign companies to be included in the scope of AMLD V, to the extent that the beneficial owner would be European. This demand was not successful, but the possibility of extending beneficial ownership provisions to foreign companies was included in the revision clause.

| **Data protection** | *Back to summary* |
|---|---|

No update in August 2019.

25th January 2018: the European Commission publishes a new website to prepare for the implementation of the GDPR

The European Commission published a new page on its website, dedicated to the implementation of the **General Regulation on Data Protection** (GDPR). The page offers several facts sheets addressed to individuals as well as businesses. Simultaneously, the European Commission published a communication providing

| Guidelines/working documents by the Article 29 Working Party in view of the entry into application of the Regulation[26] | |
|---|---|
| Right to data portability | Adopted on 4-5 April 2017 |
| Data protection officers | |
| Designation of the lead Supervisory Authority | |
| Data protection impact assessment | Adopted on 3-4 October 2017 |
| Administrative fines | Adopted on 3-4 October 2017 |
| Profiling | Work ongoing |
| Data breach | Work ongoing |
| Consent | Work ongoing |
| Transparency | Work ongoing |
| Certification and accreditation | Work ongoing |
| Adequacy referential | Work ongoing |
| Binding corporate rules for controllers | Work ongoing |
| Binding corporate rules for processors | Work ongoing |

guidance on the direct application of the GDPR. It recalls objectives of the GDPR and reviews the preparatory measures already taken at the European level.

**KEY MESSAGES FROM THE EU COMMISSION**

The communication reminds stakeholders of keys elements introduced by the new data protection rules:

- **A single set of rules for the whole European Union**, which would guarantee legal certainty for companies and a consistent level of data protection for all citizens.
- **Same rule will apply to all companies providing services in the** EU, even if those companies are based outside of the EU.
- **New and stronger rights for citizens:** the rights to information, data access and to be forgotten are strengthened. **A new right regarding the portability of data allows citizens to transfer their data from a company to another**. This should open new business opportunities for companies.
- **Protection against data breach is reinforced:** a company incurring a data breach needs to inform the data protection authority within 72 hours.
- **Binding rules and deterring fines:** all data protection authorities will be able to impose fines up to 20 million euros or, for corporates, up to 4% of the yearly global turnover.

The Commission's communication also reviews progress made by the Article 29 Working Party, which gathers national data protection authorities from all Member States.

The Commission highlights how important it is that the guidelines drafted by the Article 26 Working Party are subject to **public consultation before they are adopted.**

Taking into account the fact that the benefits and new opportunities brought by the new data protection rules are not uniformly spread across the EU, the Commission launched a new **online platform targeting SMEs** and aiming at assisting them in complying and taking advantage of the GDPR. The Commission specifies that information available online will be regularly updated to adjust to new questions raised by stakeholders.

**FACT SHEETS FOR STAKEHOLDERS**

Finally, as a complement to its Communication, the European Commission published a set of fact sheets, regarding implementation, advantages for companies and the role of stakeholders.

The Commission also recommends to companies which are not confident about their compliance status to get in touch with the relevant national data protection authorities.

The European Commission calls on Member States to accelerate the transposition of the GDPR in their national law. To date, only Germany and Austria fully transposed the GDPR, even though it **will enter into force on 25th May 2018.**

| **E-invoicing** | *Back to summary* |
|---|---|
| No update in August 2019. | |

| **European Account Preservation Order for the attachment of bank accounts** | *Back to summary* |
|---|---|
| No update in August 2019. | |

| **Financial transaction tax** | *Back to summary* |
|---|---|
| No update in August 2019 | |

**14th June 2019** – FTT: An agreement with ten Member States on financial transaction tax expected in autumn

The 14th June 2019, the ECOFIN Council discussed the new financial transactions tax (FTT) compromise. Following the ECOFIN meeting, the German finance Minister announced an agreement on the FTT compromise is within reach.

For the record, the German and French governments submitted a new proposal, less ambitious than the Commission's proposals, to spur new member States to join the enhanced cooperation framework. However, during the ECOFIN Council meeting, no other Government showed interest in joining the current intergovernmental framework (composed of France, Germany, Belgium, Portugal, Austria, Slovenia, Greece, Spain, Italy and Slovakia.)

One of the points under discussion was the pooling of revenue collected at a national level between participating Member States.
The 19th June 2019, a French and German common paper entitled "*The mutualisation of financial transaction tax revenue*" was published.
This document proposes to ensure that each State participating to get a guaranteed minimum revenue of 20 million euros. The objective is to make sure that no country leaves the project on the basis that the FTT does not generate enough revenues.
The common paper also summarizes the main points of the new compromise: the FTT will only apply to shares of companies whose market capitalisation exceeds €1bn. Initial issuance, market-making and intra-day trading will be out of the scope of application. The tax rate will not be lower than 0.2%.
Member States expects to collect €3.45 billion per year (The FTT was projected to generate between €30 and 35 billion annually in the original proposal tabled by the European Commission in 2013.)

**22nd May 2019 - FTT: A draft directive will be debated in the ECOFIN Council**

On the 22nd May 2019, during the EU Member States' ambassadors meeting (COREPER), the delegations participating in the enhanced cooperation mechanism on the European Financial Transaction Tax (FTT) asked to schedule a debate on the new compromise proposed by France and Germany at the Ecofin Council of 14th June 2019.

For the record, since 2013, the discussions on a proposal for a directive on the FTT have been taking place within the framework of the enhanced cooperation mechanism between ten Member States, namely France, Germany, Belgium, Portugal, Austria, Slovenia, Greece, Spain, Italy and Slovakia. Since 2017, the negotiations that took place between 10 states were stalled but in December 2018, the German and French governments have submitted a new proposal. Less ambitious than the Commission's proposals, to the text invites new member States to join the enhanced cooperation framework.

The compromise has not been published (yet).

- **Scope of application**

The tax would apply to shares issued by companies whose market capitalization exceeds one billion euros and whose registered office is established in at least one participating Member State.

- **A lower tax base**

As a reminder, the first two proposals from the European Commission, dated 2011 and 2013, included all types of financial instruments.

To overcome blocking points, the Franco-German compromise **reduces the base to shares only**.

Moreover, the taxation of derivatives, one of the main dividing issue of the past negotiations, should not exist in the proposal.

- **The rate**

The text provides that the tax rate for each transaction will be set by each participating Member State, but should **not be less than 0,2% nor exceed 0,3%**.

The 0,3% rate, however, will be discussed.

- **The location of taxation**

The FTT would be due to the tax authorities where the issuing entity has its head office. Therefore, the location of the transaction will have no impact.

The compromise specifies, however, that discussions on this point are still needed.

- **Revenues destination and shares**

Regarding the revenues destination, the idea of the French and German governments is to allocate the funds raised either to the EU budget or to Eurozone budgetary instrument (as current members of the enhanced cooperation framework are in the Eurozone).

In the first case, the national contributions to the EU budget of the participating countries would be reduced by the total FTT revenues collected.

In the second case, the FTT revenues would be mutualised only between the Eurozone participating countries in the enhanced cooperation via an intergovernmental agreement. The rest of Eurozone Member States not involved in the FTT group "*would need to provide a contribution based on a different key*".

If non-Eurozone countries decide to join the enhanced cooperation, they would not participate in the mutualisation of FTT revenues, but would retain the funds collected by them.

This question remains to be settled.

Regarding the revenues collection, the current version of the compromise suggests the mutualisation of revenues. The final amount allocated to a country would depend on the percentage of its gross national income (GNI), regardless of how develop capital markets are in participating countries.

However, some States expressed concerns given that it would favor some smaller States disproportionality.

- **Entry into force**

According to the Franco-German compromise, the participating Member States shall have transposed the Directive into their national legislation by 1st January 2021. The provisions would applyfrom 1st June 2021.

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**The proposal was debated at the June 14 ECOFIN Meeting.**

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2nd December 2018 : a European financial transaction tax is put back on the negotiating table

On December 2nd 2018, German and French finance ministers, Olaf Scholz and Bruno Le Maire, announced they were preparing a joint proposal for a European financial transaction tax (FTT) that would directly increase the EU budget. Participating countries would be allowed to use the revenues to offset their contributions to the wider EU budget.

The European Union has debated on a common FFT for 8 years:

- **2011: The European Commission proposes a tax applicable to the whole Union**

In September 2011, the European Commission published a proposal for a tax on financial transactions.

During years of debate, the scope of the proposed levy has been scaled back. Indeed, the European Commission's proposal seemed excessive for several countries. Some countries tried to promote a simpler version of the tax that would exempt most transactions in financial derivatives.

The negotiations failed.

- **2013: Second proposal through enhanced cooperation procedure**

As the member states have failed to come to a global consensus, 11 countries have launched an 'enhanced cooperation' mechanism, which allows at least 9 member states to progress on issues of common interest, without being held up by the other countries.

The 11 countries working on the Financial Transaction Tax project were: France, Germany, Austria, Belgium, Spain, Estonia, Greece, Italy, Portugal, Slovakia and Slovenia.  Estonia finally withdrew from the project.

The proposal involved a minimum 0.1 % tax rate for transactions in all types of financial instruments, except for derivatives which would be subject to a minimum 0.01 % tax rate.

Negotiations are currently blocked.

- **2017- 2018: the Franco-German couple tries to revive the negotiations**

The proposed scope of the FTT has been a point of contention since its inception.

Therefore, to revive the project, the French president Emmanuel Macron proposed a simplified FTT proposal: the taxation of derivatives, one of the main stumbling blocks of previous negotiations, should not exist in the Franco-German proposal.

The proposal is modelled on a system already in place in France where all transactions involving domestically issued shares by companies with a market capitalization of over 1 billion euros are subject to the tax. Transactions on shares and bonds would be taxed at 0.1%, and derivative products at 0.01%.

The proposal will concern the 27 countries of the European Union. It will have to be voted unanimously.

| **Accounting issues** | [*Back to summary*](#) |
| --- | --- |

No update in August 2019.

17th January 2018: EFRAG publishes preliminary findings of its assessment of IFRS 9 impact's on long-term investments in equity instruments

The European Financial Reporting Advisory Group (EFRAG) published letter sent to the Olivier Guersent, Director General of DG FISMA at the European Commission. Annexed to the letter, EFRAG also released preliminary findings of its impact assessment of IFRS 9's effects on long-term investment.

Following on to a request for technical advice sent on 29th March 2017, EFRAG collected **quantitative data on the impact of IFRS 9 on equity instruments**. This data was gathered through a public consultation and the analysis of annual reports.

EFRAG's early finding show that investment strategies are shaped by multiple factors, including regulatory factors but also economical and commercial factors. Respondents to the public consultation indicated that the implementation of IFRS 9 **should not impact the holding period for equities**. They mention that they plan on making use of the election in IFRS 9 to measure investments in equities measurement at **fair value through other comprehensive income** ('FVOCI').
According to data collected by EFRAG, there is **no strong view on the impact of IFRS 9 on asset allocation**. EFRAG observes that insurance companies say they are considering modifying their asset allocation decisions, without indicating how. Some respondents to the public consultation indicate that they consider allocating assets in different classed. In particular, EFRAG notes a trend to use unquoted equities as an alternative to quoted equities, since unquoted equities are less volatile and mostly collected as dividends - which are recognized in profit or loss.

EFRAG will continue its work to assess the impact of IFRS 9 in long-term investment and should publish its final report during the second semester 2018.

12th January: EBA published guidelines on disclosure requirements of IFRS 9 transitional arrangements

The European Banking Authority (EBA) published final guidelines regarding the disclosure requirements of IFRS 9 transitional arrangements or analogous expected credit losses (ECLs).

The new global accounting standard for financial instruments, IFRS 9, entered into force on 1st January 2018. In the European Union, transitional provisions provide for a progressive implementation of IFRS 9 over five years.

In its guidelines, the EBA provides a template to be used by financial institutions when reporting to supervisors on own funds, capital and leverage ratios.

The objective of these guidelines is to ensure the consistency and comparability of data reported by credit institutions during the transition period towers the full implementation of IFRS 9.

The guidelines will become applicable two months after their publication in all official languages of the European Union.

| **FinTech** | [Back to summary](#) |
|---|---|
| No update in August 2019 | |

19th of July 2019 – EBA publishes a report on the regulatory regime of FinTech

On the 19th of July, the European Banking Authority (EBA) published its analysis on the regulatory framework currently applicable to FinTech firms.
The report focuses on:

- The monitoring of national developments on the regulatory perimeter;
- The national regulatory status of FinTech firms;
- The approaches followed by national authorities when they grant authorisations under the capital requirement directive, the payment services directive and the e-money directive. The analysis focuses on the application of the principles of proportionality and flexibility.

The result of the analysis of national legislations applied to Fintech showed two trends:

- Certain activities such as payment initiation services and account information services are now being subject to the payment service directive after its transposition in the national law;
- Ancillary and non-financial services and activities of FinTech firms not subject to any regulatory regime.

Based on its findings, the EBA decided to continue observing the activities in the market and **will not put forward any specific recommendations**.

Regarding the authorisation process, the EBA notices a consensus on considering the principle of proportionality to be embedded in the current EU legislative and regulatory framework. There is also **consensus to apply the principles of proportionality and flexibility the same way for traditional and innovative business model**. The EBA will continue monitoring the application of the principle of proportionality and will assess whether it is used to fast track applications from FinTech firms for authorisation as a payment or an e-money institution.

Regarding the attachment of conditions, limitations and restrictions to the authorisations, **the EBA points out the existence of various practices consisting in the imposition of conditions** (change in the legal structure of the applicant, additional supervisory requirements, limits on deposit taking, limits on credit granting…).The EBA considers further work to ensure a fully level playing fields in this area with the development of guidelines of the CRD V setting out a methodology for granting authorisations under the CRD V.

Finally, regarding the authorisation for credit institution, the EBA considers further monitoring and analysis for the use of the special regime provided in CRD IV for FinTech credit institution which allows a lower initial capital of at least 1 million euros.

12th of July 2019 – ESMA publishes a report on the licensing of FinTech firms

On the 12th of July, the European Securities and Markets Authority (ESMA) published its report on the Licensing of FinTech business models.

This report is based on two surveys that gathered evidence from national competent authorities (NCAs) on the licensing regimes of FinTech firms in their jurisdictions:

- A first survey identifying gaps and issues in the EU legislative framework, assessing the divergence between the national legislative frameworks;
- A second survey identifying the ways in which national authorities applied the principle of proportionality and the principle of flexibility when they grant a license to FinTech firms.

In the report, the ESMA confirms that national authorities **do not distinguish** between FinTech and traditional business models in their authorisation and licensing activities.

The main findings of the report are the following:

- The ESMA underlines that the existing EU legislative framework **do not fit** within the existing rules for **crypto-assets**, **Initial Coin Offering (ICOs)** and d**istributed ledger (DLT).**
  In that regard, national authorities are calling for more clarity at the EU level with respect to the definition of financial instruments and the legal nature of crypto-assets. Tokens which are financial instruments should be subject to the full regulation and tokens that are not considered as financial instrument should be subject to a minimal level of regulation.

- **More clarity** on the governance and risk management processes for **cyber security and cloud outsourcing**

- **Links and interdependencies between the innovation facilitators and authorising approaches for innovative Fintech business models**
  Innovation facilitators are important to map approaches applied to FinTech and in identifying the areas where the legislation and licensing requirements need changes and adaptation.
  Regulatory sandboxes also have an impact on the licensing regime for FinTech.

- **Platform-type projects for facilitating corporate financing of non-listed assets**
  The licensing requirements applied to these projects (Multilateral Trading Facilities, Organised Trading Facilities…) may be disproportionate to the scope of such projects. ESMA will consider further analysis for the emergence of platforms facilitating SMEs' financing needs.

- **EU crowdfunding regime**
  The directive, in discussion between the co-legislators would enable a EU level playing field for cross-border services providers.

ESMA concludes that most innovative business models can operate within the existing EU rules and does not put forward additional recommendations to the European Commission for a change of the EU legislation.

**25th June 2019 -** Crowdfunding: The Council has issued a compromise providing for minimum harmonization

The 25th June 2019, the Council published the political compromise reached by the Member States regarding the proposal for a Regulation on crowdfunding.
As a reminder, the European Parliament already adopted its position in plenary session on March, 26th 2019.

- **Widening of the scope of the Regulation**

The European Commission's proposal for a Regulation imposed a threshold of 1 million euros for a maximum consideration for each crowdfunding offer. The Members of the ECON Committee raised to 8 million euros the threshold.
The Council aligns with the Parliament's position by raising the threshold to EUR 8 million.
However, the EUR 8 million threshold is a maximum threshold: Member States have the possibility of aligning their threshold with the one they laid down under the Prospectus Regulation.

- **National competent authorities and ESMA's roles**

In European Commission's proposal, the European Securities and Markets Authority (ESMA) had the power of:

- granting an authorization to provide crowdfunding service
- supervising crowdfunding platforms

In the text on the co-legislators, these powers fall under the competence of the competent national authorities.
The ESMA's role is limited to the establishment of a **public register** of all crowdfunding service providers operating in the Union.

- **Cross-border crowdfunding platforms**

In the texts, crowdfunding service provider might provide crowdfunding services in a Member State other than the Member State whose competent authority granted authorization.
Member state shall designate a **single point of contact for cross-border activities**. The single point of contact will be responsible for **granting authorization** to cross-border platforms and **administrative cooperation** between competent authorities as well as with ESMA.

- **Creation of two categories of investors**

The Council compromise introduces a distinction between two types of investors:

- sophisticated investors
- non-sophisticated investors

A sophisticated investor is defined as "*an investor who possesses the awareness of the risks associated with investing in capital markets and adequate resources to undertake those risks without exposing itself to undue financial consequences*" (annex II).
More precisely, sophisticated investors can be legal entities or natural persons meeting the identification criterion defined the Annex II of the Regulation.

- **Two different protection regimes**

Investor protection measures apply systematically to non-sophisticated investors (entry knowledge test and simulation of the ability to bear loss, investment limit, reflection period, etc.).

"*Sophisticated investors*" are excluded from some provisions. For instance, Member States may decide to introduce a limit to the amount of money non-sophisticated investors can invest into an individual crowdfunding project (The amount cannot be lower than EUR 1 000 per crowdfunding project or 10% of the investor's net wealth in crowdfunding projects).
**Next step:**
**The interinstitutional negotiations will start when the European Parliament' activities resume.**

**6th June 2019** - FinTech: The FSB published a report on decentralisation in the financial system

The 6th June 2019, the Financial Stability Board (FSB) published a report on the impacts of decentralised financial technologies on financial stability and supervisory framework.
Decentralised financial technologies are defined as "*technologies which may reduce or eliminate the need for intermediaries or centralised processes that have traditionally been involved in the provision of financial services*".

Decentralisation in the financial services sector generally takes one of three broad forms:

- **Decentralisation of decision-making**: This involves a move away from a single trusted financial intermediary or infrastructure towards systems in which a broad set of users is able to make decisions about whether and how to undertake financial transactions;
- **Decentralisation of risk-taking**: This involves the shift away from the retention of risk (e.g. credit and liquidity risk) on the balance sheets of individual traditional financial intermediaries towards more direct matching of individual users and providers of financial:
- **Decentralisation of record-keeping**: This involves a move away from centrally held data and records, towards systems in which the ability to store and access data is extended across broader consortia of users. Verification of such data and records may also be more distributed, for example via consensus mechanisms.

The FSB estimates that the two main technologies that are currently enabling decentralisation of financial activities are distributed ledger technologies (DLTs) and online peer-to-peer (P2P) plateforms.

- **Decentralisation of financial activities will not reach a large scale in the near term**

The report concludes that applications displaying the three forms of decentralisation – that is, full decentralisation of decision-making, risk-taking and record-keeping – seem unlikely to achieve an economically significant scale in the near term.
However, technologies that facilitate decentralisation along one or two of these dimensions may, over time, have a noticeable economic impact.
Payments and settlement, capital markets, trade finance and lending are already significantly impacted.

- **Risks and opportunities to be taken into account by regulators**

The FSB estimates that financial stability could benefit from decentralized financial activities, by leading to greater competition and diversity in the financial system, therefore, reducing the systemic importance of some existing entities.
The FSB's report also draws a list of risks for the financial stability:

- Concentrations in the ownership and operation of key infrastructure;
- Concentrations in technology;
- A possible greater degree of procyclicality in decentralised risk-taking;
- Uncertainties concerning the determination of legal liability;
- Lower consumer protection;
- Difficult recovery and resolution of decentralised structures.

- **Regulatory and supervisory adaptation to decentralisation**

Decentralisation may pose challenges for financial regulatory and supervisory frameworks, particularly those that currently focus on centralised financial institutions, or when financial services are difficult to link to specific entities and/or jurisdictions.
The FSB advises regulators and supervisors to adopt **an activity-based approach.**

**The report has been delivered to G20 Finance Ministers and Central Bank Governors for their meeting in Fukuoka on 8-9 June.**

**27th March 2019: Crowdfunding** – the European Parliament adopted its definitive position

On March 27th 2019, the European Parliament adopted its position in a plenary sitting on the proposal for a Regulation on European Crowdfunding Service Providers for Business. The Parliament discussed and voted the Committee on Economic and Monetary Affairs' (ECON) report adopted on the 9th November 2018.

As a reminder, the proposal for a Regulation of the European Commission, published on May 8th 2018, aims at creating a European label for investment- and lending-based crowdfunding platforms regulated by the European Securities and Markets Authority (ESMA).

The text adopted by the European Parliament significantly amends the European Commission's proposal by:

- Raising the EUR 1 million threshold for a maximum consideration for each crowdfunding offer to EUR 8 million.

- "Renationalizing" the institutional framework of authorization and supervision of crowdfunding offers: The powers attributed to ESMA in the European Commission's proposal for granting an authorization to provide crowdfunding service and to supervise crowdfunding platforms are transferred to the competent national authorities. The role of ESMA is reduced to a mediator function when a competent authority disagrees about the procedure or content of an action or inaction of a competent authority of another Member State.

**Next steps**
**The legislative procedure is now blocked at the level of the Council of the European Union, which has still not adopted its position.**

**26th February 2019**: FinTech - Yves Mersch believes that partnerships between banks and FinTech is the best option

On February 26th 2019, Yves Mersch, member of the Executive Board of the European Central Bank (ECB) delivered a speech on the penetration and development of FinTech and BigTech in the payment and credit markets.

1. **The development of FinTech in the payment services sector**

Yves Mersch notes that payment services is the most affected sector by competition from FinTech.

He believes that the structure of the market will change in the years to come. Many banks have already begun to adjust their strategies by investing more in technology or by partnering with FinTech.

According to him, there are two possible scenarios:

- Banks invest in their digital transformation

In this scenario, banks leverage technology to enhance their products, services and operations. It would allow banks to retain their customer relationships and core banking services. In this scenario, **risks to financial stability would be rather low, as financial services provision would remain largely subject to the existing prudential regime.**

- Banks do not invest in new technologies

In the second scenario, banks do not provide the digital financial services expected by their customers. FinTech, and especially BigTech, would dominate the market, with all the risks involved.

Yves Mersch concludes however that the reality will certainly be more complex than this binary distinction.

In any case, **the ECB will adapt its supervisory activities**.

However, the ECB member of board recalls that European regulators and supervisors should take a cautious approach, keeping in mind that **preserving financial stability should not stifle innovation**.

**2. The development of FinTech in the credit services sector**

While the payment services sector is the most affected by the development of FinTech, FinTech competition is also growing in the credit sector. Peer-to-peer lending platforms, also known as crowdlending, are an example of FinTech companies selling credits. These platforms consist of matching lenders with borrowers, who are usually individuals and businesses.
This new model of credit services offers lower fees than in the traditional industry. However, Steve Mersch believes it is currently unlikely that lending platforms threaten the banks' position in the credit market. He explains two main reasons:

- Lending platforms are **unable to perform liquidity transformation** on a significant scale: they **can't "*provide short-term liquidity services for depositors and long-term loans for borrowers*"**.
- **Lending platforms are less resilient during shocks**, "*being more prone to funding freezes and swings in credit risk appetite than banks*"

On the contrary, **banks have both insured deposits, and higher levels of capital, which supports lending during downturns**.

**3. BigTech's entrance into the payment and credit market**

Yves Mersch notes that BigTechs are entering the payment and credit markets.

These companies have many competitive advantages that allow them to rapidly penetrate markets, as such big amounts of data they can leverage in order to market their services.

**The ECB board member considers that the entry of BigTech into the financial services sector would generate several benefits for consumers:**

- These companies could help diversify the sources of credit in the economy, thereby increase investment and growth.
- By using the advanced technologies they have (predictive algorithms, machin learning and BigData), BigTechs would modernize credit service markets by making them more efficient. By speeding up the

processing of loan applications, reducing transaction costs and improving risk assessment, competition in credit markets would be stimulated.
- BigTechs are capital intensive businesses, therefore, they have the necessary financial capacities for economic shocks.

**However, Yves Mersch recalls that the entry of BigTech into the financial services markets can also present important risks:**
- BigTechs could significantly increase market concentration by exploiting the competitive advantages they have (large amounts of data, large capitalization and advanced technologies);
- BigTechs are generally less motivated by the return on their credit activity and more by the access to additional data.
- Their funding and functioning models for credit services, which often combine internal and external investors, and consist of selling loans to third-party investors, are risky.

***Next* steps :**

Yves Mersch reminds that the ECB will monitor FinTech development, as well as BigTech's motivations, funding and functioning models.

**14th February 2019**: FinTech - FSB published a report on the impact of FinTech and Bigtech on market structure and financial stability

On February 14th 2019, the Financial Stability Board (FSB) released a report on the impact of FinTech and BigTech developments on market structure and international financial stability.

1. **What would be the consequences of the development of FinTech on traditional actors?**

FinTech companies have found several niches, mainly in the areas of payment and credit offerings:
- Crowdlending platforms (or Peer-to-peer lending platforms),
- Crowdfunding platforms,
- Targeting types of customers that are often less well served by traditional banks (such as small businesses).

The FSB reports that the credit services sector could certainly be subject to increased competitive pressure from FinTech.

According to the FSB's report, innovations developed by FinTech can increased competition among financial institutions by fostering transparency and credit allocation performance. The emergence of FinTech providing bank-type services, such as credit or payment services, can therefore have an impact on the structure of the market and the behavior of traditional banks.

**However, the FSB report underlines that, so far, competitive pressures on traditional actors has been limited in most market segments: while FinTech's credit supply is growing rapidly, it remains low relative to the overall credit offer.**

Moreover, FinTech do not have sufficient access to low-cost funding or enough customers to be a serious competitive threat to traditional financial institutions in mature financial market segments.
The report concludes that FinTech and traditional players tend to be complementary.

**The competitive threat would come rather from BigTech.**

2. **What would be the consequences of the development of BigTech on traditional actors?**

BigTechs – which are large technology companies with well-established networks and large amounts of data - have entered the financial services markets. They are selling payment, credit, insurance and asset management services.

Often, BigTech associates with financial institutions by distributing their credit or insurance products.
The FSB estimates that BigTech's entry into the financial services sector can generate positive externalities for international economic growth:

- BigTech access to a large amount of data would allow them to perform better risk assessments.
- BigTech could also offer cheaper (or even free) services by using the data obtained through their traditional services.

Yet, their arrival will have others consequences, notably in terms of supervision.

- **Strengthening FinTech and BigTech supervision**

The report underlines that, although FinTech do not currently appear to be a risk to financial stability, supervisors will have to strengthen their supervision of banks. Therefore, the FSB calls on supervisors to **closely monitor any weakening of lending standards by banks or other "inappropriate" risk-taking to face the competition generated by FinTech and BigTech**.

Regarding BigTech, the FSB explains that, as BigTech's financial activities are unregulated, they can pose serious risks to the international financial stability. Moreover, the report notes that **supervisors do not really understand BigTech's motives in the financial services market**.

A better understanding of their motives will be essential to **determine whether it will be necessary to apply a regulatory framework to BigTech**.

- **Growing dependence on third parties**

In its report, the FSB notes that banks may increasingly be dependent on third parties providing services related to data processing and storage.

Data processing and storage is becoming an activity whose added value in financial services is increasing. The concentration of data by third parties may therefore have consequences on the structure of the market.

Therefore, the FSB calls on regulators and supervisors **to better monitor the activities of companies providing cloud services**.

***Next steps :***
The Financial Innovation Network (FIN) of the FSB is currently studying BigTech's activities in the financial sector.

The Basel Committee on Banking Supervision (BCBS) and the International Organization of Securities Commissions (IOSCO) will particularly monitor the increasing dependence of banks on third parties.

7th January 2019- FinTech: the ESAs published a report on innovation hubs and regulatory sandboxes

On 7th January 2019, the European Supervisory Authorities (ESAs) published a joint report which presents a situational analysis of the innovation facilitators, namely innovation hubs and regulatory sandboxes, in the European Union.
This report follows the publication of the FinTech Action Plan by the European Commission in March 2018, which mandates the ESAs to identify good practices to facilitate cooperation and coordination among innovation facilitators.

- **Innovation hubs**

An innovation hubs is defined as a point of contact for firms that raises "*enquiries with competent authorities on FinTech-related issues and to seek non-binding guidance on the conformity of innovative financial products, financial services or business models with licensing or registration requirements and regulatory and supervisory expectations*".

Innovation hubs are established in 21 Member States. The ESAs noted that start-ups are the largest group of firms using innovation hubs. On the opposite, regulated firms such as credit institutions and insurers prefer to have a dedicated contact points within the national competent authorities, including questions relating to innovation.

Innovation hubs mostly deal with questions related to:
- Regulated activities involving payment and credit services;
- New technologies, including digital customer identification tools, DLT technology, crowdfunding and peer-to-peer funding platforms, robo-advice, electronic tools for personal financial management, big data, smart contracts and cloud technology.

- **Regulatory sandboxes**

A regulatory sandbox : is defined as a scheme that enables "'*firms to test, pursuant to a specific testing plan agreed and monitored by a dedicated function of the competent authority, innovative financial products, financial services or business models. Sandboxes may also imply the use of legally provided discretions by the relevant supervisor but sandboxes do not entail the disapplication of regulatory requirements that must be applied as a result of EU law*."

Only 5 Member States (DK, LT, NL, PL and UK) have established the sandboxes system so far. The ESAs found several common features between countries:
- Sandboxes are not limited to a specific area of the financial sector, but are cross-sectoral (banking, investment, insurance, payment).
- Specific test parameters, such as limitations, restrictions and other warranties, are defined prior to admission to the testing phase.
- Throughout the test phase, it is essential that consumers, to whom a product or service under test will be provided, are properly protected (retail customers or institutional clients).
- Sandboxes may involve, during the test phase, the exercise of proportionate application of supervisory powers.

- **Challenges**

ESAs identified supervisory challenges:

- Monitoring the pace of the industry: Some authorities highlighted the difficulty of finding and retaining staff with the appropriate financial technology knowledge and experience;
- Domestic coordination between different supervisory authorities due to the cross-sectoral nature of FinTech firms;
- Cross-border cooperation: the ESAs express concerns about potential diverging approaches between the different national competent authorities to the design and functioning of innovation facilitators

▪ **Solutions**

The report stresses the need to strengthen cooperation, coordination and knowledge sharing between competent authorities (both at national and European levels). In order to solve the challenges mentioned previously, the ESAs identified two possible solutions:

- The development of the **ESAs' own-initiative guidance on cooperation and coordination** between innovation facilitators.
- The **creation of a European network** that bonds innovation facilitators.

The report also stresses that best practices monitoring should strengthen consistency in the design and functioning of innovation facilitators.

**In 2019, the ESAs will continue to monitor the work of national innovation facilitators. They could take further steps to promote a common approach to financial technology in the EU.**

**In addition, the European Commission is working on identifying obstacles to the development of financial technologies, notably through the Expert Group on Regulatory obstacles to financial innovation.**

9th November 2018 : Crowdfunding - the ECON Committee published its Report on the proposal for a Regulation on European Crowdfunding Service Providers for Business

On November 9th 2018 European Parliament's committee on economic and monetary affairs (ECON) published its Report on the proposal for a Regulation on European Crowdfunding Service Providers for Business. The ECON draft Report, written by Ashley FOX (ECR, UK) and its amendments were published respectively on August 10th and September 13th 2018.

As a reminder, the proposal for a Regulation of the European Commission, published on May 8th 2018, aims at creating a European label for investment- and lending-based crowdfunding platforms regulated by the European Securities and Markets Authority (ESMA).

▪ **New definition of " crowdfunding services "**

The article 3 of the Report provides a new definition of crowdfunding services :

✓ **Direct crowdfunding service** is the "*facilitation of matching a specific investor with a specific project owner and of matching a specific project owner with a specific investor*"
✓ **Intermediated crowdfunding service** is defined as "*the facilitation of matching an investor with a project owner and determining the pricing and packaging of offers in respect thereof, or the*

*facilitation of matching a project owner with an investor and determining pricing of offers in respect thereof, or both*."

The article 4 of the Report defines more precisely the notion of **intermediated crowdfunding service. It comprises:**

- ✓ **The placing without a firm commitment basis of transferable securities or of the facilitation of loans issued by project owners.**
- ✓ **The offer of investment advice** with regards to transferable securities or the facilitation of loans issued by project owners
- ✓ The reception and transmission of client orders in relation to transferable securities or the facilitation of loans issued by project owners.

- <u>**Scope of the Regulation**</u>

The European Commission's proposal for a Regulation imposed a threshold of EUR 1 million for a maximum consideration for each crowdfunding offer. The Members of the ECON Committee raised to 8 million euros the threshold.

In addition, Article 4 of the report provides that " *legal persons established in a third country cannot apply for authorisation as crowdfunding service providers under this Regulation*"

- <u>**Strengthening investor protection**</u>

Within the European Commission's proposal for a Regulation, there is no provision to be applied in the event of a failure of crowdfunding projects. On the contrary, the proposal states that "*crowdfunding service provider interacts with its clients through a digital platform **without taking on own risk***".

This provision has not been changed within the ECON Committee report. However, conditions for granting an authorisation to provide crowdfunding service were added to better protect investors:

- ✓ Capital requirements

Article 10. 1 (g) sof the Report states that crowdfunding service provider's will have to provide "*business continuity arrangements*" in order to "*ensure that any loan repayments and investments will continue to be administered to the investors in the event of insolvency of the prospective crowdfunding service provider*"

Moreover, crowdfunding service provider's will have to provide the proof that they are "*adequately covered or hold sufficient capital against the financial consequences of its professional liability in the event of a failure to comply with its professional obligations set out in this Regulation*."

- ✓ Due diligence requirements

The ECON Report introduced new requirements related to Due diligence. It implies demonstrating that:

- Evidence that the project owner has no criminal record regarding infringements of national commercial Law, national insolvency Law, national financial services Law, anti-money laundering Law, national fraud Law or national professional liability obligations

- Evidence that the crowdfunding platform is not established in a non-cooperative jurisdiction, as recognized by the relevant Union policy, or in a high-risk third country.

✓ Alignment of the interests of crowdfunding platform with the investors

Article 7a of the Report supplements article 7 on conflicts of interest.

The article sets a number of conditions for align their incentives with those of investors :

- **Crowdfunding platforms may participate in the funding of a project. That participation shall not exceed 2% of the capital accumulated for the project**.
- A success fee (carry) may be granted to the crowdfunding service provider whenever the project exits successfully from the crowdfunding platform.
- Crowdfunding service providers shall describe to ESMA the alignment of interests policy that they plan to use prior to the authorisation and request its approval.
- Crowdfunding platforms may modify the alignment of interests policy every three years. Any modification is subject to approval by ESMA.
- Crowdfunding platforms shall explicitly describe their alignment of interests policy on their website in a prominent place.

▪ **Exclusion of digital currencies**

As a reminder, the rapporteur Ashley Fox wanted to regulate the "Initial coin offerings" (ICO) introducing specific provisions in this Regulation.

▪ **The role of the ESMA and national authorities**

The powers attributed to ESMA in the European Commission's proposal for granting an authorization to provide crowdfunding service and to supervise crowdfunding platforms are transferred to the competent national authorities.

The ESMA's role is reduced to a mediator function when a competent authority disagrees about the procedure or content of an action or inaction of a competent authority of another Member State.

The ECON report excludes crowdfunding service providers using ICOs from the scope of the Regulation. The report, however, invites the European Commission to initiate a legislative proposal dedicated to the ICOs in the future.

▪ **Administratives and criminal sanctions**

The articles of the European Commission's proposal on administrative sanctions and other measures have been rewritten.

Member States will have to set administrative penalties applicable when crowdfunding service providers do not fulfill the obligations provided for in the Regulation.
The report also gives the power to Member States to provide for criminal penalty instead of administrative sanctions.

5th September 2018: The ESA's Joint Committee publish a report on robo-advice in financial sector

Following the publication of the first paper in 2015 on automation in financial advice and the report in 2016 on the same topic, a new analysis was published on the evolution of automation in financial advice in the securities, banking and insurance sectors over the past two years.

As a reminder, "automation in financial services" is the phenomenon by which advice is provided to customers without, or with very little human intervention. The provision of advice is based on algorithms or "decision trees".

The objective of this analysis is to determine whether legislative intervention or supervision is necessary in view of the potential risks that these innovations may pose.

The report identifies benefits and risks of the automation in financial services:

**Benefits:**

- ✓ Reduced costs for both customers and financial institutions;
- ✓ Easy access to more products and services to a wider range of consumers and wider client base for financial institutions;
- ✓ Improved quality of the service provided.

**Risks:**

- ✓ Clients having limited access to information and/or limited ability to process that information;
- ✓ Flaws in the functioning of the tool due to errors, hacking or manipulation of the algorithm;
- ✓ Legal disputes arising due to unclear allocation of liability;
- ✓ Widespread use of automated tools.

The analysis shows that the phenomenon of automation of financial services seems to be slowly increasing. The total number of companies and customer-users, however, remains limited.

The Joint committee notes that automated services are often offered through partnerships established by financial intermediaries rather than offered by FinTech firms.

Although some trends are emerging (such as the use of BigData, Chatbots, extension to a broader range of products), the conclusion of this report makes it clear that there has been no substantial change in the market since the last publication in 2016.

The Joint committee considers that, given the modest evolution of the phenomenon, no legislative action is necessary. However, considering the importance of the subject and the emergence of several business models, a new analysis should be conducted "*if and when the development of the market and market risks warrant this work*".

3rd July 2018: The EBA published two reports on FinTech

On 3 July 2018, the European Banking Authority (EBA) published two reports, as foreseen in its FinTech roadmap presented on 15 March 2018:

1. The impact of FinTech on incumbent credit institutions' business models
2. The prudential risks and opportunities arising for institutions from FinTech

**1. WHAT IS THE IMPACT OF FINTECH'S DEVELOPMENT ON INCUMBENT CREDIT INSTITUTIONS?**

The EBA notes that the fast development of technological innovations, combined with new demands from consumers, is forcing credit institutions to rethink how to offer their services as well as their business model.

According to the EBA, the key factors of transformation of credit institution models are:
- **Customer expectations and behavior;**
- **Profitability concerns**, in a context of low interest rates and higher provisioning costs;
- **Stronger competition;**
- **Regulatory framework**, with the entry into force of the second Payment Services Directive (PSD 2) and the General Data Protection Regulation (GDPR).

**The most threatened activities by the development of FinTech are the payment and settlement services as well as the activities of retail banks**, activities that are not highly capital-intensive. On the other hand, their development is seen more as an opportunity for **commercial or trading banking**, where new services can be offered while further automating certain processes.

The EBA ranks the main actors in the "FinTech arena" as follows:
**(i)** **Incumbent institutions**
**(ii)** **New digital-based institutions,** that offer fully digital services while having a credit / payment / e-money institution license
**(iii)** **Other FinTech firms**, without a credit / payment / e-money institution license, which offers services based on financial innovation and new business models / applications / products
**(iv)** **Technology providers** and ICT companies, including BigTech

**The most advanced areas of innovation are online and mobile banking, biometrics and cloud computing**. However, the institutions are **only at an exploratory stage** for the use of big data, artificial intelligence, machine learning and block chain technologies**.**

Relations between traditional actors and FinTech are very rich and varied (integration, buy-back, collaboration etc.). The advantage of the traditional players lies in their financing capacity, their expertise, their brand image and their clientele, while the FinTech bring innovative ideas, a more consumer-oriented approach and a greater appetite for new technologies.

In this new framework, traditional actors adopt different approaches, between "*digital transformation*" and "*digital disruption*", which can sometimes endanger their structures. One of the challenges is to invest in these new actors while, at the same time, mobilizing dedicated intern teams.

**According to the EBA, key risk factors impacting the sustainability of business are:**
1. **Digitalization/innovation strategies,** between proactive, reactive and passive actors
2. **Legacy ICT systems,** in particular raised by PSD 2 and GDPR
3. **Execution capabilities**
4. **Access and maintenance of talent staff**
5. **Stronger competition with the new entrants.**

The EBA believes that greater involvement of BigTech in the provision of financial services could transform the existing financial intermediation ecosystem.

In general, the EBA considers that for the moment, **FinTech do not seem to be in direct competition with traditional actors**, even though some of them have reached a critical size. **The real competition seems to be between the incumbent institutions themselves**.

It needs to be noted that in its conclusions, the EBA underlines that despite some important investments in FinTech by traditional actors ***"the benefits from FinTech investments do not seem to have materialized yet when it comes to cost reduction and revenue growth/returns****, as institutions struggle to quantify and trace the outcomes of innovative solutions.* ***This could indicate that the effects of FinTech on incumbent credit institutions are not material at this stage****."*

2. THE PRUDENTIAL RISKS AND OPPORTUNITIES ARISING FOR INSTITUTIONS FROM FINTECH

In this second report, the EBA stresses that the development of FinTech is affecting the financial services sector across its entire value chain.

According to the EBA, this situation can change the risk profile of financial institutions, leading them to review their risk management frameworks and strategies. However, **add to the emergence of new risks, innovations are also sources of prudential opportunities**.

The report develops 7 practical cases that concern:

1. **Biometric authentication using fingerprint recognition**
2. **Use of robot-advisors for investment advice**
3. **Use of big data and machine learning for credit scoring**
4. **Use of DLT (Distributed Ledger Technologies) and smart contracts for trade finance**
5. **Use of DLT in compliance processes, particularly in relation to anti-money laundering policies in the context of customer identification and verification procedures (customer due diligence)**
6. **Mobile wallet with the use of NFC (*Near Field Communication*) like Apple Pay**
7. **Outsourcing core banking/payment system to the public cloud**

In general, the EBA considers that, ***"no significant implementation of sophisticated technologies as such was noted"***. The reasons are, for the European Authority, the caution of the institutions and their lack of confidence in these technologies. Similarly, regulatory and supervisory uncertainty also inhibit their use. In this context, mobile wallets and biometrics are the most used technologies.

In terms of risks, **operational challenges, ICT (cyber security, digital fraud), legal and compliance, reputation and data use risks** are identified by the EBA.

However, the EBA concludes that the opportunities brought by these technologies "***could potentially outweigh the risk*****", if governance and risk management procedures are properly implemented.**

No formal recommendation was proposed by the EBA. Nevertheless, other reports should follow.

23rd March 2018: the ECB published guides to assessment of licence applications for banks and FinTechs

The European Central Bank (ECB) updated two guides regarding the assessment of credit institution licence application. The first covers specifically licence applications from banking FinTech which **fulfil the conditions to be considered as credit institution under the Capital Requirement Regulation (CRR)**.

The second covers licence applications from traditional banks. By editing two different guides, the ECB demonstrates that it takes into account, from a supervisory perspective, the rise of Fintech. It also reaffirms that **all actors should be subject to similar prudential requirements, disregarding their business models.**

As a reminder, article 4.1 of CRR defines a credit institution as "*an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account*".

**A GUIDE FOR FINTECHS**

In its specific FinTech guide, the ECB defines banking FinTech, subject to CRR, as "*technology-enabled innovation in financial services that could result in new business models, applications, processes or products with an associated material effect on the provision of financial services*". This definition has been drafted by the Financial Stability Board in June 2017, and the ECB demonstrates its alignment with international supervisors.

The ECB notes that banking FinTech can be subsidiaries of existing credit institutions as well as new players.

The objective of the FinTech licence application guide is to **ensure consistency in the European Union, across competent authorities, when it comes to processing licence applications.** The goal is also to make sure that FinTech fulfil a number of requirements with regards to:

- ✓ **Governance**
- ✓ **Internal organisation**
- ✓ **Activities**
- ✓ **Capital, liquidity and solvability**

Regarding this last point, the ECB underlines that, when granting a licence, competent authorities will need to pay attention to **additional capital requirement which might be required in cases of higher risks of financial losses**. This impacts in particular FinTechs in their launching phase and entities whose business model is evolving (point 16).

The ECB nevertheless **stipulates that banking FinTechs shall be subject to the same standards as other credit institutions.**

**A GUIDE FOR TRADITIONAL BANKS**

The ECB also published a general guide dedicated to licence applications from credit institutions.

The guide first recalls the relevant legislative framework for credit institutions, mentioning the **need to specify definitions used in CRR and CRD IV**. This echoes similar concerns raised by the European Banking Authority (EBA) in November 2017 regarding the ambiguities of CRR definitions when applied to other financial institutions (OFIs). The EBC thus clarifies its methodology for setting definitions of the following terms:

- ✓ **Deposit and other repayable funds**: the ECB choses the broad definition established by the Court of Justice of the European Union (ECJ) in the *Romanellli* case (c-366/97, 11/02/1999): "*other repayable funds" refers not only to financial instruments with the intrinsic characteristic of repayability, but also to those which, although not having that characteristic, are the subject of a contractual agreement to repay* *the funds paid*". With regards to deposits, the ECB refers to the definition set at article 2(1)(3) of the directive on deposit guarantee schemes. The ECB also notes that funds received in relation to specific services, in particular payment services, are outside of the scope of CRD IV and CRR.

- ✓ **Public**: the ECB clarifies the definition for prudential purpose, which implies the "*protection of a natural or legal person against entrusting funds to unsupervised entities whose financial soundness is not established*".

- ✓ **Granting credit for own account**: in such cases, the credit institution is creditor and the credits that it grants become its assets. **The ECB refers to Annex I to CRD IV which lists credit activities benefiting from mutual recognition, among which factoring.**

The guide then details guiding principles for the granting of a banking licence, in particular with regards to governance, risks management and prudential capital. Finally, the guide specifies the different steps of the application process.

**The ECB guides are note binding and apply as of their publication.**

15th March 2018: FinTech – ESAs published the Final Report on Big Data

On 15th March 2018, the Joint committee of European Financial Supervisory Authorities (ESAs) published a report on the impact of Big Data on financial companies and consumers.

The three ESAs, namely the European Securities and Markets Authority (ESMA), the European Banking Authority (EBA) and the European Insurance and Occupational Pensions Authority (EIOPA), highlight the potential risks associated with Big Data while considering that, **at this stage of development, the potential benefits outweigh the risks**. In particular, the ESAs note that many of the pitfalls identified in the report are **already partly taken into account by current legislation**.

The report prepared jointly by the three ESAs is based on the results of a public consultation conducted between December 2016 and March 2017. It aims to fulfil three objectives:

- to **map the development of Big Data** by assessing both the benefits and the risks;
- to **raise awareness among consumers of their rights** under existing legislation;
- to **raise awareness among** financial institutions of their existing legal obligations and encourage the adoption of good practices.

The analysis of the responses received in the public consultation indicates that the use of Big Data has many advantages, both for the financial industry and for the consumers, since it makes it possible **to develop tailor-made financial products and services**. In addition, Big Data improves **fraud detection mechanisms and the efficiency of internal procedures in financial institutions**.

The observations of the participants in the public consultation show that the accuracy of the data processed via Big Data mechanisms is essential to develop a suitable service or product. Equally important is the protection of the data against the cyber-attack risk. In this regard, the ESAs report reviews the existing legal provisions at European level concerning the security of information systems.

19th February: FinTech: BCBS published sound practices regarding bank-FinTech relationships

The Basel Committee on Banking Supervision (BCBS) published a report outlining sound practices related to the implications of FinTech developments for banks and bank supervisors.

In particular, the BCBS report focused on three technological innovations, which are 1° **Big Data, 2° distributed ledger technologies (DLT) and 3° cloud computing**.

Looking at FinTech, BCBCS particularly focused – through case studies – on three types of FinTech activities: **payments services, lending platforms and "neo-banks".**

**In its report, the BCBS built its analysis around five scenarios, which provide hypothesis of how FinTech could impact the financial services sector**:

1. The "best bank" scenario, in which the digitalisation and modernisation allow existing actors to improve;
2. The "new bank" scenario, in which exiting actors are challenged and replaced by new entrants;
3. The "distributed bank" scenario, in which financial services are increasingly fragmented to the benefit of specialised FinTech and of existing actors;
4. The "relegated bank" scenario, in which banks turn into service providers and in which customer relationships are owned by new intermediaries;
5. The "disintermediated bank" scenario, in which banks become irrelevant as customer can directly interact with financial services providers.

**Regarding banks' business model**, the BCBS considers that it will need to adapt to innovative uses of technologies, as well as to the increasingly involvement of third parties through outsourcing and partnerships. The BCBS also notes that the development of FinTech brings an increase in operational, strategic and profitability risks, but also in compliance and cybersecurity risks.

The BCBS underlines that, given the numerous and quick innovations in the banking sector, **banking standards and supervisory expectations will also have to adjust. However, it stated that these adjustments should not be detrimental to prudential requirements.** The BCBS highlights the importance of implementing demanding compliance standards without compromising innovation.

Regarding supervisory practices, the BCBS considers that cross-sector cooperation among banking supervisors and other supervisors will have to improve. Similarly, international cooperation among supervisors should intensify.

The development of financial technologies should also benefit supervisors according the BCBS. It indeed brings opportunities for supervisors ('SupTech'), as they can develop new tools. It also implies that supervisors' competencies need to evolve in order to be consistent with the new banking environment.

7th March 2018: the European Commission will present its FinTech Action plan

On 7th Mach, the European Commission will present its action plan to encourage and supervise the development of financial technologies - FinTech. Euralia managed to get the draft action plan titled: "*FinTech Action plan: For a more competitive and innovative European financial sector*".

In its preliminary draft, the European Commission recognizes the disruptive potential of the rise of technology-enabled innovation in financial services. Based on the recommendations made by the European Parliament in its FinTech report of 28 April 2017, the Commission highlights its cross-sectoral dimension. The Commission also intends to respond to the conclusions adopted on 19th October 2017 by the European Council and to the answers received within the public consultation held between 23 th March and 15 th June 2017.

According to the Commission, the FinTech are indeed transforming financial services, but they also drive the innovation within the digital single market and fall within the scope of the Commission's strategy for **cyber security and electronic communication**. The Commission also puts forward its concerns about the protection of personal data, especially since the General Data Protection Regulation (GDPR) comes into force in May 2018.

1. **ENABLE INNOVATIVE BUSINESS MODELS TO REACH EU SCALE**

In its action plan, the Commission recognizes the great potential of the Fintech, both for the provision of new services and for the improvement of already existing financial services. Encouraging the development of the FinTech ecosystem in the European Union involves finding the **right regulatory balance** between the necessary safeguards and the flexibility needed for innovation, all within a proportionality adjusting the requirements to the company size.

**a. Clarify and harmonize licensing requirements for FinTech**

The European Commission stresses that the **European passport** for financial services is a great tool for FinTech as it allows them to access to the entire European market, once the license has been obtained.

Based on the responses received during the public consultation, market players consider that the existing regulatory framework at European level is adapted to the development of the Fintech and that the authorization processes are sufficiently proportionate. However, according to the Commission, **it is essential to ensure that European standards are applied in the same way throughout the European Union.** In this respect, the European Commission welcomes the work done by the European Banking Authority (EBA) and the European Central Bank (ECB).

On the basis of this work, the Commission intends to evaluate the appropriateness of adjusting the European framework on cryptocurrency and the Initial Coin Offerings. In addition, the Commission plans to organize a round table on these issues in the second quarter of 2018.

**b. Develop common standards and interoperable solutions**

According to the Commission, an EU-wide FinTech market will not reach its full potential without the development of **open standards that make interoperability possible**, simplify the exchange of data between market players and facilitate competition.

The need for a greater standardisation is important in particular in blockchain/distributed ledger technologies (DLT), Application Programming Interfaces (APIs) and Identity Management.

The Commission also refers to the **revised Payment Services Directive** (PSD 2), which requires banks to open communication channels for FinTech, while ensuring compliance with the provisions of the GDPR. In this sense, the development of standardized APIs would be, according to the Commission, a solution to protect a level playing field.

**c. Set up « *the FinTech facilitators* » : the case of innovation hubs and regulatory sandboxes**

The Commission's public consultation did not lead to a consensus on the issue of *sandboxes*, innovation facilitators that benefit from a lighter regulatory framework. The Commission notes that no less than 13 Member States have set up such *sandboxes*, which support start-ups in their development phases and inform about regulatory requirements. The Commission also notes that both the ESMA and the EBA have been recently mapping existing *sandboxes* in order to highlight good practices. **As this work of the EBA and the ESMA is still ongoing, the Commission will present a Blueprint with recommendations by the end of 2018.**

## 2. SUPPORT THE UPTAKE OF TECHNOLOGICAL INNOVATION IN EUROPE

While the UK's exit from the European Union is getting closer, the European Commission seems fully aware of the need to ensure the competitiveness of the European framework in order to attract talents.

### a. Review the fitness of the existing regulation in order to ensure its technological neutrality

The European Commission reaffirms that technological neutrality is one of the **guiding principles of its action on innovation**. However, most of the rules applicable to the financial sector pre-date the emergence of FinTech, **so they should be adjusted to ensure that they are technologically neutral**. **This applies in particular to the rules on data protection (management and data transfer) and consumer knowledge (e-identification, application of anti-money laundering standards).** Likewise, the Commission notes the uncertainties regarding the law applicable to services using DLTs.

As a result, the Commission announces **the establishment of a group of experts** to assess the adequacy of the European regulatory framework in the second quarter of 2019.

### b. Remove obstacles hindering the use of *cloud* services

The European Commission takes note of the benefits that *cloud* services can offer in terms of cost savings, efficiency gains and flexibility. However, the outsourcing to *cloud* services should be harmonised and properly supervised. The Commission therefore encourages the European Supervisory Authorities (ESA) to produce guidelines on this subject, and **at the same time encourages *cloud* service providers to establish codes of conduct**.

### c. Enabling FinTech applications with the EU Blockchain initiative

The Commission emphasize that in January 2018 it launched a **European Blockchain Observatory and Forum** in order to gather expertise on this issue in a cross-sectoral manner. The Commission points out that the DLT applications, including blockchain, go beyond the financial sector.

In addition, the Commission plans to launch in early 2018 a **public consultation on the digitization of regulated information about companies listed on EU regulated markets**.

### d. Build an EU FinTech Lab and encourage the research

The European Commission announces the **establishment of an EU FinTech lab within which the European financial supervisory authorities and the national authorities would discuss with the suppliers of technological solutions in a neutral and non-commercial space/zone**. The aim is to strengthen the information of the authorities and an open dialogue with the actors.

## 3. ENHANCE SECURITY AND INTEGRITY OF THE FINANCIAL SECTOR

While the European Commission stresses the potential and many benefits of FinTech, it does not forget the risks that can arise for **financial stability and consumer protection.** Thus, within the review of the European system of financial supervision, the Commission has already proposed that the ESAs would contribute to enhancing the security and integrity of the European financial sector regarding the FinTech.

**In addition to the risks of cyber security,** the growing importance of data in the FinTech business models makes it, in the Commission's view, **particularly important for the financial sector to ensure compliance with the provisions of the General Data Protection Regulation (GDPR).**

More specifically, the Commission identifies the following areas of intervention:

a. **Promote the information sharing on cyber risks;**
b. **Identify good national practices in this area;**
c. **Evaluate the costs and benefits of a cyber security test for European financial actors.**

In spring 2018, the Commission should organize a workshop for public and private sector actors to identify barriers to information sharing on cyber risks.

**The action plan on FinTech is expected on 7th March 2018. It will also be accompanied by a legislative proposal on crowdfunding and peer-to-peer funding.**

| **Other topics of interest** | *Back to summary* |
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10th September 2019: Valdis Dombrovskis re-appointed as DG FISMA Commissioner in Von der Leyen's team

On the 10th of September, the new European Commission President elect presented her team composed of 26 members (The United Kingdom did not present a candidate).

This new team, after the European Parliament approval, should take office on the 1st November.

Valdis Dombrovskis, the current commissioner for the DG for Financial Stability, Financial Services and Capital Market Union (DG FISMA) was designed as one of the 3 Executive Vice-President of the future Commission (along with Frans Timmermans and Margrethe Vestager).

As Executive Vice-President he will be in charge the portfolio named "*An Economy that Works for People*". In parallel, he is also reappointed as commissioner for DG FISMA.

The mission letter addressed to Valdis Drombrovskis details his tasks:

As an Executive Vice-President he will:

- Coordinate the work on the action plan to implement the European Pillar of Social Rights;
- Lead the work on strengthening the role of social dialogue at European level;
- Lead the work on refocusing the European Semester so that it integrates the United Nations in order to ensure that the EU economic policy support societal and environmental goals;
- Strengthen the democratic accountability of the EU economic governance;
- Coordinate the work on the Sustainable Europe Investment Plan;

- Lead the work for a new long-term strategy for Europe's industrial future and will co-lead the SME strategy to improve their access to finance;
- Lead the work on strengthening the role of the Euro.

As the commissioner for DG FISMA he will "*pursue his work to preserve and improve financial stability, protect savers and investors and ensure the flow of capital to where it is needed*".

To that end, he will:

- **Complete the Banking Union** notably the backstop to the Single Resolution Fund and the European Deposit Insurance Scheme;
- **Accelerate the work towards a Capital Markets Union** to diversify sources of finance for companies and tackle the barriers to the flow of capital;
- Develop a green financing strategy to ensure that investments contribute to a climate-neutral economy;
- **Develop a FinTech strategy to support new digital technologies;**
- Create a new private-public fund specialising in initial public offering for SMEs;
- **Promote a new comprehensive approach to fighting money laundering;**
- Develop a new approach with Member States on cryptocurrencies;
- Make proposals to ensure Europe is more resilient to extraterritorial sanctions by third countries.

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**The Parliament's Committees will hear the Commissioners-designate between September 30th and October 8th. The European Parliament will vote in plenary on the 21th of October to validate this new College.**

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29 July 2019: the EU Commission published a Communication on Equivalence regime

On July, 29th 2019, the European Commission published a communication on Equivalence in the area of financial services. This communication explains the main purposes of equivalence, the underlying approach of equivalence decision and the recent improvements of equivalence regimes in the EU law.

**1. <u>The main purposes of equivalence</u>**

The European Commission states that "*the EU is committed to promoting open, fair and efficient financial markets that operate within rigorous prudential and conduct frameworks*" and equivalence "*is one of the key instruments at the EU's disposal in furthering that goal in the external dimension of the internal market*".

In that context, the EU equivalence policy satisfies three objectives:

- ✓ it reconciles the need for financial stability and investor protection in the EU, with the benefits of maintaining an open and globally integrated EU financial market;
- ✓ it is pivotal in promoting regulatory convergence around international standards and avoiding global market fragmentation;
- ✓ it is a major trigger for establishing or upgrading supervisory cooperation with the relevant third country partners.

The EU Commission considers that for markets participants, the advantages are the following:

- ✓ reducing (or even eliminating) overlaps in compliance requirements for both EU and third country market players;
- ✓ making certain services, products and activities of third country companies acceptable for regulatory purposes in the EU and thus facilitating their availability on the EU market;

- ✓ in some instances, enabling a coherent prudential regime to apply to EU banks and other financial institutions operating outside the EU, thus lowering the cost of EU firms' investments/exposures in third countries by facilitating capital management in particular.

If equivalences can strengthen cross-border exchanges, **it is important to specify that an equivalence decision does not automatically implies a "*European passport*"**: many equivalences, notably in the banking package (regulation and directive on capital requirements - CRR / CRD), do not give an access to the European market, only recognize the regulatory and supervisory framework of a third country.

### 2. <u>The approach of the EU Commission before equivalence decision</u>

The European Commission explains that granting equivalence is above all a *"risk management"* exercise, a balance between the potential benefits for the European financial market players and the risks associated with cross-border activities.

Three main criteria when granting equivalence to a third country:
- ✓ risk-sensitivity (impacts on EU financial stability, market integrity, investor protection and the level playing field in the EU internal market);
- ✓ compliance with the rules laid down in European law during the regulatory and supervisory assessment;
- ✓ taking into account the impact of the third country's activities on the European markets ("proportionate" assessment, reinforced in case of systemic exposures)

Others objectives, sometimes political ones, can be taken into account for the equivalence decision: international sanctions, fight against money laundering and the financing of terrorism, tax good governance or "*other relevant external policy priorities, in order to ensure the consistency of the EU's action on the international stage*". These aspects are not trivial in the context of Brexit and the UK's future financial services policy.

### 3. <u>The last improvements of equivalence regime in the EU law</u>

Equivalence decisions are unilateral and discretionary acts by the European Commission, which has the power to grant, suspend or withdraw equivalences. The grant may also be partial.

Granting equivalence involves a "positive" assessment of the third country framework, which should allow the EU to rely on the rules and work of the third country supervisor.

To be underlined that the common adhesion of the EU and a Third country to international standard does not imply "*that the Commission would automatically find that country EU equivalent in a specific area*". Supervisory cooperation, reciprocity in the treatment of EU market players can also be taken into consideration by the European Commission.

The Commission maintains it is not possible to have a homogenous approach to equivalence. The priorities are defined texts by texts, and adapted to the objectives of the latter while respecting a global approach.

EU financial services law includes around 40 provisions allowing the Commission to adopt equivalence decisions. On this basis, the Commission has taken over 280 equivalence decisions for more than 30 countries that can be seen here.

Some recent improvements have been made those past years. The process is more transparent and (the European Commission "*generally submits for public consultation draft equivalence decisions that are envisaged for adoption (30 day feedback period*)". Some changes have been introduced in the EU law, notably through amendments of the European Supervisory Authorities' Regulations. The review of these regulation reinforce the role of the ESAs in monitoring equivalent third countries. They are responsible, each one in their dedicated areas, for submitting every years a confidential report on these countries, sent to the European Parliament to the European Commission to the Council and to the other two supervisory authorities.

**Next steps: the work of monitoring equivalence schemes is constantly reviewed, whether as a result of the evolution of European law or following the development of financial markets.**

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**12th February 2019**: Taxation - the shift to qualified majority voting is seriously questioned

On 12th February 2019, the ECOFIN Council debated the European Commission's Communication published on 15th January 2019, entitled "*Towards a more efficient and democratic decision making in EU tax policy*" in which a gradual move from unanimity to qualified majority voting in taxation regulation is proposed.

During the debates, the EU member states were dividing into 3 groups:

- The first group, composed of France, Spain and Portugal, strongly supports the Commission proposal,
- The second group countries (Finland, Denmark, Austria, Germany, Greece, Belgium) is composed of which are "open" to debating, but do not agree on every point of the Communication,
- The third group, led by Ireland and Luxembourg and composed of 15 states, argues that much progress has been made in tax matters despite the unanimity voting rule.

On the European Parliament side, a debate was held on 13st February 2019 in a plenary session with the Commissioner for Taxation Pierre Moscovici.

During the debate, some MEPs of the European People's Party (EPP) expressed reluctance, arguing that the move to qualified majority voting rule would lead to a general rise in taxes in Europe and thus weaken the competitiveness of the Union at the global level.

On the contrary, the S&D and Green MEPs who took the floor during the debate expressed their support for the European Commission's proposal.

***Next steps*** :

**As a reminder, only the European Council, that is to say the Head of States and Government, will be able to vote on the proposals of the European Commission.**

**The Romanian Presidency of the Council promised that a new discussion will be scheduled within the ECOFIN Council.**

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21st January 2019: the European Union and its Member States submit proposal on the review of the Investor-state dispute settlement (ISDS)

On Monday 21st January 2019, the European Union (EU) and its Member States (MS) presented two proposals to the UN working group of the United Nations Commission on International Trade Law (UNCITRAL) who is in charge of the review of the investor-state dispute settlement (ISDS).

The first paper on the establishment of ***a "standing mechanism for the settlement of international investment disputes"*** presents the EU and MSs' proposal on the review of ISDS. They support this reform along with the idea that foreign direct investment is an important element in encouraging sustainable development to achieve the Sustainable Development Goals. Therefore, the investment dispute settlement mechanism should include those concerns.

The paper sets out ideas for the possible establishment of a **permanent multilateral investment court** with two levels of adjudication and full-time adjudicators and gives details on the settlement process: dispute avoidance mechanism, first instance, appellate tribunal, ethical requirements for adjudicators, composition and qualification…

This mechanism is modelled after other jurisdictions at the national and international level (i.e the European Court of Human Rights). The EU and MS underlines that the Members of these adjudicative bodies are composed of full time adjudicators who are appointed by States and have a high degree of independence and impartiality. Moreover, their decisions are subject to review in order to ensure correctness and predictability. More predictability on legal interpretation leads to a more efficient decision-making process and is therefore more cost-effective.

In their second position paper, the EU and the MSs suggest a working plan for the working group:

- **Step 1:** Identification and proposal by governments of their preferred reform options
- **Step 2:** Identification by the Working Group which of the reform options put forward should be the subject of further work
- **Step 3:** Discussion and decisions in respect of the priority to be given, the sequencing of the deliberations, the possibility of multiple tracks, coordination with other international organisations and inter-sessional work
- **Step 4:** Development of concrete solutions and text proposals that would be adopted by the UNCITRAL Commission and endorsed by the General Assembly of the United Nations.

**Next steps :**

**These two proposals will be discuss at the next meeting of the working group scheduled from the 1st to 5th April 2019**.

15th January 2019- Taxation: The European Commission proposes to gradually move to qualified majority voting end the rule of unanimity for tax reforms

On 15th January 2019, the European Commission published a communication entitled "Towards a more efficient and democratic decision making in EU tax policy" in which a gradual move from unanimity to qualified majority voting in taxation regulation.

- **A transition in four stages**

The communication defines a roadmap composed of four stages:

1. In the first step, qualified majority voting should be employed **for measures that have no direct impact on Member States' taxing rights, bases or rates, but are critical for combatting tax fraud, evasion and avoidance and in facilitating tax compliance for businesses** in the Single Market.

2. In the second step, qualified majority voting should cover **measures primarily of a fiscal nature designed to support other policy goals** (e.g. fight against climate change, protecting the environment or improving public health or transport policy)

3. The third step would be to focus on **areas of taxation that are already largely harmonized**, and which must evolve and adapt to new circumstances (e.g. VAT and excise duties).

4. The fourth step would be to introduce qualified majority voting on other **initiatives in the taxation area, which are necessary for the Single Market and for fair and competitive taxation** in Europe.

- **The use of "passerelle clauses"**

The European Commission considers it will not be necessary to amend the European Treaties, which is a long procedure. Instead, the Treaties provide the possibility to use "passerelle clauses" which allow to adopt measures through qualified majority voting when they are normally subject to unanimity voting.

- **A non-legislative text**

As a reminder, this roadmap is not a legislative proposal of the European Commission, but only a communication: the aim is to provoke a broad political debate before the coming elections of the European parliament.

In the light of future discussions at the European Council (composed of Head of States and Government), the European Commission will decide on concrete proposals to present.

**The European Commission calls on the Heads of States and Government to take a decision on the following three points:**

1. **Approving the roadmap presented in the Communication;**

2. **Approving the use of the passerelle clauses clause for stages 1 and 2;**

3. **Discussing the use of the passerelle clauses for stages 3 and 4.**

**The European Commission proposes that stages 1 and 2 should be completed by the end of 2019.**

27th November 2018 Brexit: State of play

**On 13th November, European and British negotiators finally reached a technical agreement on the Brexit withdrawal that was endorsed by Member States on 25th November. None of the European red lines has been crossed. The text, which provoked a new government crisis in the United Kingdom, is due to be voted by the British House of Commons on December, 11th.**

**On 13th November, a few hours after the withdrawal agreement reached between the negotiators, the Commission issued a contingency action plan in case the 27 and the UK fail to sign an agreement by 29th March 2019.**

**On 22 th November, the Council published a political declaration setting out the framework for the future relationship between the European Union and the United Kingdom.**

**I. THE WITHDRAWAL AGREEMENT**

On November 25th, the Council adopted the agreement on the first phase of the British withdrawal from the EU reached by the British Prime Minister Theresa May and the chief negotiator for the EU Michel Barnier on 13th November. At the EU level, it has now to be adopted by the European Parliament for ratification. At the UK one, a vote will take place on December, 11th at the House of Common.

The withdrawal agreement focuses namely on 4 key issues: **the financial settlement** to be paid by the UK (between 40 and 50 billion euros), **the rights of the European citizen living in the United Kingdom and vice versa**, **the transition period** up to as of 31st December 2020 as well as **the Northern Ireland issue**.

During the last few months, it has been a challenge to ensure that Brexit**, regardless of the future relationship between the EU27 and the UK**, does not imply the back of physical boundaries between Northern Ireland and the Republic of Ireland, while ensuring the integrity of the Single Market and the UK.

**The Protocol on Ireland and Northern Ireland:** In case of failure of finding an agreement before the 1st of July 2020, two options are available:

1. **The transition period will be extended by mutual agreement to be reached before 31st December between the EU 27 and the UK**

As a reminder, this transition period includes the following provisions:

- ✓ Maximum initial duration: until 31st December 2020; it could be extended until 31st December 2022;
- ✓ Compliance with all European standards that exist today in the United Kingdom under the authority of the CJEU;
- ✓ Implementation of the provisions adopted by the EU between 30th March 2019 and 31st December 2020 (except in specific cases);
- ✓ Primacy of European law over British law;
- ✓ Participation in the European budget;
- ✓ Respect for the four fundamental freedoms of the EU - including the free movement of persons;
- ✓ Exit of the entire EU decision-making process.

2. **A backstop mechanism for Northern Ireland and the Republic of Ireland will start to apply on 1st January 2021.**

This backstop will involve the :

- ✓ establishment of **a Single EU-UK customs territory between the UK and the EU until an agreement on the applicable future relationship is reached.** Therefore, no customs control between the two Ireland will be necessary.
- ✓ **continuous application of the Union's Customs code (UCC) to Northern Ireland.**

In the context of **the Single Customs Territory between the UK and the EU**, several measures to ensure a **level playing field** between EU 27 and the UK (excluding Northern Ireland) will be put in place. The Memorandum of Understanding commits the UK to respect different European and international standards, state and competition rules, social and environmental protection. The EU may take unilateral action if certain rules are not respected. It should be noted that controls will be necessary for goods from the island of Great Britain to Northern Ireland.

This backstop mechanism may be terminated at any time if both parties no longer consider it necessary.

**What are next steps?**
This first agreement, endorsed by Theresa May's cabinet on the night of 14th November, provoked a new government crisis in the United Kingdom, a prelude to a vote in the House of Commons with an uncertain outcome. Thus, five ministers and secretaries of state of her government resigned on November 15th including the ministers responsible for Brexit, Dominic Raab, who had replaced David Davis (who resigned last July). Some pro-Brexit MPs seek to submit a motion of no confidence against the Prime Minister. A vote on the withdrawal agreement is expected in the House of Commons in December with an uncertain outcome. Meanwhile, the Council of 27 met on 25th November and endorsed the text of the withdrawal agreement.

**II. COMMUNICATION OF THE EUROPEAN COMMISSION ON THE CONTINGENCY MEASURES IN CASE OF "NO-DEAL" SCENARIO:**

On 13th November, a few hours after the withdrawal agreement, the European Commission issued a Contingency Action Plan in case of no deal by 29th March 2019. Indeed, if no agreement is reached, the EU acquis will no longer be applicable in the UK as of 29th March.

This Communication, being rather minimalist in its proposed measures, provides an update on the areas where emergency measures will have to be adopted in the event of *hard Brexit/no deal*. They will be adopted unilaterally and will be temporary in nature. The Commission states that these measures are not intended to replace the provisions that the various stakeholders must take to deal with such a scenario.

**With regard to financial services**, derivatives clearing seems to be the most problematic issue for the Commission.

The Commission first recalls the importance of preparing the sector for all possible scenarios and refers to its notes published in February for each category of financial services (Banks, Asset Management, Post trade services, financial instruments - see the complete list). The European Supervisory Authorities (EBA, ESMA, EIOPA) also stressed the need to clarify supervisory expectations in the event of company relocation. Financial operators located in **the UK will no longer be able to offer their services in the single market with the current financial passport.**

Rather confident in its Communication, the Commission states that risks to financial stability have significantly decreased. These measures will make sense in the event of a rejection of the withdrawal agreement, which is likely to depend on the outcome of the vote of British MPs - and / or the continuation of Theresa May as head of the Tories Government.

**III. POLITICAL DECLARATION ON THE FUTURE RELATIONSHIP**

On 22nd November, the Council published a **political declaration setting out the framework for the future relationship between the European Union and the United Kingdom**. The text, approved by the UK and European negotiators, will be one of the annexes to the agreement, which is to be formally ratified by the EU and the UK by 29th March 2019. **However, it will have no legally binding value.**

The future agreement, based on a ***"free and fair trade"*, should guarantee:**

- the autonomy of the EU decision-making, according to its own principles in particular relating to the **integrity of the single market** and the **Customs Union** and **the indivisibility of the four fundamental freedoms of the EU (free movement of goods, persons, capital and services).**
- UK sovereignty, the protection of its internal market, the **development of an independent trade policy** and **the end of the free movement of people between the UK and the EU.**

**In terms of governance**, a joint committee with representatives of both parties will be set up, having a possibility to appeal to an independent arbitration court. However, **any provision relating to EU law will have to be subject to interpretation at the European Court of Justice, whose decision will be binding.**

**Services:** the market access will be considered according to **the rules of the host State**, whether for service providers or investors.

**Data protection issues**: the European texts allow the European Commission to recognize that the standards of a third country provide a sufficient level of protection, facilitating the transfer of data. An assessment will be launched at the end of 2020. In addition, cooperation agreements on cyber security are also planned.

**Mobility:** a system of temporary authorizations for entry and exit of persons for commercial purposes could be put in place. Other specific provisions are also planned (for students, researchers, etc.)

**Financial services:** according to the text, the EU and the UK are comitted to "**preserving financial stability, market integrity, consumer and investor protection and fair competition**", while respecting the other party's:

- **regulatory autonomy and decision-making;**
- **the possibility of deciding equivalences according to their own interests;**
- **the possibility of taking any measures where necessary for prudential reasons.**

The parties are committed to cooperating closely in the field of regulation and supervision within international bodies. Furthermore, **the assessment of equivalence to be granted respectively will have to be carried out by June 2020.** The process of adopting, suspending and withdrawing equivalence decisions should be more transparent and involve exchanges of information. It is however explicitly stated that equivalence decisions are taken independently and according to the interest of the EU or the UK.

Political and technical consultations on regulatory initiatives are also planned.

24th October 2018: Late Payments Directive - IMCO published amendments on the INI draft report

The amendments on the INI draft report on the Implementation of the Directive on combating late payment in commercial transactions were released today.

Several amendments related to **the ban of assignments for public sector receivables** were tabled by the rapporteur Lara Comi (EPP, IT). The rapporteur "*notes with great concern*" **the existence of this practice, in national legislation or contractually, and calls the EU Commission and the Member States to "*take the necessary steps*" for its elimination at the EU level.**

**Please find below the amendments concerned:**

- *"Whereas in some Member States **the circulation of public sector receivables**, which could balance the powers of the parties and lead to fairer business practices, **is prevented by assignment and enforcement bans, either introduced by law or by contract**;" (Amendment 17)*

- ***"Notes with great concern** the situation in some Member States, where public authorities have greatly delayed payments for goods and/or services supplied to them by undertakings**, included in supply contracts non-assignment clauses and prevented (through law) suppliers from enforcing their claims in courts**, so leading those businesses into extreme financial difficulties; believes that in order to support businesses whose financial management is complicated by delayed payments from public authorities, the Member States should put in place faster and more efficient VAT refund procedures, especially for SMEs" (Amendment 74)*

- *"Calls on the Member States and the Commission, in **the light of the recent case law of the Court of Justice** (Case C-555/14), **to take the necessary steps to ensure** that public authorities pay their suppliers on time, that creditors receive automatic interest and compensation when payments are late, and **that bans on judicial enforcement towards the public sector and bans on assignment of public sector receivables are eliminated from national legislation or public sector contractual practices**" (Amendment 82)*

- *"Calls on the Member States to improve their legislation and promote the implementation of the Late Payment Directive in all its parts, also by removing any domestic laws, regulation or contractual practices by the public sector that conflict with the aims of the Directive, **such as enforcement and assignment bans for public sector receivables"** (Amendment 97)*

**Next steps**

**Committee on Internal Market and Consumer protection (IMCO) agenda**

- ✓ Consideration of Amendments 21-22th November
- ✓ Vote of the Draft report in IMCO : 28th December

**Plenary agenda :**

- ✓ Plenary vote in January

10th October 2018: Late Payment directive: IMCO discussed the draft report

On October,10th , the Committee on Internal Market and Consumer protection (IMCO) at the European Parliament discussed the draft report for an own-initiative procedure (INI), assessing the implementation of the 2011/7/EU Directive as regards combating payment in commercial transactions, written by the rapporteur Lara COMI (EPP, IT) and published the 28th September.

As a reminder, the rapporteur concluded in its draft report that the late payment Directive has been applied in a patchy way within the European Union. Consequently, a considerable number of companies, particularly SMEs, have shut down because of late paying debtors.

The rapporteur Lara COMI began her presentation explaining that her aim is to call for a recast of the 2011/7/EU Directive. The rapporteur outlined its four priorities:

- ➢ **Establish stricter payment terms**: The rapporteur believes a clear deadline for the length of the payment period must be set.

- **Compulsory forms of compensation**: Lara COMI estimates that compensation must become compulsory, otherwise there would not be valuable reason to recast the Directive.
- **Stricter controls and publication of information:** State controls should be strengthened and more rigorous. Lara COMI added that she wishes to establish the Spanish model: when public bodies do not pay on time, the central state intervenes. She considers it might be an instrument of best practice. The rapporteur also believes that stigmatization is an efficient means to reduce late payment behaviors. That is the reason why provisions on "naming and shaming" should be included in the Draft report.
- **Means to accelerate the speed of payments**. The rapporteur considers that timely payment creates a virtuous circle. Lara COMI wants, therefore, that the committee reflects on how to accelerate payments in the EU

- **Unanimous view of the state of the implementation of the 2011 Directive**

All members welcomed warmly the Draft report and consider helping SMEs is an urgent matter.
Indeed, each speaker agreed on the fact that the 2011/7/EU Directive and the national legislation have not achieved the objectives they were designed to reach since many SMEs still go bust because of late paying debtors. Maria GRAPINI (S&D, RO) recalls that cash flow and liquidity are extremely important for SMEs, since they don't have lending capabilities.

- **Rejection of the "one size fit for all" approach**

Richard SULÍK (ECR, SK) and Jasenko SELIMOVIC (ALDE, SE) warmly welcomed the rejection by the rapporteur of the "one-size-fits-for-all" approach in its draft report.

- **The issue of penalties**

Jasenko SELIMOVIC (ALDE, SE) stated that provisions without sanctions do not lead to any concrete result. However, the rapporteur was skeptical about sanctions: Lara COMI estimates that infringement costs will be borne by consumers.

- **A stricter and clearer payment term**

The MEP Maria GRAPINI (S&D, RO), vice chair of the intergroup of the SMEs, recalls that SMEs regularly criticize the same point: the 2011/7/EU Directive provides too many flexibilities.
Jasenko SELIMOVIC (ALDE, SE) remarked that some member states are far more successful in dealing with late payment issues. Consequently, the question the committee has to answer is what have these states put in practice: The answer is a fixed payment term principle.
Maria GRAPINI (S&D, RO) estimates that the 2011/7/EU Directive conveys many ambiguities regarding payment terms that the report will have to excise. Maria GRAPINI agreed with the rapporteur that **it is necessary to shorten the payment deadline and the whole chain of debt.**

- **Set simplify recovery procedure or Avoid court cases/ Automatic interest**

The speakers insisted on the need to find an alternative to the use of judicial channels
Maria GRAPINI explained that**,** to benefit from penalties, companies need to trigger judicial proceedings. The problem stems from the considerable expenses that implies judicial proceedings. Moreover, by the time the court delivers its decision, SMEs will have gone bankrupt. As a consequence, Maria GRAPINI considers **the state must have a central role to play in this legislation by interacting directly with late paying debtors**.

Jasenko SELIMOVIC (ALDE, SE) agreed and added that providers are fully aware of the complexity, the cost and the slow pace of court proceedings. According to him, the current set up, in which businesses must claim their interest by themselves, has clearly not worked out. Jasenko SELIMOVIC expressed his support for an amendment on a simplified recovery procedure: “automatic interests” would be a solution.

- **Future potential provisions on setting up a beneficial banking system for SMEs**

The rapporteur Lara COMI suggested to submit amendments on factoring and setting a beneficial banking system for SMEs.

Maria GRAPINI (S&D, RO) agreed with Lara COMI, explaining further that the IMCO committee needs to **reflect on banking costs**: the MEP illustrated her opinion by explaining that, when SMEs are waiting for months for their payment, they’re lacking a source of capital that they need to operate. Consequently, SMEs contract bank loans. Maria GRAPINI **believes the cost of the interest of banking loans should be borne by those which do not pay on time**.

**Next steps: IMCO agenda:**
- Deadline for tabling amendments 17th October
- Consideration of Amendments 21-22th November
- Vote of the Draft report in IMCO: 28th December
- Plenary vote in January

28th September 2018: Late Payment directive: IMCO published its INI draft report

On 28th September 2018, the Committee on the Internal Market and Consumer Protection (IMCO) at the European Parliament published a draft report for an own-initiative procedure (INI), assessing the implementation of the Directive 2011/7/EU as regards combating late payment in commercial.

The rapporteur Lara Comi (EPP, IT) **encourages Member states to keep the late payment issues at the center of the political agenda.** Her aim is to call for a stronger implementation of the late payment directive in the EU by setting up a series of new measures.

It has to be noted that factoring is seen as an innovative means of payment by the rapporteur : “*stresses that making payments quickly is absolutely essential for the survival and growth of businesses; notes that fintech and digital technologies are revolutionizing the means and speed of payments;* ***expects, therefore, a sharp increase in electronic invoicing and the gradual replacement of traditional types of payment with innovative types (e.g. supply chain financing, factoring, etc.), so that the creditor can be paid in real time as soon as the invoice is issued” P.10***.

## I. The draft report:

Rapporteur Lara Comi based her work on the Commission’s report on the implementation of the Late Payment Directive published in 2016.

The main element emerging from the consultation with business associations is the **problem of commercial market asymmetries** : SMEs are the most likely to accept unfair payment terms or have them imposed on them by larger companies , owing to an imbalance of power and the fear of damaging business relations and losing a future contract.

According to the Commission’s report, factors leading to late payment are:

- ✓ cash-flow issues,
- ✓ imbalances of power and size between companies,
- ✓ supply chain structure,
- ✓ administrative inefficiency,
- ✓ poor access to credit,
- ✓ lack of knowledge of invoice and credit management

The propositions of the rapporteur to create a level -playing field between large and small companies are to:

- **Establish stricter payment terms**
  Some sectors are particularly vulnerable to long payment terms. Therefore, the rapporteur suggests that Member States should consider establishing stricter payment terms at sector level.

- **Get public authorities involved**
  Public authorities are responsible for enforcing administrative sanctions. Direct public interventions for enforcing the law and taking discretionary action against enterprises could help to overcome the 'fear factor 'and relieve creditors of the responsibility to take action against debtors.

- **Set a mandatory publication of information in specific databases concerning payment behavior**
  The rapporteur believes that the "name and shame" / "name and fame" processes could directly harm the company's image, and consequently, discourage late payment and help businesses choose reliable commercial partners.

- **Set up national and regional free and confidential mediation service**
  The rapporteur estimates that an alternative to court proceedings should be accessible to all companies (i.e. mediation, conciliation, arbitration and adjudication services), in order to resolve payment disputes and maintain business relations.

- **Consider mandatory forms of adequate compensation or offsetting for companies owed money by a public authority**
  According to Lara Corni, Member states and the Commission should take the necessary steps to ensure that public authorities pay their suppliers on time and that creditors receive automatic interest and compensation when payments are late.

- **Set stricter controls on large companies**
- **Take into account the specificities of each sector**
  The rapporteur estimates that there is no one-size-fits-all approach to tackling the issue of late payments: Lara Comi recalls that in some sectors longer payment deadlines, beyond 30 or 60 days, are in line with the needs of businesses and an accepted practice.

The rapporteur adds that it is also important to "***respect the freedom of contract between undertakings on the market***". Therefore, "***legislation defining payment terms differentiated by category of products or services is relevant in promoting fair practices and addressing sectoral specificities***".

## II. What's next ?

Own-initiative (INI) reports are non-legislative texts. Still, there are important as they show the position of the MEPs and draw recommendations for the European Commission on key initiatives.

This paper is only a draft report, meaning that it can be amended by the MEPs from IMCO before becoming a formal report from this committee and then from the whole European Parliament.

It is then key for us to see in which way we should try to influence this INI report and raise awareness on factoring in a Committee of the European Parliament (IMCO) usually less involved on our issues than the ECON Committee.

12th July 2018: Brexit - EU leader cautious after UK Chequers' proposals

On July, 12th 2018, the British government released its whitepaper aiming to define its negotiation stance in the Brexit process. Without rejecting those proposals in block, EU leaders yet questioned them underlining some of their red lines.

**I. UK POSITIONS IN THE NEGOTIATIONS**

1. British global approach

The key points of Theresa May's government for UK are the following:

- leaving the Single Market and the Customs Union, while ensuring the access to the single market for agricultural goods and products through the establishment of a free trade agreement (FTA)
- introduction of a new Facilitated Customs Arrangement, ie an *ad hoc* customs system, removing the need for customs checks and controls between the UK and the EU while giving room for the UK to conclude free trade agreements with third countries
- avoiding any physical border between the Republic of Ireland and Northern Ireland
- ending free movement of people and the jurisdiction of the European Court of Justice (EUCJ)
- ending UK's participation to EU budget

To summarize, they want to "*take back control of our money, laws, and borders*"

Interestingly they want to tie the two phases of the *Brexit* process, i.e. the withdrawal agreement and EU/UK future relationships.

**2. A "*hard Brexit*" for financial services?**

If the whitepaper proposes a FTA for goods with the establishment of a common regulatory area, it calls for a "*regulatory right to diverge*" when it comes to services.

**In particular, UK main principles for financial services are the following:**

- **Leaving the single market imply the end of the EU financial passport**
- Need to **insure autonomy of decision-making** of both the EU and the UK, while providing a bilateral framework based on common principles in terms of cooperation, regulatory dialogue and stability
- **Set up of an improved equivalence system, expanded to the provision of further services**

**The new equivalence system would provide:**

- ✓ **an institutional dialogue**, to discuss changes to UK or EU rules on financial services in order to "*maximise the chance of maintaining compatible rules, and to minimise the risks of regulatory arbitrage or threats to financial stability".*
- ✓ **a supervisory cooperation** that could imply UK representatives participation in supervisory colleges

- ✓ **a mediated solution** "*where equivalence is threatened by a divergence of rules or supervisory practices*";
- ✓ **reciprocal supervisory cooperation**
- ✓ **further predictability and reliability of processes and system,** as current equivalence regimes are unilaterally granted by the EU Commission and can be withdrawn in 30 days. This could imply a "***presumption against unilateral changes that narrow the terms of existing market access regimes,*** *other than in exceptional circumstances. This would mean* ***each side trying to avoid future changes that assess equivalence in entirely new ways that could destabilise an established relationship***."

Furthermore, UK government calls for the establishment of "*common principles for the governance of the relationship*", with a commitment ("*a shared attention*") "***to avoid adopting regulations that produce divergent outcomes in relation to cross-border financial services***".

The UK government **also recognizes the Court of Justice of the European Union as the interpreter of EU rules**.

Last, the UK proposes a reciprocal recognition of all existing equivalence regimes, "*taking effect at the end of the implementation period*". **Yet, Theresa May recognizes that future access to each other's markets could not be at the same current level.**

## II. EU LEADERS'S ANSWERS FOCUSED ON EU RED LINES

After the release of the UK proposal, Michel Barnier, EU Chief Negotiator made several statement, praising the progresses while underlining yet some EU core principles that seemed threatened.

On July, 26th he explained that 80% the Withdrawal Agreement, including the financial settlement and the rights of 4 million EU citizens living in the UK and British nationals in the EU, was already agreed. For both the EU and the UK, one of the biggest issue is on the island of Ireland, as a genuine system is still not agreed between both sides.

On July, 20th, Michel Barnier stated that the proposal of a Free Trade Agreement "*matches a key proposal of the European Council guidelines*" hailed the "*commitments regarding a level playing field, notably in state aid and environmental and labour standards"*.

Yet, he also explained throughout his speeches that "*the EU wants to keep control of its money, law, and borders*" and that by consequences "*the EU cannot – and will not – delegate the application of its customs policy and rules, VAT and excise duty collection to a non-member, who would not be subject to the EU's governance structures*."

EU chief negotiator also insisted on the fact that the UK defends "*free movement of goods but not of people and services*", which comes against the indivisibility of the four freedoms of the EU.

Regarding financial services, Michel Barnier emphasized the principle of autonomy, **for market access and for both the granting and the withdrawal of equivalences, meaning it would not accept any system hampering EU ability to decide its own regulation.** However, the principle of equivalence system meet the EU approach for financial services.

Brexit negotiations should start again in mid-August. The main goal is to reach an agreement by end-October as it will have to be ratified by the British parliaments and the ones of the 27 Member states.

1st July 2018: Austria takes over the Presidency of the Council of the EU

Taking over from Bulgaria, Austria will preside the Council of the European Union (EU) for the second semester 2018, until 31st December 2018. Romania will then take the Presidency for the first semester 2019.

A few days ahead of its accession to the Council Presidency, Austria published its work programme for the next six months. This programme identifies three major priorities, which are:

1. Security and immigration;
2. Digitalisation of the economy, mainly via the continuation of ongoing efforts on the digital single market and on the taxation of the digital economy;
3. Stability of the EU neighborhood.

Regarding files within the remit of the Economic and financial form of the Council (Ecofin), the Austrian Presidency insists on the continuation of ongoing projects, in particular with regards to the Banking Union, the Capital Markets Union (CMU), the Economic and Monetary Union (EMU) and taxation.

More precisely, the main files on which the Austrian Presidency aims to achieve substantial are:

- **The non-performing loans (NPL) package;**
- The European Deposit Insurance Scheme (EDIS);
- The review of the European Market Infrastructures Regulation (EMIR) with regard to the supervision of central counterparties (CCPs);
- The review of the EU financial supervision architecture;
- The prudential regime of investment firms;
- The European framework for covered bonds.

The Austrian Presidency indicates also that one of its main goal is to conclude before the end of 2018 **the interinstitutional negotiations on the banking package, including the review of the regulation and of the directive on capital requirements (CRR/CRD IV).**

25th June 2018: the EBA warns EU financial institutions against their insufficient Brexit preparations

The European Banking Authority (EBA) published an opinion on measures to be taken by financial institutions in the European Union (EU) to prepare for the exit of the United Kingdom (Brexit).

**ANITICIPATING THE WORST CASE SCENARIO**

The EBA examines critically the anticipation measures with have been adopted by EU financial institutions. It recalls that they should be ready to face a hard Brexit if no transitional or exit agreement is found by end of March 2019. The EBA also remind financial institutions that if there is no exit agreement, then there will be no transition period after March 2019.

In its opinion, the EBA considers that financial institutions from the EU 27 should also start mapping risks and anticipating responses to those risks. In particular, it draws attention to risks related to:

- Regulatory authorisations;
- Legal structures and governance;
- Access to financial markets and market infrastructures;
- Continuity of existing contracts, especially changes to the applicable law.

Specifically for the banking sector, the EBA points out the need to anticipate potential changes in the requirements for deposit guarantees as well as for recovery and resolution planning.

**INFORMING INVESTORS AND CONSUMERS**

The EBA underlines that financial institutions have to communicate with their clients on how they will be impacted by a hard Brexit. Clients have to be informed in clear and non-misleading manner of potential changes to their existing contracts. Communication in relation to new contracts to be finalized before Brexit becomes effective also has to be adapted.

**ROLE OF NATIONAL COMPETENT AUTHORITIES**

Finally, the EBA calls on national competent authorities to incentivise and accompany the speeding-up of Brexit preparation measures.

**The United-Kingdom will leave the EU at the end of March 2019. So far, no agreement on the exit or future relations has been concluded.**

24th May 2018: EMU: the European Commission to boost sovereign bond-backed securities

As part of its efforts to deepen the Economic and Monetary Union (EMU), the European Commission published a legislative proposal on sovereign bond-backed securities (SBBS).

The objective is to develop new securities which would allow investors to diversify their exposures to sovereigns. Thus, the European Commission believes that risks would be reduced overall for the banking system in the Eurozone. However it underlines that its SSBS proposal does not imply any further sharing of sovereign risks. The Commission clarified that only private investors would be sharing risks and potential losses.

Content-wise, the Commission is proposing to create a new financial product, the SBBS. The SBBS would be a diversified pool of sovereign bonds from the Eurozone and would include sovereign bonds from each Eurozone Member states in proportion to their economic weight in the Eurozone. When buying SSBSs, investors would be able to choose high or low risks types of products. The return rate will be higher for high risk SBBSs. SBBSs would not be produced by States but by private entities, which sole purpose will be to generate and manage SBBSs.

Under the Commission's proposal, SBBSs would benefit from the same regulatory regime as Eurozone sovereign bonds, in particular with regards to their prudential treatment.

The proposal for a regulation has been published for public consultation until August 7th 2018. The co-legislators will start their work after this date.

Brexit: March institutional state of play

The Brexit process is organized in two phases: (i) the withdrawal itself and the (ii) future UE/UK relationship.

**The EU Commission published in March, 19th a Draft Agreement on the withdrawal of the United Kingdom from the EU**. This document aims to make legally binding the agreement reached by the Commission and the UK government in December especially on the **financial settlement**, the **question of the European citizens living in the UK**, the **Irish border** and the **transitional period.**

Except for the Irish border issue, most of the elements of the first phase have been commonly approved.

**The key elements of the transitional period are the followings:**

- ✓ Starting on 30 March 2019, finishing at the latest on 31 December 2020
- ✓ Exit of the UK interests from the entire EU decision-making process, including in all EU institutions and bodies, whether in the European Parliament, the European Commission or the EU European Banking Authority (EBA) (Articles 123.1 and 6.1)
- ✓ Application of the European legal *acquis* as it currently exists in the United Kingdom - European standards, regulatory, supervisory, budgetary, supervisory, judicial and supervisory mechanisms compliance with the rules, all under the authority of the European Court of Justice
  Furthermore, the provisions that will be adopted by the EU between 30 March 2019 and 31 December 2020 will also have to apply in the United Kingdom (except in specific cases).
- ✓ Primacy of European law over British law (Article 122)
- ✓ Participation in the European budget (Article 128.1)
- ✓ Respect of the four fundamental freedoms of the EU - including the free movement of persons

Yet, on this first phase, an agreement on all of the provisions need to be adopted as "*nothing is agreed until everything is agreed*", meaning that the "no deal" scenario is still possible.
The first phase is expected to be finalized for next June Council meeting.

**The European Council adopted in March, 23rd, its guidelines on the future EU relationship with the UK.**

Those guidelines give a political mandate to the EU Commission for its negotiations with the British government. The main aspects of those guidelines are the followings:

- ✓ A free trade agreement (FTA) is possible but must contain safeguards against any regulatory dumping and provide sanction mechanisms.
- ✓ Any negotiations on financial services will be initiated according to an approach focused on the preservation of the financial stability and the respect and the application of the European rules.
- ✓ The Council calls on all the institutions to anticipate the consequences of the "worst case scenario", namely the absence of an agreement on 29 March 2019.

Regarding the provision of services in the EU, the goal of the FTA should be to "***allow market access to provide services under host state rules, including as regards right of establishment for providers***".

**Only one sentence refers to financial services,** stipulating that "*any future framework should safeguard financial stability in the Union and respect its regulatory and supervisory regime and standards and their application.*"

The European Council also recalls that:

- the four freedoms are indivisible
- there can be no "**cherry picking**" through participation in the Single Market based on **a sector-by-sector approach,** which would undermine the integrity and proper functioning of the Single Market.

**The European Council currently favors the use of the equivalence regime to give access to the single market for UK providers**. Those equivalence regime are given and withdrawn on a unilateral basis by the European Commission.

1st December: European Commission reports on follow-up actions to the call for evidence on the financial services regulatory framework

Having conducted a call for evidence of the European framework for financial services, which results were published on 23rd November 2016, the European Commission published a report on follow-up actions.

The report reviews actions already completed as well as planned and on-going actions. It identifies four main goals:

- **Reducing unnecessary regulatory** constraints to boost the financing of the economy;
- **Strengthen the proportionality** of the European framework without compromising its prudential objectives;
- **Reducing the administrative burden** related to supervisory reporting;
- **Enhancing the consistency** of the regulatory framework.

The report also analyses reporting requirements. Indeed, the call for evidence showed that reporting requirements were perceived as too complex and too many, as well as too frequent and too costly. The European Commission lists in its report actions that it has taken to address this concerns.

Regarding future actions, the European Commission explains that it will review reporting requirements to assess their appropriateness (see article below) and pursue its **financial disclosure standardization project** (FDS). It also announces a workshop on reporting requirements, based on the results of the fitness check being conducted until 28 February. Finally, the European Commission indicates that it will consider efficiency gains that can arise from the **digitalization and automatization** of reporting.

Through this report, the European Commission states that it intends to actively pursue its efforts to address stakeholders' concerns.

In parallel to the report, the European Commission has launched a **fitness check of supervisory reporting** requirements (see article below), which takes the form of a public consultation running until 28 February 2018.

The European Commission indicates that it will publish a follow-up report in the summer 2019.

| **Consultations** | *Back to summary* |
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**Until 15 August 2019:** consultation on technical standards on the reporting of intra-group transactions and risk concentration for Financial Conglomerates

The ESAs (ESMA, EBA and EIOPA) have launched a public consultation on their draft Technical Standards (ITSs) on the reporting of intra-group transactions and risk concentration for financial conglomerates.

These ITS are based on the FICOD directive (Financial Conglomerate) and aim at harmonizing the reporting of intra-group transactions and risks concentrations for financial conglomerates.

The consultation form is available at this link.

**Until 2nd August 2019**: Consultation on Draft Regulatory Technical Standards on mapping of derivative transactions to risk categories, on supervisory delta formula for interest rate options and on determination of long or short positions in the Standardised Approach for Counterparty Credit Risk

The draft RST ( Regulatory Technical Standards) specify the method for the mapping of derivative transactions to risk categories with a three-pronged methodology.

**Until 2nd August 2019 - EBA publishes a public consultation on technical standards on the standardised approach for counterparty credit risks**

On the 2nd of May 2019, the European Banking Authority (EBA) published a consultation on four draft regulatory Technical Standards (RTS) on the Standardised Approach for Counterparty Credit Risk (SA-CCR). These standards specify:

- the method for the mapping of derivative transactions to risks categories
- the formula for the calculation of the supervisory delta of options mapped to the interest rate risk category
- the method for determining whether derivative transactions are long or short in their risk drivers

These standards suggest a three-pronged approach:

- The first is a **qualitative approach**: this approach identifies derivative transactions that have clearly only one material risk driver. It is based on a simple criterion to be satisfied and provides proportionality in the assessment since the mapping of these derivative transactions is simple and does not require the computation of sensitivities. The EBA expects to provide the mapping for the majority of transactions.

- The second is a **qualitative and quantitative approach**: when the mapping cannot be done with the first approach, the EBA suggests that institutions use quantitative inputs. The assessment of these inputs should lead to the mapping of the transaction to one or more than one risk category, reflecting the material risk drivers.

- The third is a **fallback approach**: if the second approach does not allow to determine which of the risk drivers are material, the EBA suggests that institutions be required to allocate the derivative transactions to all the risks categories corresponding to all the risk drivers of the transaction.

**The consultation is open until 2nd of August 2019 here.**

**Until 21th June 2019 - The FSB launches an evaluation of too-big-to-fail reforms**

The Financial Stability Board (FSB) aims at evaluating the effects of the too-big-to-fail (TBTF) reforms for banks that were agreed by the G20 following the global financial crisis.

This evaluation aims at assessing whether the implemented reforms are reducing the systemic and moral hazard risks associated with systemically important banks (SIBs). It examines the broader effects of the reform on systemically important banks (SIBs).

The evaluation targets banks, other financial institutions, academics, think tanks, industry and consumers associations on the following questions:

1. *To what extent are TBTF reforms achieving their objectives as described in the terms of reference? Are they reducing the systemic and moral hazard risks associated with SIBs? Are they enhancing the ability of authorities to resolve systemic banks in an orderly manner and without exposing taxpayers to loss, while maintaining continuity of their economic functions? What evidence can be cited in support of your assessment?*
2. *Which types of TBTF policies (e.g. higher loss absorbency, more intensive supervision, resolution and resolvability, other) have had an impact on SIBs and how? What evidence can be cited in support of your assessment?*
3. *Is there any evidence that the effects of these reforms differ by type of bank (e.g. global vs domestic SIBs)? If so, what might explain these differences?*
4. *What have been the broader effects of these reforms on financial system resilience and structure, the functioning of financial markets, global financial integration, or the cost and availability of financing? What evidence can be cited in support of your assessment?*
5. *Have there been any material unintended consequences from the implementation of these reforms to date? What evidence is available to substantiate this?*
6. *Are there other issues relating to the effects of TBTF reforms that are not covered in the questions above and on which you would like to provide your views? Please substantiate your comments with evidence.*

The answers must be sent to the FSB at this address (fsb@fsb.org) before the **21th June**.

**Until the 30th August 2019** – EBA Public consultation on loan origination and monitoring

On the 19th of June, the EBA published a public consultation on its draft guidelines on loan origination and monitoring.

The overall objective of these guidelines is to improve the financial stability and resilience of the EU banking system. With these guidelines, the EBA aims at improving institutions' practices and associated governance arrangements, processes and mechanisms in relation to credit granting in order to ensure that loans are of high credit quality. These guidelines also includes consumer protection rules.

Based on the Mortgage Credit Directive (MCD), these guidelines introduce requirements for the borrowers' creditworthiness assessment and for the collection of information and data used or this assessment.

These guidelines aim at:

- Clarifying the internal governance and control framework for the granting of credits and the decision-making process;
- Describing requirements for information and data collection from borrowers, documentation and all the information used for the creditworthiness assessment;
- Providing the methodology for the valuation of immovable and movable property collateral at the point of credit granting, and monitoring and review of the value of such collateral based on the outcomes of the monitoring;

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| ▪ Specifying the ongoing monitoring of credit risk and credit exposure |
| The consultation is open until **30th September 2019** at the following link.<br>The EBA will organise a public hearing on the **20th September 2019** in Paris. Registrations are opened until the **3rd September 2019** at the following link. |

| **Agenda** | *Back to summary* |
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| 24th September 2019 Working Party on Tax Questions (Indirect Taxation - VAT) | |
| 7th October Justice and home affairs council | |
| 10th October 2019: ECOFIN Council | |
| 8th November 2019: Economic and Financial Affairs Council | |

**Realised by**

EURALIA

**Contacts :**

**Louis-Marie Durand**

Tel: +32 2 506 88 39

E-mail: louismarie.durand@euralia.eu

**Lenka Kubatkova**

Tel : +32 2 506 88 29

E-mail : lenka.kubatkova@euralia.eu

**Mathilde Quembre**

Tel : +32 2 506 88 28

E-mail : mathilde.quembre@euralia.eu

**Marie Vial**

Tel: +32 2 506 89 13

E-mail: marie.vial@euralia.eu

**EURALIA**

Rue du Luxembourg 19-21

B-1000 Brussels