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# Risk and Regulation Monthly

In October the European Central Bank (ECB) published the **Comprehensive Assessment** results, and regulators continued their work on **remuneration**, the **leverage ratio, structural reform** and **resolution regimes**. The **Fair and Effective Markets Review** also consulted on changes to fixed income, currency and commodities markets.

This note is produced for information only on a best efforts basis, and does not constitute advice of any kind.

## Capital (including stress testing)

The **ECB** disclosed the results of the Comprehensive Assessment it undertook, ahead of the transfer of prudential supervision of Eurozone banks to the Single Supervisory Mechanism (SSM). 130 banks took part in the exercise, which included an Asset Quality Review and a stress test. The stress test, conducted by the European Banking Authority (EBA), also covered non-Eurozone banks. As a result of the Comprehensive Assessment, 25 banks were found to have capital shortfalls of €24.6bn in aggregate. Taking account of capital raised since end-2013 (the cut-off date for data used by the ECB), the aggregate capital shortfall shrank to €9.5bn. Non-Performing Exposures (NPEs), a measure of loan quality, were 18.3% (€136bn) higher than previously reported. Read more in our *blog* and *access* our Comprehensive Assessment Results Analysis tool.

The **Bank of England's Financial Policy Committee (FPC)** published a *review* of the role of the leverage ratio in the UK's bank capital framework. It recommended a minimum leverage ratio of 3% for all Prudential Regulation Authority (PRA)-regulated firms; a supplementary buffer for UK global systemically important banks (G-SIBs), ring-fenced banks and large building societies (to be set at 35% of the risk-weighted systemic risk buffer); and a countercyclical leverage buffer (to be set at 35% of the risk-weighted countercyclical buffer). The review proposed moving ahead of international standards to introduce new requirements for the biggest UK banks and building societies "as soon as practicable". The requirements will initially apply at a consolidated level. All leverage buffers should be met solely with common equity tier 1 (CET1), as should 75% of the minimum ratio.

The **European Commission** *adopted* a Delegated Act amending the Capital Requirements Regulation (CRR) to align the leverage ratio with Basel Committee on Banking Supervision (BCBS) standards. These included clarifications and changes in relation to the treatment of collateral for securities financing transactions (SFTs), credit risk conversion factors in the standardised approach, cash variation margin for derivatives exposures, written credit derivatives, and centrally cleared derivatives. The rules also introduced a clause allowing intragroup exposures to be excluded from the calculation of the leverage ratio when applied at a solo level (subject to national discretion and certain conditions).

The **EBA** *published* an opinion on the application of prudential requirements to credit and investment institutions. The use of Pillar 1 and 2 waivers should be reviewed to improve alignment and to take into account how and where they interacted with individual banks' recovery and resolution strategies, as well as the new intragroup financial support regime introduced by the Bank Recovery and Resolution Directive (BRRD). The opinion will inform the European Commission's final report on the matter, due by the end of December 2014.

The **EBA** *consulted* on the materiality threshold of past due credit obligations and proposed a series of conditions on both the structure and the application of the threshold. Under the CRR, national supervisory authorities are required to set such thresholds to ensure banks assess the materiality of their past due credit obligations so that any defaults can be defined in a harmonised manner across the EU.

The **European Commission** *published* a Delegated Regulation supplementing the CRR regulatory technical standards (RTS) for determining the overall exposure in respect of transactions with underlying assets. The revisions specified the conditions and methodologies to be used to determine the overall exposure of an institution to a client or a group of connected clients, and the conditions under which the structure of transactions with underlying assets does not constitute an additional exposure. Amendments were made to the valuation of underlying exposures to transactions which themselves have underlying assets; the calculation of the exposure value, and the procedure for determining the contribution of underlying exposures to overall exposures.

The **BCBS** *published* a progress report on the adoption status of Basel II, Basel 2.5 and Basel III regulations by Committee members as of end-September 2014. Of the 27 member jurisdictions, 19 had completed adoption of Basel II, 2.5 and the risk-based capital requirements of Basel III, while the other eight were in the process of doing so. Mexico and Russia were least advanced, while the UK had yet to complete adoption of the Basel III capital conservation and countercyclical capital buffers. Progress on the other Basel III elements (G-SIB/D-SIB, liquidity and leverage ratio requirements) was assessed as much more varied across countries.

The **BCBS** *consulted* on the operational risk capital framework, addressing perceived weaknesses in the existing approaches, i.e. the Basic Indicator Approach and the Standardised Approach. The Committee proposed refining the proxy indicator for operational risk exposure by replacing gross income with a Business Indicator and improving the calibration of the regulatory coefficients based on the results of quantitative impact studies. The **BCBS** also *reviewed* implementation of operational risk management principles across 60 systemically important banks in 20 jurisdictions, finding that banks overall had made insufficient progress in implementing the principles.

The **EBA** *reported* the first results of its review on issuances of Additional Tier 1 (AT1) capital instruments. It reviewed nine, totalling €11.6bn between August 2013 and May 2014, and recommended revising or avoiding some clauses in future. The EBA also identified a number of areas where further guidance might be necessary for a common interpretation of the CRR provisions.

The **PRA** published *final rules* on credit risk mitigation, credit risk, governance and market risk, as well as supervisory statements on *credit risk mitigation* and *market risk*, in order to implement Capital Requirements Directive (CRD IV) updates. These included a requirement in relation to firms wishing to use their own estimates of volatility adjustments; new guidance on how to report risks; stricter criteria for the application of a 50% risk-weight to certain commercial real estate exposures located in non-EEA countries; and clarification of how the CRD IV limits to directorships of significant firms apply to the individuals who manage the consolidated group.

The **FPC** *updated* the anchor scenario of its banking stress test. The new scenario is to be used by firms using end-June 2014 data or for Internal Capital Adequacy Assessment Processes (ICAAPs) approved from 1 January 2015. Banks already near the end of their ICAAP production process do not need to adopt the change.

The **PRA** took a number of steps in transposing the Solvency II Directive. It *consulted* on Solvency II approvals, including the pre-application process for use of the Matching Adjustment, and provided six checklists for firms to use when submitting approval applications in an *appendix*. It *published* a letter from Andrew Bulley and Chris Moulder, PRA directors of life Insurance and general insurance respectively, with information on requirements relating to the balance sheet, technical provisions and review of own funds. The PRA also *held* a day-long industry event, where it clarified its approach to Solvency II, stating that it is not looking to 'gold-plate' EU rules and the importance of succinct rather than voluminous documentation, and contingency planning in case a firm does not receive approval for its Internal Model Approval Process. The event featured keynote speeches by *Paul Fisher* and *David Rule*, Executive Directors of Insurance Supervision and Prudential Policy, respectively.

The **PRA** *consulted* on its approach to with-profits insurance business, while the **Financial Conduct Authority (FCA)** *published* a feedback statement on FSA CP12/13: Transposition of Solvency II – which covers COBS rule changes in COBS 20 (with-profit business) and COBS 21 (unit-linked business). The PRA proposed to delete all existing prudential provisions from COBS 20 and replace them with three new prudential rules addressing the following areas: assets in the with-profit funds; distribution strategies; and support arrangements. The PRA consultation included both rule changes and changes in supervisory expectations, for example an expectation that firms will maintain, in respect of each with-profit fund, separate accounting records so as to enable the firm to satisfy all relevant requirements in relation to the fund.

**The International Association of Insurance Supervisors (IAIS)** *finalised* its Basic Capital Requirements (BCR) that will apply to Global Systemically Important Insurers (G-SIIs) following two consultations. This is the first in the IAIS' three-step project to develop group-wide global capital standards. The finalised Requirements do not differ from the consultation significantly, except for adjustments to insurance liabilities and changes to the capital requirements for non-insurance activities. The BCR should lie between the upper and lower thresholds for supervisory interventions (between the Prescribed Capital Requirement (PCR) and the Minimum Capital Requirement (MCR)), with field testing showing an average level of BCR at 75% of insurers' reported PCR.

The **PRA** *published* final rules on the implementation of the FPC's recommendation to limit new mortgage lending at high loan-to-income (LTI) ratios (at or above 4.5) to no more than 15% of the total. The PRA extended the de minimis threshold to apply on either a value or volume basis, exempting those lending less than £100mn or with fewer than 300 relevant mortgage contracts each year. Application at legal entity level was also relaxed, so a lender that is part of a group can now allocate all or part of its allowance to any other regulated entity in that group.

Elsewhere, the **Central Bank of Ireland** *consulted* on new macro-prudential measures, restricting the loan to value (LTV) and LTI ratios for mortgage lending in Ireland by regulated firms. The proposals seek to restrict lending for principal dwelling houses (PDH) above 80% LTV to no more than 15% by value of all new PDH loans, lending for PDHs above 3.5 times LTI to no more than 20% of the value of all new PDH loans, and new lending to buy-to-let above 70% LTV to no more than 10% of the value of all housing loans for investment purposes.

### Liquidity

The **BCBS** *finalised* the Net Stable Funding Ratio (NSFR) standard, intended to prevent banks from relying too heavily on short-term borrowing to fund long-term loans. The final NSFR is broadly in line with the January 2014 standard, with some amendments in relation to short-term exposures to banks and other financial institutions and derivatives exposures. Under strict conditions, certain asset and liability items are viewed as interdependent and can therefore be treated as neutral in terms of the NSFR. The standard will become a minimum requirement by 1 January 2018 and the European Commission is expected to put forward a proposal on the NSFR by end-2016.

The **European Commission** *adopted* a Delegated Regulation supplementing the CRR rules on the liquidity coverage requirement (LCR). The Regulation provided clarity on the calculation of the LCR and weightings applied to its components (including the caps and haircuts used in the calculations) and increased granularity in the application of the rules, in particular on the assessment of high-quality liquid assets (HQLA).

### Governance and risk management (including remuneration)

The **EBA** *reported* on the application of CRD IV rules on remuneration policies of banks and investment firms. Some institutions classified "role-based allowances" in a way that increased the fixed component of remuneration, which might affect the bonus cap. The EBA *issued* an Opinion requesting supervisors to ensure that by end 2014 institutions' remuneration practices on allowances comply with EU legislation. Andrew Bailey, **PRA CEO**, *spoke* at the Mansion House on prudential developments, stating that the bankers' "bonus cap is the wrong policy". (He also noted that over the past year, the capital position of UK banks had strengthened, and said the Government's announcement on annuities did not compromise the soundness of firms nor threaten policyholder protection).

The **BCBS** *consulted* on revised corporate governance principles for banks, strengthening guidance on risk governance, risk culture and compensation systems; expanding guidance on the role of the board in overseeing the implementation of risk management systems; and emphasising the importance of the board's collective, as well as individual, competence. It also provided guidance for bank supervisors in evaluating banks' processes to select board members and senior management.

Gabriel Bernardino, the **European Insurance and Occupational Pensions Authority (EIOPA)** Chair, *spoke* about the dual role of CROs. CROs need to be "independent but involved" so that they can play devil's advocate, offer challenge and alternative views, while also being involved in business developments and strategy. Having a strong CRO should be seen "as sound business practice and not a regulatory requirement."

To support Solvency II requirements, **EIOPA** *consulted* on twelve guidelines on product oversight and governance arrangements by insurers. Manufacturers' administrative, management or supervisory bodies should be responsible for the establishment, implementation, review and compliance with product oversight and governance arrangements. Guidelines also covered conflicts of interest, identification of target market, knowledge and ability of staff, product testing and monitoring, remedial action, distribution channels, outsourcing, and documentation.

The **PRA** published an updated webpage on *whistleblowing* outlining its definition of whistleblowing and the policy of its Whistleblowing Function. Further information is provided on how individuals can blow the whistle (physical and email addresses are provided, as well as a telephone number), the process once this has been done, the PRA's expectations of whistle-blowers and financial incentives.

Dame Colette Bowe *was appointed* as the new chair of the **Banking Standards Review Council (BSRC)**.

### Conduct of Business (including MiFID)

The **Fair and Effective Markets Review (FEMR)** *consulted* on changes to "reinforce confidence" in the fixed income, currency and commodities (FICC) markets. To improve market structures, possible actions included industry-led standardisation of more FICC products; improvements in transparency; removal of barriers to entry for new trading platforms; enhancements to market-driven competition; industry-led improvements to benchmark design; and steps to encourage greater compliance of benchmarks with international standards. To improve conduct, possible actions included developing codes of conduct for FICC markets; bringing trading in certain markets more fully into the scope of regulation; strengthening control and incentive structures; stronger tools to ensure firms' hiring and promotion decisions took due account of conduct; greater use of electronic surveillance tools by firms; ways to strengthen the role of the board; and stronger penalties for staff breaching internal guidelines. See our *blog* for further detail.

The **FCA** *fined* Yorkshire Building Society £4,135,600 for failings when dealing with its mortgage customers experiencing payment difficulties. Between October 2011 and July 2012, insufficient training, fragmented guidance, and weaknesses in procedures and management information led to "significant delays" in determining the most appropriate payment solutions, so some customers incurred "increased fees and associated interest". Yorkshire has started to refund customers – approximately 33,900 customers will be repaid a total of £8.4mn.

The **FCA** *consulted* on new requirements for firms selling mutual society share capital instruments to retail investors (excluding those who are sophisticated or high-net-worth), to ensure the investor has read specified risk warnings and committed not to invest more than 5% of their net assets in them. The FCA also consulted on making permanent the temporary rules, announced in August 2014, restricting the retail distribution of CoCos (contingent convertible securities). The proposed permanent rules would also impose restrictions on funds of CoCos.

The **European Commission** *found* that RBS and JP Morgan participated in an illegal cartel between March 2008 and July 2009, aimed at influencing the Swiss franc LIBOR benchmark interest rate. JP Morgan was fined €61.676mn, but RBS received immunity for revealing the existence of the cartel to the Commission.

**Intercontinental Exchange (ICE) Benchmark Administration (IBA)**, which took over the administration of LIBOR in February 2014, *proposed* a number of enhancements to it. These included setting a universal approach, with a more prescriptive calculation methodology that the LIBOR Oversight Committee will keep under review; expanding the universe of transactions; ensuring that transaction-based submissions are used to the greatest extent possible and defining a waterfall methodology for when there are insufficient transactions to produce a reliable submission; widening the window for eligible transactions so that LIBOR is based on as many transactions as possible; and defining the role of qualitative methods so that expert judgment only had a place as a last resort.

The **Serious Fraud Office (SFO)** *charged* a former Tullett Prebon Group Ltd employee for manipulation of LIBOR.

Wonga *agreed* with the **FCA** to make significant changes to its business as the FCA said that Wonga "was not taking adequate steps to assess customers' ability to meet repayments in a sustainable manner". Approximately 330,000 customers who are more than 30 days in arrears will have the balance of their loan written off and 45,000 who are between 0 and 29 days in arrears will be asked to repay their debt without interest and charges and given an option to do so over an extended period. Wonga also introduced new interim lending criteria.

Linda Woodall, **FCA** Director of Mortgage and Consumer Lending, *spoke* about the **FCA's** work in the six months since it took responsibility for the consumer credit market, with firm-specific visits and more thematic work, looking at home-collected credit, and debt management, and in the near future debt collection firms and pawnbrokers. The FCA had concerns in a number of areas: the quality of advice provided by debt management companies, financial promotions, outsourcing, debt collection letters and compliance with the FCA principles.

The **FCA** *fined* Sesame Ltd, the UK's largest network of financial advisors, £1.598mn for setting up a "pay to play" scheme, which in the FCA's view effectively "undermined" the ban on commission payments introduced by the Retail Distribution Review (RDR).

The **FCA** *fined* two former directors of Pritchard Stockbrokers Limited £10,500 and £14,000 respectively and banned them from the financial services industry for failing to protect client money. The individuals' "recklessness" contributed to "a shortfall of £3mn of client money and resulted in significant consumer detriment". They relied upon "an undocumented and opaque offshore facility" in order to correct a deficit in Pritchard's client money, used client money to pay for business expenses, and did not inform the FCA when shortfalls in client money occurred.

The **International Organization of Securities Commissions (IOSCO)** *consulted* on nine principles regarding the custody of collective investment schemes' (CIS) assets, focusing on aspects relating to the custody function, such as asset segregation, and the appointment and ongoing engagement of custodians. Except in limited circumstances, CIS assets should be entrusted to a third party, functionally independent, custodian.

**EIOPA** *consulted* on recommendations in technical advice to the Commission on conflicts of interest in sales of insurance-based investment products, under amendments to the Insurance Mediation Directive (IMD) contained in MiFID II. It also published a summary of responses from the earlier *discussion paper.*

The **FCA** *published* a feedback statement on the conduct rule changes stemming from the transposition of Solvency II. Firms were "broadly supportive of the proposals, although the FCA has "sought to simplify and clarify the consulted-on rules".

The October **Financial Ombudsman Service (FOS)** newsletter *considered* under-insurance, lifetime mortgages and financial hardship. The FOS said some insurers provided misleading advice to customers, asked confusing questions or left consumers to estimate the value of items themselves. Consumer complaint data was also published and showed that in Q3 2014, 65% of complaints to the FOS were linked to Payment Protection Insurance, with the remainder principally about current accounts, packaged bank accounts and mortgages.

The **Lending Standards Board (LSB)** *revised* the Lending Code to reflect the FCA's role as regulator of the consumer credit market, including debt collection agencies and debt purchase firms, and amending provisions relating to credit assessments and unauthorised credit card transactions. The **FCA** and **LSB** also *signed* a memorandum of understanding (MoU) on the framework for co-operation and communication in carrying out their respective functions under the Banking Conduct Regime, the Consumer Credit Regime and the Lending Code.

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

The **Financial Stability Board (FSB)** *issued* a number of documents on resolution regimes. It reissued its Key Attributes of Effective Resolution Regimes with sector guidance covering insurers, financial market infrastructures (FMIs) and protection of client assets, as well as on information sharing and cooperation between authorities. The approach to resolution should be extended beyond the designated Systemically Important Financial Institutions (SIFIs) to all firms which "could be systemically significant or critical upon failure". The **FSB** also *consulted* on guidance on the identification of insurers' critical functions and critical shared services and on *cooperation and information sharing* with host authorities of jurisdictions not represented on crisis management groups (CMGs).

The **Committee on Payments and Market Infrastructures (CPMI)** and **IOSCO** *published* final guidance to FMIs and relevant national authorities on developing and implementing recovery plans, focusing on the recovery tools available to FMIs.

The **Bank of England** *outlined* its approach to the resolution of banks, building societies and investment firms. It set out the Bank's resolution toolkit, the toolkit's application, and the Bank's role in the three phases of resolution – stabilisation, restructuring and exit. There were no changes to existing rules. Ahead of this publication, relevant **UK and US authorities** *took part* in an exercise simulating the failure of a G-SIB, aimed at furthering both parties' understanding of the existing challenges and coordination required for successful cross-border resolution.

The **PRA** *published* a discussion paper on the principles that firms' operational arrangements should satisfy to facilitate recovery actions, resolution or post-resolution restructuring of firms. The proposals aim to ensure that firms make requisite changes so that services necessary for the continuity of deposit-taking (and other critical functions) operate if a firm fails. Any future proposals would be applied on a proportionate basis, while the extent to which a firm should restructure its operational arrangements would depend on whether its failure would affect the UK financial system, whether it had critical economic functions, the resolution strategies that may be applied to the firm, and whether there were barriers to following those strategies.

The **PRA** *consulted* on implementation of ring-fencing measures for designated ring-fenced banks (RFBs). Key provisions require RFBs not to own entities which conduct excluded or prohibited activities, nor be owned by such firms – instead, affected banking groups should operate a 'sibling' structure. At least half of an RFB's board must be independent non-executive directors, while current employees or directors of other group entities cannot constitute more than a third of board members. RFBs must have sufficient risk management and internal audit resources "identifiable as dedicated to it," and have arrangements in place to ensure continuity of services and facilities to ring-fenced bodies. See our *blog* for further details.

The **EBA** *consulted* on draft guidelines clarifying the relationship between the sequence in which liabilities should be written down or converted when the bail-in power introduced by the BRRD is used, and the hierarchy of capital instruments in the CRR. Authorities should treat capital instruments which rank equally in insolvency in the same way, whatever their other qualities, and should apply the same treatment to instruments which are partially included in the calculation of own funds, as to instruments which are fully included.

The **EBA** *consulted* on draft RTS and guidelines under the BRRD specifying the conditions that competent authorities should assess when authorising intra-group financial support to a company that meets the requirements for early intervention. The overall aim of the RTS and guidelines is to establish a harmonised legal framework to facilitate group support and enhance certainty by addressing current legal obstacles. The EBA measures include capital and liquidity projections and the need for the terms of the support to reflect the default risk of the recipient.

The **FSB** *reported* on the implications of banking structural reforms in the US, UK and EU. While authorities in jurisdictions implementing such reforms felt the measures promoted global financial stability, some other jurisdictions expressed concern over potential negative cross-border implications, including effects on the efficiency of cross-border groups, complications to crisis management and resolvability, decreased liquidity of financial markets, regulatory arbitrage, and leakage to the shadow banking system. The report also found that regulatory restrictions to banking structures which provide greater ex-ante transparency and certainty to the market and authorities in a resolution scenario could nevertheless affect the mobility of cross-border capital flows.

The **PRA** *proposed* changes to the rules on insurance policyholder protection, so that the Financial Services Compensation Scheme (FSCS) covered 100% rather than 90% of a subset of insurance products: (1) annuities and other products which are payable in the form of income or other regular payment; (2) claims arising from the death, incapacity due to injury of the policyholder or unemployment insurance; (3) claims made under contracts for professional indemnity.

The **PRA** *consulted* on depositor protection to implement the recast Deposit Guarantee Schemes Directive (DGSD II). Depositors protected by the FSCS should have continuity of access to their accounts during the course of a resolution. Changes to the single customer view requirements on firms were also proposed.

The **EBA** *found* that the Bulgarian National Bank (BNB) and the Bulgarian Deposit Insurance Fund (BDIF) were breaching the DGSD. The EBA formally requested the BNB to ensure that depositors with Corporate Commercial Bank (KTB) and Commercial Bank Victoria had access to funds protected under the DGSD by 21 October 2014.

### Regulatory perimeter

The **European Securities and Markets Authority (ESMA)** *issued* final draft RTS on clearing obligations for OTC interest rate derivatives required under the European Markets Infrastructure Regulation (EMIR). The RTS clarified the clearing obligation procedure, structure of the Interest rate derivative classes and classes of OTC derivatives to be subject to the clearing obligation. They also set out dates of application and categories of counterparties and remaining maturity of the contracts subject to frontloading. ESMA also *consulted* on the clearing obligation for FX non-deliverable forwards under EMIR and *updated* questions and answers on EMIR implementation. The update provided further guidance on reporting to trade repositories including a *validation table*.

The **European Commission** *adopted* its equivalence decisions for the regulatory regimes of CCPs (central counterparties) in Australia, Hong Kong, Japan and Singapore. The CCPs in these countries will be able to obtain recognition in accordance with the conditions set out in Article 25 of EMIR and be used by market participants to clear standardised OTC derivatives as required by EU legislation.

The **FSB** *published* its fourth annual global shadow banking monitoring report. Based on assets of Other Financial Intermediaries (OFIs), non-bank financial intermediation grew by $5tn in 2013 to reach $75tn. By absolute size, advanced economics had the largest non-bank financial systems, but emerging market jurisdictions showed the fastest growth. Overall, the "level of interconnectedness" between the banking and non-bank financial system declined in 2013. For the first time, the report was accompanied by a dataset on aggregate levels of non-bank financial intermediation by jurisdiction.

The **FSB** *finalised* its regulatory framework for haircuts on non-centrally cleared SFTs and consulted on the application of haircut floors to cover non-bank to non-bank transactions (excluding those backed by government securities). The FSB recommended that regulators set qualitative standards for the methodologies that firms use to calculate collateral margins/haircuts and review those standards by end 2017. BCBS should review existing regulatory requirements for the calculation of collateral haircuts by end 2015. For non-centrally cleared SFTs between banks and non-banks (other than government securities), the framework of floors set out in the document should be incorporated into Basel III by end 2015, for implementation by end 2017. Compared to the consultation, the haircut floors have been raised. The FSB also *published* a document on procyclicality of haircuts, based on the first stage of its quantitative impact study.

In response to a European Commission call for advice, the **EBA** *published* a discussion paper on criteria for simple, standard and transparent securitisations. The paper suggested a two-stage approach, in which the minimum credit quality of the underlying exposures was dealt with after the other criteria. The paper set out six recommendations, including a holistic review of the regulatory framework for securitisation and other investment products; creation of a framework for simple, standard and transparent securitisations; criteria defining these terms; criteria defining 'qualifying' securitisations; a differentiated treatment for 'qualifying' securitisation positions; and principles on the implementation of a regulatory treatment for 'qualifying' securitisation positions.

**HM Treasury** *consulted* on the designation of payment systems for regulation by the new Payment Systems Regulator (PSR), which will assume regulatory responsibility for these systems on April 1 2015. Using four criteria, including the number, value and nature of the transactions that systems presently process or are likely to process, HMT proposed to designate the following systems: Visa, MasterCard, Bacs, CHAPS, Faster Payments, LINK, Cheque and Credit, and Northern Ireland Clearing. American Express and PayPal were excluded. Designation will bring firms under the remit of the PSR, which will have powers to ensure that the systems do not restrict competition in the sector, and to order the owners to break these up or sell them if they are restricting competition.

**ESMA** *agreed* to the emergency short selling measures introduced by CONSOB in Italy, covering a ban on new net short positions (or an increase in existing positions) on shares issued by Banca MPS and Banca Carige.

**EIOPA** *published* guidelines on the use of the legal entity identifier (LEI) following an earlier consultation. EIOPA recommended that national competent authorities (NCAs) ensure that all institutions under their supervisory remit obtain a LEI code from 31 December 2014.

The **European Systemic Risk Board (ESRB)** *extended* the deadlines for national authorities and the EBA to report on their supervision of the funding of credit institutions.

### Rethinking the domestic and international architecture for regulation

The **FPC** *published* a statement following an announcement by Chancellor George Osborne that the FPC should be given additional powers to guard against financial stability risks from the housing market. The FPC recommended it be granted powers to require the PRA and FCA to force lenders to place limits on mortgage lending (owner-occupied and buy-to-let) by reference to LTV and LTI ratios. HM Treasury subsequently *consulted* on the FPC's housing market powers. The FPC also *published* a letter from Mark Carney, Bank of England Governor, to the Chancellor in relation to the Help to Buy scheme; no changes are currently required on financial stability grounds to the house price cap for eligibility and the fee charged to lenders.

**Mark Carney** *spoke* about the regulatory work under way internationally and lessons learned. Major improvements including a strengthening of bank capital requirements globally, a transformation of shadow banking, and safer derivative markets. However, more work was needed to address "too big to fail" and to build an open global financial system. This would require intensive co-operation across national boundaries to mitigate the risk of ring-fencing or subsidiarisation affecting international markets; rigorous and transparent peer-review and assessment processes to ensure consistent application of agreed standards without having unintended consequences; and regulators being alert to new and emerging vulnerabilities.

The **FCA** *issued* a feedback statement on responses to Project Innovate, established to support industry innovation by opening the FCA's doors to businesses with innovative approaches that can benefit consumers in financial services markets.

The **ECB** *published* a Regulation setting out the arrangements under which the ECB will levy an annual fee for the expenditures incurred in relation to its new supervisory role.

**EIOPA** published its 2015 – 2016 action plan for colleges of supervisors. Implementation of Solvency II remained the key focus. Priorities were formulating data requirements, improving transparency, considering sub-group supervision, and assessing the adequacy of Own Risk and Solvency Assessments (ORSAs), and internal model review procedures. EIOPA also *disclosed* the insurance groups for which a college had been set up, 93 in 2014.

**IAIS** *published* an application paper on supervisory colleges, where it provided best practices and examples relevant for all phases of a college's work. Improving group supervision and the use of ORSAs were also the *focus* of the recent meeting of the EU – US insurance project.

**IAIS** *reported* on how its members comply with four of the IAIS Insurance Core Principles (ICPs), relating to legal entity licencing, suitability of key persons in control functions, corporate governance, and effective risk management. Depending on the ICP, between 6 and 9 of the 69 participating authorities were recorded as observing the ICPs only partially, but none were recorded as non-observant. **IAIS** also *published* a paper on approaches to conduct of business supervision taken by IAIS members in their compliance with the ICPs.

### Disclosure, valuation and accounting

The **European Commission** *adopted* a report assessing the economic consequences of country-by-country reporting (CBCR) by banks and investment firms under CRD IV. Stakeholders expected CBCR to have some positive impact on the transparency and accountability of, and public confidence in, the European financial sector. Nevertheless, transparency would benefit from additional guidance to ensure consistent implementation.

The **FCA** *published* an update to its 2013 data strategy. It has established an Information Governance Board to review data and information requests that the FCA makes more than once and/or from more than one source. The FCA also explored the implications of reducing data requested from firms, instead drawing on alternative sources, such as commercial data, and trialled a cataloguing tool to record centrally details of the data and information the FCA holds. The FCA also *published* the first edition of its new data bulletin, where it will publish its *data sets* on a regular basis.

The **ECB** *consulted* on a draft Regulation on reporting of supervisory financial information, including information on balance sheet items such as financial assets, non-performing exposures and financial liabilities, and on income and expenses such as impairment due to credit losses.

### Information security and data privacy

**EU ministers** suggested businesses should not need to notify customers of data breaches where the information concerned is encrypted. The Justice and Home Affairs Committee of the EU's Council of Ministers agreed the plans as part of a wider partial *agreement of proposed changes to EU data protection laws*. The ministers broadly backed plans for the introduction of breach notification requirements for companies across the EU, but agreed that these requirements would not apply where "appropriate technological protection measures" had been taken to protect data that had been lost or stolen from being accessed by people not authorised to see it.

The **European Union Agency for Network and Information Security (ENISA)** *held* the biggest ever cyber security exercise in Europe, when more than 200 organisations and 400 cyber-security professionals from 29 European countries tested their readiness to counter cyber-attacks in a day-long simulation.

### Financial crime

Alun Milford, **SFO** General Counsel, *spoke* on Deferred Prosecution Agreements (DPAs), providing advice to firms on how the SFO would decide whether to offer a DPA. DPAs are intended to incentivise firms to self-report corporate wrongdoing in exchange for increased leniency. Only prosecutors can initiate DPAs. Any invitation to DPA negotiations would depend on "a number of factors, but its hallmark [would] be co-operation and the free supply of relevant information." Firms' internal investigations carried out into potentially corrupt practices or corporate crimes should not be employed to obstruct criminal investigations by prosecutors.

The **Financial Action Task Force (FATF)** issued a number of publications: outcomes from the experts' meeting on *corruption*; outcomes of its Paris *plenary* meeting; a *guidance* on establishing an effective risk-based approach to money laundering regulation for the banking sector; and a *guidance* on transparency and beneficial ownership. The latter focused on the implementation of two FATF Recommendations related to the transparency of beneficial ownership of legal persons and legal arrangements. As usual, the FATF pointed to jurisdictions to which countries are recommended to apply counter-measures (Iran and North Korea) and jurisdictions with strategic deficiencies in anti-money laundering and counter terrorism financing (Algeria, Ecuador, Indonesia and Myanmar).

### Other

***EBA***, ***EIOPA*** and ***ESMA*** published versions of their 2015 work programmes, with ambitious plans for producing technical standards, and work also on supervision, and consumer protection. To that end, the remaining work on CRD IV, and new tasks under the BRRD and the revision of the DGSD, will be priorities for the EBA. Solvency II, IMD II and Product Information Documents for packaged retail and insurance-based investment products will be keeping EIOPA busy. ESMA will continue to focus on MiFID II, the Market Abuse Directive II, and Credit Rating Agencies III (CRA III). The Joint Committee of the European Supervisory Authorities also *issued* its work plan for the next year reinforcing its priorities in the areas of consumer protection and cross-sectoral risk analysis, and regulatory work in the areas of financial conglomerates, anti-money laundering and credit rating agencies.

**IOSCO** *released* a securities markets risk outlook for 2014-2015 (parts of which it later *withdrew*). It identified five risks: (i) the resurgence of high-yield products and the return of leverage; (ii) the search for yield and volatility affecting emerging markets; (iii) risks stemming from central clearing, such as the inherent pro-cyclicality of margin calls, variability in collateral quality, or the varying level of CCP capitalisation; (iv)the increased use of collateral and risk transfer; and (v) corporate governance failures.

The **Treasury Select Committee** *reported* on its inquiry into Project Verde regarding the Co-operative Bank's bid to acquire 632 branches of Lloyds Banking Group. The report examined the causes of the Co-operative's financial problems, the circumstances that led to its successful Verde bid, the collapse of the bid and its consequences. The inquiry revealed failings at different levels, including in the bank's governance and the bidding process itself.

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