Deloitte.

Prudential Regulation Review
February 2018

February saw a number of important regulatory developments.

The European Supervisory Authorities (ESAs) issued a warning to EU consumers regarding the risks of buying virtual currencies (VCs), citing the lack of a regulatory framework and consumer protection as reasons for VCs being unsuitable as investment or savings products.

CENTRE for REGULATORY STRATEGY EMEA

Capital (including stress testing and macro prudential)

Sabine Lautenschläger, Member of the Executive Board of the ECB and Vice-Chair of the Supervisory Board of the ECB, spoke on macro prudential policy. She explained the institutional backdrop to macro prudential policy, and also outlined the four major risks identified by the ECB. These include the risk of a sudden reversal of risk premia; the low profitability of banks; the risk that markets might again doubt the ability of public and private borrowers to service their debt; and liquidity risks in the non-bank sector which might spill over into the entire financial system.

Adam Farkas, Executive Director of the EBA, delivered a speech on bank business models at the Deutsche Bundesbank Conference where he highlighted the significantly strengthened capital positions of EU banks and noted that they are now perceived by market participants as more stable and resilient. He noted the challenges posed by remaining asset quality issues and said these would continue to have implications on profitability. The speech argued that banks will continue to change their business models, propelled by factors such as technology, Basel III, and initiatives such as the Capital Markets Union (CMU) and that this would likely lead ultimately to a reduction in the number of banks- but a more efficient, stable and competitive banking sector.

The European Banking Authority (EBA) issued an Opinion following notification from the National Bank of Belgium (NBB) of its intention to modify capital requirements in order to address an increase in macro prudential risk related to the Belgian residential real estate market. The EBA acknowledged the NBB's warnings of vulnerability and did not object to the deployment of the macro prudential measure.

The European Systemic Risk Board (ESRB) published a report on macro prudential structural buffers and revised Handbook on Operationalising Macro-prudential Policy in the Banking Sector. The publications included additional guidance for national authorities on Other Systemically Important Institution buffer calibration; the categories of long-term non-cyclical risks that the Single Rulebook can address; and the potential to use the leverage ratio to complement structural buffers.

Crisis Management (including special resolution, systemically important firms, and business continuity)

Following the decision by the ECB to declare ABLV Bank, AS and its subsidiary ABLV Bank Luxembourg S.A. as 'failing or likely to fail', the Single Resolution Board (SRB) determined that resolution action was not necessary as it was not in the public interest. As a consequence, the winding up of the banks will take place under the law of Latvia and Luxembourg, respectively.

The SRB published the non-confidential version of documents related to the resolution of Banco Popular. These documents can now be publically disclosed, given the time that has lapsed since the resolution action and careful consideration of financial stability concerns. The available documents include the 2016 Resolution Plan, the Marketing Decision, and the Sale Process Letter.

The Financial Stability Board (FSB) published its peer review of Hong Kong, examining over-the-counter (OTC) derivative market reforms, and also published its peer review of Singapore, examining the macro prudential policy framework. Both reviews examined the framework for resolution of financial institutions. Singapore's review showed that the active use of macro prudential policies by the Monetary Authority of Singapore (MAS) has helped to mitigate housing price appreciation and moderate household leverage. However, additional work remains on several areas, including extending the scope of liabilities subject to bail-in to senior debt.

Disclosure, valuation and accounting

The ECB published a Feedback Statement on the draft ECB regulation on statistical reporting requirements for pension funds. The regulation aims to remedy shortcomings of the current un-harmonised and incomplete quarterly statistics on pension funds published since June 2011. The most important changes were (i) a postponement of the first reporting deadline, beginning with quarterly data for the third quarter of 2019; (ii) an increase of the reporting threshold from €10 million to €25 million (in assets), which follows a transitional approach to reach 80% coverage of total assets by 2022; (iii) a phasing-in period to align with EIOPA's supervisory reporting requirements; and (iv) a clarification of the term "pensions fund managers", which is changed to "pension manager".

The Basel Committee on Banking Supervision (BCBS) consulted on revisions to the Pillar 3 disclosure framework. Proposed changes include new or revised requirements for credit risk, operational risk, the leverage ratio and CVA; benchmarking of Risk Weighted Assets (RWAs) calculated by internal models; and an overview of risk management, key prudential metrics and RWAs.

Governance and risk management (including remuneration)

The EBA updated its methodological guide on risk indicators and detailed risk analysis tools, providing guidance for EBA compilers of risk indicators and internal users on methodology; transparency on the EBA's computation methodology; and enabling other competent authorities to compute and compare indicators for different samples of banks.

Information security and data privacy

Steven Maijoor, the Chairman of ESMA, delivered a keynote speech at a Fintech and Digital Innovation Conference, in which he presented the two strands to developing a "measured approach to FinTech", the first being to monitor innovations diligently and intelligently, and the second to take action in a measured way. On this basis, the Commission's plan to extend the mandate of the European Supervisory Authorities will enable them to: (i) pursue convergence on licensing requirements for FinTech firms; (ii) clarify and update the supervisory outsourcing framework; (iii) coordinate national technological innovation hubs; and (iv) develop cyber stress testing modalities.

Liquidity

The ESRB recommended that the European Commission propose a common legal framework governing the inclusion of additional liquidity management tools for EU funds to be used in stressed market conditions, which will likely lead to increased scrutiny of liquidity management processes and tools, and new and potentially extensive liquidity and leverage reporting requirements for UCITS funds.

Regulatory perimeter

The ESAs issued a pan-EU warning to consumers regarding the risks of buying Virtual Currencies (VCs) with the view that VCs are "unsuitable as investment, savings or retirement planning products". Because VCs and the exchanges where consumers can trade them are not regulated under EU law, consumers buying VCs do not receive any protection associated with regulated financial services.

Agustín Carstens General Manager of the BIS, delivered a speech at Goethe's University's House of Finance, in which he encouraged authorities to be prepared to protect consumers and investors amid the rise of crypto currencies around the world. Mr Carstens insisted on the need for regulators and supervisors to ensure that crypto currencies are not used to conduct illegal activities and that they do not pose a threat to financial stability.

The BCBS published its Sound Practices on the implications of Fintech developments for banks and bank supervisors. The document highlights the potential impact of new technologies on banks' future business models, and lists the main risks and opportunities that they could represent for the banking sector, along with options for regulators to tackle these risks.

The Bank for International Settlements' (BIS) Committee on Payments and Market Infrastructures (CPMI) launched a report on issues and challenges in the cross-border retail payments market, informed by a detailed analysis of the market. The CPMI's view is that safe alternative clearing and settlement arrangements could improve the efficiency of the cross-border retail payment market, including better links between national payment infrastructures and companies that require both payers and receivers to hold accounts.

Central Bank of Ireland

An economic letter considers whether reducing the risk of repossession resulted in more Irish borrowers defaulting on their mortgages. The issues and methodology are explored in more detail in a research technical paper entitled the impact of repossession risk on mortgage default.

Contact Us

Our firm's website, www.deloitte.ie provides world-leading continuously updated information source on international and local topics such as Risk Advisory.

For more details on the above please contact your client service partner or our Irish Risk Advisory contacts:

Sean Smith
Partner – Regulatory Risk
T: +353 1 417 2306
E: seansmith1@deloitte.ie

John Kernan
Director – Regulatory Risk
T: +353 1 417 8983
E: jkernan@deloitte.ie

Olumuyiwa John Farayibi
Manager – Regulatory Risk
T: +353 1 417 3096
E: ofarayibi@deloitte.ie

Senan Ryan
Consultant Regulatory Risk
T: +353 1 417 8630
E: senryan@deloitte.ie

CENTRE *for* **REGULATORY STRATEGY** **EMEA**