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Banking Law Update

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REGULATORY DEVELOPMENTS

Financial Conduct Authority (FCA)

Anti-Money Laundering

The FCA has published the results of its thematic review into *Anti-Money Laundering and Anti-Bribery and Corruptions Systems and Controls: Asset Management and Platform Firms* (October 2013). The review focused on investment management rather than the banking and insurance sectors. While a number of firms had good risk management practices a number of common weaknesses arose in 22 firms within the sample. Feedback had been provided to the firms involved with the review. FCA chief executive, Martin Wheatley, had separately called for greater transparency in the asset management sector at the 2013 Asset Management Conference. The FCA also set out a strategy based on short and long-term reforms to ensure that London remained one of the principal centres for asset management and investment decision making at the conference.

FCA, 31.10.2013

Cooperative Bank

The FCA has supported the announcement by the Treasury to conduct an investigation into the affairs of the Cooperative Bank and the actions of relevant authorities. This is to be undertaken under Financial Services Act 2012, s 77. The FCA will support the investigation and make available all necessary resources without prejudicing any other ongoing criminal or regulatory proceedings. The FCA was considering undertaking a formal enforcement investigation.

FCA, 22.11.2013

Crowd Funding

The FCA has issued a consultation paper on *The FCA's regulatory approach to crowd funding* (*and similar activities*) (November 2013) CP13/13. This examines the regulatory implications of loan based crowd funding or peer-to-peer lending platforms and investment based crowd funding. This allows individuals, organisations and businesses to raise funds through online portals, or crowd funding platforms, to finance or refinance activities. While some crowd funding is unregulated, certain activities are regulated and require exemption from the FCA.

FCA, 24.10.2013

Dealing Commission

The FCA has published a consultation paper on *Use of dealing commission* (November 2013) CP13/17. This considers changes to the Conduct of Business Sourcebook (COBS) to ensure that investment managers take appropriate decisions and control costs on behalf of clients in using dealing commission to pay for goods and services. Dealing commissions from customers' funds are used to purchase execution-related and research goods

and services. This follows thematic work on conflicts of interest between asset managers and their customers, proposed EU changes to the Markets in Financial Instruments Directive (MiFID) on commissions and the review undertaken by the Investment Management Association (IMA). It was estimated that dealing commissions were £3 billion in the UK in 2012. Specific changes are proposed in connection with the criteria for determining exempt research, defining corporate access and the purchase of eligible research through bundled packages.

FCA, 25.11.2013

Derivatives Trader Ban

The Upper Tribunal has directed the FCA to ban former derivatives trader, David John Hobbs, from carrying out any role in regulated financial services following an appeal to the Court of Appeal by the FCA on the Tribunal's earlier direction that no action should be taken against Hobbs. The FCA had issued a Decision Notice in July 2010 including a prohibition order and financial penalty of £175,000 after Hobbs had instructed the broker, Andrew Charles Kerr while he had been a proprietary trader at Mizuho International plc to purchase 600 lots of September 2007 coffee futures on the Euronext Liffe Exchange in August 2007. The Tribunal determined that Hobbs had lied to the FCA and to the Tribunal although it ruled that he had not committed market abuse. The FCA appealed the ruling on the basis of fitness and proprietary with the Court of Appeal referring the matter back to the Tribunal after it had found as a matter of fact that he had not been fit and proper.

FCA, 17.12.2013

Graphene

The Financial Conduct Authority (FCA) has issued a statement expressing concern with regard to investment in the carbon based graphene used in electrical display screens, circuits and batteries. Boiler rooms were suspected of attempting to sell graphene related investments through a graphene investment firm to potential retail investors. This follows the sale of other high risk products such as carbon credits, rare earth metals and overseas land and crops. The FCA notes that the retail market for graphene is uncertain with manufacturing companies purchasing materials directly in bulk without retail involvement. Sellers may also be using questionable and high pressure sales tactics with vulnerable consumers being targeted. Most of the firms identified as promoting and selling graphene investments were not authorised within the UK which meant that investors would not have access to the Financial Ombudsman Service or Financial Services Compensation Scheme.

FCA, 30.12.2013

Integrity and Culture

FCA Chief Executive, Martin Wheatley, has given an address on "Modelling integrity through culture" at the FCA Markets Conference 2013. Martin

Wheatley reviewed the global regulatory agenda and new regulatory landscape following the global financial crisis. Against this background, the FCA had strengthened its structure and acquired a stronger sense of direction. Much of the reform had focused on preventing systemic and organisational failure with the new focus on conduct and culture issues. The FCA had established a regime that was practical and successful in shifting firm behaviour and individual accountability. The objective was to develop a culture of transparency, confidence and ultimately integrity across the financial services industry which provided depth to liquidity in London markets and reinforced the UK's stature as a global financial centre. The FCA would also work as a global authority to create a pragmatic, consultative and cooperative approach to regulation at the international level.

FCA, 19.11.2013

Investment Firms CRD IV

The FCA has issued a policy statement PS13/10 on implementation of the EU Capital Requirements Directive (CRD) IV for UK investment firms. CRD IV consists of Directive 2013/36/EU and Regulation (EU) 575/2013 which implements the Basel III requirements for banks and investment firms. The statement contains feedback on three earlier consultation papers CP13/6, 13/9 and 13/12 and made rules and guidance. The FCA has adopted five principles in transposing CRD IV of legal minimum implementation, intelligent or strict copy-out, pragmatic and proportionate, minimise need for change and forward looking. The rules include guidance on proportionality for BIPRU firms and IFPRU firms under the FCA Remuneration Code SYSC 19C and A, the CRD IV Instrument 2013, GENPRU and BIPRU Amendments Instrument, Consequential Amendments Instrument, Governors and Remuneration Instrument, Reporting Instrument and AIFMD and UCITS Consequential Amendments Instrument 2013.

FCA, 13.12.2013

LBG Fine

Lloyds Banking Group (LBG) has been fined £23,038,800 for serious sales incentives failings which is the largest fine ever imposed by the FCA for retail conduct failings. The fines relate to the incentive structures at Lloyds TSB Bank plc and Bank of Scotland plc in connection with advised sales of investment products (including share ISAs) and protection products (including critical illness or income protection) between January 2010 and March 2012. Lloyds TSB advisers had sold more than 630,000 products to over 399,000 customers with £1.2 billion in investments and £71 million in protection premia. Halifax advisers had sold 380,000 products to over 239,000 customers with £888 million invested and £38 million in protection premia. Bank of Scotland advisers had sold 84,000 products to over 54,000 customers with £170 million invested and £9 million paid in protection premia. Advisers were rewarded through incentive schemes which paid variable based salaries, individual and team bonuses and one-off payments and prizes. The FCA considered that the systems and controls used by the

firms to manage the incentive schemes were inadequate with bonuses being paid when sales had been unsuitable or potentially unsuitable. Managers monitoring good practice were also assessed against sales targets which created a clear conflict of interest. The incentive schemes had created significant risks that the firms were not able to mitigate. The FCA had increased the fine by 10% as the FSA had earlier warned about the use of poorly managed incentive schemes with Lloyds TSB Bank plc previously having been fined in 2003 for the unsuitable sale of bonds. The total fine of £35,048,556 million was reduced by 20% on early settlement. Lloyds TSB Bank plc was fined £16,407,300 and Bank of Scotland plc £11,631,500.

FCA, 11.12.2013

Listing

The FCA published a consultation paper on *Enhancing the effectiveness of the Listing Regime: feedback to CP12/25 and further consultation on related issues* (November 2013) CP13/15. The purpose is to protect minority shareholders in premium listed companies through the provision of additional voting rights and greater influence on key decisions to avoid controlling shareholder abuse. The document includes feedback on the earlier consultation paper, near-final rules, consultation on the new or revised proposals and associated draft rules.

FCA, 5.11.2013

Listing Rules

The FCA has issued a policy statement PS13/11 containing changes to the Listing Rules following the production by the Department for Business, Innovation and Skills (BIS) of the Directors' Remuneration Reporting Regulations (SI 2013/1981) and the Narrative Reporting Regulations (SI 2013/1970). This follows an earlier consultation paper CP13/7 in August 2013. The objective of the regulations was to reduce unnecessary administrative obligations on premium listed companies incorporated in the UK including specifically only requiring compliance with one set of directors' remuneration disclosure requirements. The new requirements came into effect on 13 December 2013 for listed companies with a financial year ending on or after 30 September 2013 and which had not published their annual financial report before 13 December 2013.

FCA, 13.12.2013

London Metal Exchange

The FCA has issued a statement on the London Metal Exchange's (LME) warehousing arrangements. The FCA is responsible for the oversight of the LME as a recognised investment exchange. The warehousing arrangements are not directly regulated although relevant to the functioning of the market. These were concerned with the receipt, holding and delivery of metal traded through LME contracts. The LME had undertaken a number of initiatives to manage potential conflicts of interest in warehouse ownership and to reduce

queue lengths. The FCA was working with the LME to ensure that the changes were consistent with its regulatory obligations.

FCA, 7.11.2013

Market Abuse Appeal

The Court of Appeal has upheld two decisions by the Upper Tribunal (Tax and Chancery Chamber) in relation to charges of market abuse by the Canadian company, Swift Trade Inc and former director Peter Beck. The Tribunal had held in January 2013 that the FCA had been correct in determining that the layering activity involving contracts for differences was in relation to a qualifying investment as set out in the Financial Services Markets Act, that the company had effected the transactions or orders and thereby engaged in market abuse. The FCA considered that the firm knew that the orders placed in CFDs would be automatically reflected in share orders and constitute market abuse. Layering involved the entering into of large orders on the LSE order book to move share prices with the market adjusting to the increase in supply and demand with profits being earned from follow-up trades on the movement. The decision by the Tribunal to uphold the dissolution of the company after the issue of a Warning Notice was also upheld.

FCA, 19.12.2013

Mis-selling Complex Investments

The Upper Tribunal has upheld the decision by the FCA to fine Westwood Independent Financial Planners £100,000 for communications and suitability failings in connection with the sale of geared traded endowment policies (GTEPs). GTEPs were complex long-term products with the company advising investors to remortgage their homes to invest in them. The company had failed to take reasonable care to ensure that its recommendations were suitable and had not provided information in a clear and fair way. £509,123 had been generated in commissions through the sale of 50 GTEPs with many of the plans subsequently having fallen in value. The FCA considered that the firm had breached PRIN 7 and 9.

FCA, 27.11.2013

Mortgage Market Review

The FCA has issued a policy statement on data reporting as a final document following its Mortgage Market Review (MMR). The objective of the MMR was to improve responsible lending with the FCA having to review and enhance its data collection following its consultation paper CP13/02 on data reporting. The policy statement contains the final rules on data collection which will come into effect on 1 January 2015. The FCA is responsible for the regulation of the residential mortgage market in the UK with the principal reforms being published in October 2012.

FCA, 16.12.2013

Occupational Pension Scheme Bans

The FCA has banned three men from working in the financial services industry and another from holder key positions following a review of the activities of CBW Trustees Ltd and CBW Pensions Forensics Ltd by the Pension Regulator (PPR) which had uncovered significant misconduct. Michael Conley, director of CBW Pensions Forensics, and Andrew Powell, independent adviser to the company, were considered to lack integrity. Martin Wynn, owner of the Independent Financial Adviser (IFA), G&G Financial Services Ltd, and Daniel Conway, director of the IFA Staverton Wealth Management Ltd, were considered to have been incompetent and incapable of properly discharging their duties. The two IFAs had been appointed to advise six occupational pension schemes with investments being unnecessarily moved frequently to generate over £4 million in commission with pension holders receiving lower incomes as pension assets were placed in potentially unsuitable higher risk investments.

FCA, 17.12.2013

Outsourcing

The FCA has conducted a thematic review on *Outsourcing in the asset management industry* (November 2013) TR13/10. This specifically examined the possibility of poor outcomes arising for consumers either through inadequate contingency planning in the event of the failure of a service provider and through inadequate oversight of the service provider. The review confirmed that improvements had been achieved on resilience and oversight with oversight principally being limited through insufficient internal expertise. Asset managers were directed to review and enhance their contingency planning and to review the effectiveness of their oversight arrangements.

FCA, 4.11.2013

Price Comparison Websites

The FCA has undertaken a thematic review of insurance price comparison websites (PCWs) examining 14 PCWs which represent 90% of the market. The FCA accepts that PCWs provide a valuable service although concerns arose with regard to transparency and fairness and ensuring that sufficient information was provided on product quality in addition to cost. The review would focus on motor, travel and home insurance which were the most popular purchased products.

FCA, 24.11.2013

RBS

The Financial Conduct Authority (FCA) has considered the reports produced by Sir Andrew Large on *RBS Independent Lending Review* (25 November 2013) and by Lawrence Tomlinson, *Banks' Lending Practices: Treatment of Businesses in Distress* (25.11.2013). The FCA acknowledges that commercial banking is not a regulated activity under the Financial Services and

Markets Act 2000 although the reports contain concerns if the allegations are made, in particular, in the second report are substantiated. The FCA has agreed with RBS that an independent skilled person will be appointed under FSMA s 166 to review the allegations with Clifford Chance being appointed to examine the allegations made. The FCA would consider whether the review reveals issues that fall within its remit and would write to other banks requesting confirmation that they have not engaged in any similar poor practices.

FCA, 29.11.2013

Recognised Investment Exchanges

The FCA has published a consultation paper on *Competition in the market for services provided by a Recognised Investment Exchange: proposed amendments to REC* (November 2013) CP13/16. The FCA became responsible for supervising trading infrastructure and participant conduct in April 2013. The new rules and guidance were intended to promote effective competition in the interest of consumers including in the markets for services provided by RIEs which would improve choice and innovation and limit excessive fees and trading costs. The document contains specific proposals to inter alia clarify the competition considerations used to determine where an RIE satisfies the Recognition Requirements, impose restrictions on third party service providers and increase disclosure through the annual reports of a Recognised Overseas Investment Exchange (ROIE).

FCA, 18.11.2013

Regulatory Fees and Levies

The Financial Conduct Authority (FCA) has produced a consultation paper on *Regulatory fees and levies: policy proposals for 2014/15* (October 2013) cp 13/14. This covers FCA fees and levies, the Financial Ombudsman Service, the Financial Services Compensation Scheme (FSCS) and the Money Advice Services (MAS). The FCA fees policy is intended to be neutral and not inadvertently interfere with the market or distort competition. The paper includes proposed new fees for consumer credit as from April 2014 (chapter 2) and a new fee-block for firms carrying out investments holding client money or safeguarding and administering custody assets (chapter 3). The definitions of income are simplified with a new annual fee for approved reporting mechanisms (ARMs) to be introduced to avoid cross-subsidisation by firms that do not use ARMs. Further technical amendments are made to the fees manual with a new allocation of MAS costs across firms. There is also a clarification of the definition of income for intermediaries (chapter 4), an annual fee for approved reporting mechanisms (ERMs) (chapter 5), electronic payment application fees (chapter 6) and Money Advice Service (MAS) levies (chapter 7).

FCA, 31.10.2013

Virtual Currencies

The FCA has issued a warning to consumers on virtual currencies following the issuance of a statement by the European Banking Authority (EBA) highlighting potential risks in buying, holding or trading in virtual currencies such as bitcoin. The use of virtual currencies had grown significantly with investors potentially not being fully aware of the risks involved. Virtual currencies were a form of unregulated digital money that is not issued or guaranteed by a central bank and does not constitute legal tender. Virtual currencies had moved from computer gaming and social network use to being accepted by retailers, restaurants and entertainment venues. Bitcoin had created a model for other decentralised, peer-to-peer virtual currencies or crypto currencies transferred through digital wallets. Bitcoin can be purchased through exchange platforms or ″mined″ through solving complex algorithms. The EBA noted investors may lose money on an exchange platform, currency may be stolen from digital wallets, no refund rights arose with virtual currencies not constituting legal tender, currency values may vary and possibly collapse, criminal organisations may be involved and separate value added tax or capital gains tax liabilities may arise.

FCA, 19.12.2013

Wholesale Gas Manipulation

The FCA and Ofgem have conducted a review into allegations of manipulation of wholesale gas prices in September 2012. Ofgem is responsible for the regulation of the physical gas market with FCA overseeing gas based financial derivatives. The authorities concluded that no evidence could be found of market manipulation with no further action being taken. The FCA and Ofgem would continue to monitor energy in financial markets and work together in the event of misconduct being revealed.

FCA, 7.11.2013

Prudential Regulation Authority (PRA)

Funding for Lending Scheme Capital Offset

The PRA confirmed that it would extend the capital offset for corporate lending under the Funding for Lending Scheme (FLS) with the offset for household lending ending on 31 December 2013. The FLS has been set up with other measures to support additional lending the real economy in June 2012. The FSA issued a statement in September 2012 providing for capital offsets which allowed firms participating in the scheme to offset any additional Pillar 1 capital charges that would arise with a reduction in Pillar 2 capital buffer requirements. The FLS was extended by the Bank of England in April 2013 to 30 January 2015. Offsets would continue for net new lending to private non-financial corporations to support small and medium businesses until end January 2015.

PRA, 28.11.2013

Parliamentary Commission on Banking Standards

The Bank of England published its response to the final report by the Parliamentary Commission on Banking Standards (PCBS) in October 2013. The statement deals with the specific recommendations directed to the Bank of England including individual responsibility and senior level accountability, bank governance, banking market competition and reinforced regulatory responsibility. The Bank welcomed the report and would take forward the recommendations subject to certain exceptions. The paper also notes the work that was carried out in connection with other recommendations including on accounting, order and disclosure, whistleblowing, Bank and PRA governance and accountability and payment systems.

Bank of England, 7.10.2013

Practitioner Panel

The Prudential Regulation Authority (PRA) has established a Practitioner Panel to represent the interests of the financial services industry. The 13 members of the panel were nominated by trade associations representing PRA regulated firms. The Panel held its first meeting on 29 November 2013 at which Martin Gilbert, CEO of Aberdeen Asset Management, was appointed Chair with Brian McCrory, Director of the Belfast Teachers Credit Union, appointed Deputy Chair. The Panel is to meet, at least, quarterly with members being appointed on three year terms.

PRA, 12.12.2013

UK Bank Stress Testing

The Prudential Regulation Authority (PRA) has issued a discussion paper on *A framework for stress testing the UK banking system* (October 2013). This sets out the principal features for a proposed framework for stress testing banks in the medium term prepared by Bank of England staff under the direction of the Financial Policy Committee (FPC) and the PRA Board. The FPC had recommended in March 2013 that the Bank and PRA develop an appropriate stress testing regime which would specifically assess the UK banking system's capital adequacy. The purpose is to provide a quantitative, forward-looking assessment of the capital adequacy of the system and the individual institutions within it with stress tests being carried concurrently across banks, building societies and PRA-designated investment firms. A number of scenarios would be examined including common strategies and specific scenarios for individual institutions. These are developed in further specific sections. A number of basic principles are referred to covering purpose, frequency, coverage, scenario design, scenario application, amplification mechanisms and communication (Box 1 p10). International experience with the stress testing is reviewed (Box 2 p11). Additional sections are included on asset quality reviews, scenario modelling, outputs and remedial and policy actions and disclosure. The FPC has power to issue recommendations or directions with the PRA having a range of other regulatory enforcement powers.

PRA, 1.10.2013

Strengthening Capital Standards

The Prudential Regulation Authority (PRA) has issued a Statement following its consultation paper on *Strengthening capital standards: implementing CRD IV* (August 2013) cp5/13 which was issued on 2 August 2013. This sought opinion on PRA implementation of the EU Capital Requirements Directive IV 2013/36/EU of 26 June 2013 (CRD IV) and Capital Requirements Regulation 575/2013 of 26 June 2013 (CRR) which gave effect to the Basel Committee *Basel III* requirements within the EU. The PRA had issued a Supervisory Statement on ″Capital and leverage ratios for major UK banks and building societies″ in November 2013 (ss3/13). This set out the PRA's expectations in relation to the capital and leverage ratios for the eight largest UK banks and building societies (Barclays, Cooperative Bank, HSBC, Lloyds Banking Group, Nationwide, Royal Bank of Scotland, Santander UK and Standard Chartered). This set out the Common Equity Tier 1 (CET1) capital ratio and Tier 1 leverage ratio from 1 January 2014 under the CRR. The CET1 capital adjustments were those specified by the PRA under its capital shortfall exercise with the results having been published on 20 June 2013. Compliance was to be on a consolidated basis except where a separate plan had been agreed with the PRA. The PRA would no longer apply the ″4/6/8″ capital framework set by the Financial Services Authority (FSA) in 2008 nor the definition of CET1 communicated by the FSA to the British Bankers' Association (BBA) on 1 May 2009. The PRA would introduce final CET1 definitions in early course. The PRA confirmed in its November Statement that CET1 would be increased to 4% from 1 January 2014 – 31 December 2014 and 4.5% from 1 January 2015. Tier 1 (CET1 plus Additional Tier 1) would be 5.5% in 2014 and 6% in 2015. Total capital (Tier 1 plus Tier 2) would remain at 8%. Pillar 2A risks, business risks not otherwise captured under the CRR such as pension risk, should be covered by 56% CET1 from 1 January 2015. Firms will generally be required to maintain a 7% CET1 capital ratio (including the 2.5% conservation buffer) and a 3% Tier 1 leverage ratio after adjustments to risk-weighted assets (RWAs). The two other buffers referred to in the August 2013 consultation document include the 0–2.5% counter-cyclical buffer (CCyB) and 0–3.5% systemic risk buffer as determined by the Financial Stability Board (FSB). It is expected that the CRR and CRD will require 100 technical standards to be produced by the European Banking Authority (EBA). The PRA imposes a separate Pillar 2B capital requirement on potential forward-looking exposures such as changes in the economic environment through its Capital Planning Buffer (CPB) within its existing Internal Capital Adequacy Assessment Process (ICAAP) and Supervisory Review and Evaluation Process (SREP).

PRA, 29.11.2013

Bank for International Settlements (BIS)

Asia Decoupling

The Bank for International Settlements has published a working paper on "Asia's decoupling: fact, forecast or fiction?" (December 2013) no 438 by Lillie Lam and James Yetman. Asia Pacific economies were considered to have been decoupling from other economies with measures of real economic co-movement indicating a downward trend. This process was reversed during the international financial crisis with co-movement increasing to historically high levels. The paper examines co-movement patterns which demonstrate a high degree of sensitivity to changes in macroeconomic volatility over time with co-movement being linked to underlying trade and financial integration. Co-movement should strengthen with increased international linkages and with decoupling being referred to as a fiction rather than a fact or a forecast.

BIS, 23.12.2013

Basel Implementation Progress

The Basel Committee has published a *Progress report on implementation of the Basel regulatory framework* (October 2013) which covers member adoption of Basel II, Basel 2.5 and Basel III at end September 2013. The results are produced as part of the Committee's RCAP referred to above with assessment reports being published on China and Switzerland and earlier assessments of Singapore and Japan. Brazil and Australia were being assessed with Canada, the EU and US to begin later in 2013 following earlier preliminary assessments of the EU and the US. The assessment methodology examines draft regulations published or unpublished and final rules published and enforced. A three part grading system is used with implementation completed (green), implementation in process (yellow) and no implementation (red).

BIS, 9.10.2013

Central Bank Independence

Stephen G Cecchetti, BIS Economic Advisor and Head of the Monetary and Economic Department, also spoke on 'Central bank independence – a path less clear' at the Bank of Mexico Conference. Cecchetti compared central bankers after the crisis to mountaineers after an avalanche trying to regroup and decide how to proceed safely. Earlier consensus on central bank objectives and independence had supported the Great Moderation until the most recent crisis. Cecchetti refers to, 'Broader, deeper and more open-ended responsibilities for financial stability have dragged central banks into politically charged territory.' with the need to balance a number of different objectives which may conflict. 1. Cecchetti added that, 'The aims of financial stability policy elude easy definition and measurement, transparency faces limits, and accountability remains elusive.' With the large scale purchase of financial assets as part of unconventional monetary policy 'taking several central banks into previously unexplored territory.' Earlier new consensus arose from an improved understanding of the relationship between the

financial system and the macro economy as well as improvements in public policy decision making. The consensus model assumed that prudential, fiscal and monetary policy could be separated. With differences in timing specifically reducing conflicts with prudential policy being timeless, fiscal policy low-frequency and long-term and monetary policy high-frequency and short-term. 2. This was supported by empirical models that accurately predicted the response of target variables, including output and inflation, to instrument changes and specifically the policy rate. This was supported by the delegation of clearly defined tasks to independent monetary and regulatory agencies. It was nevertheless realised that central bank independence conflicted with representative democracy with delegation being supported by clearly stated objectives, avoiding functional overlaps which would require trade-offs and negotiation and effective accountability principally secured through transparency. The consensus view supported the delegation of monetary and regulatory policy with fiscal policy being retained by the government. 3. A series of conflicts had since arisen following the crisis. Monetary policy affected fiscal policy through central bank balance sheets, fiscal policy influence monetary and regulatory policy through financing choices, monetary policy influenced regulatory policy through bank balance sheets, regulatory policy influenced fiscal policy through the treatment of sovereign debt and regulatory policy influenced monetary policy by adjusting borrowing costs. The policies had become even more interconnected following the crisis with restoring financial stability expected to involve costs on central banks as well. 3/4. It was necessary to adopt a new non-consensus or non-standard model. Central banks had specifically to improve their understanding of the relationship between the financial system and real economy and include debt as an important form of financing into macroeconomic models. Further governance difficulties also arose with regard to the absence of a simple operational definition of financial stability and clear numerical measures. It was more difficult to secure transparency in explaining financial stability outcomes with transparency possibly increasing institutional fragility in connection with prudential policy. There was also an increased need for discretionary decisions which were inherently more political. Additional inter-agency collaboration was also required which specifically included greater involvement of political representatives within the larger decision-taking processes. This was particular clear in connection with the development of a number of new macro-prudential models. The last 50 years were occupied with the development of a new monetary policy solution with the future requiring the integration of monetary and financial stability policy in a new model. Institution independence was nevertheless still necessary especially with the value of depoliticising decision taking through delegation although more complex inter-institutional relations would have to be constructed.

BIS, 14.10.2013

General Manager of the BIS, Jaime Caruana, has given an address before a Bank of Mexico international conference on ‘The changing nature of central bank independence’ with the event covering ‘Central bank independence – Progress and challenges’, Mexico City, 14–15 October 2013. Caruana noted

that central bank independence had traditionally focused on insulating monetary policy from political intervention with new pressures having been created that might prevent the timely normalisation of the extraordinary monetary easing adopted since the global financial crisis. Two specific pressures had arisen in terms of financial dominance and expectations dominance. Financial dominance arose from the highly indebted nature of financial markets and private sectors which reflected earlier fiscal dominance where governments failed to take effective control of their finances. Expectations dominance was concerned with an unrealistic reliance on the provision of continuing monetary accommodation to correct underlying faults. Central banks had reduced policy rates and kept them extraordinarily low or at zero in some countries for an extended period with total central bank balance sheets doubling in size to over $9 trillion or a quarter of GDP. Monetary accommodation had created conditions within which borrows' balance sheets could be repaired and structural reforms undertaken to restore strong, balanced and sustainable growth although monetary policy was not a substitute for these reforms. A substantial amount of private sector deleveraging and bank recapitalisation had been undertaken although labour rigidities and sectoral rebalancing remained unfulfilled in many economies with total public and private debt rising to almost $35 trillion between end 2007 and 2013. Prolonged monetary accommodation had overburdened central banks and threatened their reputation and credibility with unrealistic expectations arising with regard to what they could deliver. Pre and post-crisis low policy rates in advanced economies had generated upward pressure on emerging market exchange rates with a downward pressure on bond yields and higher levels of dollar borrowing and capital flows with financial bubbles arising in the absence of higher rates and currency intervention. These trends reversed midyear. The announcement of the beginning of US tapering mid-2013 produced a sell-off of equities and bonds in global markets with monetary policy having to be tightened despite weak macroeconomic conditions. Central banks had to normalise monetary conditions in a balanced and timely manner with markets accepting that normalisation was inevitable. Extraordinary monetary measures should be kept as reserve instruments in future. Use of central bank balance sheets confused the limits between monetary and fiscal policies with this threatening operational independence over time. Central banks can only control short-term rates with other asset returns, such as long-term government bond yields, being dependent on government action which undermines instrument independence. Unconventional monetary policy generated significant additional market and credit risks for central banks with the possible need for financial support from the government following substantial losses undermining operational autonomy. Other technical revisions could be considered, such as with reserves interest payment, collateral ranges and collateral rates targeting, although these were more operational and did not contradict the need for effect continuing central bank autonomy.

BIS, 17.10.2013

Central Counterparties

The Committee on Payment and Settlement Systems (CPSS) has published a paper with the International Organisation of Securities Commissions (IOSCO) on *Public quantitative disclosure standards for central counterparties* (October 2013). CCPs had to disclose relevant information to allow the risks related to their use to be properly understood. The CPSS and IOSCO had published a *Disclosure Framework* in December 2012 with additional guidance on the quantitative data that the CCP should disclose more frequently being included within the latest document. This should allow a comparing of CCP risk controls, including on financial condition and resources to withstand losses, provide an understanding of CCP risks and assess their systemic importance.

BIS, 15.10.2013

Critical Service Providers

The Committee on Payment and Settlement Systems (CPSS) and the International Organisation of Securities Commissions (IOSCO) have published a consultative document on *Assessment methodology for the oversight expectations applicable to critical service providers* (December 2013). Critical service providers were included in the CPSS IOSCO *Principles for financial market infrastructures* (April 2012) Annex F with financial market infrastructures (FMIs) being dependent on the continuous and adequate functioning of third-party service providers such as information technology and messaging providers. The latest document establishes an assessment methodology and guidance for authorities in assessing the critical service providers of an FMI against the oversight expectation set out in Annex F.

BIS, 18.12.2013

Effective Exchange Rate Indices

The BIS has expanded its effective exchange rate (EER) indices to cover 61 economies with the addition of Colombia, Luxemburg and the United Arab Emirates. Weights have been revised to reflect 2008–2010 trade data. Nominal EERs are calculated as geometric weighted averages of bilateral exchange rates and real EERs weighted averages adjusted to reflect consumer prices. Broad indices are provided for 61 economies and narrow indices for 27 economies.

BIS, 15.11.2013

Equity Investments

The Basel Committee has published a revised policy framework for the prudential treatment of banks' investments in the equity of funds held in the banking book including hedge funds, managed funds and investment funds. Equity investments are covered under Basel II with the new standards to come into effect in January 2017. The revised standards reflect a fund's leverage, clarify the application of internal ratings-based approaches for credit risk and take into account funds' underlying investments with a 1250%

risk weight being applied where there is insufficient transparency regarding a fund's investment activity. Banks are generally required to apply a ″look-through″ approach to identify the underlying assets in investing in funds with a staged approach being adopted where this is not always possible. Three approaches are included with the ″look-through approach″ (LTA), ″mandate based approach″ (MBA) and ″fall-back approach″ (FBA).

BIS, 13.12.2013

Financial Stability

BIS General Manager, Jaime Caruana, has given a speech on ″Addressing risks to financial stability″ before the 49th SEACEN Governors' Conference and High-Level Seminar, Nepal, 21 November 2013. The financial system had been made more resilient through increased capital and liquidity buffers although regulation could not always follow financial innovation. Supervision had to be proactive and focus on systemic risk with monetary policy filling in the ″cracks″ in the regulatory framework and limiting incentives to increase leverage. Bank lending had to be monitored with parallel capital market financing especially following growth in external bond issuance by Asian firms.

BIS, 26.11.2013

Global Liquidity and East Asia

The BIS has published a working paper by Dong He and Robert N McCauley on 'Transmitting global liquidity to East Asia: policy rates, bond yields, currencies and dollar debt' (October 2013) no 431. The paper examines the transmission of conventional and unconventional monetary policy on major advanced Eastern Asian economies through monetary policy reactions, integrated bond markets and induced currency appreciation. The importance of an expansion in the use of the US dollar credit as a transmission mechanism is highlighted with increased growth in China and Hong Kong in contrast to Korea.

BIS, 4.10.2013

Global Liquidity Indicators

The BIS has published updates on indicators for global liquidity conditions from October 2013 with revisions being published twice annually. This follows G20 activities and earlier work by the BIS and Committee on the Global Financial System (CGFS). The statements include credit aggregates within global liquidity indicators and supplementary indicators including monetary liquidity, funding liquidity and risk appetite. The data is provided in the form of graphs. Global growth in interbank credit was virtually zero with outstanding domestic and international bank credit being substantially above pre-crisis levels and with central bank assets remaining at around $10 trillion.

BIS, 15.10.2013

Global Systemically Important Banks

The BIS has published additional information on the Global-Systemically Important Bank (G-SIB) methodology. This includes the denominations used to calculate the scores of banks in the 2012 exercise and the cut-off score and bucket thresholds used to identify the updated list of G-SIBs produced by the FSB. This will allow banks to calculate their end 2012 scores and determine their positions within the buckets which will determine higher loss absorbency (HLA) requirements which come into effect from January 2016. This reflects the updated assessment methodology published by the Committee in July 2013. The FSB publishes an updated list of G-SIBs every November since 2011. HSBC and JPMorgan Chase were assigned to Bucket 4 (2.5%) with Barclays, BNP Paribas, Citigroup and Deutsche Bank in Bucket 3 (2%). Bucket 2 (1.5%) consisted of Bank of America, Credit Suisse, Goldman Sacs, Group Crédit Agricole, Mitsubishi UFJFG, Morgan Stanley, Royal Bank of Scotland and UBS with the others in Bucket 1 (1%).

BIS, 11.11.2013

Liquidity Regulation and Monetary Policy

The BIS has published a working paper by Morten Bech and Todd Keister on 'Liquidity regulation and implementation of monetary policy' (October 2013) no 432. The paper examines the effects of the Basel III liquidity coverage ratio (LCR) requirement for banks to hold high-quality liquid assets against a 30 day stress test period on the implementation of monetary policy which was principally carried out through controlling short-term interest rates on central bank reserve assets. Standard monetary policy implementation models are used to assess the LCR requirement effects which indicate that if there is an LCR shortfall with the link between open market operations and the overnight interest rate being affected and the yield curve becoming steeper, this may require operational adjustments as the new liquidity requirements are introduced.

BIS, 10.10.2013

Liquidity Stress Testing

The Basel Committee has published survey results on *Liquidity stress testing: a survey of theory, empirics and current industry and supervisory practices* (October 2013). This was prepared by the Research Task Force's Workgroup on Liquidity Stress Testing to review current practices and identify gaps to attempt to produce clearer guidance. The paper includes a literature review of factors relating to liquidity stress, a review of stress testing methods, banks' liquidity stress testing best practices and additional issues including the interaction between banks and non-bank financial intermediaries, integrating capital, liquidity and contagion stress testing and the role of the central bank as lender of last resort.

BIS, 23.10.2013

Market Volatility and Foreign Exchange

The BIS has produced a paper on *Market volatility and foreign exchange intervention in EMEs: what has changed?* (October 2013). This examines the significant capital flows to and from emerging market economies (EMEs) in the five years following the crisis with some countries having to resist appreciation pressures and then intervene to avoid significant depreciation pressure. The collection of papers follows a Deputy Governors' meeting of major EMEs in Basel on 21–22 February 2013. Issues examined include the role of flexible exchange rates in stabilising an economy and promoting a stable financial development, changes in intervention motives and strategy and measuring intervention effects. Flexible exchange rates can smooth output volatility although volatile rates increase volatility and become a separate source of vulnerability. Intervention was generally intended to limit volatility rather than achieve a specific exchange rate with exchange rate policy having to be consistent with monetary policy. The overall effectiveness of foreign exchange intervention was unclear. It did assist signalling although overall effectiveness may have arisen due to its use with other measures to limit capital flows and prevent the build up of foreign exchange positions in the markets. Intervention had no clear effect in some cases and may have exaggerated volatility.

BIS, 25.10.2013

Navigating the Great Recession

The BIS published a working paper on ″Navigating the Great Recession: what role for monetary policy?″ (December 2013) no 74. This reproduces the papers submitted at the 12th BIS Annual Conference in Lucerne, Switzerland on 20–21 June 2013. This includes the opening address by Stephen Cecchetti, former BIS Economic Adviser, and keynote address by Finn Kydland, University of California, Santa Barbara. Papers cover such matters as ″Cyclical macroeconomic policy, financial regulation and economic growth″ (December 2013) no 434 by Philippe Aghion and Enisse Kharroubi, ″Is monetary policy overburdened?″ (December 2013) no 435 by Athanasios Orphanides, ″Global spillovers and domestic monetary policy″ (December 2013) no 436 by Menzie D Chinn and ″International monetary policy coordination: past, present and future″ (December 2013) no 437 by John B Taylor. The paper on cyclical macroeconomic policy concludes that raising regulatory requirements for bank capital can improve financial stability and preserve economic growth if complemented with more countercyclical macroeconomic and regulatory policy. The second paper examines public policy goals of full employment, fiscal sustainability and financial stability which may overburden monetary policy and concludes that this may diminish and compromise the independence and credibility of central banks and reduce the effectiveness in maintaining price stability and contributing to crisis management. The third paper examines unconventional monetary policy with quantitative and credit easing and forward guidance which may increase volatility in global markets although they support global rebalancing by encouraging the revaluation of emerging market currencies. The fourth paper examines

concerns with cross-border monetary policy spillovers and recommends the adoption of an expanded rules based system for central banks similar to the 1980s and 1990s which should operate within an international cooperative equilibrium.

BIS, 23.12.2013

OTC Derivatives

The BIS has published the latest statistics on OTC derivatives for the first half of 2013. This combines the results produced by the semi-annual survey of derivatives dealers in 13 countries and the Triennial Central Bank Survey of dealers in 34 countries. Total notional amounts totalled $693 trillion by end June 2013 up from $633 trillion. Gross market values decreased from $25 trillion to $20 trillion with gross credit exposures (allowing for legally enforceable bilateral netting but excluding collateral) was $3.9 trillion. The BIS notes that notional amounts had increased with the use of central counterparties (CCPs) as this involved the recording of two rather than a single contract. Interest rate contracts were the largest segment with $577 trillion in notional amounts.

BIS, 7.11.2013

Payment, Clearing and Settlement

The CPSS has released its annual report on *Statistics on payment, clearing and settlement systems in the CPSS countries* (September 2013). This includes data for 2012 and earlier years with individual country tables and comparative tables. Some provisional data is included to be finalised later.

BIS, 30.9.2013

Preliminary International Banking Statistics

The BIS has published its latest *Preliminary International Banking Statistics* for the period to end June 2013. This confirms a further decline in banks' cross-border claims on borrowers in advanced economies especially to non-bank parties. Claims fell $229 billion or 2% to $11.4 trillion. Cross-border interbank claims fell $244 billion or 1.4% to $16.9 trillion following a continuing fall since late 2011 and especially in Europe. Banks had increasingly relied on funding from non-banks with an increase of $259 billion which represented almost one third of total cross-border liabilities. This included $139 billion in the US and $73 billion in the UK. Results varied in emerging markets.

BIS, 21.10.2013

Property Price Statistics

The Bank for International Settlements (BIS) has published property price statistics from 50 countries with the approval of national data providers. The statistics are made available under Recommendation 19 of the Financial Stability Board (FSB) report to the G20 Finance Ministers and Central Bank Governors on 'The Financial Crisis and Information Gaps' (October 2009).

Country coverage of the data differs due to different property buying and selling procedures and without any international standards for property price statistics. Eurostat is preparing a draft *Handbook on Residential Property Price Indices* under an Inter-Secretariat Working Group on Price Statistics. A draft is available for comment.

BIS, 31.10.2013

Quarterly Review

The Bank for International Settlements (BIS) has published its latest *Quarterly Review* for December 2013. The BIS notes that a search for yield (SFY) had continued with financial markets rallying in advanced economies following the Federal Reserve decision to postpone tapering. The S&P 500 had risen to record highs with stock and bond markets and other economies strengthening. Corporate bonds spreads had tightened with risky US non-financial firms paying 7% per annum on average. Corporate spreads and default rates had remained low. Rating agencies assessed banks to be weaker than during the financial crisis with authorities attempting to remove too-big-to-fail subsidies. Banks had to continue to fully recognise losses in their portfolios and raise capital with the European Central Bank (ECB) to conduct an asset quality review and stress test. Bonds and stock market prices recovered after a fall in anticipation of the US Federal Reserve continuing with asset purchases and low policy rates. Cross-border claims on BIS reporting banks had declined in the second quarter 2013 having been stable in the first quarter with banks cutting their cross-border lending to all sectors. Trading in the foreign exchange market reached $5.3 trillion per day in April 2013 which represented a 35% increase from 2010. Non-dealer financial institutions represented the most active part of the market including smaller banks, institutional investors and hedge funds. Trading fell $300 billion per day to $5 trillion in October 2013. The review contains other articles on the anatomy of the global foreign exchange market which had risen to $5.3 trillion per day, foreign exchange trends, emerging economy foreign exchange, treatment of sovereign risk within the Basel capital framework, emerging markets and tapering, international bond issuance, currency trading, retail trading in the foreign exchange market and derivatives markets and OTC interest rate derivatives markets.

BIS, 8.12.2013

Regulatory Consistency Assessment Programme

The Basel Committee has produced revised procedures and processes for conducting country assessments under its 'Regulatory Consistency Assessment Programme' (RCAP) which was initially adopted in 2012. All member countries had agreed to undergo an RCAP assessment of their standards to implement the Basel III frameworks in accordance with the timeline set. This replaces the April 2012 RCAP paper. The objective is to promote the full and consistent adoption of Basel III covering Basel II, 2.5 and III (set out in Annexe 1). The programme also assesses the consistency and completeness of the adopted standards and significance of any deviations in the domestic

regulatory framework. This is carried out on a jurisdictional and thematic basis. The RSAP is consistent with the FSB's *Coordination Framework for Monitoring the Implementation of Agreed G20/FSB Financial Reforms* and the IMF/World Bank's *Financial Sector Assessment Programmes* (*FSAPs*) which also cover Basel *Core Principles* implementation. The paper sets out the objectives of the RCAP assessment framework, the four assessment phases (preparatory phase, off and on-site assessment phase, review, approval and publication phase and follow-up) and the assessment methodology (with a general approach, compliance scale and assessment grading).

BIS, 15.10.2013

Securitisation

The Basel Committee on Banking Supervision has published a second consultative document on revisions to its securitisation framework. The Committee had considered the comments received on its first consultation document in December 2012 with specific changes being adopted with regard to the hierarchy of approaches and calibration or capital requirement. The framework would include three approaches based on an internal ratings-based option, an external ratings-based option for specific securitisations and a standard approach for other banks. The Committee decided to replace its Modified Supervisory Formula Approach (MSFA) with the Internal Ratings-Based Approach which reflects the IRB charge on the underlying pool of exposures including expected losses. The calibration revisions had resulted in lower capital requirements being imposed although these were still higher than the previous regime. Other proposed revisions and clarifications are included with proposed rules text being set out in the annex. The Committee would carry out a second Quantitative Impact Study (QIS) with final measures being published subsequently.

BIS, 19.12.2013

Strengthening Bank Capital

Stefan Ingves, Chairman of the Basel Committee on Banking Supervision and Governor of the Sveriges Riksbank, has given an address on ″Strengthening bank capital – Basel III and beyond″ before the Ninth High Level Meeting for the Middle East & North Africa Region in Abu Dhabi, 18 November 2013. Ingves stated that strengthening bank capital did not simply involve requiring banks to hold additional capital but to ensure the effective functioning of the capital regime as a whole with the Committee focusing on the quantity, quality, consistency and reliability of bank capital ratios across the world. The quantity and quality of capital was increased especially with regard to going-concern loss-absorbing Common Equity Tier 1 (CET1) capital. Average CET1 of the 101 largest internationally active banks (the Group 1 banks) at end 2012 was 9.2% with overall shortfalls having fallen from €400 billion to €115 billion. The Committee was also working on implementation with the G20 Leaders requiring that Basel III be implemented in a ″full, timely and consistent″ manner. This required continuing monitoring, evaluation and analysis of outcomes in addition to imposing

new rules and regulations. The Committee established a Regulatory Consistency Assessment Programme (RCAP) in 2012 which included peer review assessments of domestic implementation effects. The consistency of the risk modelling outcomes of individual banks was also being studied to improve comparability of results. Two studies had been conducted using hypothetical portfolios which revealed substantial differences in supervisory and practice based factors. The Committee was working to establish a comprehensive view of relevant trading and banking book and operational risk. Further initiatives would be undertaken on supervisory action RCAP assessments, Pillar 3 disclosure enhancements, model constraints, possible flaws and benchmarks and confirming the role of the leverage ratio as a backstop within the regulatory framework.

BIS, 18.11.2013

Trading Book Review

The Basel Committee on Banking Supervision has issued a second consultative paper on *Fundamental review of the trading book: A revised market risk framework* (October 2013). This follows an earlier consultation paper in May 2012 which contained recommendations to improve trading book capital requirements. The latest document develops these and provides draft text. This includes a more clear and less permeable boundary between the trading book and the banking book. A revised risk measurement approach with a move from value-at-risk (VAR) to expected shortfall to include 'tail risk' with calibration based on a period of significant financial stress. Market illiquidity has been included with the use of 'liquidity horizons' in the market risk metric with an additional risk assessment tool for trading desks with exposure to complex illiquid products such as structured finance. A strengthened risk sensitive standardised approach is provided for less sophisticated banks. A revised internal models based approach has been prepared with a tighter model approval process and more consistent identification and capitalisation of material risk factors with hedging and diversification being based on empirical confirmation. The relationship between the standardised and models based approaches has been strengthened through closer calibration and with all banks being required to calculate on a standardised basis with mandatory public disclosure of the standardised charges on a desk-by-desk basis. The Committee is considering using the standardised approach as a floor or surcharge to the models based approaches in all cases subject to Quantitative Impact Study results. Securitisation and non-securitisation exposures have been further revised to create a closer alignment between the trading book and banking book treatment of credit risk.

BIS, 31.10.2013

The Basel Committee has published a second report on the *Regulatory Consistency Assessment Programme* (*RCAP*) – *Second Report on risk-weighted assets for market risk in the trading book* (December 2013). The Committee had conducted an initial study in January 2013 which was extended to include more representative and complex trading positions. Results had demonstrated significant variation in the outputs of market risk

internal models used to calculate regulatory capital with variability increasing with more complex trading positions. The results confirm the need for improved public disclosure and the collection of regulatory data to understand market risk risk-weighted assets, limiting the range of modelling choices for banks and harmonising supervisory practices on model approval. Most of the detail in the paper was set out in annexes 1–6. Seventeen banks in nine countries participated with the phase two findings confirming the earlier phase one results.

BIS, 17.12.2013

Financial Stability Board (FSB)

Asia Group

The FSB Regional Consultative Group for Asia (RCGA) held its fifth meeting in Tokyo in October 2013. The FSB policy priorities and work plan were reviewed with discussion focusing on shadow banking with in Asia and the FSB's high level policy framework for strengthened shadow banking oversight. A proportional approach would have to be adopted having regard to local national circumstances and regulations. Other matters covered included systemically important financial institutions (SIFIs) over-the-counter derivatives implementation, credit rating reliance and governance and oversight of financial benchmarks. Reference was made to regional vulnerabilities and financial stability concerns including the potential impact on quantitative easing reduction.

FSB, 30.10.2013

FSB and IMF

The FSB and IMF have published their *Fourth Progress Report on the Implementation of the G-20 Data Gaps Initiative* (September 2013). The G20 ministers and governors supported the progress made at their July 2013 Moscow meeting on closing information gaps under the FSB and IMF G20 Data Gaps Initiative (DGI) and the work achieved since November 2012. Substantial progress had been made dealing with all of the 20 DGI recommendations with significant data enhancements coming on-stream. G20 economies demonstrated strong support and ownership for the DGI. The momentum had nevertheless to be maintained and adequate resources provided for the necessary statistical work. Strengthened collaboration between national agencies and continued international cooperation, collaboration and consultation was essential. The paper examines implementation status, including the development and enhancement of the conceptual and statistical frameworks, implementation issues, links to policy work and other initiatives and strategy and priorities going forward. Ongoing work would concentrate on implementation and communication. A fifth progress report would be produced in 2014 and a sixth report in 2015.

FSB, 14.10.2013

Global Shadow Banking Monitoring

The FSB has published a third annual *Global Shadow Banking Monitoring Report* (November 2013). This provides data from 25 countries and the euro area as a whole representing 80% of global GDP and 90% of global financial system assets. The assets of non-bank financial intermediaries (excluding insurance companies, pension funds and public financial institutions) increased by $5 trillion to $71 trillion between 2012 and 2013. This represents around 24% of total financial assets and 50% of banking system assets and 177% of GDP. Non-bank financial intermediation increased by 8.1% with higher relative volumes in advanced rather than emerging economies. The share of non-bank financial intermediary assets had increased from 35% to 37% in the US and fallen from 33% to 31% in the EU. An initial macro-mapping step 1 process was adopted with a risk-focussed step 2 which examined exposures in terms of non-bank financial intermediation, non-bank credit intermediation and then non-bank credit intermediation with bank-like systemic risks (including maturity transformation, liquidity transformation, imperfect risk transfer and leverage). Specific activities included money market funds, broker dealers, structured finance vehicles, financial companies and hedge funds. The FSB had issued a number of policy recommendations in connection with strengthening oversight and control of the shadow banking system in August 2013.

FSB, 14.11.2013

Global Adherence

The FSB has published a statement on "Annual update on global adherence to regulatory and supervisory standards on international cooperation and information exchange" (December 2013). This includes updated information on the countries assessed to date to encourage the adherence to the FSB standards on international cooperation and information exchange. The review work began in March 2010 following the G20 April 2009 London Summit with the FSB being asked to develop a toolbox of measures to promote adherence with similar being undertaken by the Global Forum on Transparency and Exchange of Information for Tax Purposes and the Financial Action Task Force on anti-money laundering and terrorist financing. Forty five of the jurisdictions examined by the FSB had demonstrated sufficiently strong adherence with 14 others taking actions recommended by the FSB. Only a small number of jurisdictions, including Libya (subsequently suspended) and Venezuela, had decided not to engage with the FSB in the process and have therefore been identified as non-cooperative.

FSB, 18.12.2013

Haircut Consultation

The FSB has published comments on its August 2013 report on *Policy Framework for Addressing Shadow Banking Risks in Securities Lending and Repos*. This included proposals on the establishment of minimum standards for methodologies to calculate haircuts on non-centrally cleared securities financing transactions with a framework of numerical haircut floors set out

in Annex 2 to the report. The FSB has set up a Workstream on Securities Lending and Repos (WS5) to assess financial stability risks and develop recommendations. Thirteen policy recommendations were included within the FSB's earlier November 2012 report on *Shadow Banking Risks in Securities Lending and Repos*. The FSB work on shadow banking examined five specific areas of systemic risk including banking system spill-over effects, money market funds (MMFs) runs, securitisation, securities financing and repos and other shadow banking entities and activities.

FSB, 20.12.2013

Middle East and North Africa

The Regional Consultative Group for the Middle East and North Africa (RCG-MENA) held its fourth meeting in Istanbul in September 2013. The work of the FSB was reviewed on financial regulatory reform, vulnerabilities and regional financial stability issues. Subjects considered included the D-SIB and Global-SIFI frameworks intended to end too-big-to-fail and implementation challenges in home and host countries in adopting them. Other issues referred to included OTC derivatives, compensation and local institutional reforms and insurance market revision work experience.

FSB, 26.9.2013

Moscow Meeting

The FSB met in Moscow on 8 November 2013. The meeting discussed vulnerabilities in the financial system and progress achieved in reforming and strengthening the resilience of the global financial system since the financial crisis. Specific areas of continuing policy work were discussed including building resilient financial institutions, ending too-big-to-fail, shadow banking and derivatives markets. Accounting and auditing initiatives were referred to and the work of the Regional Consultative Groups discussed with the FSB's review of its governance and representation functions.

FSB, 8.11.2013

Regional Consultative Group

The Regional Consultative Group (RCG) for the Commonwealth of Independent States (CIS) of the Financial Stability Board (FSB) held its third meeting in Moscow in October 2013. The meeting noted the outcomes of the Russian G20 presidency and the FSB's agenda including on correcting 'Too-big-to-fail'. The meeting reviewed the separate work on the Global Legal Entity Identifier System (GLEIS) and framework for domestic systemically important banks (D-SIBs) with members to review their own regulatory for D-SIBs. Regional financial stability issues were examined with specific reference to a report prepared by Russian experts for the RCG.

FSB, 30.10.2013

Regional Consultative Group for the Americas

The fifth meeting of the FSB Regional Consultative Group (RCG) for the Americas met in Rio de Janeiro, Brazil on 2 December 2013. Vulnerabilities in the global financial system and regional financial stability issues were referred to including the effects of changes in accommodative monetary policies. Continuing FSB initiatives were reviewed with discussions focusing on too-big-to-fail, high-level policy recommendations on strengthening the oversight and regulation of shadow banking and recent developments on cross-border cooperation in implementing OTC derivatives reforms.

FSB, 2.12.2013

Risk Culture Questions

The Financial Stability Board has published a set of questions in support of its November 2013 guidance on *Supervisory Interaction with Financial Institutions on Risk Culture*. The original Guidance had been published in November 2013 (below). Two sets of six questions have been issued on general questions and indicators of a sound risk culture. These includes gaps, areas requiring further elaboration or clarity, definitions, tools, expected supervisory response and engagement. Indicator questions were concerned with sufficiency, examples, senior management examination, roles, tools or processes and possible descriptors.

FSB, 23.12.2013

Risk Management Practices

The FSB has published two papers on strengthening risk management practices within financial institutions as part of its work to deal with systemically important financial institutions (SIFIs). The FSB, *Principles for an Effective Risk Appetite Framework* (November 2013) were updated following an initial consultation in July 2013 and an earlier peer review of risk governance in February 2013. The document contains a number of key definitions on risk appetite, capacity, limits and profile. Specific principles are established with regard to risk appetite framework (RAF), risk appetite statement, risk limits and roles and responsibilities including with regard to board of directors, chief executive officer, chief risk officer, chief financial officer, business line leaders and legal entity-level management and internal audit. Another document consisted of a consultation paper on FSB, *Guidance on Supervisory Interaction with Financial Institutions on Risk Culture* (November 2013). This sets out the foundational elements to promote some risk cultures within financial institutions (including risk governance, risk appetite and compensation), assist supervisors identify core practices and attitudes within risk culture and provides general supervisory guidance on tone (including leading by example, assessing espoused values, ensuring common understanding and awareness of risk and learning from risk culture failures), accountability (ownership of risk, escalation process, and enforcement), effective challenge (open to dissent and stature of risk management) and incentives (remuneration and performance and talent development and succession planning). This forms part of the FSB's attempt to strengthen

supervision more generally including through the establishment of strong and unambiguous mandates, independence to act, sufficient quality and quantity of resources and ensuring that supervisors have a full suite of powers to carry out their functions.

FSB, 18.11.2013

Securities Financing Transactions

The FSB has announced the second stage of its Quantitative Impact Study (QIS2) on the proposed regulatory framework for Securities Financing Transactions following its report and policy recommendations in August 2013. QIS1 consisted of a data request to 17 financial intermediaries including banks and broker-dealers in 12 countries covering historical haircut distributions on a pre-crisis, post-crisis and current basis to assist calibrate minimum haircut proposals. QIS2 would consist of a more comprehensive quantitative assessment of the impact of the haircut proposals on minimum standards for firm calculations and numerical floors for certain transactions.

FSB, 5.11.2013

Sub-Saharan Africa

The RCG for Sub-Saharan Africa held its fourth meeting in Port Louis, Mauritius. The meeting considered Basel III, too-big-to-fail, increased supervisory effectiveness, enhanced cross-border cooperation, shadow banking and derivatives markets. Reference was made to global financial system vulnerabilities and regional financial stability concerns including continued weak growth prospects in advanced economies and decline in investment in the region. The meeting also examined shadow banking, credit ratings and risk management including risk governance, appetite and culture. A workshop would be held on effective resolution regimes for financial institutions.

FSB, 22.10.2013

International Organisation of Securities Commissions (IOSCO)

Affiliate Members

The affiliate members group within IOSCO has been renamed the Affiliate Members Consultative Committee (AMCC) which met in December to discuss its enhanced role and function. The AMCC agreed to work with IOSCO through its General Secretariat on securities markets issues and with IOSCO's wider membership. The internal changes were agreed by IOSCO in September 2013 with the AMCC replacing the earlier Self-Regulatory Organisations Consultative Committee (SROCC) made up of securities exchanges, financial market infrastructures, investor protection funds and other organisations. AMCC would focus on investment data management, emerging risks and cyber threats in line with IOSCO's wider research and policy work. José Carlos Doherty, CEO of the Brazilian Financial and Capital Market Association (ANBIMA) was appointed Chairman.

IOSCO, 16.12.2013

Central Counterparty Disclosure

The Committee on Payment and Settlement Systems has issued a report with IOSCO on *Publish quantitative disclosure standards for central counterparties* (October 2013). The purpose is to provide guidance on the disclosure by CCPs of relevant information to allow proper assessment of the risks undertaken. This follows the earlier *Disclosure Framework* published by the CPSS and IOSCO in December 2012. Stakeholders should be able to compare CCP risk controls, including financial condition and resources to withstand potential losses, acquire a clear, accurate and full understanding of the risks involved, assess relevant systemic concerns and determine participation risks. A separate cover note was provided seeking comment on additional consultation issues.

IOSCO, 15.10.2013

CRA Supervisory Colleges

Supervisory Colleges have been established for Standard & Poor's, Moody's and Fitch which held their inaugural meetings on 5–6 November 2013 in New York. IOSCO had recommended the establishment of the colleges in its final report on *Supervisory Colleges for Credit Rating Agencies* (July 2013) FR08/13. Colleges will allow for the exchange of information concerning CRA compliance with relevant regulations and implementation and adherence to the IOSCO Code of Conduct for CRAs. They will also facilitate the establishment of rating models and methodologies, internal controls, conflict of interest management and procedures to handle material non-public information which will overall assist better understand the exposures created by internationally active CRAs. The S&P and Moody's colleges are chaired by the US Securities and Exchange Commission (SEC) with the Fitch College chaired by the European Securities and Markets Authority (ESMA).

IOSCO, 27.11.2013

Cybercrime

IOSCO has reported to the FSB on a number of continuing initiatives including cybercrime in securities markets, long-term investment, crowd funding and cross-border regulation. IOSCO held a round table to examine cybercrime and its threat to the stability of the global financial system. This attempted identify the key sources of cybercrime threats, impacts and possible responses. IOSCO had published data survey results and a staff working paper with the World Federation of Exchanges (WFE) on *Cybercrime, Securities Markets and Systemic Risk* (July 2013). Work continued on improving resilience, coordination, information exchange and cooperation, deterring criminals, monitoring exposures, examining systemic risk threats, information provision and incorporating cyber risk issues into financial policy work. IOSCO supported initiatives to ensure that capital markets carried out an important role in supporting long term investment in growth and emerging and developed economies following the work of the G30

Working Group on Long-Term Finance and G20 Study Group on Financing for Investments Workplan. IOSCO was developing guidance to support Peer-to-peer lending and equity crowd funding as an alternative source to bank lending. This would examine retail investor protection issues, risk disclosure, platform and intermediary failure issues, cross-border implications and identification and limitation of systemic risk within the crowd funding environment. IOSCO had set up a Task Force to develop a toolbox of measures on the regulation of foreign firms on a cross-border basis. A questionnaire would be sent out to IOSCO members with a consultation paper being produced in 2014.

IOSCO, 18.11.2013

EMIR

EU Commissioner, Michel Barnier has responded to IOSCO's letter of 22 November 2013 on the interpretation of EU Regulation 648/2012 on OTC derivatives, central counterparties and trade repositories (EMIR). The European Securities and Markets Authority (ESMA) had received comparative technical advice on the legal and supervisory arrangements of central counterparties (CPPs) in Australia, Hong Kong, India, Japan, Singapore and South Korea with the Commission comparing the arrangements with those provided for under EMIR. The Commission will consult with relevant authorities on any differences. The Commission will also set an appropriate timeframe for assessing CCP exposures for capital adequacy purposes under the Capital Requirements Regulation (575/2013 (CRR).

IOSCO, 20.12.2013

Financial Benchmarks Principles

IOSCO released a public communiqué in October 2013 on 'Implementation of the Principles for Financial Benchmarks' which encouraged administrators to take all necessary action to comply with IOSCO's *Principles for Financial Benchmarks* before July 2014.

IOSCO, 30.10.2013

FMI Recovery

IOSCO has published the responses to its consultation paper published with the Committee on Payment and Settlement Systems (CPSS) on *Recovery of Financial Market Infrastructures* (August 2013). This provided guidance to assist FMIs develop recovery plans in response to threats to viability and financial strength that could otherwise prevent them from providing critical services on a continuing basis to participants and markets. Issues covered included recovery plans and planning, recovery tools, appropriateness assessments, impact, incentives, participant default and liquidity shortfalls and other losses. This supplements the earlier CPSS IOSCO *Principles for Financial Market Infrastructures* (April 2012).

IOSCO, 8.11.2013

Hedge Fund Survey

IOSCO has released a review of regulatory action to understand the hedge fund industry with its *Report on the Second IOSCO Hedge Fund Survey* (October 2013). The purpose is to collect information from hedge fund managers and advisers on markets, trading activities, leverage, funding and counterparty information as part of the wider G20 initiative to reduce risk in hedge fund trading. This provides valuable information in an area with traditionally limited data although some limitations are accepted. Most funds were based in the US or the UK with information being collected from 1,044 qualifying funds. Funds under management represent $1.9 trillion in total net assets with funds generally being based in off-shore financial centres and, in particular, the Cayman Islands. The most commonly used strategy was equity oriented followed by macro-oriented and multi-strategy funds. Detailed information is provided on the use of leverage and market exposure and on liquidity risk. The survey should be of value in assisting authorities promote international cooperation monitoring systemic risk within the hedge fund sector as well as provide additional insight and provide a forum for discussion.

IOSCO, 21.10.2013

Islamic Capital Market Products

The International Organisation of Securities Commissions (IOSCO) has issued a joint publication with the Islamic Financial Services Board (IFSB) and Securities Commission Malaysia (SC) on 'Disclosure Requirements for Islamic Capital Market Products' (September 2013) which was initially produced at the IOSCO 38th Annual Conference in Luxembourg on 15–19 September 2013. This follows a joint Round Table on Disclosure Requirements for Islamic Capital Market (ICM) products in Kuala Lumpur in September 2012. The document examines the need to develop necessary international regulatory standards and best practices on ICM disclosure with relevant issues, risks and challenges reviewed, in particular, with regard to *Sukuk* and Islamic Collective Investment Schemes (ICISs). The work represents a significant step in the development and enhancement of international regulatory standards and best practices in this area. IOSCO have published earlier papers on *Islamic Capital Market Fact Finding Report* (2004) and *Analysis of the Application of IOSCO's Objectives and Principles of Securities Regulation for Islamic Securities Products* (2008).

IOSCO, 31.10.2013

Market Structure Changes

IOSCO has published a final report on *Regulatory Issues Raised by Changes in Market Structure* (December 2013). The report identifies issues and risks created by existing or developing market structures and considers how these may be dealt with. Four specific sets of recommendations are made with regard to promoting market liquidity and efficiency, price transparency and investors' execution quality with regulators also monitoring the impact of market fragmentation on market quality. This follows a G20 request to

develop recommendations on the promotion of market integrity and efficiency to mitigate the risks created by continuing technological developments. This follows IOSCO's earlier reports on *Regulatory Issues Raised by the Impact of Technological Changes on Market Integrity and Efficiency* (2011) and *Technological Challenges to Effective Market Surveillance Issues and Regulatory Tools* (2013). This also updates IOSCO's report on *Transparency and Market Fragmentation* (2001). The report follows a number of fact finding exercises on trading spaces, regulatory and rules review, liquidity provision in different trading spaces in equities and Exchange Trade Funds (ETFs) and industry dialogue. Authorities should specific monitor the impact of fragmentation on market integrity and efficiency, the availability and timeliness of information, order handling rules and best execution and liquidity access.

IOSCO, 13.12.2013

Price Reporting Agencies

IOSCO has published a final report on *Principles for Oil Price Reporting Agencies* (*PRAs*) (December 2013) which sets out principles to support the reliability of oil price assessments referenced in derivatives contracts within IOSCO member jurisdictions. The principles were prepared following the G20 Leaders' request in November 2011. The PRA Principles are to be implemented by October 2013 with IOSCO to review implementation. IOSCO will review the need for further amendment and revision in light of its *Principles for Financial Benchmarks* (July 2013).

IOSCO, 18.12.2013

Retail Structured Products

IOSCO has published a final report on *Regulation of Retail Structured Products* (December 2013). This outlines the regulatory options that authorities may consider in regulating the sale of retail structured products. The purpose of the toolkit is to enhance investor protection following the increased popularity of complex financial tools to retail investors which specifically combine derivatives with other financial instruments. Concerns arose specifically following the global financial crisis with investors' ability to understand products, design, disclosure, suitability, mis-selling and post-sale product controls. The toolkit contains 15 regulatory tools within 5 sections covering regulatory approach to retail structured products, regulation of product design and issuance, product disclosure and marketing, distribution and post-sales practices. IOSCO began to consider retail structured products in February 2012 with a survey and follow-up roundtable and working group appointment.

IOSCO, 20.12.2013

Risk Identification Implementation

IOSCO produced its final report on *Thematic Review on the Implementation of Principles 6 and 7 of the IOSCO Objectives and Principles of Securities*

Regulation (September 2013). Principles 6 and 7 require authorities to monitor, mitigate and manage systemic risk and review the regulatory perimeter regularly. This is the first review produced by IOSCO's Assessment Committee which was set up in 2012 to promote full, effective and consistent implementation of IOSCO Principles and Standards. The 31 jurisdictions reviewed had made good progress in developing relevant processes and procedures with further work being required to establish necessary processes to manage and mitigate systemic risk. Regulatory perimeter processes had often been informal rather than formal. Ten recommendations were made to improve regulatory practice including with regard to structure, regulatory process, intra-jurisdictional and cross-border cooperation and coordination and culture and resourcing.

IOSCO, 30.9.2013

Securities Markets Risk Outlook

IOSCO has published its first *Securities Markets Risk Outlook for 2013–2014* (October 2013) which examines significant trends, vulnerabilities and risks within securities markets from a systemic perspective. This follows research work undertaken by the IOSCO Research Department and the Committee on Emerging Risks (CER) including staff from 30 authorities from national jurisdictions. The four main exposures identified were concerned with risks related to the low interest rate environment, collateral management, derivatives markets and capital flows to and from emerging markets. Low interest rates had created significant spill-over effects with potential risks for securities markets including through increased leverage with a search for yield including in CDOs and leveraged real estate investment funds. The availability of high-quality collateral had been substantially reduced which could affect pricing following increased regulatory demand for collateral especially within bank holding companies with OTC dealer operations and central banks accepting collateral from commercial banks. Significant challenges arose in transferring risk from bilateral OTC contracts to the new central counterparties (CCPs) being set up to manage OTC derivatives risks. An earlier significant inflow of capital into emerging market economies had been followed by a sharp outflow with the announcement of US tapering of expansionary monetary policy with emerging securities markets having to be strengthened further.

IOSCO, 15.10.2013

Securities Statistics Web Portal

The Research Department of the International Organisation of Securities Commissions (IOSCO) has established a statistics web portal which provides a global overview of securities market activity. This will allow for the centralised monitoring of global trends, risks and vulnerabilities, allow market recovery to be compared and provide detailed information on specific markets including corporate debt, covered bonds, securitised products,

Islamic finance, equity IPO volumes, equity market valuations, syndicated lending and housing price indices. The portal will be updated on a monthly basis.

IOSCO, 28.11.2013

Trading Fee Models

IOSCO has published a final report on *Trading Fee Models and their Impact on Trading Behaviour* (December 2013). This overviews global trading fees and global trading fee models and their influence on trading behaviour. Authorities have encouraged competition between trading venues which has been further strengthened through technological advances which have specifically reduced the cost of establishment and liquidity provision. Trading has become fragmented across multiple venues dealing in the same instruments and competing within and between jurisdictions with many securities being cross-listed. This has provided greater investor choice with venues competing in terms of trading systems and technology, market models and trading fees and trading fee structures. The report follows an earlier questionnaire exercise with 22 jurisdictions and 70 trading venues responding. The key findings are set out with regard to market context, description of trading fee models and trading fees and incentives and effects. No specific conclusions have been drawn at this time on the impact or effect of trading fees and models on trading behaviour although the area will be monitored over time.

IOSCO, 13.12.2013

International Association of Insurance Supervisors (IAIS)

Annual Conference

The IAIS held its 20th Annual Conference in Taipei with over 600 members, observers and interested parties attending. The theme of the conference was ‘Building Sustainable Insurance Supervision in a Changing World’ with panels examining issues including insurance and financial stability, population aging, frontline supervision and supervisory education, increased access to insurance, the ComFrame and group wide supervision, global climate change impact and consumer protection frameworks and guarantee funds. IAIS published the results of its Expert Review Teams Self-Assessment and Peer Review of its ICPs 1, 2 and 23 immediately before the conference. Application papers, which provide practical examples of case studies of insurance supervisory issues, were also released on *Combating Money Laundering and Terrorist Financing* was also released on 17 October 2013. The 21st conference would be held in Amsterdam in October 2014.

IAIS, 18.10.2013

Coordinated Implementation Framework

The International Association of Insurance Supervisors (IAIS) has produced the 2013 draft of its Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) intended to ensure the effect

group-wide supervision of internationally active insurance groups (IAIGs). This develops the requirements and guidance set out in the IAIS *Insurance Core Principles* (*ICPs*) which are applied on a legal and group-wide basis. A global insurance capital standard will be incorporated within ComFrame. The initiative was necessary in light of the increased importance of IAIGs in global insurance markets and the need for an internationally coherent framework for the supervision of large global groups. IAIS has also adopted a Coordinated Implementation Framework (CIF) to strengthen its implementation commitment and delivery of existing strategic objectives especially through regional engagement, partner relations, resource focus and better alignment and coordination of implementation activities.

IAIS, 18.10.2013

International Swap Derivatives Association (ISDA)

The International Swaps and Derivatives Association (ISDA) has launched a legal challenge with other financial authorities against the Commodity Futures Trading Commission's (CFTC) Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations (the Cross-Border Rule) published in July 2013. The legal action was taken by ISDA and the Securities Industry and Financial Markets Association (SIFMA) and the Institute of International Bankers (IIB). The agencies support efforts to improve transparency and limit systemic risk although they are concerned with the continuing efforts by the CFTC to control global swaps markets through unpredictable "guidance" documents, advisories and directives and to avoid rulemaking requirements. The Cross-Border Rule could require the double execution and reporting of transactions and significant increased administrative, legal and financial costs with non-US counterparties becoming increasingly reluctant to transact with US based dealers and other firms. It is argued that the rule violates existing agreements between global policymakers and is contrary to G20 Commitments to implement global standards consistently and ensure a level playing field at the same time as avoid market fragmentation. ISDA was one of the commissioning agencies for a review conducted by PWC on *Financial transaction tax: The impacts and arguments. A literature review* (21 November 2013) which outlines the EU proposal for a financial transaction tax (FTT) and the key arguments for and against the proposal. ISDA has responded to the Treasury's consultation on widening the Special Resolution Regime (SRR) established under the Banking Act 2009 to include investment firms and banking group companies as well as central counterparties (CCPs). ISDA supports restricting the extension to investment firms with initial capital of €730,000 or more (EUR 730k investment firms) under the EU CRD 2006/49/EC with the Treasury producing a separate Code of Practice for CCPs in light of the significant differences between CCPs and banks and investment firms.

Additionally the International Swaps and Derivatives Association (ISDA) has commented on the FSB *Assessment Methodology for the Key Attributes of Effective Resolution Regimes* following the original Key Attributes for Effective Resolution Regimes in October 2011. ISDA fully supports the Key

Attributes and the proposed methodology with specific references being made to question 3 governing set-off, netting, collateralisation and asset segregation, temporary stays of early termination rights, extensions and conditions and safeguards. ISDA and the Securities Industry and Financial Markets Association (SIFMA) have welcomed the decision by the US Commodity Futures Trading Commission (CFTC) to dismiss its appeal against their challenge to its 2011 Position Limits Rule which were considered to adversely affect liquidity and increase price volatility in the commodities and wider derivatives markets. ISDA has launched with the British Bankers Association (BBA), the Investment Management Association (IMA) and Markit a new EMIR (European Market Infrastructure Regulation) Counterparty Classification Tool on the ISDA and Markit online ISDA Amend service. This will allow businesses to classify themselves under the EMIR taxonomy following completion of a series of questions. The Joint Associations Committee (JAC comprising ISDA, the International Capital Market Association (ICMA) and the Association for Financial Markets in Europe (AFME)) have commented on the Joint Forum consultation document on *Point of Sale disclosure in the insurance, banking and securities sector* (April 2013). ISDA has hosted a statement from Commodityfact.org on 'The essential role of banks for physical commodities' which supports an IHS report on 'The role of banks in physical commodities' which confirms the position that the development of commodity derivatives markets does not cause higher prices itself and assists mitigate shocks that would otherwise arise (including climate shocks and supply chain disruption such as from civil wars) with market participants suffering without bank participation. ISDA has issued a number of comments with other financial agencies on the FSB consultation document on *Application of the Key Attribute of Effective Resolution Regimes to Non-Bank Financial Institutions*. A final response has also been produced on the CPSS IOSCO paper on *Recovery of financial market infrastructures* with the Institute of International Financial (IIF) and The Clearing House (TCH). A 2013 Account Control Agreement (ISDA ACA) has been produced to assist negotiations involving arrangements with the segregation of Independent Amounts (IA) held with a third party custodian. ISDA has produced a series of 'frequently asked questions' (FAQ) on a potential Credit Default Swap (CDS) Credit Event on US sovereign debt which notes the relevant elections that parties can make with a three day grace period although it notes that a ratings downgrade by itself does not trigger a default. The Depository Trust & Clearing Corporation's CDS data warehouse noted that around $3.6 billion of CDS credit protection had been sold on US sovereign debt although any payments would be reduced by the recovery value received on the underlying US obligations covered. ISDA and JAC have commented on the UK HM Treasury and Department for Business Innovation and Skills (BIS) on *Banking Reform: draft secondary legislation* (July 2013) which include allowing ring-fenced banks to be allowed to sell simple derivatives products subject to safeguards. A research note was produced by ISDA on *CDS Market Summary: Market Risk Transaction Activity* (October 2013). While total notional CDS outstandings had decreased, trading activity had increased by 15% between 2012 and 2013

having followed lightly in 2011 and 2012. The reduction in notional size was explained in terms of portfolio compression (or trade 'tear-ups') which was used to reduce transaction numbers and size. CDS notionals outstanding in 2007 were 58.2 trillion falling to 41.9 trillion in 2008, 32.7 trillion in 2009, 29.9 trillion in 2010, 28.6 trillion in 2011 and 25.1 trillion in 2012. Compression had nevertheless removed $85.7 trillion in CDS notional by end 2012 with market activity increasing to $17.3 in 2013.

ISDA, 10.2013

EUROPEAN DEVELOPMENTS

Mortgage Credit Directive

On 10 December 2013 the European Parliament adopted the Mortgage Credit Directive, which now needs to be considered and adopted by the Council.

This directive aims to ensure that all consumers who purchase a property or take out a loan secured against their home are adequately informed and protected against the risks arising from such transactions. It also seeks to improve the level of cross-border activity in this market in order to benefit consumers.

The text adopted can be read at: http://goo.gl/amSk11

The Commission has also updated its FAQ on the proposed directive: http://europa.eu/rapid/press-release_MEMO-13-1127_en.htm

Payment accounts directive

Negotiation have continued on the proposed directive on the transparency and comparability of payment account fees, payment account switching and access to a basic payment account has continued. This directive includes provisions ensuring that anyone legally residing in the EU should have the right to open a basic payment account, and this right should not be denied on grounds of nationality or place of residence. It also provides for the fees and rules for these accounts to be transparent and comparable, and that it should be easy to switch to another basic account offering better terms.

In December 2013 the Council published the current text of its proposed compromise, which can be viewed at: http://goo.gl/UXA6dn

On 19 November 2013 the ECB published an opinion on the Commission's draft directive, which strongly supports the proposals:
http://www.ecb.europa.eu/ecb/legal/pdf/en_opinion_con_2013_77__directive_on_payment_accounts.pdf

Single Resolution Mechanism

Negotiations are continuing as to the legislative texts to introduce a Single Resolution Mechanism. This is regarded as a necessary complement to the Single Supervisory Mechanism.

On 19 December 2013 the Council published its general approach on the proposed Single Resolution Mechanism Regulation, which will now form the basis for negotiation with the European Parliament. This consists of a draft regulation (which would enter into force on 1 January 2015 with the key provisions becoming active on 1 January 2016) and a decision by Euro-area member states committing them to negotiate, by 1 March 2014, an intergovernmental agreement on the functioning of the single resolution fund. This Council further proposes that this agreement would include arrangements for the transfer of national contributions to the fund and their progressive mutualisation over a 10-year transitional phase. It would also endorse the bail-in rules established in the bank recovery and resolution directive as applicable to the use of the single fund.

The draft regulation agreed by the Council provides for a single resolution board with broad powers in cases of bank resolution. Upon notification by the European Central Bank that a bank is failing or likely to fail, or on its own initiative, the board would adopt a resolution scheme placing the bank into resolution. It would determine the application of resolution tools and the use of the single resolution fund. Decisions by the board would enter into force within 24 hours of their adoption, unless the Council, acting by simple majority on a proposal by the Commission, objected or called for changes.

More information can be found on the Commission's banking union website: http://ec.europa.eu/internal_market/finances/banking-union/

On 6 November the ECB also published an opinion on the Commission's draft regulation, which can be viewed at:
http://www.ecb.europa.eu/ecb/legal/pdf/en_con_2013_76_f_sign.pdf

Single Supervisory Mechanism

On 15 October 2013 the Council adopted regulation 1024/2013 conferring specific tasks on the European Central Bank concerning policies in relation to the prudential supervision of credit institutions ('the SSM Regulation'), which entered into force on 3 November 2013.

The SSM Regulation provides for a single prudential supervisory regime across the Eurozone, overseen by the ECB. The ECB will assume its full supervisory role on 4 November 2014, from which time it will have exclusive competence to carry out all key aspects of the prudential supervision of credit institutions in the Eurozone.

More information can be found on the new Banking Supervision section of the ECB's website: http://www.ecb.europa.eu/ssm/html/index.en.html and the Commission's banking union website: http://ec.europa.eu/internal_market/finances/banking-union/.

The SSM Regulation operates in parallel to the development by the EBA of the single rulebook to apply across the EU. In order to facilitate coordination between the ECB as prudential supervisor and the EBA's role in producing the rulebook, the SSM Regulation was accompanied by Regulation 1022/2013. This amends the regulation that established the EBA,

refining its obligations and powers to better tie into the ECB's duties. The EBA has continued to publish Regulatory Technical Standards as part of the Single Rulebook project.

ISLAMIC FINANCE DEVELOPMENTS

Exposure Drafts on Islamic Financial Contracts (Sharia Requirements and Optional Practices)

As part of the objective to strengthen the Sharia-compliance culture among Islamic financial institutions (IFIs), Bank Negara Malaysia (the Bank) is issuing a series of policy documents on Sharia contracts to enhance the end-to-end compliance with Sharia.

These Exposure Drafts (EDs) outline the Sharia requirements and optional practices relating to *wadi'ah, hibah, kafalah, wakalah, wa'd, tawarruq and bai' 'inah* respectively to facilitate IFIs in developing Islamic financial services and products.

The Bank invites written comments from the public on these EDs, including suggestions for particular issues or areas to be further clarified/elaborated further and any alternative proposal that the Bank should consider.

Written comments in the form of softcopy are preferable and may be submitted to shariahstandard@bnm.gov.my by 10 January 2014.

Bank Negara Malaysia 03.01.14

http://www.bnm.gov.my/index.php?ch=en_announcement&pg=en_announcement_all&ac=269&lang=en

Leading International Rating Agencies Reaffirm the Islamic Development Bank Group's 'AAA' Rating

The three leading international rating agencies, Standard & Poor's, Moody's and Fitch Ratings, have all reaffirmed their credit rating of the Islamic Development Bank (IDB) for 2012 with a stable outlook. The ratings reaffirmed by these agencies are as follows: Standard & Poor's: AAA, A-1+Stable; Fitch Ratings: AAA, F-1+Stable; Moody's: Aaa, P-1 Stable. The IDB is currently the highest-rated institution in the Muslim world and among regional and international multilateral development banks. The ratings are underpinned by the Bank's strong financial profile, the relevance of its policies, continued shareholder support for successive capital increases and prudential financial and risk management policies.

The IDB is a multilateral development bank that was established with the purpose of fostering the economic development and social progress of its member countries and Muslim communities in non-member countries in accordance with the principles of Islamic financing. The IDB will celebrate its 40th anniversary on the occasion of the next Annual Meeting of its Board of Governors, to be held in Jeddah, Saudi Arabia during 25–26 June 2014, and will continue its reform exercise in order to achieve the objectives of its 2020 Vision.

The Islamic Development Bank 29.12.13

http://www.isdb.org/irj/portal/anonymous/idb_news_en

The Islamic Financial Services Board Council Adopts Two New Standards for the Islamic Financial Services Industry

The Council of the Islamic Financial Services Board (IFSB) has resolved to approve the adoption of two new Standards in its 23rd Meeting in Doha, Qatar, yesterday. The two documents are:

1. IFSB-14: Standard on Risk Management for *Takāful* (Islamic Insurance) Undertakings; and
2. IFSB-15: Standard on Revised Capital Adequacy for Institutions offering Islamic Financial Services (other than *Takāful* Institutions and Islamic Collective Investment Schemes).

[Both documents were summarised in December 2012 and January 2013 Bulletins].

The 23rd Meeting of the IFSB Council was hosted and chaired by H.E. Sheikh Abdulla Saoud Al-Thani, Governor, Qatar Central Bank and attended by the President of the Islamic Development Bank, 17 governors and governors' representatives from among the members of the Council and four Full members representatives of the IFSB.

IFSB-14: Standard on Risk Management for *Takāful* (Islamic Insurance) Undertakings

IFSB-14 aims to provide guidance to the industry in understanding the types of risks that the *Takāful* industry is exposed to. The current global market conditions necessitate the relevant regulatory and supervisory authorities to continue strengthening the industry. With the best practices set forth by this Standard, it provides a *Sharī'ah*-compliant mechanism in the development of a risk management framework for *Takāful* undertakings.

Taking into consideration the specificities of Islamic finance, IFSB-14 highlights the key risks which are specific to *Takāful* undertakings, i.e. *Sharia* non-compliance risk, risks arising from segregation of funds, and risks relating to the use of *Re-Takāful*. The document further illustrates the responsibilities and functions of key management functions in ascertaining the effectiveness of the risk management framework. It is hoped that the Standard will provide a guideline to all the industry stakeholders in creating a safe and prudent environment for the growth, sustainability and development of the *Takāful* industry.

IFSB-15: Standard on Revised Capital Adequacy for Institutions offering Islamic Financial Services (other than *Takāful* Institutions and Islamic Collective Investment Schemes) (IIFS)

IFSB-15 is a revised and enhanced version of two previous IFSB standards on capital adequacy, namely IFSB-2: Capital Adequacy Standard for IIFS

(published in 2005) and IFSB-7: Capital Adequacy Requirements for *Sukūk*, Securitisations and Real Estate Investments (published in 2009). IFSB-15 also adopts key Basel III proposals on capital components and macroprudential tools for the IIFS.

This Standard aims to assist the implementation of a capital adequacy framework that will ensure effective coverage of risk exposures of the IIFS and allocation of appropriate capital to cover these risks, based predominantly on the Standardised Approach. In order to achieve these objectives, IFSB-15 provides guidance on the features and criteria for high-quality regulatory capital components, including Additional Tier and Tier 2, which comply with *Sharia* rules and principles. Similarly, IFSB-15 provides new guidance on macroprudential tools, such as capital buffers, leverage ratio and domestic systemically important banks, which will facilitate supervisory authorities in achieving the goal of protecting the banking system and the real economy from system-wide shocks.

IFSB-15 also provides more elaborate guidance on capital adequacy treatment of various risk exposures related to *Sharī'ah*-compliant products and services, including *Sukūk*, securitisation and real estate. The new Standard has revised and consolidated earlier guidance on the treatment of profit sharing modes of financing, as well as expanded guidance on credit risk mitigation techniques as well as calculation of capital charge for various approaches of market and operational risks. These revisions endeavour to enhance the loss absorption capacity of the IIFS and provide a more comprehensive framework for the application of risk weights aligned closely to the underlying risk exposures.

Supervisory authorities among the IFSB member countries are expected to start the implementation of IFSB-15 in their respective jurisdictions by January 2015.

The Islamic Financial Services Board 28.10.13

http://www.ifsb.org/preess_full.php?id=242&submit=more

The Islamic Financial Services Board Issued a New Exposure Draft

This new Exposure Draft(ED-16) is the latest step taken by the Islamic Financial Services Board to revise its *Guidance on Key Elements in the Supervisory Review Process of Institutions Offering Islamic Financial Services* (*IIFS*) [excluding Islamic Insurance (Takāful) Institutions and Islamic Mutual Funds] (IFSB-5) in December 2007. Following the issuance of IFSB-5 the global regulatory landscape witnessed a number of developments and reforms which have resulted in the issuance of various publications by the Basel Committee on Banking Supervision (BCBS). Accordingly, the overall aim of this document is to revise and replace IFSB-5 in setting forth guidance on key elements in the supervisory review process for authorities supervising IIFS (excluding Islamic insurance (Takāful) institutions and

Islamic collective investment schemes) taking into consideration the specificities of the IIFS, the lessons learned from the crisis, while complementing the existing international standards on the supervisory review process, in particular those of the BCBS. This document represents the views of the IFSB on (a) the IFSB standards that the IIFS are expected to observe; and (b) the practices that supervisory authorities are expected to apply. The areas addressed by this guidance include, inter alia:

(a) regulatory capital requirements;

(b) internal capital adequacy assessment process (ICAAP);

(c) risk management, including enterprise risk management;

(d) corporate and Sharia governance;

(e) securitisation exposures;

(f) concentration risk and counterparty credit risk;

(g) assessment of the rate of return risk in the banking book;

(h) sound stress testing practices;

(i) Islamic windows operations;

(j) consolidated and home-host supervision, and supervisory colleges; and

(k) transparency and market discipline.

This document takes a risk-based approach to the process of supervisory review. Accordingly, later in the document the supervisory implications of the various categories of risk that IIFS face in their operations will be discussed. This document is intended to foster convergence towards best practice among authorities supervising IIFS by establishing a minimum standard, enabling such supervisory authorities to meet their requirements when carrying out the roles expected of them in the light of IFSB standards.

One of the key issues that this document deals with is the role of supervisory authorities in relation to Sharia governance. It is an area that most supervisory authorities find difficult to manage.

ED-16 provides that supervisory authorities should require that each IIFS has a properly functioning Sharia governance system in place, which clearly demonstrates, inter alia: (a) clear terms of reference regarding the SSB's mandate, reporting line and responsibility; and (b) well-defined operating procedures and lines of reporting. The supervisory authority should satisfy itself that an IIFS's Sharia governance system covers the relevant ex-ante and ex-post processes. While the former (ex-ante compliance) concerns: (a) the issuance of Sharia pronouncements/resolutions; and (b) compliance checks before the product is offered to the customers, the latter (ex-post compliance) is about internal Sharia review and Sharia governance reporting.

Supervisory authorities should verify that the Sharia Supervisory Board (SSB) or comparable body is provided with full information on any product or transaction on which a pronouncement is sought, including having its

attention drawn to any areas of possible difficulty identified to the IIFS's management. Supervisory authorities should also verify whether the following elements have been reflected by the IIFS in the Sharia governance mechanism:

(a) issuance procedures of relevant Sharia pronouncements/resolutions and dissemination of information on such Sharia pronouncements/ resolutions to the operative personnel of the IIFS who monitor the day-to-day compliance with the Sharia pronouncements/resolutions;

(b) an internal Sharia compliance review/audit for verifying that Sharia compliance has been achieved; and

(c) an annual Sharia compliance review/audit for verifying that the internal Sharia compliance review/audit has been appropriately carried out and its findings have been duly noted by the Sharia board.

The full document is available on: http://www.ifsb.org/

The Islamic Financial Services Board 28.10.13

INTERNATIONAL DEVELOPMENTS

Developing Local Currency Bond Market: A New Diagnostic Framework

A new diagnostic framework (DF) to assist policymakers in developing bond markets in local currency was released on 7th October. The DF can help analyse the state and efficiency of local currency bond markets (LCBMs) and provide the basis for designing a strategy for market deepening with appropriate sequencing of policy action and delivery of associated technical assistance.

The DF is presented in a new report authored jointly by the IMF, World Bank, European Bank for Reconstruction and Development, and Organization for Economic Co-operation and Development. The report analyses the main elements necessary to deepen domestic bond markets in emerging and developing economies.

The development of a diagnostic framework was endorsed by the G-20 in November 2011 to support the development of LCBMs in emerging markets. In the aftermath of the global financial crisis, development of LCBMs was identified as essential to: (i) increase financing options to meet emerging market needs, including for infrastructure; (ii) prevent excessive reliance on intermediation through global financial centres; (iii) help resolve global imbalances by providing savings instruments for emerging market households; and (iv) improve resilience to shocks.

The paper is the result of a collaborative effort among international financial institutions and has benefited from extensive consultation with stakeholders, including country authorities in emerging markets at various stages of deepening their local currency bond markets, such as South Africa, Turkey, and Uruguay.

International Monetary Fund 08.10.13

http://www.imf.org/external/np/sec/pr/2013/pr13393.htm

Donors pledge US$18.9 million to Strengthen Technical Assistance on Anti-Money Laundering and Combating the Financing of Terrorism

International donors renewed their support for the International Monetary Fund's (IMF) technical assistance in Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT). During a session held yesterday in Washington, D.C., they pledged $18.9 million to the work of the Trust Fund, strengthening the second five-year phase of the global AML/CFT program, which will begin operations on May 1, 2014.

Pledges from Switzerland, Luxembourg, the United Kingdom, Norway, Japan, France, the Netherlands, and Saudi Arabia meet about three-fourths of the stated needs of the Trust Fund over the next five years. The prospects for securing the remaining resources are very good, as discussions are ongoing with a number of other donors who also are interested in contributing to the Trust Fund, including Qatar and Korea.

Phase Two of the Trust Fund builds on the momentum of the successful first phase, which began in April 2009. Since that time, 69 projects have started, including focused bilateral engagements, regional workshops, and appointing advisers. An independent evaluation conducted in early 2012 gave high marks to the Trust Fund. Similar to Phase One, the design of the program for Phase Two will concentrate on longer-term and more focused work in selected countries to deliver sustainable results.

Sean Hagan, General Counsel and Director of the Legal Department, said, "This successful round of pledges from donors is a strong endorsement of the work and its quality, effectiveness and management, under this Trust Fund since 2009. Anti-money laundering and combating terrorist financing efforts remain of real importance to financial stability. Demand for our services remains very high, and the second phase of this Trust Fund will enable us to maintain our important and valued capacity development efforts."

Sharmini Coorey, Director of the IMF's Institute for Capacity Development, added, "This vote of confidence in the Trust Fund is greatly appreciated. Our capacity development efforts are augmented and expanded when we work in partnership with donors towards shared ends."

In an increasingly interconnected world, financial stability is closely linked with financial integrity. Money laundering and terrorist financing activities can undermine the soundness and stability of financial institutions and systems, discourage foreign investment, and distort international capital flows. Moreover, problems in one country can quickly spread to other countries in the region or in other parts of the world. Individual countries benefit from robust AML/CFT regimes, as enhanced financial sector integrity and stability facilitates their integration into the global financial system.

They also contribute to more transparent governance and effective fiscal administration. The integrity of national financial systems is thus essential to financial sector and macroeconomic stability both on a national and international level.

International Monetary Fund 18.12.13

http://www.imf.org/external/np/sec/pr/2013/pr13527.htm

London Stock Exchange is Creating a New Way of Identifying Islamic Finance Opportunities by Launching a World-Leading Islamic Market Index

The Prime Minister unveiled ground-breaking plans for a new Islamic index on the London Stock Exchange today as he declared Britain is open for business at the opening of the World Islamic Economic Forum.

The Prime Minister delivered his message to more than 1,800 political and business leaders from over 115 countries who have travelled to London for the ninth World Islamic Economic Forum – and the first held outside a Muslim country.

Global Islamic investments have soared by 150% since 2006 and are expected to be worth £1.3 trillion next year.

In a speech 29th October, the Prime Minister announced that:

- the government would like the UK to become the first country outside of the Islamic world to issue an Islamic bond; the Treasury is working on the practicalities of issuing a bond-like Sukuk worth around £200 million, which we hope to launch as early as next year

- London Stock Exchange is creating a new way of identifying Islamic finance opportunities by launching a world-leading Islamic Market Index; strengthening FTSE's leading position as a developer of innovative, alternatively-weighted indices, this index will be another global first for the City of London

- the UK government is partnering with the Shell Foundation to create a new £4.5 million grant to boost the work of the Nomou initiative – a growth fund that provides skills and finance to small businesses across the Middle East and the Gulf, which will provide opportunities for British companies in the longer-term

HM Treasury 29.10.13

https://www.gov.uk/government/news/pm-to-unveil-plans-for-new-islamic-index-on-london-stock-exchange

The Dubai Financial Services Authority Signs Agreements With Italian Regulators

The Dubai Financial Services Authority (DFSA) entered into two important agreements, with the Commissione Nazionale per le Società e la Borsa (Italian Securities and Exchange Commission) or CONSOB and Bank d'Italia (Bank of Italy), in Rome.

CONSOB is the public authority responsible for regulating the Italian securities market and protecting the investing public. It also conducts investigations with respect to potential infringements of insider dealing and market manipulation law.

The Bank of Italy is the central bank of the Republic of Italy and is responsible, among other issues, for the stability and efficiency of the financial system, regulating, co-ordinating, and controlling the provision of credit.

Mr Ian Johnston, Chief Executive of the DFSA said:

> "The DFSA is very pleased to have settled these protocols with each of Italy's financial supervisors. In doing so, our Italian counterparts have expressed their confidence in the DFSA's equivalence with international standards and our willingness and ability to share information and assist. This is especially important as two of Italy's largest financial institutions have branches in the Dubai International Financial Centre (DIFC). These just completed arrangements will give confidence to investors that both home and host supervisors are working closely together in Dubai and in Rome to ensure sound supervision of these institutions."

The Dubai Financial Services Authority 30.12.13

http://www.dfsa.ae/WhatsNew/DispForm.aspx?ID=275

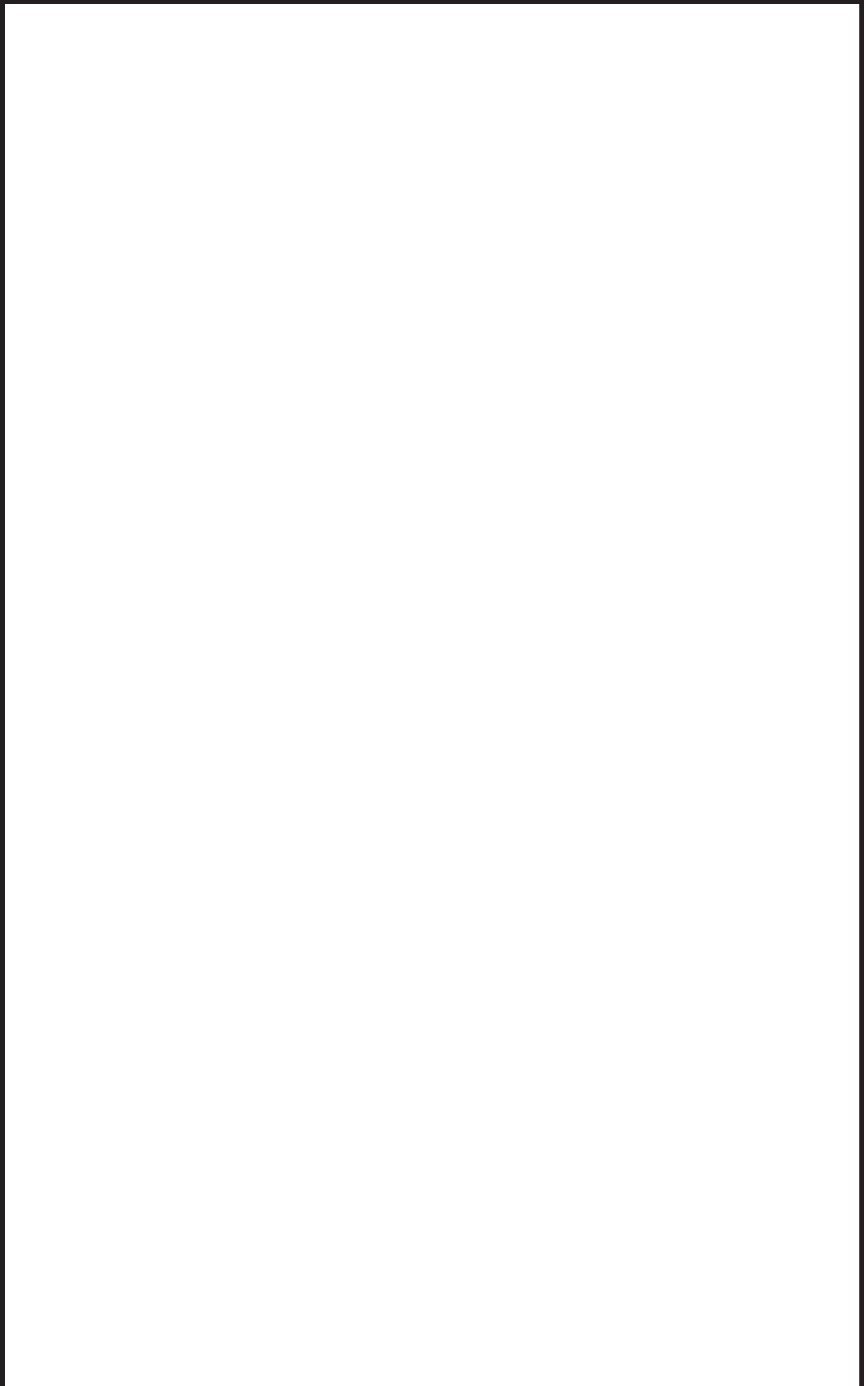
The Dubai International Financial Centre Commissioner of Data Protection and UK Information Commissioner Sign Landmark Agreement

The DIFC Commissioner of Data Protection, the independent regulator set up to uphold data privacy for individuals in or from DIFC, signed a Memorandum of Understanding (MoU) with the UK Information Commissioner's Office. The memorandum outlined a mutual agreement that both parties would collaborate on a formal basis on their shared commitment to uphold and enforce data protection rights in their respective jurisdictions.

The premise of the MoU is to establish a formal basis for cooperation, including the investigation of suspected offences under the UK Data Protection Act 1998 and the Data Protection Law, DIFC Law No.1 of 2007. Under the new agreement, the DIFC Commissioner of Data Protection and the UK Information Commissioner agree to discuss issues of concern to their respective organisations when an issue of mutual interest or concern arises.

The Dubai International Financial Centre 16.12.13

http://www.difc.ae/news/difc-commissioner-data-protection-and-uk-information-commissioner-sign-landmark-agreement



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