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MIFID II: ESMA ISSUES Q&AS ON DOUBLE VOLUME CAP

On 04 November 2016, the European Securities and Markets Authority (ESMA) issued a Question and Answers (Q&A) document regarding the implementation of the “double” volume cap (DVC) under the Markets in Financial Instruments Directive and Regulation (MiFID II / MiFIR). This mechanism limits the use of reference price waivers and negotiated price waivers under the new transparency regime of MiFID II.

The Q&A mechanism is a tool used to promote common supervisory approaches and practices. More precisely, this Q&A document is a more transparent approach to provide responses to questions asked by the public. It gives detailed response on the following topics:

- Clarifications of what data should be taken into consideration with respect to volumes traded under MiFID I waivers in 2017
- The application of the DVC regarding Mutually Traded Funds (MTF) only shares, depository receipts, certificates, and newly issued instruments
- Mid-month reports

Any requirements under MiFID I with regard to the reliability of reference price waivers will maintain validity under MiFIR. However, one little difference may occur in terms of setting eligible prices that can be used by the reference price system. Former negotiated transactions in liquid shares under MiFID I should count towards the DVC and should be reported by

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MiFID II

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trading venues for the DVC calculation. Concerning the percentage of trading in a financial instrument carried out under the reference price waiver and the negotiated transactions waiver, different scenarios need to be considered. In addition to that, the information for shares newly admitted to trading will be published by ESMA.

This Q&A mechanism will be updated on a continual basis, because more regulatory and implemented technical standards need to be clarified over time.

IMPACTS

The Q&A serves its purpose by providing clarity to competent authorities and firms on the application of the MiFID and MiFIR transparency requirements. In particular, trading platforms, brokers and financial companies issuing securities will be impacted by the pre-trade transparency standards. The entire MiFID II regulatory and implementing technical standards will be applicable from 03 January 2018.

Please find the draft delegated regulation and its annex [here](#).

MIFID II: ESMA CONSULTS ON RTS FOR THE CONSOLIDATED TAPE FOR NON-EQUITY INSTRUMENTS

On 03 October 2016, ESMA issued a consultation paper that seeks stakeholders' views on the draft Regulatory Technical Standards (RTS) ESMA is required to write under Article 65(8)(c) of Directive 20014/65/EU with regard to the consolidated tape (CT) for non-equity instruments. ESMA shall develop a draft RTS that specify the financial instrument data that must be provided in the data stream. For non-equity instruments ESMA should also specify trading venues and Approved Publication Arrangements (APAs) that should be included. Given the higher complexity of the non-equity tape and having in mind that the provision on the non-equity tape of Article 65(2) of MiFID II will only apply from September 2019, ESMA has decided to deliver the draft RTS for the non-equity tape at a later stage.

ESMA considers it important to provide a draft RTS that is balanced between being sufficiently attractive for potential consolidation tape providers (CTPs) while allowing a user-friendly approach. To increase the probability of a viable business case for the non-equity CT, ESMA has considered allowing CTPs to specialize in only one of 13 classes or a group of asset classes

rather than all types of very structurally different non-equity instruments.

In ESMA's view CTPs should not be required to collect information from all trading venues and APAs since the cost of including those sources would be very high relative to the added value for end-users. Therefore, ESMA recommends CTPs to exclude trading venues and APAs with insufficient size. ESMA assessed a number of different options to deem a source significant enough to be mandatorily included in a CT. In the end it was decided that the entire data stream of a particular asset class of a trading venue or APA should be included in the CT if the size of the source taking into account all instruments of that specific asset class reported by the source exceed a certain threshold.

ESMA proposed that the threshold should be determined both in terms of volume and number of transactions reported. Similar rules apply to the threshold that is based on number of trades. ESMA considers that optimally the assessment of the threshold should be performed by APAs and trading venues since they have aggregated information on the numerator, i.e. the volume and number of trades reported per asset class. Alternatively, such assessments can be made by CTPs, but this approach has the drawback that each CT would have to carry out these calculations for each potential source, which appears to be very burdensome and not efficient.

In order to ensure a smooth transition into the new regime and to treat all trading venues and APAs on the same basis, ESMA considers it important to use the same reference point for all tests. ESMA proposes that the first assessments on whether the mandatory minimum thresholds included in the CT are reached should be carried out based on data spanning the period of 01 July 2018 to 31 December 2018, with results published by 01 March 2019. The assessments would be carried out and published twice a year. ESMA suggests that a trading venue or an APA that falls below the minimum threshold for three consecutive periods will no longer be required to be included in the CT. In any case, a CT will be free to include sources that report trades below the thresholds if it wishes to do so.

IMPACTS

It is too early to discuss the possible impact of the introduction of a CT for non-equity instruments. However, there are already some general questions about the introduction of the CT for both equity and non-equity instruments. For example, it is not fully clear who will be interested in the role of becoming a CTP and how they are going to compete with already

established and well-known data providers such as Bloomberg or Thomson Reuters. MiFID II suggests that CTPs would consolidate post-trade information into a continuous electronic data stream and make it publicly available as close to real time as possible, on a reasonable commercial basis and free of charge after 15 minutes. CTPs will have to purchase this data from trading venues and ensure that they will get enough customers who will use paid services in order to cover CTPs' costs.

MAR: ESMA PUBLISHES GUIDELINES ON INSIDE INFORMATION RELATED TO COMMODITY DERIVATIVES

On 30 September 2016, ESMA issued a final report that provides the information related to commodity derivatives markets or related spot markets for the purpose of the definition of inside information on commodity derivatives. Article 7(5) of the Market Abuse Regulation (MAR) requires ESMA to issue a guideline to establish a non-exhaustive indicative list of information that:

- Relates:
 - Directly or indirectly to commodity derivatives as financial instrument admitted to trading or traded on a trading venue
 - Directly to a spot commodity market
- Meets the three criteria laid down in MAR for defining inside information in relation to financial instruments:
 - Being non-public
 - Being precise
 - Being likely to have a significant price effect if it was made public on the commodity derivatives themselves or on the related spot commodity contract;
- Is *“reasonably expected to be disclosed or required to be disclosed in accordance with legal or regulatory provisions at Union or national level, market rules, contract, practice or custom, on the relevant commodity derivatives markets or spot markets”*.

Additional wording has also been introduced in the guidelines to clearly indicate that the guidelines are not meant to further specify the concepts of preciseness of the information nor price sensitivity. These two criteria will have to be taken into account separately when assessing whether information is considered inside information on a case by case basis. With regard to inside information in relation to commodity derivatives, MAR defines the following terms: commodity, spot commodity market, spot market and commodity derivatives.

INFORMATION RELATED TO COMMODITY DERIVATIVES

DEFINITION FROM ARTICLE 3(1) OF MAR

COMMODITY	Any goods of a fungible nature that are capable of being delivered, including metals and their ores and alloys, agricultural products and energy such as electricity
SPOT COMMODITY CONTRACT	Contract for the supply of a commodity traded on a spot market which is promptly delivered when the transaction is settled, and a contract for the supply of a commodity that is not a financial instrument, including physically settled forward contract
SPOT MARKET	A commodity market in which commodities are sold for cash and promptly delivered when the transaction is settled, and other non-financial markets, such as forward markets for commodities
COMMODITY DERIVATIVES	Those financial instruments defined in point 44(c) of Article 4(1) of MiFID II, which relate to a commodity or an underlying referred to in Section C(10) of Annex I to MiFID II

Figure 1: Definition of commodity-related terms
(Source: own representation)

The underlyings referred to in section C(10) of Annex I to MiFID II are: climatic variables, freight rates, inflation rates, other economic statistics and assets, rights obligations, indices and measures not otherwise mentioned in Section C of Annex I to MiFID II. This has an impact on what can be considered a spot commodity contract and whether a “related spot market” exists under MAR. In other words, there may not be any related spot market, within the scope of MAR for certain types of “Commodity derivatives”. Based on the MAR definition, commodity derivatives that have crude metals, agricultural products and energy (including oil and gas) as underlying, are considered to have a related spot market. At the same time commodity derivatives with underlyings from the section C(10) of Annex I to MiFID II do not have a related spot market.

In the consultation paper (CP) on draft guidelines on the MAR (ESMA/2016/444) published on 30 March 2016, ESMA has provided some examples of information related directly / indirectly to commodity derivatives or to spot commodity contracts. Based on the responses, ESMA has revised the final guidelines. For example, regarding information related directly to commodity markets, ESMA decided that some examples of

information that effect the market microstructure are no longer included for consistency, given that their relevance and potential price impact seem considerably smaller than the other examples contained in the guidelines. Another example of information, but this time regarding the information relating indirectly to commodity derivatives, that was not included in the final guidelines comes from the field of freights (shipping). In the CP, ESMA asked whether the “goods” subject to the freight contract or their condition of carriage should be considered as information indirectly related to derivatives on freight rates. Based on responses, ESMA decided that such information should not be disclosed because, inter alia, it is unlikely to have price impact on freight rates, and hence freight derivatives. And finally, the last group of examples contains information directly related to spot commodity contracts. ESMA defines four different groups of products:

WHOLESALE ENERGY PRODUCTS (ELECTRICITY & GAS)	Final guidelines maintain the example relating to the existence in some jurisdictions of national requirements with regard to the energy markets for disclosure of information relating to the auctions of spot markets within a certain delay after the day of delivery
OIL-RELATED PRODUCTS & GAS	<ul style="list-style-type: none"> Statistical information made publicly available in the JODI database on oil and gas News or press releases about the outcome of the conferences held by producing countries (e.g. OPEC) during which in particular production levels are discussed and agreed upon No information about infrastructure, storage facilities and transportation will be included
METAL COMMODITIES	Required to be published according to the rules or practice of the relevant metal commodities markets, when it concerns figures about the stocks or stock movement of metal commodities in warehouses and storage facilities
AGRICULTURAL COMMODITIES	<ul style="list-style-type: none"> Information from private entities regarding changes in conditions governing the storage The statistics on commodities at national level published by public entities Information required to be published according to the practice of the relevant commodity market when information concerns production, imports, exports and stored quantity

Figure 2: Examples of information directly related to spot commodity contracts expected to be disclosed
(Source: own representation)

IMPACTS

Overall, all the changes in information disclosure will contribute to a higher level of transparency in the market for commodity derivatives. Implementing the required changes needs to be prepared carefully to avoid regulatory breaches and corresponding fines.

UCITS & AIFMD: ESMA ISSUES GUIDELINES ON REMUNERATION

On 14 October 2016, ESMA issued two sets of guidelines:

- The Undertakings for Collective Investment in Transferable Securities Directive (UCITS) Remuneration Guidelines; and
- The Alternative Investment Fund Managers Directive (AIFMD) Remuneration Guidelines.

The purpose of the Guidelines is to ensure that management companies (MCs) defined under Article 2(1)(b) of the UCITS Directive as well as investment companies (called UCITS) that have not designed an MC, have converging practices on remuneration governance, requirements on risk alignment, and disclosure.

14 December 2016 is the deadline for National Competent Authorities (NCAs) to notify ESMA whether they will or intend to comply with these Guidelines as well as their reasons for non-compliance. Afterwards, ESMA will publish a compliance table based on the responses obtained from the NCAs. Both guidelines will apply from 01 January 2017.

UCITS REMUNERATION GUIDELINES

The UCITS Remuneration Guidelines address MCs under UCITS Directive in relation to their remuneration policy and practices for their identified staff.

CATEGORY	GUIDELINE	KEY ELEMENTS
REMUNERATION DEFINITION	<p>MCs shall ensure that remuneration is not paid through vehicles or methods evading provisions.</p> <p>When delegating remuneration functions (e.g. risk management), MCs must ensure that entities are subject to remuneration requirements.</p>	<p>Remuneration (fixed or variable) may consist of:</p> <ul style="list-style-type: none"> • All forms of payments paid by MCs • Any amount paid by the UCITS itself • Any transfer of units or shares of the UCITS <p>Dividends or similar distributions that partners / owners received are excluded; unless remuneration circumvents remuneration rules.</p>
IDENTIFIED STAFF	<p>MCs shall identify identified staff based on their functions and demonstrate to competent authorities how they have assessed and selected their identified staff.</p> <p>High-earning staff (staff with similar remunerations as senior managers or risk takers) must be considered as identified staff.</p>	<p>Identified staff include:</p> <ul style="list-style-type: none"> • Executive and non-executive members of the management body of MCs • Senior management • Control functions (e.g. risk management, internal audit, compliance) • Hedging investment team (HR, Admin, etc.) • Other risk takers (staff whose activities may affect the risk profile of the management company or of the managed UCITS)
PROPORTIONALITY	<p>When defining measures to implement remuneration principles, NCAs shall consider MCs' size, internal organization, and the complexity of their activities. In other words, some MCs will need to apply more sophisticated policies and practices for fulfilling the requirements.</p>	<p>Proportionality based on MCs' characteristics:</p> <ul style="list-style-type: none"> • Size. Value of MCs' capital, their assets under management, liabilities, as well as their number of staff and subsidiaries • Internal organization. Legal structure of the MCs or of the UCITS, internal governance, listing on regulated markets • Nature, scope and complexity. Investment policies, strategies, cross-border activities <p>Proportionality based on staff categories:</p> <ul style="list-style-type: none"> • Size of obligations in which a risk taker may enter on behalf of the management company • Size of the group of persons who collectively have a material impact on the company's risk profile • Structure of staff remuneration
MCS PART OF A GROUP	<p>Guidelines apply to all MCs.</p>	<p>There is no exception to the application of the Guidelines, including subsidiaries of credit institutions.</p>
APPLICATION OF SECTORAL RULES	<p>For employees performing services under UCITS Directive and under AIFMD, remuneration shall be determined either:</p> <ul style="list-style-type: none"> • On pro rata basis • By applying sectoral remuneration 	<p>Pro rata basis</p> <p>MCs must, to the extent possible, single out the individual actives based on, for instance, time or assets under management.</p> <p>Sectorial remuneration</p> <p>Variable remuneration should always be paid on AIF- or UCITS instruments (e.g. units or shares of the AIF or UCITS concerned, or equivalent ownership interests, or share-linked instruments or equivalent non-cash instruments)</p>
FINANCIAL SITUATION OF MCS	<p>MCs shall ensure that they maintain a prudent balance between sound financial situation and the remuneration payout.</p>	<p>MCs becoming unable to maintain sound financial situation shall implement adjustments such as reducing payments and trigger performance adjustments (e.g. malus or clawback). Moreover, MCs shall ensure that its financial situation is not adversely affected by:</p> <ul style="list-style-type: none"> • Overall pool of variable remuneration that will be awarded • The variable remuneration to be paid out in that year

GOVERNANCE OF REMUNERATION	MCs shall have in place a governance remuneration structure which is applicable for the whole company.	<p>MCs must have a:</p> <ul style="list-style-type: none"> • Management body. Supervisory function responsible of the design, approval, and oversight of the remuneration policy. It should take input from all competent corporate functions (risk, compliance, HR, strategic planning, etc.) • Remuneration committee. Responsible for supporting management bodies with recommendations and independent advice on remuneration systems • Control functions. Active role in designing, overseeing, and reviewing remuneration policies in other areas
GENERAL REQUIREMENTS ON RISK ALIGNMENT	MCs shall apply general risks adjustments to the remuneration packages of identified staff.	<p>MCs general risk alignment encompasses:</p> <ul style="list-style-type: none"> • General remuneration. Policies shall consider conservative valuation and not ignore risk factors that can put MCs under stress, e.g. concentration or liquidity risk • Discretionary pension benefits. Payment shall be vested after a retention period of five years and not vested all at once incorporating individual risk adjustments. When possible, benefits should be paid in the form of instruments (UCITS units or equivalent non-cash units) • Severance pay. Payments shall be based on performance and include early termination. "Golden parachute" agreement is deemed inconsistent with this guideline • Personal hedging. Staff members shall not hedge their personal remuneration
SPECIFIC REQUIREMENTS ON RISK ALIGNMENT	<p>MCs shall apply specific risks adjustments to the remuneration packages of identified staff considering all risks (on- and off-balance sheet) using qualitative and quantitative measures over time.</p> <p>Qualitative: involvement of experts is needed. Process must be documented.</p> <p>Quantitative: IRR, EBITDA, etc.</p>	<p>MCs specific risk alignment encompasses:</p> <ul style="list-style-type: none"> • Fully flexible policy on variable remuneration. Remuneration shall decrease as result of negative performance and can go down to zero • Risk alignment. Remuneration shall link strategy and objectives to performance (measured qualitatively and quantitatively). There must be an accrual period before the payout begins • Awards. Remuneration shall include ex-ante risk adjustments • Pay-out process. MCs shall include cash vs. instrument payment, accrued and deferred period, as well as the ex-ante and ex-post risk adjustments
DISCLOSURE	MCs shall disclose information that is clear and easily understandable to external and internal counterparties.	<p>Disclosure:</p> <ul style="list-style-type: none"> • External. At least on annual basis and as soon as information becomes available. Report shall include how remuneration was calculated containing all assessed factors and criteria in the processes • Internal. MCs shall make accessible to all staff members their remuneration policies as well as the information that has been disclosed externally. Staff must know in advance the criteria affecting their remuneration. Appraisal processes shall be properly documented

Figure 3: UCITS Guidelines on Remuneration (Source: own representation based on published guidelines)

AIFMD REMUNERATION GUIDELINES

The AIFMD Remuneration Guidelines aim to amend Paragraph 33, Section VIII of the current Guidelines on Remuneration for MCs under the AIFMD (ESMA/2013/232). The amendment relates to the remuneration rules for AIFMDs which are subsidiaries of a credit group stating that there shall not be any exception to the application to any AIFMs.

IMPACTS

The enforcement of the Guidelines on Remuneration will directly impact management companies under UCITS and under AIFMD as they will need to revisit their policies and procedures to be compliant with the Remuneration Guidelines. On one side, MCs' governance policies will need to clearly state the role of the board of directors and of supervisory committees; while on the other side, HR departments will need to adjust job descriptions incorporating obligations and compliance requirements for identified staff. Moreover, NCAs will need to also implement mechanisms for enforcement and supervision of the Guidelines.

Please find the ESMA Guidelines on Remuneration practices [here](#).

NEW DEVELOPMENTS IN CORPORATE GOVERNANCE: EBA REVISES ITS GUIDELINES ON INTERNAL GOVERNANCE

On 28 October 2016, the European Banking Authority (EBA) published a draft of the revised guidelines on internal governance (Guidelines). The Guidelines will be available for discussion until the end of January 2017. Its finalized version will replace the EBA Guidelines on Internal Governance (GL 44) which were originally published on 27 September 2011.

The revised Guidelines mainly extend and work out in more details the requirements stipulated by the GL 44. For example, they:

- Draw deeper distinctions between the management and supervisory functions of the management body;
- Put complex structures in more profound focus;
- Elaborate specifications towards risk culture and code of conduct.

Some insights into the forthcoming changes:

APPLICATION OF THE PROPORTIONALITY PRINCIPLE

The drafted Guidelines introduce the detailed description of the proportionality principle which the GL 44 had left out. In general, the principle implies that the Corporate Governance arrangements will be consistent with the institution's risk profile and business model. It means that the significant and complex institutions shall have more sophisticated arrangements in contrast to less complex organizations. The Guidelines propose to assess the definitions "complexity" and "significance" in terms of an institution's size, nature, scale and scope of activities.

Additionally, the EBA developed a range of distinct criteria for the assessment, such as the underlying business model and the ownership structure.

MANAGEMENT AND SUPERVISORY FUNCTIONS

Depending on their functions, the Guidelines provide more granular distinction between the members of the management body:

- Executive members who perform management function; and
- Non-executive members performing supervisory function.

The management function implies active engagement in the institution's business activities and decision-making processes. Whereas the supervisory function suggests that the non-executive members monitor and constructively challenge the actions and decisions made by the executive members. The drafted regulation requires that all roles and responsibilities of the executive members shall be properly documented and consequently approved by the non-executive members.

INDEPENDENT MEMBERS IN THE SPECIALIZED COMMITTEES

In contrast to the GL 44, the drafted Guidelines introduce requirements around the setting up of specialized committees, their composition and processes. In particular, the Guidelines oblige significant institutions, at a minimum, to establish a risk and a nomination committee and allow institutions to decide what other committees should be set up. Whereas the GL 44 principally lists all possible specialized committees, the revised Guidelines recommend reasonable interaction between the specialized committees through the so-called "cross-participation" when the chair or a member of one committee can have a membership in the other committees.

Further, the Guidelines (unlike the GL 44) specify requirements concerning the independent members. Above all, it requires that the majority of the risk committee members are independent. Moreover, the document necessitates that the chair of each committee will be an independent member. The description of the independent members is contained in the other drafted publications - namely, in the joint ESMA and EBA Guidelines on the assessment of the suitability of members of the management body and key function holders. The latter specifies that the independent members shall not execute management functions or be under any undue influence impeding objective judgment.

AVOIDANCE OF THE COMPLEX STRUCTURES AND PRODUCTS

The GL 44 merely requires the management understand the risks which may arise when the institutions operate through

- The special purpose or related structures; or
- Not transparent or not compliant with the international banking standards jurisdictions

Whereas, the reviewed document explicitly recommends that firms avoid establishing such complex structures and products. In view of the recent Panama events, the revised Guidelines intend to strengthen the transparency of the offshore activities, organizational and operational structures. The Guidelines state that the institutions shall refrain from the opaque structures when:

- Clear economic rationale is missing; or
- Legal purpose is absent; or
- Financial crime connection may exist.

The EBA introduces new criteria which the institutions shall take into account when deciding whether to establish such structures or products. The criteria include, for example, the extent to which the structure can be used to hide the ultimate beneficial owner or to which it will serve an apparent lawful purpose. It is also required that firms document the decision to establish a complex structure. Such decision shall be justifiable for the case if the competent authority requires it to be rationalized.

SPECIFICATION OF THE RISK CULTURE

The GL 44 already contains the recommendation to develop an institution's risk culture through policies, communication and training. The revised document stipulates the content of such policies and trainings, namely:

- Institution's activities and strategy;
- Risk profile;
- Staff responsibilities concerning risk taking and management.

Additionally, the Guidelines outline in detail the elements of sound risk culture which were missing in the GL 44. For example, the culture should promote open communication and effective challenge in relation to the decision-making processes.

CORPORATE VALUES FOR EXTERNAL PROVIDERS

The GL 44 generally stipulates that the management shall develop high ethical and professional standards. Whereas the Guidelines pinpoint that the institutions shall develop ethical standards not only for the staff but also for external services providers. The developed standards shall then be taken into consideration regarding outsourcing activities.

Whereas the GL 44 solely requires written policies on the implementation of the standards, the drafted document provides distinct elements which shall be covered by such policies. For example, the policies shall define acceptable and unacceptable behaviors connected with financial misconduct as well as economic and financial crime. Besides this, the document introduces the requirement to establish the function which will be responsible for the evaluation of the code of conduct breaches.

STATEMENTS ON THE CONFLICTS OF INTEREST

The Guidelines extend the conflict of interest policy introduced by the GL 44. It recommends including additional mandatory elements like the requirement to abstain from voting in case the executive member's objectivity is compromised or the requirement to obtain a binding consultative advice from the independent members in case the transactions are with related parties. The drafted Guidelines also introduce the obligation to provide written statements when a conflict of interest is identified. Such statements shall clarify the approach to mitigation or resolution of the identified conflict.

IMPACTS

The drafted regulation is aimed at harmonizing Internal Governance processes, arrangements and mechanisms of both credit institutions and investment firms. In comparison to the GL 44, it provides more details on the application of certain principles and measures, and introduces explicit examples and criteria.

	GUIDELINES 44 OF 27 SEPTEMBER 2011	GUIDELINES OF 28 OCTOBER 2016
PROPORTIONALITY PRINCIPLE	Provides no explanation of the proportionality principle	Introduces criteria for the assessment of institutions' complexity and significance
MANAGEMENT AND SUPERVISORY FUNCTIONS	Describes the functions in general	Provides extended and more comprehensive list of requirements for the functions
SPECIALIZED COMMITTEES	Distinctly lists specialized committees: an audit, a risk, a remuneration, a nomination or human resources committee and / or a governance or ethics or compliance committee	Requires a risk, a nomination, an audit committee and other committees and introduces requirements towards setting up, composition and roles of the committees
COMPLEX AND NON-TRANSPARENT STRUCTURES	Provides broad description of the structures	Provides more details on such structures and simultaneously restrict its application
RISK CULTURE	Provides general insight into the risk culture	Stipulates the content of the policies and trainings related to the risk culture
CORPORATE VALUES AND CODE OF CONDUCT	Gives overall requirements towards ethical standards-related policies	Provides mandatory elements of the corporate values-related policies and stipulates the necessity to introduce the function which will be responsible for the evaluation of the breaches of the code of conduct
CONFLICTS OF INTEREST	Lists a few elements of the conflicts of interest policy	Extends the mandatory elements of the conflicts of interest policy and introduces an obligation to provide written statements in case of identification of a conflict of interest

Figure 4: General overview of the changes in Internal Governance (Source: own presentation based on the Guidelines)

In order to address the revised requirements on the Internal Governance arrangements and processes, it will be required to conduct a gap analysis of the existing policies and procedures as well as assessing its compliance with the forthcoming requirements. The institutions shall also be prepared to provide related reports, written statements and trainings.

EBA PUBLISHES WORK PROGRAM FOR 2017

On 12 October 2016, the EBA published its comprehensive work program for 2017 in accordance with Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 to provide the European banking sector with clear and detailed perspectives of the agency's objectives and activities from 2017 to 2020.

This multi-annual work program package gives a summary and focus of priorities, strategic aims and deliverables the EBA wants to fulfil on certain areas within the forthcoming years. Based on urgent requests from the European Commission and the Financial Services industry, the adaption of EBA's 2017-2020

multi-annual work package resulted in an activity definition as per workload, resources and business needs in the light of legislation, transparency and accountability. As a result, **seven strategic areas and 38 annual work program activities** were defined and supported by key performance indicators (KPIs) for future tracking.

Since the release of the first official annual work program for 2014, the EBA is willing to promote its mission within the banking sector by facing several challenges within the landscape. Following the affirmation of building a single regulatory and supervisory framework for the entire banking sector in the EU member states, to ensure an efficient and stable market, the EBA plays an important role in harmonizing prudential rules. With the usage of regular risk assessment reports, transparency exercises and stress tests, vulnerability of the EU banking sector is assessed pre-emptively and sustainably. By monitoring the functioning of the single rulebook and working towards intelligent proportionality between regulation and complexity, the EBA tries to find consistent approaches in the best way. Furthermore, non-performing assets and restoring of lending capacity is still a major topic for adjustments of balance sheets of financial institutions. In particular, the setting of the bank-specific "Minimum requirement for own funds and

eligible liabilities (MREL)” will be a driving key factor. Finally, the uprising of digital banking, FinTech companies and consumer protection per se enlarges the playground of the banking sector through technological and regulatory questions. Consequently, reshaping of the annual work packages led to the following discussed development plan of seven strategic areas:

1. Play a central role in the regulation and policy framework with the development and maintenance of the Single Rulebook

The first strategic area comprises twelve activities alone, from capital requirements and internal governance for anti-money laundering over new focus on liquidity risk or leverage ratios to bond securitization, audit and operational risk aspects. The EBA contributes with these initiatives to the development of **one single rulebook** to govern the EU banking sector comprising Euro and non-Euro countries.

2. Promote efficient and coordinated crisis management of credit institutions, investment firms and financial market infrastructures in the EU

Through ongoing development of the mentioned rulebook and fostering of resolution and recovery schemes to facilitate cross-border cooperation and mediation, the EBA wants to secure a **coherent mutual crisis management approach** within the industry. This covers: non-banking resolution policies, oversight and convergence of these as well as deposit guarantee scheme-related task groups, further development of resolution plans and assessment of resolvability is triggered.

3. Promote the convergence of supervisory methodologies and practices to a high standard

To ensure consistent convergence of supervisory methodologies, six activities have been defined to oversee the colleges of supervisors of the largest cross-border banks. Through future-oriented expansion of the development of methodologies, additional guidelines and implementation of practices, high standards will be established and applied within the industry. Within this section, monitoring efforts for crisis preparedness are foreseen to secure early intervention.

4. Identify and analyze trends, potential risks and vulnerabilities stemming from the microprudential level across borders and sectors

Going into economical microprudential aspects and key risks follows the goal to maintain the functionality and integrity of EU’s financial market and system. While taking part in the established stress test work in

an unaffected manner, transparency exercises, improvement of data infrastructure as well as quality-assured risk analytics will be strengthened via maintenance and assessment activities. Additional transparency will be established thanks to publication of detailed data on balance sheet information covering for example the composition of capital, risk-weighted assets (RWA) by risk type, risk exposures or non-performing loans of EU banks in a regular manner.

5. Maintain and develop the common supervisory reporting framework, and strengthen its role as the data hub for the collection, use and publishing of data on EU banks

In addition to data infrastructure and analytics, one objective of EBA within this strategic field is to enhance its own role as a serious data hub for European banks. The focus is on technical interpretation and usage of tools, infrastructure and processing, data quality assurance and improvement of existing dashboards or statistics. Hence, the only decisive tasks regarding databases deal with transparency and risk infrastructure (including its tools).

6. Protect consumers, monitor financial innovation and contribute to efficient, secure and easy retail payments in the EU

In an economy with constant development, new innovations and consumer needs have to be monitored centrally to enhance protection of affected stakeholders. After damaged trust in financial systems and banking institutions among the population, personal usage of financial services has to be offered in a fair and transparent way across the market. As a result, the EBA delivers within three defined activities: a common terminology, free information documents and the statement of fees towards consumers to guarantee no hidden terms within contracts. For financial innovation, regular supervision will continue to find an appropriate balance between new customer benefits, technological progress and maximum risk. This includes guideline contribution for an easy retail payment system under the mandates of the revised Payment Service Directive (PSD2) or standardization of monitoring methods.

7. Be a competent, responsible and professional organization, with effective corporate governance and efficient processes

Last but not least, effectiveness and efficiency shall be a cornerstone for the EBA to be seen as competent, responsible and professional organization within the financial industry. Additionally, the Joint Committee of the European Supervisory Authorities (ESAs) published its own work program for 2017, defining complementary

goals in the light of industry security, legislative products and cross-sectoral risk analysis. Aiming for effective cooperation with all ESAs, synergies shall be used to assure accountability for all actions, secure skilled workforce involvement and high flexibility in information exchange. Furthermore, constant analysis of policies, processes of all departments and internal control standards support these objectives sustainably.

KPI OVERVIEW

Concluding on the strategic areas and the 38 activities behind, the EBA's prioritization (which is affected by reduced budget assigned by the Commission) focuses on several subtopics which need partly legal requirements and mutual alignment with the overall strategy. Concentrating on liquidity and leverage ratios, credit risk and credit risk modelling, recovery planning and early intervention, as well as improvements for the consumer protection, the EBA anticipates a successful year and a sustainable start in their multi-annual work program. As a pillar to effective realization, certain KPIs have been put in place to monitor progress in all strategic areas, as the following graph shows. From the different types, each KPI affects certain strategic areas, counting available or used resources as input, deliverables as output, effects of an output as result and effects of the EBA output as impact. With an annual update, the landscape in banking may be compared against the dashboard as shown on the next page.

ASSESSMENT OF EBA'S WORK SCHEDULE

To summarize, the EBA program will be an ambitious endeavor after reprioritization of set goals in the light of a considerable number of expected legislative reforms within the EU. By increasing the ability of supervisory data collection and small adjustments to last year's work program, impacts are expected to be manageable by local authorities. From this perspective, local authorities will focus on being in line with the changes within the European supervisory framework, duties on information collection and obedience of institutional rules and licensing process principles. As these aspects were predictable and anticipated, effects will be gradual and small for local banks within the financial industry. In general, the upcoming years will show to what extent the realization from 2017 to 2020 can be achieved by the EBA and its framework.

Sources:

Please find Press Release here:

<http://www.eba.europa.eu/-/eba-publishes-work-programme-for-2017>

Please find EBA's Work Program 2017 here:

<http://www.eba.europa.eu/documents/10180/1617016/2017+EBA+Work+Programme.pdf>

Please find ESA's Work Program 2017 here:

<https://esas-joint-committee.europa.eu/Publications/JC%20Work%20Programme/JC%202016%2042%20%28Joint%20Committee%20Work%20Programme%202017%20-%20Final%29.pdf>

EBA 2017 WORK PROGRAM – KPI OVERVIEW

KPI	TARGET 2017	TYPE	Regulatory and policy framework	Crisis management	Supervisory convergence	Risk analysis	EU data hub	Consumer protection, financial innovation and payments	EBA organization
Number of guidelines delivered and recommendations	55	Output	⚡	⚡	⚡			⚡	
Number of reports and opinions delivered and warnings issued	25	Output	⚡	⚡	⚡			⚡	
Percentage of the work program's mandated tasks delivered on time	Above 80%	Output	⚡	⚡	⚡	⚡	⚡	⚡	⚡
Composite indicator of supervisory and resolution convergence	Above 70%	Impact		⚡	⚡				
Percentage of completed yearly assessments of colleges	100%	Output/Result		⚡	⚡				
Feedback on training from seminar participants	'Good' rates exceed 85%	Output/Result	⚡	⚡	⚡			⚡	⚡
Data processing	Up to X days delay	Output/Result					⚡		
Assessment of risks and thematic studies	3 risk reports & 2 thematic studies	Output				⚡			
Transparency and data dissemination	Annual publication of transparency data	Output					⚡		
Budget execution (percentage committed of commitment appropriations)	96%	Input							⚡
Number of critical and important audit recommendations received	Target by the end of the year below '3'	Output							⚡
Establishment plan achieved (%)	100%	Output/Result							⚡
Achievements of the target stated in the service level agreements (SLAs)	98%	Output							⚡
Number of visits to the EBA website	#	Impact	⚡	⚡	⚡	⚡	⚡	⚡	⚡

Figure 5: Source - graph published by EBA



CONTACT

If you would like to find out more about Capco's Regulatory expertise around the subject areas discussed within this article or if you have any other questions related to our Regulatory Monitoring Newsletter, please contact the Regulatory Monitoring team: **CE_CM_RegMonEditors@capco.com**.

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